Unit – 4

Strategic Evaluation and control

Strategic evaluation and control could be defined as the process of determining the effectiveness of a given strategy in achieving the organizational objectives and taking corrective action wherever required. The purpose of strategic evaluation is to evaluate the effectiveness of strategy in achieving organizational objectives. In this manner, through the process of strategic evaluation and control, the strategists attempt to answer two sets of questions such as these:

(a) Are the premises made during strategy formulation proving to be correct? Is the strategy guiding the organization towards its intended objectives? Are the organization and its managers doing things which ought to be done? Is there a need to change and reformulate the strategy?

(b) How is the organization performing? Are the time schedules being adhered to? Are the resources being utilized properly? What needs to be done to ensure that resources are utilized properly and objectives are met?

Importance of Strategic Evaluation

The process of strategic management requires that strategists lay down the objectives of the organization and then formulate strategies to achieve them. The process of implementation of strategy starts with the identification of key managerial tasks which form the basis for the creation of organizational structure and design of systems. Here, it should be reiterated that the segregation of key managerial tasks leads to a situation where individual managers are required to perform a small portion of the overall tasks required to implement a strategy. The fact that individually a manager performs a set of functions which are interrelated to the other tasks—that managers elsewhere in the organization are doing makes it clear that the tasks have to be coordinated. The importance of strategic evaluation lies in its ability to coordinate the tasks performed by individual managers and also groups, division, or strategic business units (SBUs) through control of performance. In the absence of coordinating and controlling mechanisms, individual managers may pursue goals which are inconsistent with the overall objectives of the department, division, SBU, or the whole organization.

Strategic evaluation helps to keep a check on the validity of strategic choice. An ongoing process of evaluation would, in fact, provide feedback on the continued relevance of the strategic choice made during the formulation phase. This is due to the efficacy of strategic evaluation to deter- mine the effectiveness of strategy.

Congruence between decisions and intended strategy: During the course of strategy implementation, managers are required to take scores of decisions. Strategic evaluation can help to assess whether the decisions match the intended strategy requirements. This is due to the inherent nature of any administrative system which leaves some amount of discretion in the hands of managers. In the absence of such evaluation, managers would not explicitly know how to exercise such as discretion.

Need for feedback, appraisal and reward: There is a need within an organization to receive feedback on the current performance so that an appraisal can be done and good performance be rewarded. This is essential for the motivation of employees.

Successful culmination of the strategic management process: Strategic evaluation, through its process of control, feedback, rewards, and review helps in a successful culmination of the strategic management process.

Creating inputs for new strategic planning: Lastly, the process of strategic evaluation provides a considerable amount of information and experience to strategists that can be useful for new strategic planning.

Participants in Strategic Evaluation

Board of Directors: In this way, the Board is required to perform the functions of strategic evaluation in more generalized terms. But there is a lot of variation among Indian companies in the way through which the Board may perform its control functions. In some companies, the Board may have the real authority to oversee strategic evaluation while in others, its authority may be usurped by others like the chief executive or a higher de facto authority such as the family council, in the case of family-owned companies, the headquarters in the case of multinational company (MNC) subsidiaries, or the controlling ministry in the case of public sector companies. For example, Murugappa Corporate Board at the Murugappa group of companies assumed responsibilities of governance, strategic advice, and mentoring in 1999 when realization dawned that it was no longer possible for family members to retain operational control of the group companies.

Chief executive officer: a chief executive should not sit in judgement over the performance of the organization under his or her control. Rather, the chief executive should be evaluated on the basis of organization's performance and the long-term value created. This leads to the question of who should evaluate the chief executive. Normally, the evaluation of a person should be done by an individual or a group to whom he reports. In most cases the chief executive officer (CEO) would be evaluated by the board of directors as it is also responsible for the selection, compensation, and termination of the CEO. This is the reason why it is so important to have an independent board. In cases where the chief executive is accountable to no one in particular (as this is possible in the case of an entrepreneurial organization), it is difficult to allocate the responsibility apart from relying on self-evaluation. But in other cases, the ownership pattern can determine who should evaluate the chief executive. Thus, the family council in family-owned companies and majority shareholders in other cases could evaluate a chief executive's performance. It is also interesting to observe how outsiders view CEO performance. Frost & Sullivan CEO of the Year Award used to be given each year to the CEO who had demonstrated leadership excellence within his/her industry. Parameters such as gains in market share, decisions that improved earnings and were responsible for growth the company as well as leadership that affected observable changes in the industry were the common CEO performance measurement criteria Frost & Sullivan utilized in the selection process.

The SBU or profit centre heads may be involved in performance evaluation at their levels and may facilitate evaluation by corporate-level executives form the group of persons who are primarily responsible for operational control based on financial analysis, budgeting, and reporting.

Audit and executive committees set up by the Board or the chief executive may be charged with the responsibility of continuous screening of performance.

The corporate planning staff or department may also be involved in a supporting role for strategic evaluation.

Barriers to Evaluation

Any evaluation is a sensitive exercise. It has to be handled with due care and caution to serve a useful purpose. We could point out five major types of barriers in evaluation and also suggest the means to deal with them next:

Difficulties in measurement: The process of evaluation is fraught with dangers of difficulties in measurement. These mainly relate to the reliability and validity of measurement techniques used for evaluation, lack of quantifiable objectives or performance standards, and the inability of the information system to provide timely and valid information. The control system may be distorted and may not evaluate uniformly or may measure attributes which are not intended to be evaluated. The solutions lie in using reliable and validated measurement systems and standardized procedures for measurement, quantification of objectives as far as possible, and enhance the quality of information system. Use of information technology (IT) for performance management helps to minimize the problem of untimely information.

Resistance to evaluation: The evaluation process involves controlling the behaviours of individuals and, like any similar organizational mechanism, is likely to be resisted by managers. Such resistance can be reduced by open communication with the participants in the evaluation process. A related issue is of being proven wrong or losing face. Top executives, particularly those who have formulated the strategy, sometimes fail to notice the negative signals that the control system provides. This might not be deliberate but happen owing to the human tendency to underrate negative signals and highlight positive ones regarding an issue one supports. Objectivity is an effective means to avoid such a tendency to occur.

Short-termism: Managers often tend to rely on short-term implications of activities and try to measure the im- mediate results. Often, the long-term impact of performance on strategy and the extended effect of strategy on performance are ignored. This is so since immediate assessment seems to be the easy way out and taking into account the long-term implications may be seen as too tedious. Obviously, a change of emphasis on achieving long-term results rather than short-term gains can help to correct this bias.

Relying on efficiency vs effectiveness: It is instructive to remember that efficiency is ‘doing the things rightly' while effectiveness is ‘doing the right things. There is often a genuine confusion among managers as to what constitutes effective performance. Measuring wrong parameters may lead to a situation where the right type of performance does not get rewarded. In fact, sometimes performance that does not really contribute to achievement of objectives may be rewarded if assessed on the basis of efficiency alone. The solution lies in creating a sharp focus on effectiveness as opposed to mere efficiency.

Strategic Control

The process of strategic management makes it clear that a strategy is formulated on the basis of several assumptions. These relate to the environmental and organizational factors that are dynamic and eventful. There is a considerable gap between the time a strategy is formulated and when it is implemented. The process of implementation is itself time-consuming. During this intervening period, there is a possibility that the assumptions. In this manner, strategic controls are early warning systems and differ from post-action controls that evaluate only after the implementation is completed. You could think of strategic control as analogous to the continuous evaluation system used in your management institute and distinguish it from the end-of-the term examination system used in traditional universities.

The four basic types of strategic controls are:

1. Premise control
2. Implementation control
3. Strategic surveillance
4. Special alert control

The following sub-sections address each of these four strategic controls.

Premise Control

Every strategy is based on certain assumptions about environmental and organizational factors. Some these factors are highly significant and any change in them can affect the strategy to a large extent. Premise control is necessary to identify the key assumptions and keep track of any change in them so as to assess their impact on strategy and its implementation. for instance, a company may base its strategy on important assumptions related to environmental factors (e.g. favorable government policies), industrial factors (e.g. changing nature of competition), and organizational factors (e.g. expected breakthrough in research and development (R&D)). Premise control serves the purpose of continually testing the assumptions to find out whether they are still valid or not. This enables the strategists to take corrective action at the right time rather than continuing with a strategy based on erroneous assumptions. The responsibility for premise control can be assigned to the corporate planning staff that can identify key assumptions and keep a regular check on their validity.

Implementation Control

The implementation of a strategy results in a series of plans, programmes, and projects. Resource allocation is done for implementing these. Implementation control is aimed at evaluating whether the plans, programmes, and projects are actually guiding the organization towards its predetermined objectives or not. If, at any time, it is felt that the commitment of resources to a plan, programme, or project would not benefit the organization as envisaged, they have to be revised. In this manner, implementation control may lead to strategic rethinking.

Implementation control may be put into practice through identification and monitoring of strategic thrusts such as an assessment of the marketing success of a new product after pre-testing or checking the feasibility of a diversification programme, after initial attempts at seeking technological collaboration. In the first case, the company may evaluate whether the new product launch will really be advantageous or it should be abandoned in favor of another programme. In the second case, implementation control can help to determine whether a diversification move will actually succeed or not.

Strategic Surveillance

The premise and implementation types of strategic controls are specific in nature. Strategic surveillance, on the other hand, is aimed at a more generalized and overarching control 'designed to monitor a broad range of events inside and outside the company that are likely to threaten the course of a firm's strategy'. Strategic surveillance can be done through a broad-based, general monitoring on the basis of selected information sources to uncover events that are likely to affect the course of strategy of an organization.

Special Alert Control

The last of the strategic control systems is the special alert control, which is based on a trigger mechanism for rapid response and immediate reassessment of strategy in the light of sudden and unexpected events. Special alert control can be exercised through the formulation of contingency strategies and assigning the responsibility of handling unforeseen events to crisis management. Examples of such events can be the sudden fall of a government at the central or state level, instant change in a competitor's posture, an unfortunate industrial disaster, a breach in information security, or a natural catastrophe.

Crises are critical situations that occur unexpectedly and threaten the course of a strategy. Organizations that hope for the best and prepare for the worst are in a vantage position to handle any crisis. Crisis management follows certain steps such as: signal detection, preparation/prevention, containment/damage limitation, and recovery leading to organizational learning.13 The first step of signal detection can be performed by the special alert control systems.

Operational Control

It can be seen that operational control is aimed at allocation and use of organizational resources through evaluation of the performance of organizational units such as divisions or SBUs to assess their contribution to the achievement of organizational objectives. Operational control is concerned with action or performance and this is probably the reason why it is so extensively used in organizations. In this section we see how the process of evaluation is applied for exercising operational control.

Process of Evaluation

The process of evaluation basically deals with four steps:

1. Setting standards of performance
2. Measurement of performance
3. Analyzing variances
4. Taking corrective action

Setting standards of Performance

Strategists encounter the following three questions while dealing with standard setting:

(a) What standards to set?

(b) How to set these standards? and

(c) In what terms do we express these standards?

A three-pronged basic approach to standard-setting could be used to settle these issues.

1. The key managerial tasks, derived from the strategic requirements, can be analyzed for finding out the key areas of performance. Standards can then be set in each of these key result areas.

2. The special requirements for the performance of the key tasks can help to determine the type of standards to set.

3. Performance indicators that best express the special requirements could then be decided upon to be used for evaluation.

Applying this approach to the case of a company which adopts a market development strategy, it can be said that one of the key managerial tasks is to expand market presence and enhance market visibility. The special requirement is to raise the overall market share and two indicators that could satisfy the requirements could be: increase in sales revenue and efficiency of sales force. This company can use these two indicators to measure its operational performance in marketing.

Quantitative criteria: Performance evaluation on the basis of quantitative criteria can be done in two ways: an organization can assess how it has performed as compared to its past achievements and it can also compare its performance with the industry average or that of major competitors. There are several criteria—mainly financial in nature—that can be used. Companies can evaluate their performance on an annual basis for the last 10 years or so on the basis of criteria like net profit, stock price, dividend rates, earnings per share, return on capital, return on equity, market share, growth in sales, days lost per employee as a result of strikes, production costs and efficiency, distribution costs and efficiency, and employee turnover, absenteeism, and satisfaction indexes.14

Companies can also evaluate performance on the basis of industry averages provided in industry reports published in leading business newspapers such as and magazines.

Qualitative criteria: The quantitative criteria, with all their characteristic objectivity and sophistication, cannot be sufficient for an overall assessment of performance. There has to be a set of qualitative criteria for a subjective assessment of factors such as capabilities, core competencies, risk-bearing capacity, business agility, strategic clarity, flexibility, and workability. Qualitative criteria play a major role in strategic control for evaluating strategy before implementation but can be used in operational control too. Glueck and Jauch suggest three sets of qualitative criteria: consistency, appropriateness, and workability.15 Consistency tests strategy with respect to objectives, environmental assumptions, and internal conditions. Appropriateness assesses the strategy from the viewpoint of resources capabilities, risk preference, and time horizon. Lastly, workability checks strategy with regard to its feasibility and stimulation.

Measuring Performance

The evaluation process operates at the performance level as action takes place. Exhibit 14.2 shows how this happens. Note that actual performance is depicted within a dotted boundary as it not a part of the evaluation process. Standards of performance act as the benchmark against which the actual performance is to be compared. It is important, however, to understand how the measurement of performance can take place. The information system is the key element in any measurement exercise. Operationally, measuring is done through accounting, reporting, and communication systems. A variety of evaluation techniques (described in the next section) are used for measurement. Apart from the method of measuring performance, the other important aspects of measurement relate to the difficulties, timing, and periodicity in measuring.

- Difficulties in measurement: If standards are appropriately set, and if means are available for measuring performance, evaluation is a fairly easy task. But there are several activities for which it is difficult to set standards and measure performance. For instance, it is relatively easier to measure the contribution of workers as compared to that of managers. Likewise, it is not so difficult to measure individual effort as it is to assess departmental performance. The solution lies in developing verifiable objectives, stated in quantitative and qualitative terms, against which performance can be measured.

- Timing of measurement: Timing relates to the point of time at which evaluation has to take place. In general, it could be said that delay in measurement can defeat the purpose of evaluation itself. On the other hand, measuring before timing cannot serve the purpose either. It is better to measure at critical points in a task schedule. Generally, the critical points would be at the end of a definable activity or the conclusion of the task. For instance, in a project implementation schedule, there could be several critical points at which measurement can take place. This is called milestone review done at the end of each phase of a project.

- Periodicity in measurement: A related issue to timing is periodicity, which deals with the issue of ‘how often to measure'. Normally, financial statements like budgets, balance sheets, and profit and loss accounts are prepared every year so the periodicity is on an annual basis. But there might be several functions like production and marketing where measurement will have to be done for shorter duration, possibly on a monthly or a weekly basis.

Analyzing Variances

The measurement of actual performance and comparing it with the standard or budgeted performance leads to an analysis of variances. Broadly, the following three situations may arise:

1. The actual performance matches the budgeted performance.
2. The actual performance is better, i.e. deviates positively over the budgeted performance.
3. The actual performance is below, i.e. deviates negatively from the budgeted performance.

The first situation is ideal but not realistic. In practice, the actual performance rarely matches the budgeted performance. Here, the strategists would have to specify a range of tolerance limits between which the results may be accepted satisfactorily. So, actual performance which deviates from the budgeted performance within the tolerance limits established can be acceptable and the variance is considered as not significant.

The second situation is welcome as it an indication of superior performance. But exceeding the target continually should be considered as unusual and a check needs to be done for testing the validity of standards and the efficacy of the measurement system. Exhibit 14.2 takes care of this situation by having feedback from the variance analysis to standards.

The third type of situation is alarming as it indicates a shortfall in achievement. The strategists need to pinpoint the areas where performance is below standard and go into the causes of deviation. Corrective action is taken on the basis of the analysis of the causes of deviation.

Evaluation by the top management can be facilitated if analysis of variance is presented in the form of a simple device that could be termed as the variance chart. The same principle is applied in making control charts for statistical quality control.

Taking Corrective Action

Three courses for corrective action: checking of performance, checking of standards, and reformulating strategies, plans, and objectives.

Initiating corrective action is not an insignificant part of the evaluation process: it involves a variety of managerial functions which are performed during strategy implementation. For instance, checking of performance requires going into the details of organizational structure and systems, as well as behavioral implementation. Performance is affected adversely due to a number of factors such as distortions in resource allocation, inappropriateness of structure and systems, and wrong leadership and motivational styles. If the evaluation process shows that performance is consistently lower than expected, the strategists would have to undertake an in-depth analysis and diagnosis of the factors that might be responsible for bad performance. Taking corrective action for checking performance is, therefore, a significant part of the day-to-day activities of managers.

Checking of standards is less frequent than a performance check but it will have to be done as soon as it is felt that there is nothing significantly wrong with performance. Standards check may result in a lowering of standards if it is concluded that organizational capabilities do not match the performance requirements. It may also lead to an elevation of standards if conditions have improved for better performance to take place. For instance, better equipment, improved system, and upgraded skills are sure to make existing standards partly irrelevant. Productivity frontiers too keep moving farther and competitive pressures compel companies to continually strive to improve their operational effectiveness. In such a situation, standards check would become necessary.

A more radical and infrequent corrective action is to reformulate strategies, plans, and objectives. Strategic, rather than operational, control will lead to the conclusion that strategies call for reformulation, or plans need to be remodeled, or objectives have to be redefined. Reformulation of strategy will take us back to the process of strategic management where a fresh strategic choice has to be made. Remodeling of plans will entail a new resource allocation pattern and subsequent changes in strategy implementation. Redefinition of objectives, however, takes us full circle to the start of the strategic management process.