Unit 1 Tutorials: Planning

INSIDE UNIT 1

What Do Managers Do?

by Sophia

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WHAT'S COVERED

In this lesson, you will learn about this course and what managers do to help organizations achieve top performance. Specifically, this lesson will cover:

1. About Principles of Management
2. Introduction to Managing and Performing
3. Managers in Action

1. About Principles of Managment

So, you're in this course and you may have pondered, or discussed with others, what this course will be about. Principles of Management is an introductory course that uses the leading, planning, organizing, and controlling approach to management. Management is a broad business discipline, and this course covers many areas such as human resource management and strategic management, as well behavioral areas such as motivation. Finally, we all made an effort to present a balanced approach to gender and diversity throughout the challenges in the the use of the terms "male" and "female" when referring to generic managers or employees. Additionally, most lessons contain vocabulary terms and reflection questions learners can use to assure themselves that they have mastered the chapter concepts.

HINT

In this course, you will complete a final Touchstone assignment that illustrates your comprehension of the course material and demonstrates application of knowledge. You will select an organization (for-profit or non-profit) that you are familiar with to perform an internal and external analysis. Hints like this one have been added throughout the lessons to indicate when the content you are learning applies to your final assignment.

You probably have some preconceptions of what management is and what managers do. You have probably had a job where you had a manager whom you had to report to. You may have followed news reports on successful managers like Jeff Bezos of Amazon or Sheryl Sandberg of Facebook and want to learn what made them successful so you can emulate their practices in your career. You may have the impression that management is basically just common sense and that you really don't need to take this course except that you must meet your degree requirements.

You may be an accounting or marketing major who is taking this class because it is required for completion of your degree, but you don't think you will ever need what you learn in this class during your career since you don't plan on applying for HR jobs upon graduation. But regardless of where you are in your career, what you get out of this course will be very valuable. If your first job out of college is or will be as an accountant, sales representative, or another entry-level position, you will appreciate the roles that your managers, both direct and senior level, play in an organization and the behaviors and actions that will get you recognized and appreciated as a valuable member of the team.

2. Introduction to Managing and Performing

Most management textbooks would say that managers spend their time engaged in planning, organizing,

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staffing, directing, coordinating, reporting, and controlling. These activities, as Hannaway found in her study of managers at work, “do not, in fact, describe what managers do" (Hannaway, 1989, p. 39). At best they seem to describe vague objectives that managers are continually trying to accomplish.

The real world, however, is far from being that simple. The world in which most managers work is a “messy and hectic stream of ongoing activity" (Eccles & Nohria, 1992, p. 47). You will never be bored as a manager! A manager’s tasks vary greatly throughout each day, and management positions often come with a great deal of responsibility. As you go through this course, consider some of the challenges of being a manager and how you might apply what you are learning to your own career aspirations.

3. Managers in Action

Managers are in constant action. Virtually every study of managers in action has found that they “switch frequently from task to task, changing their focus of attention to respond to issues as they arise, and engaging in a large volume of tasks of short duration" (Hannaway, 1989, p. 39). Mintzberg observed CEOs on the job to get some idea of what they do and how they spend their time. He found, for instance, that they averaged 36 written and 16 verbal contacts per day, almost every one of them dealing with a distinct or different issue. Most of these activities were brief, lasting less than nine minutes (Mintzberg, 1973).

Kotter studied a number of successful general managers over a five-year period and found that they spend most of their time with others, including subordinates, their bosses, and numerous people from outside the organization. Kotter’s study found that the average manager spent just 25% of his or her time working alone, and that time was spent largely at home, on airplanes, or commuting. Few of them spent less than 70% of their time with others, and some spent up to 90% of their working time this way (Kotter, 1999).

Kotter also found that the breadth of topics in their discussions with others was extremely wide, with unimportant issues taking time alongside important business matters. His study revealed that managers rarely make “big decisions” during these conversations and rarely give orders in a traditional sense. They often react to others’ initiatives and spend substantial amounts of time in unplanned activities that aren’t on their calendars. He found that managers will spend most of their time with others in short, disjointed conversations. “Discussions of a single question or issue rarely last more than ten minutes,” he notes. “It is not at all unusual for a general manager to cover ten unrelated topics in a five-minute conversation" (Kotter, 1999, p. 145-159). More recently, managers studied by Sproull showed similar patterns.

> ↱ EXAMPLE During the course of a day, they engaged in 58 different activities with an average duration of just nine minutes (Sproull, 1984).

Interruptions also appear to be a natural part of the job. Stewart found that the managers she studied could work uninterrupted for half an hour only nine times during the four weeks she studied them (Stewart, 1967). Managers, in fact, spend very little time by themselves. Contrary to the image offered by management textbooks, they are rarely alone drawing up plans or worrying about important decisions. Instead, they spend most of their time interacting with others—both inside and outside the organization.

> DID YOU KNOW
>
> If casual interactions in hallways, phone conversations, one-on-one meetings, and larger group meetings are included, managers spend about two-thirds of their time with other people (Eccles & Nohria, 1992).

As Mintzberg has pointed out, “Unlike other workers, the manager does not leave the telephone or the meeting to get back to work. Rather, these contacts are his work" (Mintzberg, 1973, p. 37).

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BIG IDEA

The interactive nature of management means that most management work is conversational (Pondy, 1978). When managers are in action, they are talking and listening.

Studies on the nature of managerial work indicate that managers spend about two-thirds to three-quarters of their time in verbal activity (Mintzberg, 2009). These verbal conversations, according to Eccles and Nohria, are the means by which managers gather information, stay on top of things, identify problems, negotiate shared meanings, develop plans, put things in motion, give orders, assert authority, develop relationships, and spread gossip. In short, they are what the manager's daily practice is all about. "Through other forms of talk, such as speeches and presentations," they write, "managers establish definitions and meanings for their own actions and give others a sense of what the organization is about, where it is at, and what it is up to" (Eccles & Nohria, 1992, p. 47-48).

SUMMARY

In this lesson, you learned that **Principles of Management** is an introductory course that uses the leading, planning, organizing, and controlling approach. You also learned about what managers do to help organizations achieve top performance. Despite common preconceptions of what managers do and the link between **managing and performing**, understanding the wide variety of tasks, range of responsibilities, and challenges associated with being a manager will be valuable in your own career path, whatever that may be. One key characteristic you learned about is that **managers are always in action**, engaging in a large number of tasks of short duration every day. Successful managers spend most of their working hours with other people, talking with and listening to others on a breadth of topics, encompassing both unimportant issues as well as important business matters.

Best of luck in your learning!

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The Roles Managers Play

by Sophia

WHAT'S COVERED

In this lesson, you will learn about the roles managers play in organizations. You will be introduced to the three core management roles in an organization: Interpersonal, Informational, and Decisional. Each role is then broken down into specific characteristics that further define the nature of duties performed within them. Specifically, this lesson will cover:

1. Interpersonal Roles
2. Informational Roles
3. Decisional Roles

BEFORE YOU START

In Mintzberg's seminal study of managers and their jobs, he found the majority of them clustered around three core management roles: Interpersonal, Informational, and Decisional.

1. Interpersonal Roles

Managers are required to interact with a substantial number of people in the course of a workweek in the **Interpersonal Role**. They host receptions, take clients and customers to dinner, meet with business prospects and partners, conduct hiring and performance interviews, and form alliances, friendships, and personal relationships with many others. Numerous studies have shown that such relationships are the richest source of information for managers because of their immediate and personal nature (Mintzberg, 1990).

Three of a manager's roles arise directly from formal authority and involve basic interpersonal relationships.

Interpersonal Roles	Description
The Figurehead Role	As the head of an organizational unit, every manager must perform some ceremonial duties. In Mintzberg's study, chief executives spent 12% of their contact time on ceremonial duties; 17% of their incoming mail dealt with acknowledgments and requests related to their status.
The Leader Role	Managers are also responsible for the work of the people in their unit, and their actions in this regard are directly related to their role as a leader. The influence of managers is most clearly seen, according to Mintzberg, in the leader role. Formal authority vests them with significant power and influence. Leadership determines, in large part, how much power they have (Mintzberg, 1990). Examples include the return of Starbucks founder Howard Schultz to re-energize and steer his company, and Amazon CEO Jeff Bezos and his ability to innovate during a downturn in the economy (McGregor, 2008).

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The Liaison Role	Popular management literature has had little to say about the liaison role until recently. This role, in which managers establish and maintain contacts outside the vertical chain of command, becomes especially important in view of the finding of virtually every study of managerial work that managers spend as much time with peers and other people outside of their units as they do with their own subordinates. Surprisingly, they spend little time with their own superiors. In Rosemary Stewart's study, 160 British middle and top managers spent 47% of their time with peers, 41% of their time with people inside their unit, and only 12% of their time with superiors.

TERM TO KNOW

Interpersonal Role
One of three major roles identified in Mintzberg's seminal study of managers in which managers form and maintain professional relationships both within and outside the organization.

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2. Informational Roles

In the **Informational Role**, managers are required to gather, collate, analyze, store, and disseminate many kinds of information. In doing so, they become information resource centers, often storing huge amounts of information in their own heads, moving quickly from the role of gatherer to the role of disseminator in minutes. Although many business organizations install large, expensive management information systems to perform many of those functions, nothing can match the intuitive power of a well-trained manager's brain.

Informational Roles	Description
The Monitor Role	As monitors, managers are constantly scanning the environment for information, talking with liaison contacts and subordinates, and receiving unsolicited information, much of it as a result of their network of personal contacts. A good portion of this information arrives in verbal form, often as gossip, hearsay, and speculation.
The Disseminator Role	In the disseminator role, managers pass privileged information directly to subordinates, who might otherwise have no access to it. Managers must not only decide who should receive such information, but how much of it, how often, and in what form. Increasingly, managers are being asked to decide whether subordinates, peers, customers, business partners, and others should have direct access to information 24 hours a day without having to contact the manager directly.
The Spokesperson Role	In the spokesperson role, managers send information to people outside of their organizations: an executive makes a speech to lobby for an organizational cause, or a supervisor suggests a product modification to a supplier. Increasingly, managers are also being asked to deal with representatives of the news media, providing both factual and opinion-based responses that will be printed or broadcast to vast unseen audiences, often directly or with little editing. The risks in such circumstances are enormous, but so too are the potential rewards in terms of brand recognition, public image, and organizational visibility.

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TERM TO KNOW

Informational Role

One of three major roles identified in Mintzberg's seminal study of managers in which managers gather, collate, analyze, store, and disseminate many kinds of information both within and outside the organization.

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3. Decisional Roles

In the **Decisional Role**, ultimately, managers are charged with the responsibility of making decisions on behalf of both the organization and the stakeholders with an interest in it. Such decisions are often made under circumstances of high ambiguity and with inadequate information. Often, the other two managerial roles—interpersonal and informational—will assist a manager in making difficult decisions in which outcomes are not clear and interests are often conflicting.

Informational Roles	Description
The Entrepreneur Role	In the role of entrepreneur, managers seek to improve their businesses, adapt to changing market conditions, and react to opportunities as they present themselves. Managers who take a longer-term view of their responsibilities are among the first to realize that they will need to reinvent themselves, their product and service lines, their marketing strategies, and their ways of doing business as older methods become obsolete and competitors gain an advantage.
The Disturbance or Crisis Handler Role	While the entrepreneur role describes managers who initiate change, the disturbance or crisis handler role depicts managers who must involuntarily react to conditions. Crises can arise because bad managers let circumstances deteriorate or spin out of control, but just as often good managers find themselves in the midst of a crisis that they could not have anticipated but must react to just the same.
The Resource Allocator Role	The third decisional role of resource allocator involves managers making decisions about who gets what, how much, when, and why. Resources, including funding, equipment, human labor, office or production space, and even the boss’s time are all limited, and demand inevitably outstrips supply. Managers must make sensible decisions about such matters while still retaining, motivating, and developing the best of their employees.
The Negotiator Role	The final decisional role is that of negotiator. Managers spend considerable amounts of time in negotiations: over budget allocations, labor and collective bargaining agreements, and other formal dispute resolutions. In the course of a week, managers will often make dozens of decisions that are the result of brief but important negotiations between and among employees, customers and clients, suppliers, and others with whom managers must deal (Mintzberg, 1990).

TERM TO KNOW

Decisional Role

One of three major roles identified in Mintzberg's seminal study of managers in which managers make decisions on behalf of both the organization and the organization's stakeholders.

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SUMMARY

In this lesson, you learned about the roles managers play in organizations. You were introduced to the three core management roles: Interpersonal, Informational, and Decisional. Each role was then broken down into specific characteristics that further define the nature of duties performed within them. For instance, the **Interpersonal Role** comprises how managers form and maintain professional relationships both within and outside the organization, in the roles of figurehead, leader, and liaison. In the **Informational Role**, managers are required to gather, collate, analyze, store, and disseminate many kinds of information. This type of role involves managers playing the part of a monitor, a disseminator, and a spokesperson. Lastly, in the **Decisional Role**, a manager is responsible for making decisions on behalf of both the organization and its stakeholders; this role may involve decisions made by a manager through the lens of entrepreneur, crisis handler, resource allocator, or negotiator—and often with the assistance of the Interpersonal and Informational Roles.

Best of luck in your learning!

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TERMS TO KNOW

Decisional Role

One of three major roles identified in Mintzberg's seminal study of managers in which managers make decisions on behalf of both the organization and the organization's stakeholders.

Informational Role

One of three major roles identified in Mintzberg's seminal study of managers in which managers gather, collate, analyze, store, and disseminate many kinds of information both within and outside the organization.

Interpersonal Role

One of three major roles identified in Mintzberg's seminal study of managers in which managers form and maintain professional relationships both within and outside the organization.

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Major Characteristics of the Manager's Job

by Sophia

WHAT'S COVERED

In this lesson, you will learn about the characteristics effective managers display. You will also learn about the variety in a manager’s job duties along with their responsibilities in an organization. Specifically, this lesson will cover:

1. Characteristics Effective Managers Display
2. Roles Emphasized in a Manager’s Job
3. Managerial Responsibilities
4. Variations in Managerial Work
    a. Management by Level
    b. Management by Department or Function

1. Characteristics Effective Managers Display

Time is fragmented. Managers have acknowledged from antiquity that they never seem to have enough time to get all those things done that need to be done. In the latter years of the twentieth century, however, a new phenomenon arose: demand for time from those in leadership roles increased, while the number of hours in a day remained constant. Increased work hours was one reaction to such demand, but managers quickly discovered that the day had just 24 hours and that working more of them produced diminishing marginal returns. According to one researcher, “Managers are overburdened with obligations yet cannot easily delegate their tasks. As a result, they are driven to overwork and forced to do many tasks superficially. Brevity, fragmentation, and verbal communication characterize their work” (Mintzberg, 1990, p. 167).

Values compete and the various roles are in tension. Managers clearly cannot satisfy everyone. Employees want more time to do their jobs, while customers want products and services delivered quickly and at high-quality levels. Supervisors want more money to spend on equipment, training, and product development; shareholders want returns on investment maximized. A manager caught in the middle cannot deliver to each of these people what each most wants, and decisions are often based on the urgency of the need and the proximity of the problem.

The job is overloaded. In recent years, many North American and global businesses were reorganized to make them more efficient, nimble, and competitive. For the most part, this reorganization meant decentralizing many processes along with the wholesale elimination of middle management layers. Many managers who survived such downsizing found that their number of direct reports had doubled.

CONCEPT TO KNOW

Classical management theory suggests that seven is the maximum number of direct reports a manager can reasonably handle. In practice, however, the number can vary depending on the industry, task complexity, worker qualifications, and experience.

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Today, high-speed information technology and remarkably efficient telecommunication systems mean that many managers have as many as 20 or 30 people reporting to them directly.

BIG IDEA

Efficiency is a core skill. With less time than they need, with time fragmented into increasingly smaller units during the workday, with the workplace following many managers out the door and even on vacation, and with many more responsibilities loaded onto managers in downsized, flatter organizations, efficiency has become the core management skill of the twenty-first century.

2. Roles Emphasized in a Manager's Job

The entrepreneur role is gaining importance. Managers must increasingly be aware of threats and opportunities in their environment. Threats include technological breakthroughs on the part of competitors, obsolescence in a manager's organization, and dramatically shortened product cycles. Opportunities might include product or service niches that are underserved, out-of-cycle hiring opportunities, mergers, purchases, or upgrades in equipment, space, or other assets. Managers who are carefully attuned to the marketplace and competitive environment will look for opportunities to gain an advantage.

The leader role is also gaining importance. Managers must be more sophisticated as strategists and mentors. A manager's job involves much more than simple caretaking in a division of a large organization. Unless organizations are able to attract, train, motivate, retain, and promote good people, they cannot possibly hope to gain advantage over the competition. Thus, as leaders, managers must constantly act as mentors to those in the organization with promise and potential. When organizations lose a highly capable worker, all else in their world will come to a halt until they can replace that worker.

THINK ABOUT IT

Even if they find someone ideally suited and superbly qualified for a vacant position, they must still train, motivate, and inspire that new recruit, and live with the knowledge that productivity levels will be lower for a while than they were with their previous employee.

3. Managerial Responsibilities

An important question often raised about managers is: What responsibilities do managers have in organizations? According to our definition, managers are involved in planning, organizing, leading, and controlling. Managers have described their responsibilities that can be aggregated into nine major types of activity. These include:

1. *Long-range planning*. Managers occupying executive positions are frequently involved in strategic planning and development.
2. *Controlling*. Managers evaluate and take corrective action concerning the allocation and use of human, financial, and material resources.
3. *Environmental scanning*. Managers must continually watch for changes in the business environment and monitor business indicators such as returns on equity or investment, economic indicators, business cycles, and so forth.

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4. *Supervision*. Managers continually oversee the work of their subordinates.
5. *Coordinating*. Managers often must coordinate the work of others both inside the work unit and out.
6. *Customer relations and marketing*. Certain managers are involved in direct contact with customers and potential customers.
7. *Community relations*. Contact must be maintained and nurtured with representatives from various constituencies outside the company, including state and federal agencies, local civic groups, and suppliers.
8. *Internal consulting*. Some managers make use of their technical expertise to solve internal problems, acting as inside consultants for organizational change and development.
9. *Monitoring products and services*. Managers get involved in planning, scheduling, and monitoring the design, development, production, and delivery of the organization's products and services.

As we shall see, not every manager engages in all of these activities. Rather, different managers serve different roles and carry different responsibilities, depending upon where they are in the organizational hierarchy. We will begin by looking at several variations in managerial work.

4. Variations in Managerial Work

Although each manager may have a diverse set of responsibilities, including those mentioned above, the amount of time spent on each activity and the importance of that activity will vary considerably. The two most salient perceptions of a manager are (1) the manager's level in the organizational hierarchy and (2) the type of department or function for which he is responsible. Let us briefly consider each of these.

4a. Management by Level

We can distinguish three general levels of management: executives, middle management, and first-line management. **Executive managers** are at the top of the hierarchy and are responsible for the entire organization, especially its strategic direction. **Middle managers**, who are at the middle of the hierarchy, are responsible for major departments and may supervise other lower-level managers. Finally, **first-line managers** supervise rank-and-file employees and carry out day-to-day activities within departments (Katz, 1974).

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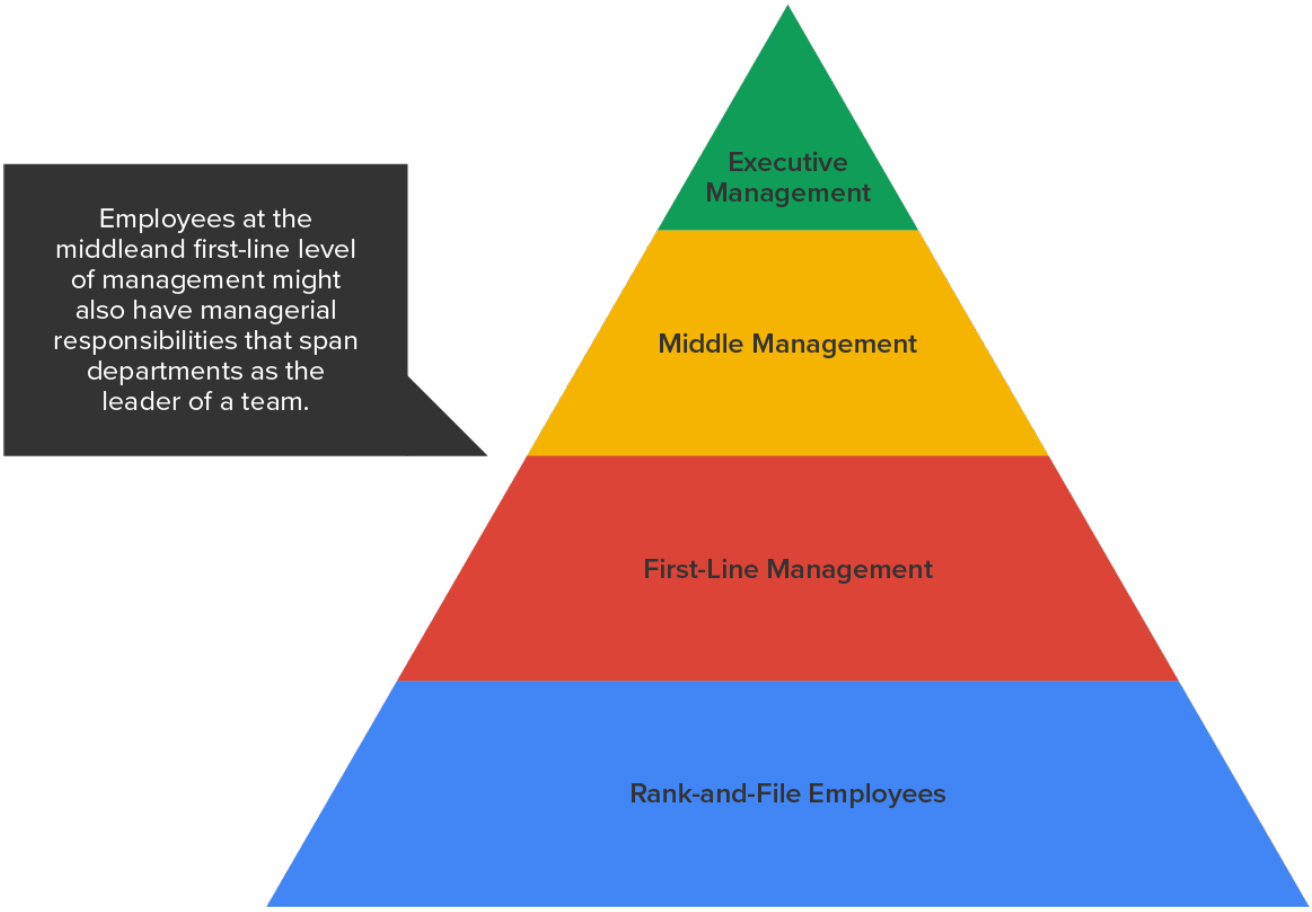

We can distinguish three types of managerial skills:

1. *Technical skills*. Managers must have the ability to use the tools, procedures, and techniques of their special areas. An accountant must have expertise in accounting principles, whereas a production manager must know operations management. These skills are the mechanics of the job.
2. *Human relations skills*. Human relations skills involve the ability to work with people and understand employee motivation and group processes. These skills allow the manager to become involved with and lead his or her group.
3. *Conceptual skills*. These skills represent a manager's ability to organize and analyze information in order to improve organizational performance. They include the ability to see the organization as a whole and to understand how various parts fit together to work as an integrated unit. These skills are required to coordinate the departments and divisions successfully so that the entire organization can pull together.

As shown in the image below, different levels of these skills are required at different stages of the managerial hierarchy. That is, success in executive positions requires far more conceptual skills and less use of technical skills in most (but not all) situations, whereas first-line managers generally require more technical skills and fewer conceptual skills. Note, however, that human relations skills, or people skills, remain important for success at all three levels in the hierarchy.

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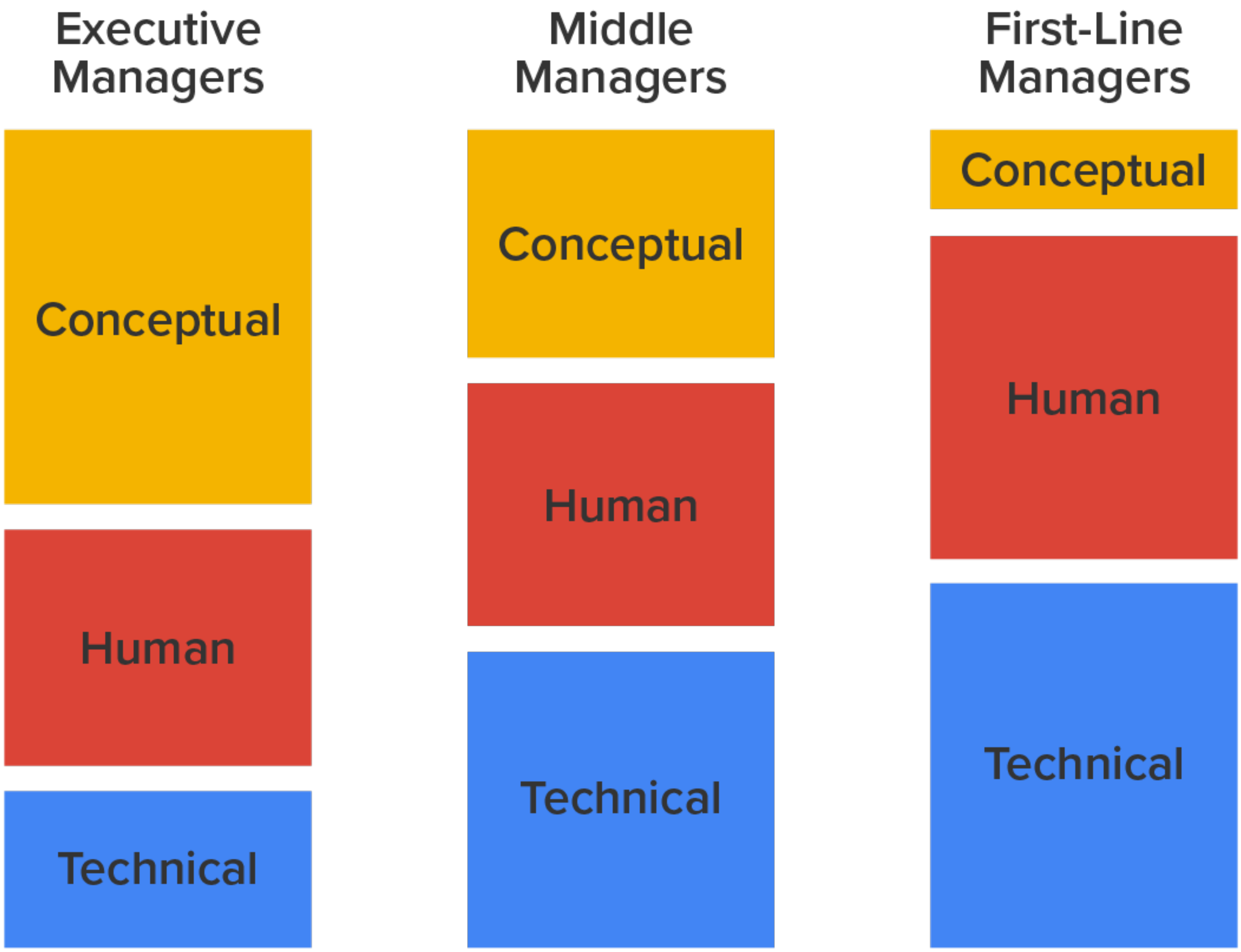

TERMS TO KNOW

Executive Managers
Generally, a team of individuals at the highest level of management of an organization.

Middle Management
The managers in an organization at a level just below that of senior executives.

First-line Management
The level of management directly managing nonmanagerial employees.

4b. Management by Department or Function

In addition to the level in the hierarchy, managerial responsibilities also differ with respect to the type of department or function. There are differences found for quality assurance, manufacturing, marketing, accounting and finance, and human resource management departments, among others.

The emphasis on and intensity of managerial activities varies considerably by the department the manager is assigned to.

At a personal level, knowing that the mix of conceptual, human, and technical skills changes over time and that different functional areas require different levels of specific management activities can serve at least two important functions. First, if you choose to become a manager, knowing that the mix of skills changes over time can help you avoid a common complaint that often young employees want to think and act like a CEO before they have mastered being a first-line supervisor. Second, knowing the different mix of management activities by functional area can facilitate your selection of an area or areas that best match your skills and

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interests.

HINT

In many firms, managers are rotated through departments as they move up in the hierarchy. In this way, they obtain a well-rounded perspective on the responsibilities of the various departments. In their day-to-day tasks, they must emphasize the right activities for their departments and their managerial levels. Knowing what types of activity to emphasize is the core of the manager's job. In any event, we shall return to this issue when we address the nature of individual differences in the next tutorial.

THINK ABOUT IT

Describe and explain the three types of managerial skills and how they relate to each level of management.

SUMMARY

In this lesson, you learned about the **characteristics effective managers display**, noting that in the twenty-first century, where managers have less time and more responsibilities, efficiency has become the core management skill. The **roles emphasized in a manager's job** include the entrepreneur role, as managers must increasingly be aware of threats and opportunities in their environment, as well as the leader role, in which they act as both strategist and mentor. You also learned that **managerial responsibilities** in an organization can be aggregated into nine major types of activity surrounding planning, organizing, leading, and controlling. While not every manager engages in all of these activities, each manager may have a diverse set of responsibilities. You learned about the **variations in managerial work**, exploring how managerial responsibilities differ with respect to a manager's **level** within the organizational hierarchy as well as the type of **department or function**.

Best of luck in your learning!

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TERMS TO KNOW

Executive Managers
Generally, a team of individuals at the highest level of management of an organization.

First-line Management

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The level of management directly managing nonmanagerial employees.

Middle Management

The managers in an organization at a level just below that of senior executives.

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Overview of Managerial Decision-Making

by Sophia

WHAT'S COVERED

In this lesson, we look at characteristics of decision-making that can help you make better decisions and, ultimately, be a better manager. Specifically, this lesson will cover:

1. Decision Making
2. Deciding When to Decide
    a. What's the Right (Correct) Answer?
    b. What's the Right (Ethical) Answer?

1. Decision Making

Managers and business owners make decisions on a daily basis. Some are big, like the decision to start a new business, but most are smaller decisions that go into the regular running of the company and are crucial to its long-term success. Some decisions are predictable, and some are unexpected. In this lesson, we look at important information about decision-making that can help you make better decisions and, ultimately, be a better manager.

Decision-making is the action or process of thinking through possible options and selecting one.

It is important to recognize that managers are continually making decisions and that the quality of their decision-making has an impact—sometimes quite significant—on the effectiveness of the organization and its stakeholders. **Stakeholders** are all the individuals or groups that are affected by an organization (such as customers, employees, shareholders, etc.).

Members of the top management team regularly make decisions that affect the future of the organization and all its stakeholders, such as deciding whether to pursue a new technology or product line. A good decision can enable the organization to thrive and survive long-term, while a poor decision can lead a business into bankruptcy. Managers at lower levels of the organization generally have a smaller impact on the organization's survival, but can still have a tremendous impact on their department and its workers. Consider, for example, a first-line supervisor who is charged with scheduling workers and ordering raw materials for her department. Poor decision-making by lower-level managers is unlikely to drive the entire firm out of existence, but it can lead to many adverse outcomes such as:

- reduced productivity if there are too few workers or insufficient supplies;
- increased expenses if there are too many workers or too many supplies, particularly if the supplies have a limited shelf life or are costly to store; and
- frustration among employees, reduced morale, and increased turnover (which can be costly for the organization) if the decisions involve managing and training workers.

TERMS TO KNOW

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Decision-Making

The action or process of thinking through possible options and selecting one.

Stakeholders

All the individuals or groups that are affected by an organization (such as customers, employees, shareholders, etc.).

---

2. Deciding When to Decide

While some decisions are simple, a manager's decisions are often complex ones that involve a range of options and uncertain outcomes. When deciding among various options and uncertain outcomes, managers need to gather information, which leads them to another necessary decision: how much information is needed to make a good decision? Managers frequently make decisions without complete information; indeed, one of the hallmarks of an effective leader is the ability to determine when to hold off on a decision and gather more information, and when to make a decision with the information at hand. Waiting too long to make a decision can be as harmful for the organization as reaching a decision too quickly. Failing to act quickly enough can lead to missed opportunities, yet acting too quickly can lead to organizational resources being poorly allocated to projects with no chance of success.

Effective managers must decide when they have gathered enough information and must be prepared to change course if additional information becomes available that makes it clear that the original decision was a poor one. For individuals with fragile egos, changing course can be challenging because admitting to a mistake can be harder than forging ahead with a bad plan. Effective managers recognize that given the complexity of many tasks, some failures are inevitable. They also realize that it's better to minimize a bad decision's impact on the organization and its stakeholders by recognizing it quickly and correcting it.

2a. What's the Right (Correct) Answer?

It's also worth noting that making decisions as a manager is not at all like taking a multiple-choice test; with a multiple-choice test, there is always one best answer. This is rarely the case with management decisions. Sometimes a manager is choosing between multiple good options, and it's not clear which will be the best. Other times there are multiple bad options, and the task is to minimize harm. Often there are individuals in the organization with competing interests, and the manager must make decisions knowing that someone will be upset no matter what decision is reached.

2b. What's the Right (Ethical) Answer?

Sometimes managers are asked to make decisions that go beyond just upsetting someone—they may be asked to make decisions in which harm could be caused to others. These decisions have ethical or moral implications. Ethics and morals refer to our beliefs about what is right vs. wrong, good vs. evil, virtuous vs. corrupt. Implicitly, ethics and morals relate to our interactions with and impact on others—if we never had to interact with another creature, we would not have to think about how our behaviors affected other individuals or groups. All managers, however, make decisions that impact others. It is therefore important to be mindful about whether our decisions have a positive or a negative impact. "Maximizing shareholder wealth" is often used as a rationalization for placing the importance of short-term profits over the needs of others who will be affected by a decision—such as employees, customers, or local citizens (who might be affected, for example, by environmental decisions). Maximizing shareholder wealth is often a short-sighted decision, however, because it can harm the organization's financial viability in the future (Stout, 2012). Bad publicity, customers boycotting the organization, and government fines are all possible long-term outcomes when managers make choices that cause harm in order to maximize shareholder wealth. More importantly, increasing the wealth of

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shareholders is not an acceptable reason for causing harm to others.

THINK ABOUT IT

What are some positive outcomes of decision-making for an organization? What are some possible negative outcomes?

As you can see from these brief examples, management is not for the faint of heart! It can, however, be incredibly rewarding to be in a position to make decisions that have a positive impact on an organization and its stakeholders. We see a great example of this in the In Context box.

IN CONTEXT

SUSTAINABILITY AND RESPONSIBLE MANAGEMENT

Brewing Sustainable Success

The focus of a manager or a business owner is often primarily on doing well (making a profit). Sometimes, though, organizational leaders choose to pursue two big goals at once: doing well and simultaneously doing good (benefiting society in some way). Why? Generally because they think it's an important thing to do. The business provides an opportunity to pursue another goal that the founders, owners, or managers are also passionate about. In the case of New Belgium Brewing, the company's cofounders, Jeff Lebesch and Kim Jordan, were passionate about two things: making great beer and environmental stewardship. So it should come as no surprise that their brewery is dedicated to reducing its environmental footprint. The brewery has created a culture that fosters sustainability in a wide range of ways, such as by giving employees a bicycle on their one-year anniversary as a way to encourage them to ride bicycles to work. The organization is also active in advocacy efforts, such as the "Save the Colorado" (River) campaign, and it works hard to promote responsible decision-making when it comes to environmental issues. In fact, as far back as 1999, following an employee vote, the brewery began to purchase all of its electricity from wind power, even though it was more expensive than electricity from coal-burning power plants (which meant reduced profitability and less money for employee bonuses).

While the brewery still relies primarily on wind power, it also now generates a portion of its electricity onsite—some from rooftop solar panels, and even more from biogas, the methane gas byproduct that is created by microbes in the brewery's water treatment plant. The company cleans the wastewater generated from beer production, and in doing so it generates the biogas, which is captured and used for energy to help run the brewery.

Brewing is water-intensive, so New Belgium works hard to reduce water consumption and to recycle the water that it does use. The company also reduces other types of waste by selling used grain, hops, and yeast to local ranchers for cattle feed. The company, which has been employee-owned since 2013, also works with the local utility through a Smart Meter program to reduce their energy consumption at peak times.

All of these efforts at doing good must come at a cost, right? Actually, research shows that companies that are committed to sustainability have superior financial performance, on average, relative to those that are not. In coming up with creative ways to reduce, reuse, and recycle,

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employees often also find ways to save money (like using biogas). In addition, organizations that strive to do good are often considered attractive and desirable places to work (especially by people who have similar values) and are also valued by the surrounding communities. As a result, employees in those organizations tend to be extremely committed to them, with high levels of engagement, motivation, and productivity. Indeed, it seems clear that the employees at the New Belgium Brewery are passionate about where they work and what they do. This passion generates value for the organization and proves that it is, in fact, possible to do well while having also made the decision to do good. And in the case of New Belgium Brewery, that means working to protect the environment while also making delicious beer.

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BRAINSTORM

1. What challenges does New Belgium Brewery face in pursuing environmental goals?
2. Can you think of any other examples of companies that try to "do good" while also doing well?
3. Would you like to work for an organization that is committed to something more than just profitability, even if it meant your salary or bonus would be smaller?

REFLECT

1. What are some positive outcomes of decision-making for an organization? What are some possible negative outcomes?
2. How is managerial decision-making different from a multiple-choice test?
3. In addition to the owners of a business, who are some of the other stakeholders that managers should consider when making decisions?

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SUMMARY

In this lesson, you learned characteristics of **decision-making**—the action or process of thinking through possible options and selecting one—that can help you make better decisions and, ultimately, be a better manager. It is important to recognize that managers, whether top-level or lower-level, are continually making decisions that have an impact on the effectiveness of the organization and its stakeholders. A manager's decisions often involve a range of options and outcomes, requiring them to gather information, which leads them to another necessary decision: **deciding when to decide**. Lastly, you learned that managers are asked to choose between multiple options, both good and bad, to determine **what is the right (correct) answer**, and sometimes are asked to make decisions that have ethical and moral implications, to determine **what is the right (ethical) answer**.

Best of luck in your learning!

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TERMS TO KNOW

Decision-making
The action or process of thinking through possible options and selecting one.

Stakeholders
All the individuals or groups that are affected by an organization (such as customers, employees, shareholders, etc.).

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Programmed and Nonprogrammed Decisions

by Sophia

WHAT'S COVERED

In this lesson, you will learn about programmed and nonprogrammed decisions. You will also learn about the six steps of the decision-making process. Specifically, this lesson will cover:

1. Programmed Decisions
2. Nonprogrammed Decisions
3. The Decision-Making Process

BEFORE YOU START

What is the difference between programmed and nonprogrammed decisions? Because managers have limited time and must use that time wisely to be effective, it is important for them to distinguish between decisions that can have structure and routine applied to them (called programmed decisions) and decisions that are novel and require thought and attention (nonprogrammed decisions).

1. Programmed Decisions

Programmed decisions are those that are repeated over time and for which an existing set of rules can be developed to guide the process. These decisions might be simple, or they could be fairly complex, but the criteria that go into making the decision are all known or can at least be estimated with a reasonable degree of accuracy.

> EXAMPLE Consider a retail store manager developing the weekly work schedule for part-time employees. The manager must consider how busy the store is likely to be, taking into account seasonal fluctuations in business. Then, she must consider the availability of the workers by taking into account requests for vacation and for other obligations that employees might have (such as school). Establishing the schedule might be complex, but it is still a programmed decision: it is made on a regular basis based on well-understood criteria, so structure can be applied to the process.

For programmed decisions, managers often develop **heuristics**, or mental shortcuts, to help reach a decision.

THINK ABOUT IT

The retail store manager may not know how busy the store will be the week of a big sale, but might routinely increase staff by 30% every time there is a big sale (because this has been fairly effective in the past).

Heuristics are efficient—they save time for the decision maker by generating an adequate solution quickly.

HINT

Heuristics don't necessarily yield the optimal solution—deeper cognitive processing may be required for

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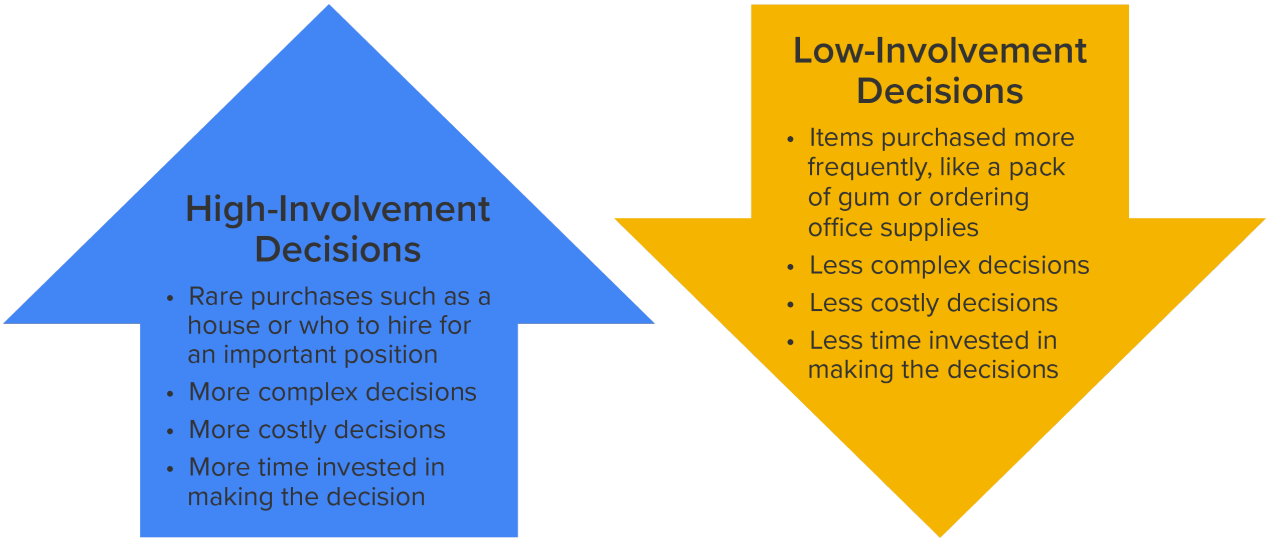
that. However, they often yield a good solution.

Heuristics are often used for programmed decisions because experience in making the decision over and over helps the decision maker know what to expect and how to react. Programmed decision-making can also be taught fairly easily to another person. The rules and criteria, and how they relate to outcomes, can be clearly laid out so that a good decision can be reached by the new decision maker. Programmed decisions are also sometimes referred to as routine or **low-involvement decisions** because they don't require in-depth mental processing to reach a decision. High- and low-involvement decisions are illustrated below.



TERMS TO KNOW

Programmed Decisions
Decisions that are repeated over time and for which an existing set of rules can be developed to guide the process.

Heuristics
Mental shortcuts that allow a decision maker to reach a good decision quickly. They are strategies that develop based on prior experience.

Low-Involvement Decisions
Programmed decisions that don't require in-depth mental processing to reach a decision.

2. Nonprogrammed Decisions

In contrast, **nonprogrammed decisions** are novel, unstructured decisions that are generally based on criteria

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that are not well-defined. With nonprogrammed decisions, information is more likely to be ambiguous or incomplete, and the decision maker may need to exercise some thoughtful judgment and creative thinking to reach a good solution. These are also sometimes referred to as nonroutine decisions or **high-involvement decisions** because they require greater involvement and thought on the part of the decision maker.

THINK ABOUT IT

Consider a manager trying to decide whether or not to adopt a new technology. There will always be unknowns in situations of this nature. Will the new technology really be better than the existing technology? Will it become widely accepted over time, or will some other technology become the standard?

The best the manager can do in this situation is to gather as much relevant information as possible and make an educated guess as to whether the new technology will be worthwhile. Clearly, nonprogrammed decisions present the greater challenge.

TERMS TO KNOW

Nonprogrammed Decisions
Novel, unstructured decisions that are generally based on criteria that are not well-defined.

High-Involvement Decisions
Nonprogrammed decisions that don’t require greater involvement and thought on the part of the decision maker.

3. The Decision-Making Process

While decisions makers can use mental shortcuts with programmed decisions, they should use a systematic process with nonprogrammed decisions. The decision-making process can be broken down into a series of six steps, as follows:

STEP BY STEP

1. Recognize that a decision needs to be made.
2. Generate multiple alternatives.
3. Analyze the alternatives.
4. Select an alternative.
5. Implement the selected alternative.
6. Evaluate its effectiveness.

While these steps may seem straightforward, individuals often skip steps or spend too little time on some steps. In fact, sometimes people will refuse to acknowledge a problem (Step 1) because they aren’t sure how to address it. We’ll discuss the steps in more depth later when we review ways to improve the quality of decision-making.

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REFLECT

1. Give an example of a programmed decision that a manager might face.
2. Give an example of a nonprogrammed decision.
3. What are heuristics, and when are they helpful?
4. How are programmed and nonprogrammed decisions connected to the reflective and reactive systems in the brain?

SUMMARY

In this lesson, you learned about programmed and nonprogrammed decisions. **Programmed decisions**, also known as low-involvement decisions, are those that are repeated over time and for which an existing set of rules can be developed to guide the process. For these types of decisions, managers often develop **heuristics**, or mental shortcuts, to help them quickly and efficiently reach a decision. **Nonprogrammed decisions**, referred to as high-involvement decisions, are novel, unstructured decisions that require more thought and attention. You also learned that when a decision maker is faced by a more challenging nonprogrammed decision, they can break down **the decision-making process** into a series of six steps.

Best of luck in your learning!

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TERMS TO KNOW

Heuristics

Mental shortcuts to help reach a decision.

High-Involvement Decisions

Nonprogrammed decisions that don't require greater involvement and thought on the part of the decision maker.

Low-Involvement Decisions

Programmed decisions that don't require in-depth mental processing to reach a decision.

Nonprogrammed Decisions

Novel, unstructured decisions that are generally based on criteria that are not well-defined.

Programmed Decisions

Decisions that are repeated over time and for which an existing set of rules can be developed to guide the process.

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Barriers to Effective Decision-Making

by Sophia

WHAT'S COVERED

In this lesson, you will learn the barriers that make effective decision-making difficult. Specifically, this lesson will cover:

1. Bounded Rationality
2. Escalation of Commitment
3. Time Constraints
4. Uncertainty
5. Personal Biases
6. Conflict

BEFORE YOU START

What barriers exist that make effective decision-making difficult? There are a number of barriers to effective decision-making. Effective managers are aware of these potential barriers and try to overcome them as much as possible.

1. Bounded Rationality

While we might like to think that we can make completely rational decisions, this is often unrealistic given the complex issues faced by managers. Nonrational decision-making is common, especially with nonprogrammed decisions. Since we haven't faced a particular situation previously, we don't always know what questions to ask or what information to gather. Even when we have gathered all the possible information, we may not be able to make rational sense of all of it, or to accurately forecast or predict the outcomes of our choice. **Bounded rationality** is the idea that for complex issues we cannot be completely rational because we cannot fully grasp all the possible alternatives, nor can we understand all the implications of every possible alternative. Our brains have limitations in terms of the amount of information they can process. Similarly, as was alluded to earlier in the Challenge, even when managers have the cognitive ability to process all the relevant information, they often must make decisions without first having time to collect all the relevant data—their information is incomplete.

TERM TO KNOW

Bounded Rationality

The idea that for complex issues we cannot be completely rational because we cannot fully grasp all the possible alternatives, nor can we understand all the implications of every possible alternative.

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2. Escalation of Commitment

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Given the lack of complete information, managers don't always make the right decision initially, and it may not be clear that a decision was a bad one until after some time has passed.

> EXAMPLE Consider a manager who had to choose between two competing software packages that her organization will use on a daily basis to enhance efficiency. She initially chooses the product that was developed by the larger, more well-established company, reasoning that they will have greater financial resources to invest in, ensuring that the technology is good. However, after some time it becomes clear that the competing software package is going to be far superior. While the smaller company's product could be integrated into the organization's existing systems at little additional expense, the larger company's product will require a much greater initial investment, as well as substantial ongoing costs for maintaining it. At this point, however, let's assume that the manager has already paid for the larger company's (inferior) software.

BRAINSTORM

Will she abandon the path that she's on, accept the loss on the money that's been invested so far, and switch to the better software? Or will she continue to invest time and money into trying to make the first product work?

Escalation of commitment is the tendency of decision makers to remain committed to poor decisions, even when doing so leads to increasingly negative outcomes. Once we commit to a decision, we may find it difficult to reevaluate that decision rationally. It can seem easier to "stay the course" than to admit (or to recognize) that a decision was poor. It's important to acknowledge that not all decisions are going to be good ones, in spite of our best efforts. Effective managers recognize that progress down the wrong path isn't really progress, and they are willing to reevaluate decisions and change direction when appropriate.

TERM TO KNOW

Escalation of Commitment
The tendency of decision makers to remain committed to poor decisions, even when doing so leads to increasingly negative outcomes.

---

3. Time Constraints

Managers often face time constraints that can make effective decision-making a challenge. When there is little time available to collect information and to rationally process it, we are much less likely to make a good nonprogrammed decision. Time pressures can cause us to rely on heuristics rather than engage in deep processing.

HINT

While heuristics save time, they don't necessarily lead to the best possible solution.

The best managers are constantly assessing the risks associated with acting too quickly against those associated with not acting quickly enough.

---

4. Uncertainty

In addition, managers frequently make decisions under conditions of uncertainty—they cannot know the

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outcome of each alternative until they've actually chosen that alternative.

THINK ABOUT IT

Consider, for example, a manager who is trying to decide between one of two possible marketing campaigns. The first is more conservative but is consistent with what the organization has done in the past. The second is more modern and edgier, and might bring much better results…or it might be a spectacular failure.

The manager making the decision will ultimately have to choose one campaign and see what happens, without ever knowing what the results would have been with the alternate campaign. That uncertainty can make it difficult for some managers to make decisions, because committing to one option means forgoing other options.

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5. Personal Biases

Our decision-making is also limited by our own biases. We tend to be more comfortable with ideas, concepts, things, and people that are familiar to us or similar to us. We tend to be less comfortable with that which is unfamiliar, new, and different. One of the most common biases that we have, as humans, is the tendency to like other people who we think are similar to us (because we like ourselves) (Aberson, Healy, & Romero, 2000). While these similarities can be observable (based on demographic characteristics such as race, gender, and age), they can also be a result of shared experiences (such as attending the same university) or shared interests (such as being in a book club together). This "similar to me" bias and preference for the familiar can lead to a variety of problems for managers:

- Hiring less-qualified applicants because they are similar to the manager in some way
- Paying more attention to some employees' opinions and ignoring or discounting others
- Choosing a familiar technology over a new one that is superior
- Sticking with a supplier that is known over one that has better quality, and so on.

It can be incredibly difficult to overcome our biases because of the way our brains work. The brain excels at organizing information into categories, and it doesn't like to expend the effort to rearrange once the categories are established. As a result, we tend to pay more attention to information that confirms our existing beliefs and less attention to information that is contrary to our beliefs, a shortcoming that is referred to as **confirmation bias** (Kolbert, 2017).

In fact, we don't like our existing beliefs to be challenged. Such challenges feel like a threat, which tends to push our brains towards the reactive system and prevent us from being able to logically process the new information via the reflective system. The **reflective system** of decision-making in the brain is logical, analytical, and methodical.

It is hard to change people's minds about something if they are already confident in their convictions.

↱ EXAMPLE When a manager hires a new employee who she really likes and is convinced is going to be excellent, she will tend to pay attention to examples of excellent performance and ignore examples of poor performance (or attribute those events to things outside the employee's control). The manager will also tend to trust that employee and therefore accept their explanations for poor performance without verifying the truth or accuracy of those statements.

The opposite is also true; if we dislike someone, we will pay attention to their negatives and ignore or discount their positives. We are less likely to trust them or believe what they say at face value. This is why

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politics tend to become very polarized and antagonistic within a two-party system. It can be very difficult to have accurate perceptions of those we like and those we dislike. The effective manager will try to evaluate situations from multiple perspectives and gather multiple opinions to offset this bias when making decisions.

TERMS TO KNOW

Confirmation Bias

A shortcoming where people tend to pay more attention to information that confirms their existing beliefs and less attention to information that is contrary to their beliefs.

Reflective System

System of decision-making in the brain that is logical, analytical, and methodical.

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6. Conflict

Finally, effective decision-making can be difficult because of conflict. Most individuals dislike conflict and will avoid it when possible. However, the best decision might be one that is going to involve some conflict.

> EXAMPLE Consider a manager who has a subordinate who is often late to work, causing others to have to step away from their responsibilities in order to cover for the late employee. The manager needs to have a conversation with that employee to correct the behavior, but the employee is not going to like the conversation and may react in a negative way. Both of them are going to be uncomfortable.

The situation is likely to involve conflict, which most people find stressful. Yet, the correct decision is still to have the conversation even if (or especially if) the employee otherwise is an asset to the department.

If the bad behavior is not corrected, it will continue, which is going to cause more problems in the workplace in the long run. Other employees may recognize that this behavior is allowed, and they may also start coming to work late or engaging in other negative behaviors. Eventually, some employees may become sufficiently frustrated that they look for another place to work. It's worth noting that in this situation, the best employees will find new jobs the most quickly. It's important for managers to recognize that while conflict can be uncomfortable (especially in the short-term), there are times when it is necessary for the group, department, or organization to function effectively in the long run.

It is also helpful to think about conflict in terms of process conflict or relationship conflict (Jehn & Mannix, 2001). **Process conflict**, conflict about the best way to do something, can actually lead to improved performance, as individuals explore various options together in order to identify superior solutions. **Relationship conflict** is conflict between individuals that is more personal and involves attacks on a person rather than an idea. This kind of conflict is generally harmful and should be quelled when possible. The harm from relationship conflict arises at least in part because feeling personally attacked will cause an individual to revert to the **reactive system** of the brain.

Effective managers should be particularly aware of the possibility of relationship conflict when giving feedback and should keep feedback focused on behaviors and activities (how things are done) rather than on the individual.

BIG IDEA

Being aware of and dealing with relationship conflict points to why **emotional intelligence** and empathy are beneficial in organizational leaders. Such leaders are more likely to be attentive to the harmful

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consequences of relationship conflict.

REFLECT

1. Explain the concept of confirmation bias.
2. List and describe at least three barriers to effective decision-making.
3. When is conflict beneficial, and when is it harmful? Why?

TERMS TO KNOW

Process Conflict
Conflict about the best way to do something; conflict that is task-oriented and constructive, and not focused on the individuals involved.

Relationship Conflict
Conflict between individuals that is more personal and involves attacks on a person rather than an idea.

Reactive System
System of decision-making in the brain that is quick and intuitive.

Emotional Intelligence
The ability to understand and manage emotions in oneself and in others.

SUMMARY

In this lesson, you learned the barriers that make effective decision-making difficult, noting that effective managers try to overcome them as much as possible. **Bounded rationality** is the idea that for complex issues we cannot be completely rational because we cannot fully understand all the possible alternatives or all the implications of every possible alternative. **Escalation of commitment** refers to the tendency of decision makers to remain committed to poor decisions, even when doing so leads to increasingly negative outcomes. You learned that managers often face **time constraints** that can make effective decision-making a challenge, and that they frequently make decisions under conditions of **uncertainty**. You also learned that decision-making is limited by our own**personal biases**—for example, exhibiting a tendency to like other people who we think are similar to us. Lastly, you learned that effective decision-making can be difficult due to **conflict**, which individuals tend to avoid whenever possible, even though the best decision might be one that is going to involve some conflict.

Best of luck in your learning!

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TERMS TO KNOW

Bounded Rationality
The idea that for complex issues we cannot be completely rational because we cannot fully grasp all the possible alternatives, nor can we understand all the implications of every possible alternative.

Confirmation Bias
A shortcoming where people tend to pay more attention to information that confirms their existing beliefs and less attention to information that is contrary to their beliefs.

Emotional Intelligence
The ability to understand and manage emotions in oneself and in others.

Escalation of Commitment
The tendency of decision makers to remain committed to poor decision, even when doing so leads to increasingly negative outcomes.

Process Conflict
Conflict about the best way to do something; conflict that is task-oriented and constructive, and not focused on the individuals involved.

Reactive System
System of decision-making in the brain that is quick and intuitive.

Reflective System
System of decision-making in the brain that is logical, analytical, and methodical.

Relationship Conflict
Conflict between individuals that is more personal and involves attacks on a person rather than an idea.

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Improving the Quality of Decision-Making

by Sophia

WHAT'S COVERED

In this lesson, you will learn about decision-making techniques, including the six steps in the decision-making process. You will also learn about the four steps involved in ethical decision-making. Specifically, this lesson will cover:

1. Decision-Making Techniques
2. The Importance of Experience
3. Techniques for Making Better Programmed Decisions
4. Techniques for Making Better Nonprogrammed Decisions
   a. Recognizing That a Decision Needs to Be Made
   b. Generating Multiple Alternatives
   c. Analyzing Alternatives
   d. Selecting an Alternative
   e. Implementing the Selected Alternative
   f. Evaluating the Effectiveness of Your Decision

1. Decision-Making Techniques

Managers can use a variety of techniques to improve their **decision-making** by making better-quality decisions or making decisions more quickly. The table below summarizes some of these tactics that may improve individual decision-making.

Type of Decision	Technique	Benefit
Programmed decisions	Heuristics (mental shortcuts)	Saves time
	Satisficing (choosing first acceptable solution)	Saves time
Nonprogrammed decisions	Systematically go through the six steps of the decision-making process.	Improves quality
	Talk to other people.	Improves quality: generates more options, reduces bias
	Be creative.	Improves quality: generates more options
	Conduct research; engage in evidence-based decision-making.	Improves quality
	Engage in critical thinking.	Improves quality

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	Think about the long-term implications.	Improves quality
	Consider the ethical implications.	Improves quality

TERM TO KNOW

Decision-Making

The action or process of thinking through possible options and selecting one.

2. The Importance of Experience

An often overlooked factor in effective decision-making is experience. Managers with more experience have generally learned more and developed greater expertise that they can draw on when making decisions. Experience helps managers develop methods and heuristics to quickly deal with programmed decisions and helps them know what additional information to seek out before making a nonprogrammed decision.

3. Techniques for Making Better Programmed Decisions

In addition, experience enables managers to recognize when to minimize the time spent making decisions on issues that are not particularly important but must still be addressed. As discussed previously, heuristics are mental shortcuts that managers take when making programmed (routine, low-involvement) decisions. Another technique that managers use with these types of decisions is satisficing. When **satisficing**, a decision maker selects the first acceptable solution without engaging in additional effort to identify the best solution. We all engage in satisficing every day.

TERM TO KNOW

Satisficing

When a decision maker selects the first acceptable solution without engaging in additional effort to identify the best solution.

4. Techniques for Making Better Nonprogrammed Decisions

For situations in which the quality of the decision is more critical than the time spent on the decision, decision makers can use several tactics. As stated previously, nonprogrammed decisions should be addressed using a systematic process. We therefore discuss these tactics within the context of the decision-making steps. To review, the steps include the following:

STEP BY STEP

1. Recognize that a decision needs to be made.
2. Generate multiple alternatives.

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3. Analyze the alternatives.
4. Select an alternative.
5. Implement the selected alternative.
6. Evaluate its effectiveness.

4a. Recognizing That a Decision Needs to Be Made

Ineffective managers will sometimes ignore problems because they aren't sure how to address them. However, this tends to lead to more and bigger problems over time. Effective managers will be attentive to problems and opportunities and will not shy away from making decisions that could make their team, department, or organization more effective and more successful.

4b. Generating Multiple Alternatives

Often a manager only spends enough time on this step to generate two alternatives and then quickly moves to the next step in order to make a quick decision. A better solution may have been available, but it wasn't even considered. It's important to remember that for nonprogrammed decisions, you don't want to rush the process. Generating many possible options will increase the likelihood of reaching a good decision. Some tactics to help with generating more options include talking to other people (to get their ideas) and thinking creatively about the problem.

- *Talk to other people.* Managers can often improve the quality of their decision-making by involving others in the process, especially when generating alternatives. Other people tend to view problems from different perspectives because they have had different life experiences. This can help generate alternatives that you might not otherwise have considered. Talking through big decisions with a mentor can also be beneficial, especially for new managers who are still learning and developing their expertise; someone with more experience will often be able to suggest more options.
- *Be creative.* We don't always associate management with creativity, but creativity can be quite beneficial in some situations. In decision-making, creativity can be particularly helpful when generating alternatives. **Creativity** is the generation of new or original ideas; it requires the use of imagination and the ability to step back from traditional ways of doing things and seeing the world. While some people seem to be naturally creative, it is a skill that you can develop. Being creative requires letting your mind wander and combining existing knowledge from past experiences in novel ways. Creative inspiration may come when we least expect it (in the shower, for example) because we aren't intensely focused on the problem—we've allowed our minds to wander. Managers who strive to be creative will take the time to view a problem from multiple perspectives, try to combine information in news ways, search for overarching patterns, and use their imaginations to generate new solutions to existing problems. We'll review creativity in more detail in future Challenges.

TERM TO KNOW

Creativity
The generation of new or original ideas.

4c. Analyzing Alternatives

When implementing this step, it is important to take many factors into consideration. Some alternatives might be more expensive than others, for example, and that information is often essential when analyzing options. Effective managers will ensure that they have collected sufficient information to assess the quality of the

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various options. They will also utilize the tactics described below: engaging in evidence-based decision-making, thinking critically, talking to other people, and considering long-term and ethical implications.

- *Do you have the best quality data and evidence?* **Evidence-based decision-making** is an approach to decision-making that states that managers should systematically collect the best evidence available to help them make effective decisions. The evidence that is collected might include the decision maker's own expertise, but it is also likely to include external evidence, such as a consideration of other stakeholders, contextual factors relevant to the organization, potential costs and benefits, and other relevant information. With evidence-based decision-making, managers are encouraged to rely on data and information rather than their intuition. This can be particularly beneficial for new managers or for experienced managers who are starting something new. (Consider all the research that Rubio and Korey conducted while starting Away).
- *Talk to other people.* As mentioned previously, it can be worthwhile to get help from others when generating options. Another good time to talk to other people is while analyzing those options; other individuals in the organization may help you assess the quality of your choices. Seeking out the opinions and preferences of others is also a great way to maintain perspective, so getting others involved can help you to be less biased in your decision-making (provided you talk to people whose biases are different from your own).
- *Are you thinking critically about the options?* Our skill at assessing alternatives can also be improved by a focus on critical thinking. **Critical thinking** is a disciplined process of evaluating the quality of information, especially data collected from other sources and arguments made by other people, to determine whether the source should be trusted or whether the argument is valid.

An important factor in critical thinking is the recognition that a person's analysis of the available information may be flawed by a number of logical fallacies that they may use when they are arguing their point or defending their perspective. Learning what those fallacies are and being able to recognize them when they occur can help improve decision-making quality.

- *Have you considered the long-term implications?* A focus on immediate, short-term outcomes—with little consideration for the future—can cause problems. For example, imagine that a manager must decide whether to issue dividends to investors or put that money into research and development to maintain a pipeline of innovative products. It's tempting to just focus on the short-term: providing dividends to investors tends to be good for stock prices. But failing to invest in research and development might mean that in five years the company is unable to compete effectively in the marketplace, and as a result the business closes. Paying attention to the possible long-term outcomes is a crucial part of analyzing alternatives.
- *Are there ethical implications?* It's important to think about whether the various alternatives available to you are better or worse from an ethical perspective, as well. Sometimes managers make unethical choices because they haven't considered the ethical implications of their actions. In the 1970s, Ford manufactured the Pinto, which had an unfortunate flaw: the car would easily burst into flames when rear-ended. The company did not initially recall the vehicle because they viewed the problem from a financial perspective, without considering the ethical implications (Trevino & Brown, 2004). People died as a result of the company's inaction. Unfortunately, these unethical decisions continue to occur—and cause harm—on a regular basis in our society. Effective managers strive to avoid these situations by thinking through the possible ethical implications of their decisions. The decision tree below is a great example of a way to make managerial decisions while also taking ethical issues into account.

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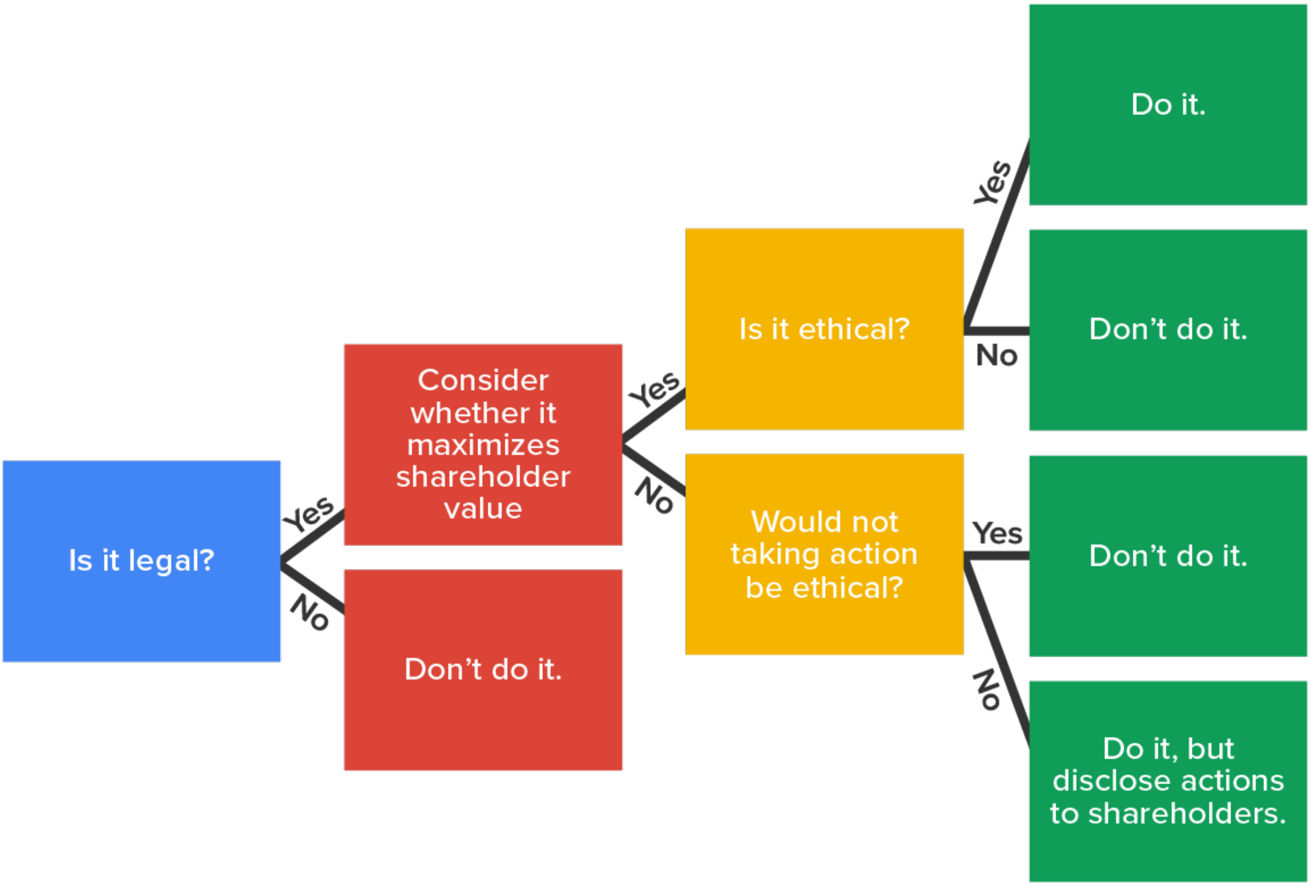

Thinking through the steps of ethical decision-making may also be helpful as you strive to make good decisions. James Rest's ethical decision-making model (Rest, 1986) identifies four components to ethical decision-making:

1. Moral sensitivity—recognizing that the issue has a moral component;
2. Moral judgment—determining which actions are right vs. wrong;
3. Moral motivation/intention—deciding to do the right thing; and
4. Moral character/action—actually doing what is right.

Note that a failure at any point in the chain can lead to unethical actions! Taking the time to identify possible ethical implications will help you develop moral sensitivity, which is a critical first step to ensuring that you are making ethical decisions.
Once you have determined that a decision has ethical implications, you must consider whether your various alternatives are right or wrong—whether or not they will cause harm, and if so, how much and to whom. This is the moral judgment component. If you aren't sure about whether something is right or wrong, think about how you would feel if that decision ended up on the front page of a major newspaper. If you would feel guilty or ashamed, don't do it! Pay attention to those emotional cues—they are providing important information about the option that you are contemplating.

This step in the ethical decision-making model involves making a decision to do what is right, and the next step involves following through on that decision.

THINK ABOUT IT

Consider a situation in which your boss tells you to do something that you know to be wrong. When you push back, your boss makes it clear that you will lose your job if you don't do what you've been told to do. Now, consider that you have a family at home who relies on your income. Making the decision to do what you know is right could come at a substantial cost to you personally. In these situations, your best course

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of action is to find a way to persuade your boss that the unethical action will cause greater harm to the organization in the long term.

TERMS TO KNOW

Evidence-Based Decision-Making

An approach to decision-making that states that managers should systematically collect the best evidence available to help them make effective decisions.

Critical Thinking

A disciplined process of evaluating the quality of information to determine whether the source should be trusted or whether the argument is valid.

4d. Selecting an Alternative

Once alternative options have been generated and analyzed, the decision maker must select one of the options. Sometimes this is easy—one option is clearly superior to the others. Often, however, this is a challenge because there is not a clear "winner" in terms of the best alternative. As mentioned earlier in the Challenge, there may be multiple good options, and which one will be best is unclear even after gathering all available evidence. There may not be a single option that doesn't upset some stakeholder group, so you will make someone unhappy no matter what you choose. A weak decision maker may become paralyzed in this situation, unable to select among the various alternatives for lack of a clearly "best" option. They may decide to keep gathering additional information in hopes of making their decision easier. As a manager, it's important to think about whether the benefit of gathering additional information will outweigh the cost of waiting. If there are time pressures, waiting may not be possible.

- *Recognize that perfection is unattainable.* Effective managers recognize that they will not always make optimal (best possible) decisions because they don't have complete information and/or don't have the time or resources to gather and process all the possible information. They accept that their decision-making will not be perfect and strive to make good decisions overall. Recognizing that perfection is impossible will also help managers to adjust and change if they realize later on that the selected alternative was not the best option.
- *Talk to other people.* This is another point in the process at which talking to others can be helpful. Selecting one of the alternatives will ultimately be your responsibility, but when faced with a difficult decision, talking through your choice with someone else may help you clarify that you are indeed making the best possible decision from among the available options. Sharing information verbally also causes our brains to process that information differently, which can provide new insights and bring greater clarity to our decision-making.

4e. Implementing the Selected Alternative

After selecting an alternative, you must implement it. This may seem too obvious to even mention, but implementation can sometimes be a challenge, particularly if the decision is going to create conflict or dissatisfaction among some stakeholders. Sometimes we know what we need to do but still try to avoid actually doing it because we know others in the organization will be upset—even if it's the best solution. Follow-through is a necessity, however, to be effective as a manager. If you are not willing to implement a decision, it's a good idea to engage in some self-reflection to understand why.

THINK ABOUT IT

If you know that the decision is going to create conflict, try to think about how you'll address that conflict

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in a productive way. It's also possible that we feel that there is no good alternative, or we are feeling pressured to make a decision that we know deep down is not right from an ethical perspective.

These can be among the most difficult of decisions. You should always strive to make decisions that you feel good about—which means doing the right thing, even in the face of pressures to do wrong.

4f. Evaluating the Effectiveness of Your Decision

Managers sometimes skip the last step in the decision-making process because evaluating the effectiveness of a decision takes time, and managers, who are generally busy, may have already moved on to other projects. Yet evaluating effectiveness is important. When we fail to evaluate our own performance and the outcomes of our decisions, we cannot learn from the experience in a way that enables us to improve the quality of our future decisions.

BIG IDEA

Attending fully to each step in the decision-making process improves the quality of decision-making and, as we've seen, managers can engage in a number of tactics to help them make good decisions.

BRAINSTORM

1. If you were faced with an ethical dilemma, from whom would you seek advice?
2. Describe some decisions that might be good for an organization's profitability in the short-term, but bad for the organization in the long-term.
3. What factors would you take into consideration if you were thinking about leaving your job rather than do something unethical?

REFLECT

1. Explain what satisficing is and when it may be a good strategy.
2. What are the six steps in the decision-making process?
3. What are the four steps involved in ethical decision-making?

SUMMARY

In this lesson, you learned about **decision-making techniques** that can be used by managers to help them make better-quality decisions or make decisions more quickly. You learned that the **importance of experience** is often overlooked in effective decision-making; however, it enables managers to recognize when to minimize the time spent making decisions on less important issues. Other **techniques for making better programmed decisions** include using heuristics and satisficing. You also learned that for high-involvement decisions, decision makers can tap into **techniques for making better nonprogrammed decisions**, using the six steps in the decision-making process:**recognizing that a decision needs to be made**; **generating multiple alternatives**; **analyzing alternatives**; **selecting an alternative**; **implementing the selected alternative**; and **evaluating the effectiveness of your decision**. Lastly, you learned that it is important to consider various alternatives from an ethical perspective, exploring the four components to ethical decision-making: moral sensitivity, moral judgment, moral motivation/intention, and moral character/action.

Best of luck in your learning!

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TERMS TO KNOW

Creativity
The generation of new or original ideas.

Critical Thinking
A disciplined process of evaluating the quality of information to determine whether the source should be trusted or whether the argument is valid.

Decision-Making
The action or process of thinking through possible options and selecting one.

Evidence-Based Decision-Making
An approach to decision-making that states that managers should systematically collect the best evidence available to help them make effective decisions.

Satisficing
When a decision maker selects the first acceptable solution without engaging in additional effort to identify the best solution.

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Group Decision-Making

by Sophia

WHAT'S COVERED

In this lesson, will learn about the advantages and disadvantages of group decision-making. You will also learn techniques a manager can use to improve the quality of group decision-making. Specifically, this lesson will cover:

1. Advantages of Group Decisions
2. Disadvantages of Group Decisions
3. How to Form a Quality Group
4. Decision-Making Conclusions

BEFORE YOU START

What are the advantages and disadvantages of group decision-making, and how can a manager improve the quality of group decision-making? Involving more people in the decision-making process can greatly improve the quality of a manager's decisions and outcomes. However, involving more people can also increase conflict and generate other challenges. We turn now to the advantages and disadvantages of group decision-making.

1. Advantages of Group Decisions

An advantage to involving groups in decision-making is that you can incorporate different perspectives and ideas. For this advantage to be realized, however, you need a diverse group. In a diverse group, the different group members will each tend to have different preferences, opinions, biases, and stereotypes. Because a variety of viewpoints must be negotiated and worked through, group decision-making creates additional work for a manager, but (provided the group members reflect different perspectives) it also tends to reduce the effects of bias on the outcome. For example, a hiring committee made up of all men might end up hiring a larger proportion of male applicants (simply because they tend to prefer people who are more similar to themselves). But with a hiring committee made up of an equal number of men and women, the bias should be canceled out, resulting in more applicants being hired based on their qualifications rather than their physical attributes.

Having more people involved in decision-making is also beneficial because each individual brings unique information or knowledge to the group, as well as different perspectives on the problem. Additionally, having the participation of multiple people will often lead to more options being generated and to greater intellectual stimulation as group members discuss the available options. **Brainstorming** is a process of generating as many solutions or options as possible and is a popular technique associated with group decision-making.

All of these factors can lead to superior outcomes when groups are involved in decision-making. Furthermore, involving people who will be affected by a decision in the decision-making process will allow those individuals to have a greater understanding of the issues or problems and a greater commitment to the solutions.

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TERM TO KNOW

Brainstorming

A process of generating as many solutions or options as possible, a popular technique associated with group decision-making.

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2. Disadvantages of Group Decisions

Group decision-making is not without challenges. Some groups get bogged down by conflict, while others go to the opposite extreme and push for agreement at the expense of quality discussions. **Groupthink** occurs when group members choose not to voice their concerns or objections because they would rather keep the peace and not annoy or antagonize others. Sometimes groupthink occurs because the group has a positive team spirit and camaraderie, and individual group members don't want that to change by introducing conflict. It can also occur because past successes have made the team complacent.

Often, one individual in the group has more power or exerts more influence than others and discourages those with differing opinions from speaking up (**suppression of dissent**) to ensure that only their own ideas are implemented. If members of the group are not really contributing their ideas and perspectives, however, then the group is not getting the benefits of group decision-making.

TERMS TO KNOW

Groupthink

Group members choose not to voice their concerns or objections because they would rather keep the peace and not annoy or antagonize others.

Suppression of Dissent

One individual in the group has more power or exerts more influence than others and discourages those with differing opinions from speaking up to ensure that only their own ideas are implemented.

---

3. How to Form a Quality Group

Effective managers will try to ensure quality group decision-making by forming groups with diverse members so that a variety of perspectives will contribute to the process. They will also encourage everyone to speak up and voice their opinions and thoughts prior to the group reaching a decision. Sometimes groups will also assign a member to play the devil's advocate in order to reduce groupthink. The **devil's advocate** intentionally takes on the role of critic. Their job is to point out flawed logic, to challenge the group's evaluations of various alternatives, and to identify weaknesses in proposed solutions. This pushes the other group members to think more deeply about the advantages and disadvantages of proposed solutions before reaching a decision and implementing it.

The methods we've just described can all help ensure that groups reach good decisions, but what can a manager do when there is too much conflict within a group? In this situation, managers need to help group members reduce conflict by finding some common ground—areas in which they can agree, such as common interests, values, beliefs, experiences, or goals. Keeping a group focused on a common goal can be a very worthwhile tactic to keep group members working with rather than against one another. The following table summarizes the techniques to improve group decision-making.

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Type of Decision	Technique	Benefit
Group decisions	Have diverse members in the group.	Improves quality: generates more options, reduces bias
	Assign a devil's advocate.	Improves quality: reduces groupthink
	Encourage everyone to speak up and contribute.	Improves quality: generates more options, prevents suppression of dissent
	Help group members find common ground.	Improves quality: reduces personality conflict

TERM TO KNOW

Devil's Advocate

Person who intentionally takes on the role of critic. Their job is to point out flawed logic, to challenge the group's evaluations of various alternatives, and to identify weaknesses in proposed solutions.

4. Decision-Making Conclusions

Decision-making is a crucial daily activity for managers. Decisions range from small and simple, with straightforward answers, to big and complex, with little clarity about what the best choice will be. Being an effective manager requires learning how to successfully navigate all kinds of decisions. Expertise, which develops gradually through learning and experience, generally improves managerial decision-making, but managers rarely rely solely on their own expertise. They also conduct research and collect information from others, pay attention to their own biases and to ethical implications, and think critically about the information that they have received to make decisions that will benefit the organization and its stakeholders.

REFLECT

1. Explain why group decision-making can be more effective than individual decision-making.
2. What are some things that can prevent groups from making good decisions?
3. As a manager, what can you do to enhance the quality of group decision-making?

SUMMARY

In this lesson, you learned about the **advantages and disadvantages of group decision-making**. You also learned techniques a manager can use to improve the quality of group decision-making. Involving groups in decision-making allows a manager to incorporate different perspectives and ideas (dependent upon having a diverse group), reduce the effects of bias on the outcome, and generate more options through brainstorming. On the other hand, challenges encountered with group decision-making include groupthink and suppression of dissent. You explored **how to form a quality group**, by having diverse members, assigning a devil's advocate, encouraging everyone to contribute, and reducing conflict by helping members find common ground. Lastly, you summarized key **decision-making conclusions** about the characteristics of an effective manager.

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TERMS TO KNOW

Brainstorming

A process of generating as many solutions or options as possible, a popular technique associated with group decision-making.

Devil's Advocate

Person who intentionally takes on the role of critic. Their job is to point out flawed logic, to challenge the group's evaluations of various alternatives, and to identify weaknesses in proposed solutions.

Groupthink

Group members choose not to voice their concerns or objections because they would rather keep the peace and not annoy or antagonize others.

Suppression of Dissent

One individual in the group has more power or exerts more influence than others and discourages those with differing opinions from speaking up to ensure that only their own ideas are implemented.

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Gaining Advantages by Understanding the Competitive Environment

by Sophia

WHAT'S COVERED

In this lesson, you will learn why managers study their competitive environment using a process called strategic analysis. You will also learn how to differentiate between internal factors and external factors in a firm's competitive environment. Specifically, this lesson will cover:

1. Why Firms Need To Analyze Their Competitive Environment
2. The Competitive Environment

1. Why Firms Need To Analyze Their Competitive Environment

Strategic analysis is the process that firms use to study and understand the many different layers and aspects of their competitive environment.

BRAINSTORM

Why do firms spend time and money trying to understand what is going on around them?

Firms do not operate in a vacuum. They are impacted by forces and factors from both inside and outside their organizations. Understanding these forces and factors is crucial to achieving success as an organization.

EXAMPLE The growth in the Spanish-speaking population in the United States has led many firms to change the signage in their stores and labels on their products to include Spanish, in order to make their stores easier to shop in and their products easier to identify for this growing market.

The external environment is continually changing, and the most successful firms are able to prepare for and quickly adapt to environmental changes as needed.

To react to change more easily and develop products consumers want, managers and consultants engage in **environmental scanning**—the systematic and intentional analysis of both a firm's internal state and its external, competitive environment. From a local coffee shop to an international corporation, firms of all sizes benefit from strategic analysis.

TERMS TO KNOW

Strategic Analysis
The process that firms use to study and understand the many different layers and aspects of their competitive environment.

Environmental Scanning

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The systematic and intentional analysis of both a firm's internal state and its external, competitive environment.

2. The Competitive Environment

A firm's **competitive environment** includes components inside the firm and outside the firm.**External factors** are things in the global environment that may impact a firm's operations or success, such as a rise in interest rates or a natural disaster. External factors cannot be controlled, but they must be managed effectively and it is important to understand them so that the firm can be successful.

THINK ABOUT IT

The unemployment rate will affect a firm's ability to hire qualified employees at a reasonable rate of pay. If unemployment is high, meaning that a lot of people are looking for jobs, then a firm will probably have a lot of applicants for any positions it needs to fill. It will be able to choose more highly qualified applicants to hire and may be able to hire them at a lower pay rate because the employee would rather work for a lower pay rate than not have a job at all. On the other hand, when unemployment is low, meaning that not many people are looking for jobs, firms may have to offer higher pay or settle for lower qualifications to find someone to fill a position.

Internal factors are characteristics of the firm itself. To plan to compete against other firms, a firm needs to understand what physical, financial, and human resources it has, what it is good at, and how it is organized.

EXAMPLE Walmart has a sophisticated IT system that tracks inventory and automatically orders products before they run out, by calculating how long it will take for the new product to arrive and comparing that to the rate at which the product is selling off the shelves. Their perpetual inventory system orders new product so that it arrives just as the product on the shelves is running out. As a result, Walmart stores do not need to have storage space for inventory, dramatically reducing costs. All Walmart inventory is on the store shelves, ready to be sold to customers.

BRAINSTORM

How does this system benefit Walmart?

It does not have to spend money on storing or keeping track of inventory, all products in the store can generate revenue because they are available for customers to buy, and when the system is working optimally, the store never runs out of items customers want.

HINT

In the Touchstone assignment, you will recommend changes to your selected organization's strategy and structure. You will also consider any associated ethical implications of the organization's strategy and structure. The assignment requires you to apply SWOT analysis, PESTEL analysis, Porter's Five Forces of Industry Analysis, Porter's Generic Strategies, and organization design concepts related to strategy-structure fit. You will prepare a slide deck containing your analysis and recommendations that could be presented to the organization's Board.

REFLECT

Why do managers use strategic analysis? How are internal factors different from external factors in a

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firm's competitive environment?

TERMS TO KNOW

Competitive Environment
Includes components inside the firm and outside the firm that may impact the firm's success.

External Factors
Things in the global environment that may impact a firm's operations or success; examples are a rise in interest rates or a natural disaster.

Internal Factors
Characteristics of the firm itself including the physical, financial, and human resources it has, what it is good at, and how it is organized.

SUMMARY

In this lesson, you learned why managers study their competitive environment using a process called strategic analysis. You started the lesson by examining **why firms need to analyze their competitive environment**, which is to understand the many forces and factors from both inside and outside the organization that impact its ability to succeed. Part of this process involves environmental scanning, an analysis of a firm's internal state and external environment, which enables managers to react to change more easily and develop products consumers want. You also learned how to differentiate between these internal factors and external factors in a firm's **competitive environment**. External factors are things in the global environment that may impact a firm's operations or success, such as a rise in interest rates, the unemployment rate, or a natural disaster, while internal factors are characteristics of the firm itself, like its inventory system.

Best of luck in your learning!

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TERMS TO KNOW

Competitive Environment
Includes components inside the firm and outside the firm that may impact the firm's success.

Environmental Scanning
The systematic and intentional analysis of both a firm's internal state and its external, competitive environment.

External Factors
Things in the global environment that may impact a firm's operations or success; examples are a rise in interest rates, or a natural disaster.

Internal Factors
Characteristics of the firm itself including the physical, financial, and human resources it has, what it is good at, and how it is organized.

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Strategic Analysis

The process that firms use to study and understand the many different layers and aspects of their competitive environment.

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Using SWOT for Strategic Analysis

by Sophia

WHAT'S COVERED

In this lesson, you will learn about SWOT analysis, and what it can reveal about a firm. Specifically, this lesson will cover:

1. An Introduction to SWOT Analysis
   a. Strengths
   b. Weaknesses
   c. Opportunities
   d. Threats
2. The Limitations of SWOT Analysis

1. An Introduction to SWOT Analysis

You may already have heard of one very common tool firms use to analyze their strategic and competitive situations: **SWOT analysis**, which is an acronym for **s**trengths, **w**eaknesses, **o**pportunities, and **t**hreats. Firms use SWOT analysis to get a general understanding of what they are good or bad at and what factors outside their doors might present chances for success or difficulty. Let's take a look at SWOT analysis piece by piece.

TERM TO KNOW

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SWOT Analysis

An acronym for strengths, weaknesses, opportunities, and threats. Firms use SWOT analysis to get a general understanding of what they are good or bad at and what factors outside their doors might present chances for success or difficulty.

HINT

As you work on the Touchstone assignment, you will need to apply what you have learned about SWOT to identify 4-6 internal strengths, internal weaknesses, external opportunities and external threats.

1a. Strengths

A firm's **strengths** are, put simply, what it is good at. Nike is good at marketing sports products, McDonald's is good at making food quickly and inexpensively, and Ferrari is good at making beautiful fast cars. When a firm analyzes its strengths, it compiles a list of its capabilities and assets. Does the firm have a lot of cash available? That is a strength. Does the firm have highly skilled employees? Another strength. Knowing exactly what it is good at allows a firm to make plans that exploit those strengths. Nike can plan to expand its business by making products for a sport it doesn't currently serve. Its sports marketing expertise will help it successfully launch that new product line.

TERM TO KNOW

Strengths

What a firm is good at.

1b. Weaknesses

A firm's **weaknesses** are what it is not good at—things that it does not have the capabilities to perform well. Weaknesses are not necessarily faults; remember that not all firms can be great at all things. When a firm understands its weaknesses, it will avoid trying to do things it does not have the skills or assets to succeed in, or it will find ways to improve its weaknesses before undertaking something new. A firm's weaknesses are simply gaps in capabilities, and those gaps do not always have to be filled within the firm.

SWOT analysis alerts firms to the gaps in their capabilities so they can work around them, find help in those areas, or develop capabilities to fill the gaps.

DID YOU KNOW

Paychex is a firm that handles payroll for over 600,000 firms (Paychex, 2017). Paychex processes hours, pay rates, tax and benefits deductions, and direct deposit for firms that would rather not have to perform those tasks themselves. A large firm would need to have a team of employees dedicated to fulfilling that task and equip that team with software systems to do the job efficiently and accurately.

For Paychex, these capabilities are a company strength—that's what it does. Other companies that do not have the resources to develop this capability or may not be interested in doing so can hire Paychex to do the job for them.

HINT

In the same way you identified some of the organization's strengths, you must now identify some of its weaknesses (4-6) for your Touchstone assignment. Recall that strengths and weaknesses are factors that are internal to the organization.

TERM TO KNOW

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Weaknesses

What a firm is not good at—things that it does not have the capabilities to perform well.

1c. Opportunities

Strengths and weaknesses are internal to an organization, but opportunities and threats are always external. An **opportunity** is a potential situation that a firm is equipped to take advantage of. Think of opportunities in terms of things that happen in the market. Opportunities offer positive potential; however, sometimes a firm is not equipped to take advantage of an opportunity which is why considering the entire SWOT analysis is important before deciding what to do. For example, as cities are becoming more populated, parking is becoming scarcer. Younger consumers who live in cities are starting to question whether it makes sense to own a car at all when public transportation is available and parking is not. Sometimes, however, a person might need a car to travel outside the city or transport a special purchase. Daimler, the manufacturer of Mercedes-Benz and Smart cars, started a car-sharing service in Europe, North America, and China called Car2Go to offer cars to this new market of part-time drivers. By establishing Car2Go, Daimler has found a way to sell the use of its products to people who would not buy them outright.

HINT

Opportunities are external to the firm and are often similar across firms in the same industry. Using the SWOT framework, identify 4-6 opportunities your organization may be in a position to take advantage of for the Touchstone.

TERM TO KNOW

Opportunity

A potential external situation that a firm is equipped to take advantage of.

1d. Threats

When a manager assesses the external competitive environment, he/she labels anything that would make it harder for the firm to be successful as a **threat**. A wide variety of situations and scenarios can threaten a firm's chances of success, from a downturn in the economy to a competitor launching a better version of a product the firm also offers. A good threat assessment looks thoroughly at the external environment and identifies threats to the firm's business so it can be prepared to meet them. Opportunities and threats can also be a matter of perspective or interpretation. For example, the Car2Go service that Daimler developed to serve young urban customers who don't own cars could also be cast as a defensive response to the trend away from car ownership in this customer group. Daimler could have identified decreasing sales among young urban professionals as a threat and developed Car2Go as an alternative way to gain revenue from these otherwise lost customers.

HINT

Like opportunities, threats are often similar across organizations in the same industry. A common threat, for example, is competition. Using the SWOT framework, you will identify 4-6 threats your organization may be facing in the Touchstone.

TERM TO KNOW

Threat

Anything in the competitive environment that would make it harder for a firm to be successful.

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2. The Limitations of SWOT Analysis

Although a SWOT analysis can identify important factors and situations that affect a firm, it only works as well as the person doing the analysis. It can also be beneficial to complete a SWOT analysis for each of a firm's top three or four competitors to get a better sense of the organization's overall competitive position. Generally, strengths and weaknesses will differ, but opportunities and threats will be the same among firms in the same industry and region.

BIG IDEA

SWOT analysis can generate a good evaluation of the firm's internal and external environments, but it is more likely to overlook key issues because it is difficult to identify or imagine everything that could, for example, be a threat to the firm.

That's why the remainder of this Challenge will present tools for developing a strategic analysis that is more thorough and systematic in examining both the internal and external environments that firms operate in.

REFLECT

1. Explain the elements of a SWOT analysis.
2. What information does a SWOT analysis provide managers? What information might it miss?

SUMMARY

In this lesson, you covered **an introduction to SWOT analysis**, a common tool firms use to analyze their strategic and competitive situations. You learned that SWOT is an acronym for **strengths**, **weaknesses**, **opportunities**, and **threats**. Firms use this type of analysis to evaluate what they are good at (strengths), what they are not good at (weaknesses), potential situations that a firm is equipped to take advantage of (opportunities), and anything that would make it harder for the firm to be successful (threats). You also learned that while a SWOT analysis can identify important factors and situations that affect a firm, there are **limitations of SWOT analysis**, as it relies on the ability of the person performing the analysis and it can sometimes overlook key issues.

Best of luck in your learning!

Source: Access for free at https://openstax.org/books/principles-management/pages/1-introduction

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TERMS TO KNOW

Opportunity

A potential external situation that a firm is equipped to take advantage of.

SWOT Analysis

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An acronym for strengths, weaknesses, opportunities, and threats. Firms use SWOT analysis to get a general understanding of what they are good or bad at and what factors outside their doors might present chances for success or difficulty.

Strengths
What a firm is good at.

Threat
Anything in the competitive environment that would make it harder for a firm to be successful.

Weaknesses
What a firm is not good at—things that it does not have the capabilities to perform well.

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A Firm's External Macro Environment: PESTEL

by Sophia

WHAT'S COVERED

In this lesson, you will learn how to articulate a firm's external macro environment and the tools strategists use to understand it. Specifically, this lesson will cover:

1. External Macro Environment
2. PESTEL and Factor Categories
   a. Political Factors
   b. Economic Factors
   c. Sociocultural Factors
   d. Technological Factors
   e. Environmental Factors
   f. Legal Factors

1. External Macro Environment

The world at large forms the **external environment** for businesses. A firm must confront, adapt to, take advantage of, and defend itself against what is happening in the world around it to succeed. To make gathering and interpreting information about the external environment easier, strategic analysts have defined several general categories of activities and groups that managers should examine and understand. The diagram below illustrates layers and categories found in a firm's environment.

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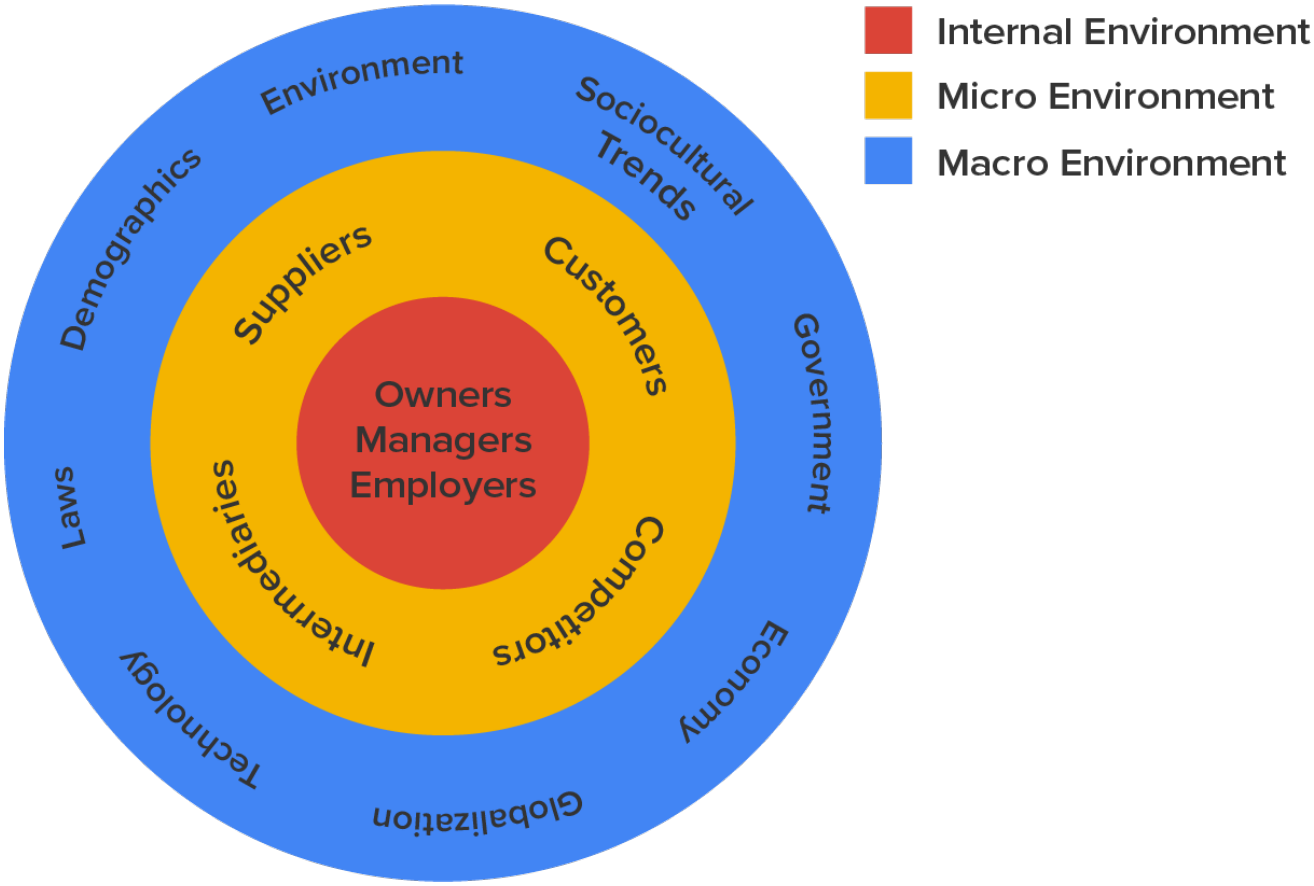

A firm's **macro environment** contains elements that can impact the firm but are generally beyond its direct control. These elements are characteristics of the world at large and are factors that all businesses must contend with, regardless of the industry they are in or type of business they are. In the diagram above, the macro environment is indicated in blue. Note that the terms contained in the blue ring are all "big-picture" items that exist independently of business activities. That is not to say that they do not affect firms or that firm activities cannot affect macro environmental elements; both can and do happen, but firms are largely unable to directly change things in the macro environment.

BIG IDEA

Strategists study the macro environment to learn about facts and trends that may present opportunities or threats to their firms. However, they do not usually just think in terms of SWOT. Strategists have developed more discerning tools to examine the external environment.

TERMS TO KNOW

External Environment
The world at large forms the external environment for businesses.

Macro Environment
A firm's macro environment contains elements that can impact the firm but are generally beyond its direct control. These elements are characteristics of the world at large and are factors that all businesses must contend with, regardless of the industry they are in or type of business they are.

2. PESTEL and Factor Categories

PESTEL is a tool that reminds managers to look at several distinct categories in the macro environment. Like

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SWOT, PESTEL is an acronym. In this case, the letters represent the categories to examine: **p**olitical factors, **e**conomic factors, **s**ociocultural factors, **t**echnological factors, **e**nvironmental factors, and **l**egal factors. When using PESTEL to analyze a specific firm's situation, the overlap between different categories of PESTEL factors can sometimes happen just as it can with SWOT.

Remember our earlier example: When urban millennials decide that car ownership is no longer attractive, car manufacturers' sales are threatened. However, those same manufacturers might be able to adapt their sales methods to offer millennials car-sharing services, taking advantage of the opportunity to earn revenue from millennials who want access to cars for vacations or big shopping trips. PESTEL can also reveal multiple impacts from a single element in the external environment.

> ↱ EXAMPLE Decreasing interest in car ownership among urban millennials would be a sociocultural trend. However, the technological connectedness of those same urban millennials is exactly what makes it possible for ride-sharing services such as Uber and Lyft to thrive—their services are app-based and provide convenience both by connecting drivers and passengers quickly and by making transactions cashless.

The table below describes the components of PESTEL, which will be discussed individually below.

Component of PESTEL	Description
Political Factors	Tax rates, tariffs, trade agreements, labor, and environmental regulations
Economic Factors	Employment levels, interest rates, exchange rates
Sociocultural Factors	Demographic trends, consumer preferences, market diversity
Technological Factors	The internet, smartphones, connectivity, automation
Environmental Factors	Resources scarcity, recycling, alternative energy sources
Legal Factors	Contracts, laws, intellectual property rights

TERM TO KNOW

PESTEL

A tool that reminds managers to look at several distinct categories in the macro environment. PESTEL is an acronym with each letter representing categories to examine: political factors, economic factors, sociocultural factors, technological factors, environmental factors, and legal factors.

2a. Political Factors

Political factors in the macro environment include taxation, tariffs, trade agreements, labor regulations, and environmental regulations. Note that in the PESTEL framework, factors are not characterized as opportunities or threats. They are simply things that a firm can take advantage of or treat as problems, depending on its own interpretation or abilities.

DID YOU KNOW

American Electric Power, a large company that generates and distributes electricity, may be negatively impacted by environmental regulations that restrict its ability to use coal to generate electricity because of pollution caused by burning coal. However, another energy firm has taken advantage of the government's interest in reducing coal emissions by developing a way to capture the emissions while producing power. The Petra Nova plant, near Houston, was developed by NRG and JX Nippon, who received Energy

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Department grants to help fund the project (Mooney, 2017).

BIG IDEA

Although firms do not directly make government policy decisions, many industries and firms invest in lobbying efforts to try to influence government policy development to create opportunities or reduce threats.

TERM TO KNOW

Political Factors

Include taxation, tariffs, trade agreements, labor regulations, and environmental regulations.

2b. Economic Factors

All firms are impacted by the state of the national and global economies. The increased interdependence of individual country economies has made evaluating the **economic factors** in a firm's macro environment more complex. Firms analyze economic indicators to make decisions about entering or exiting geographic markets, investing in expansion, and hiring or laying off employees. As discussed earlier in this tutorial, employment rates impact the quantity, quality, and cost of employees available to firms. Interest rates impact sales of big-ticket items that consumers normally finance, such as appliances, cars, and homes. Interest rates also impact the cost of capital for firms that want to invest in expansion. Exchange rates present risks and opportunities to all firms that operate across national borders, and the price of oil impacts many industries, from airlines and transportation companies to solar panel producers and plastic recycling companies.

BIG IDEA

Many scenarios can be a threat to one firm and an opportunity to another, so economic factors should not be assumed to be intrinsically good or bad.

TERM TO KNOW

Economic Factors

Firms analyze economic indicators to make decisions about entering or exiting geographic markets, investing in expansion, and hiring or laying off employees.

2c. Sociocultural Factors

Quite possibly the largest category of macro environmental factors an analyst might examine are **sociocultural factors**. This broad category encompasses everything from changing national demographics to fashion trends and many things in between. **Demographics**, a subset of this category, includes facts about income, education levels, age groups, and the ethnic and racial composition of a population. All of these facts present market challenges and possibilities. Firms can target products to specific market segments by studying the needs and preferences of demographic groups, such as working women (they might need daycare services but not watch daytime television), college students (who would be interested in affordable textbooks but couldn't afford to buy new cars), or the elderly (who would be willing to pay for lawn-mowing services but might not be interested in adventure tourism).

Changes in people's values and interests are also included in this category.

DID YOU KNOW

Environmental awareness has spurred demand for solar panels and electric and hybrid cars. A general interest in health and fitness has created industries in gyms, home gym equipment, and organic food. The popularity of social media has created an enormous demand for instant access to information and services, not to mention smartphones.

BIG IDEA

Values and interests are constantly changing and vary from country to country, creating new market opportunities as well as communication challenges for companies trying to enter unfamiliar new markets.

TERMS TO KNOW

Sociocultural Factors
This broad category encompasses everything from changing national demographics to fashion trends and many things in between.

Demographics
A subset of the sociocultural factors category; it includes facts about income, education levels, age groups, and the ethnic and racial composition of a population.

2d. Technological Factors

The rise of the Internet may be the most disruptive technological change of the last century. The globe has become more interconnected and interdependent because of the fast, low-cost communications and information-sharing the Internet provides.

DID YOU KNOW

Customer service agents in India can serve customers in Kansas because technology has advanced to the point that the customer's account information can be instantly accessed by the service provider in India.

How else have **technological factors** impacted business? The Internet is not the only technological advance that has transformed how businesses operate. Automation has increased efficiency for manufacturers. MRP (materials requirement planning) systems have changed how companies and their suppliers work together, and global-positioning technology has helped construction engineers manage large projects more accurately. Consumers and firms have nearly unlimited access to information, and this access has empowered consumers to make more informed buying decisions and challenged firms to develop ways to analyze the large amounts of data their businesses generate. Developing information technologies, which are soon to become more common across industries, include artificial intelligence and machine learning—which may further transform the way we live and work.

TERM TO KNOW

Technological Factors
This category includes the Internet, automation, and consumer's increased access to information to make buying decisions.

2e. Environmental Factors

The physical environment, which provides natural resources for manufacturing and energy production, has always been a key part of human business activity. As resources become scarcer and more expensive, **environmental factors** impact businesses more every day. Firms are developing technology to operate more cleanly and using fewer resources. Political pressure on businesses to reduce their impact on the natural environment has increased globally and dramatically in the 21st century.

EXAMPLE In 2017, London, Barcelona, and Paris announced their plans to ban cars with internal

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combustion engines over the next few decades, in order to combat air quality issues (Smith, 2017). This external environment category often overlaps with others in PESTEL because concern for the environment is also a sociocultural trend, as more consumers look for recycled products and buy electric and hybrid cars. On the political front, firms are facing increased regulation around the world on their carbon emissions and natural resource use. Although SWOT would characterize these factors as either opportunities or threats, PESTEL simply identifies them as aspects of the external environment that firms must consider when planning for their futures.

TERM TO KNOW

Environmental Factors

The physical environment, which provides natural resources for manufacturing and energy production.

2f. Legal Factors

Legal factors in the external environment often coincide with political factors because laws are enacted by government entities. This does not mean that the categories identify the same issues, however. Although labor laws and environmental regulations have deep political connections, other legal factors can impact business success.

DID YOU KNOW

In the streaming video industry, licensing fees are a significant cost for firms. Netflix pays billions of dollars every year to movie and television studios for the right to broadcast their content. In addition to the legal requirement to pay the studios, Netflix must consider that consumers may find illegal ways to view the movies they want to see, making them less willing to pay to subscribe to Netflix.

Intellectual property rights and patents are major issues in the legal realm.

Note that some external factors are difficult to categorize in PESTEL. For instance, tariffs can be viewed as either a political or economic factor while the influence of the Internet could be viewed as either a technological or social factor. While some issues can overlap two or more PESTEL areas, it does not diminish the value of PESTEL as an analytical tool.

HINT

You will perform a Macro Environment Analysis of your chosen organization and apply the PESTEL framework to identify 1-3 relevant factors. Using the PESTEL framework for strategic analysis will help you gain a better understanding of your organization's external environment, and strengthen your overall presentation for the Touchstone assignment.

REFLECT

1. Describe a firm's macro environment.
2. What does PESTEL stand for? How do managers use PESTEL to understand their firm's macro environment?

TERM TO KNOW

Legal Factors

Laws and regulations that can impact business success. These factors commonly have deep political connections.

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SUMMARY

In this lesson, you learned to how to articulate a firm's **external macro environment** and the tools strategists use to understand it. The world at large forms the external environment for businesses, while a firm's macro environment contains elements that can impact the firm but are generally beyond its direct control. These elements are "big-picture" items that exist independently of business activities. You learned that strategists study the macro environment to learn about facts and trends that may present opportunities or threats to their firms, utilizing a tool called **PESTEL**, which is an acronym that represents the **factor categories** to examine in the macro environment: **political factors**, **economic factors**, **sociocultural factors** (like demographics), **technological factors**, **environmental factors**, and **legal factors**. Remember, when using this tool, overlap between different categories of PESTEL factors can sometimes happen, similar to SWOT, and in the PESTEL framework, factors are not characterized as opportunities or threats—they are simply things that a firm can take advantage of or treat as problems, depending on its own interpretation or abilities.

Best of luck in your learning!

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TERMS TO KNOW

Demographics
A subset of the sociocultural factors category; it includes facts about income, education levels, age groups, and the ethnic and racial composition of a population.

Economic Factors
Firms analyze economic indicators to make decisions about entering or exiting geographic markets, investing in expansion, and hiring or laying off employees.

Environmental Factors
The physical environment, which provides natural resources for manufacturing and energy production.

External Environment
The world at large forms the external environment for businesses.

Legal Factors
Laws and regulations that can impact business success. These factors commonly have deep political connections.

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Macro Environment

A firm's macro environment contains elements that can impact the firm but are generally beyond its direct control. These elements are characteristics of the world at large and are factors that all businesses must contend with, regardless of the industry they are in or type of business they are.

PESTEL

A tool that reminds managers to look at several distinct categories in the macro environment. PESTEL is an acronym with each letter representing categories to examine: political factors, economic factors, sociocultural factors, technological factors, environmental factors, and legal factors.

Political Factors

Include taxation, tariffs, trade agreements, labor regulations, and environmental regulations.

Sociocultural Factors

This broad category encompasses everything from changing national demographics to fashion trends and many things in between.

Technological Factors

This category includes the Internet, automation, and consumer's increased access to information to make buying decisions.

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A Firm's Micro Environment: Porter's Five Forces

by Sophia

WHAT'S COVERED

In this lesson, you will learn how to articulate a firm’s external micro environment and the tools strategists use to understand it. Specifically, this lesson will cover:

1. External Micro Environment
2. Porter’s Five Forces
   a. Industry Rivalry
   b. The Threat of New Entrants
   c. The Threat of Substitutes
   d. Supplier Power
   e. Buyer Power

1. External Micro Environment

A firm’s **micro environment** is illustrated in the diagram below. These entities are all directly connected to the firm in some way, and firms must understand the micro environment in order to successfully compete in an industry. All firms are part of an **industry**—a group of firms all making similar products or offering similar services; for example, automobile manufacturers or airlines. Firms in an industry may or may not compete directly against one another, as we’ll discuss shortly, but they all face similar situations in terms of customer interests, supplier relations, and industry growth or decline.

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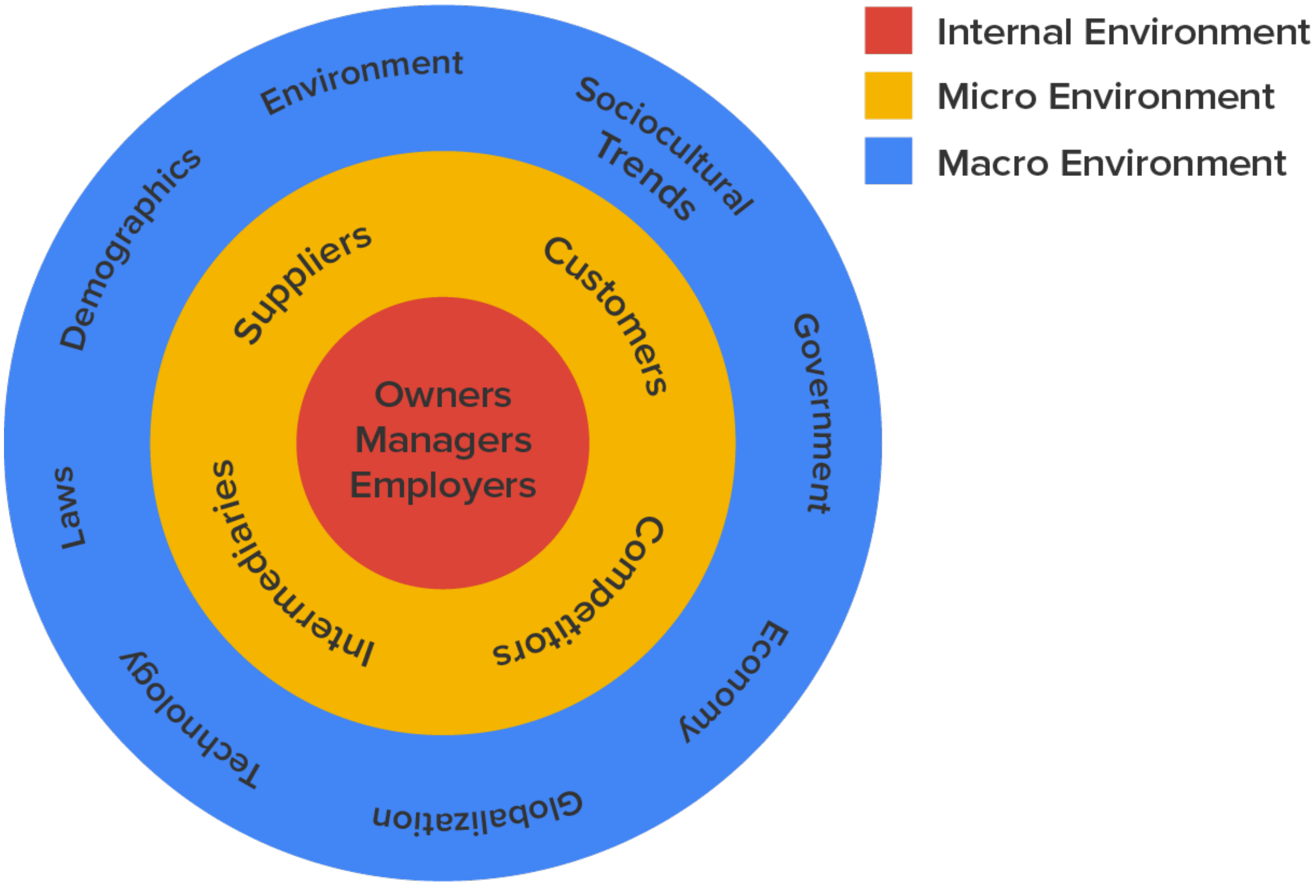

TERMS TO KNOW

Micro Environment

The middle layer of elements in a firm's external environment, primarily concerned with a firm's industry situation.

Industry

A group of firms all making similar products or offering similar services; for example, automobile manufacturers or airlines.

2. Porter's Five Forces

Harvard strategy professor Michael Porter developed a framework to evaluate a firm's micro environment. **Porter's Five Forces** is a tool used to examine different micro-environmental factors in order to understand the impact each has on a firm in an industry. Each of the forces represents an aspect of competition that affects a firm's potential to be successful in its industry. It is important to note that this tool is different than Porter's generic strategy typology that we will discuss later.

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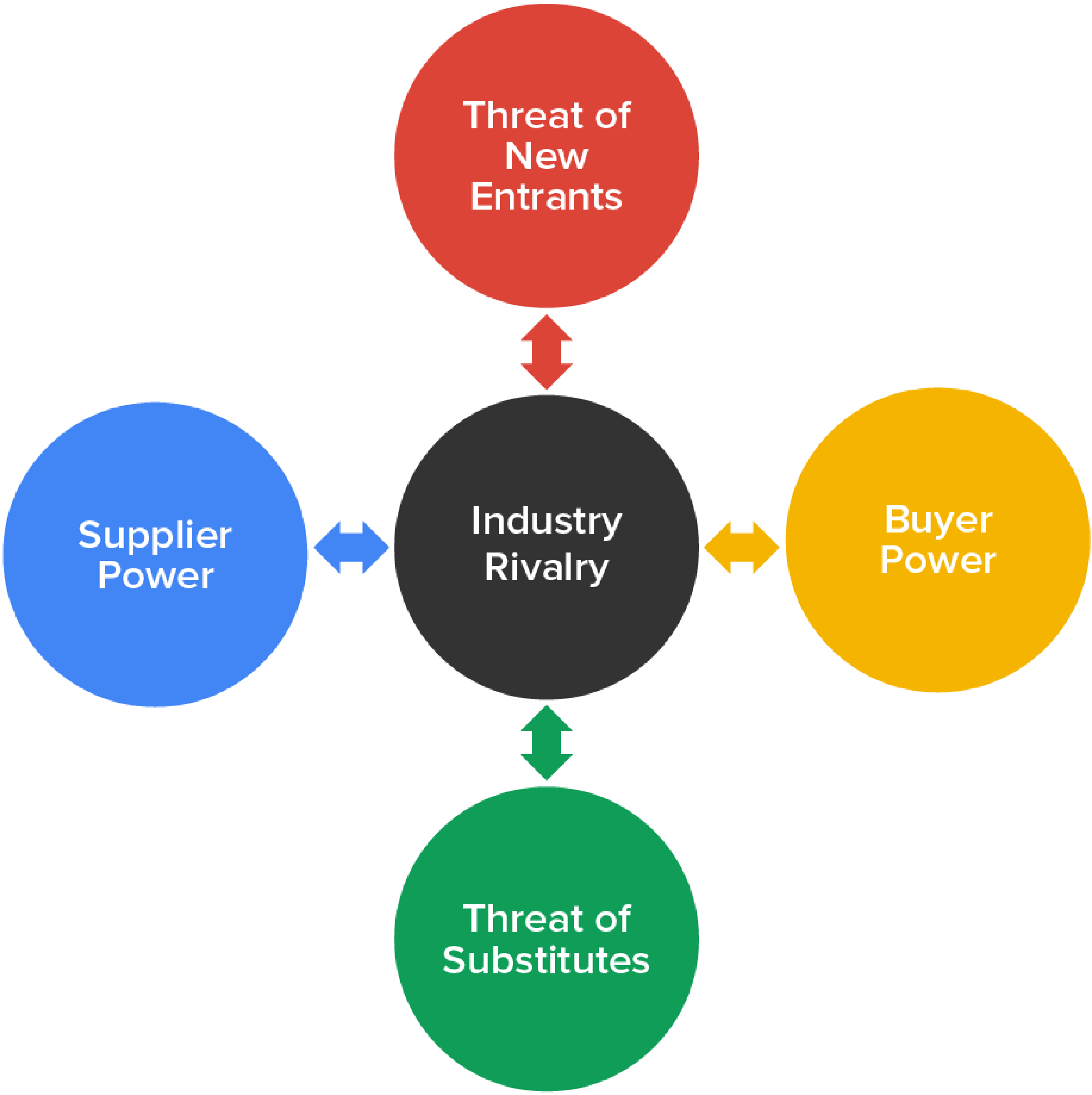

TERM TO KNOW

Porter's Five Forces

A tool used to examine different micro-environmental factors in order to understand the impact each has on a firm in an industry

2a. Industry Rivalry

Industry rivalry, the first of Porter's forces, is in the center of the diagram. Note that the arrows in the diagram show two-way relationships between rivalry and all of the other forces. This is because each force can affect how hard firms in an industry must compete against each other to gain customers, establish favorable supplier relationships, and defend themselves against new firms entering the industry.

When using Porter's model, an analyst will determine if each force has a strong or weak impact on industry firms. In the case of rivalry, the question of strength focuses on how hard firms must fight against industry rivals (competitors) to gain customers and market share. Strong rivalry in an industry reduces the profit potential for all firms because consumers have many firms from which to purchase products or services.

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TERM TO KNOW

Industry Rivalry

One of Porter's Five Forces; refers to the intensity of competition between firms in an industry.

2b. The Threat of New Entrants

In an industry, there are incumbent (existing) firms that compete against each other as rivals. If an industry has a growing market or is very profitable, however, it may attract **new entrants.** These either are firms that start up in the industry as new companies or are firms from another industry that expand their capabilities or target markets to compete in an industry that is new to them. Different industries may be easier or harder to enter depending on **barriers to entry**—factors that prevent new firms from successfully competing in the industry. Common barriers to entry include cost, brand loyalty, and industry growth.

EXAMPLE The firms in the airline industry rarely face threats from new entrants because it is very expensive to obtain the equipment, airport landing rights, and expertise to start up a new airline.

Brand loyalty can also keep new firms from entering an industry, because customers who are familiar with a strong brand name may be unwilling to try a new, unknown brand. Further, industry growth may increase or decrease the chances a new entrant will succeed.

TERMS TO KNOW

New Entrants

One of Porter's Five Forces, the threat of new entrants assesses the potential that a new firm will start operations in an industry.

Barriers to Entry

Industry factors (such as high start-up costs) that can prevent new firms from successfully launching new operations in that industry.

2c. The Threat of Substitutes

In the context of Porter's model, a **substitute** is any other product or service that can satisfy the same need for a customer as an industry's offerings. Be careful not to confuse substitutes with rivals. Rivals offer similar products or services and directly compete with one another. Substitutes are completely different products or services that consumers would be willing to use instead of the product they currently use. Margarine and butter are examples of product substitutes.

TERM TO KNOW

Substitute

One of Porter's Five Forces; products or services outside a firm's industry that can satisfy the same customer needs as industry products or services can.

2d. Supplier Power

Virtually all firms have suppliers who sell parts, materials, labor, or products.**Supplier power** refers to the balance of power in the relationship between firms and their suppliers in an industry. Suppliers can have the upper hand in a relationship if they offer specialized products or control rare resources.

EXAMPLE When Sony develops a new PlayStation model, it often works with a single supplier to develop the most advanced processor chip it can for their game console. That means its supplier will be able to command a fairly high price for the processors, an indication that the supplier has power. On the other hand, a firm that needs commodity resources such as oil, wheat, or aluminum in its

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operations will have many suppliers to choose from and can easily switch suppliers if price or quality is better from a new partner.

TERM TO KNOW

Supplier Power
One of Porter's Five Forces; describes the balance of power in the relationship between firms in an industry and their suppliers.

2e. Buyer Power

The last of Porter's forces is **buyer power**, which refers to the balance of power in the relationship between a firm and its customers. If a firm provides a unique good or service, it will have the power to charge its customers premium prices, because those customers have no choice but to buy from the firm if they need that product. In contrast, when customers have many potential sources for a product, firms will need to attract customers by offering better prices or better value for the money if they want to sell their products.

One protection firms have against buyer power is **switching costs**, the penalty consumers face when they choose to use a particular product made by a different company. Switching costs can be financial (the extra price paid to choose a different product) or practical (the time or hassle required to switch to a different product).

THINK ABOUT IT

Think about your smartphone. If you have an iPhone now, what would be the penalty for you to switch to a non-Apple smartphone? Would it just be the cost of the new phone? Smartphones are not inexpensive, but even when cell phone service providers offer free phones to new customers, many people still don't switch. The loss of compatibility with other Apple products, the need to transfer apps and phone settings to another system, and the loss of favorite iPhone features are enough to keep many people loyal to their iPhones.

REFLECT

Describe each of Porter's Five Forces. What information does each provide a manager trying to understand his/her firm's micro environment?

HINT

Porter's Five Forces of Industry Analysis is a time-tested framework for better understanding the industry your organization competes in. While firms in the same industry often face similar challenges, Porter's Five Forces framework will help you better understand how well the organization you selected for your Touchstone assignment is positioned relative to competitors.

TERMS TO KNOW

Buyer Power
In the relationship between a firm and its customers, buyers with high power can negotiate product price or features, while buyers with low power cannot.

Switching Costs
Penalty, financial or otherwise, that a consumer bears when giving up the use of a product currently being used to select a competing product or service.

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SUMMARY

In this lesson, you learned how to articulate a firm's **external micro environment** and the tools strategists use to understand it. The micro environment is the middle layer of elements in a firm's external environment consisting of entities that are all directly connected to the firm in some way such as suppliers, customers, competitors, and intermediaries; firms must understand the micro environment in order to successfully compete in an industry. You learned about **Porter's Five Forces**, a tool used to examine different micro-environmental factors in order to understand the impact each has on a firm in an industry. The five forces are **industry rivalry**, **the threat of new entrants**, **the threat of substitutes**, **supplier power**, and **buyer power**.

Best of luck in your learning!

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TERMS TO KNOW

Barriers to Entry
Industry factors (such as high start-up costs) that can prevent new firms from successfully launching new operations in that industry.

Buyer Power
In the relationship between a firm and its customers, buyers with high power can negotiate product price or features, while buyers with low power cannot.

Industry
A group of firms all making similar products or offering similar services, for example automobile manufacturers or airlines.

Industry Rivalry
One of Porter's Five Forces; refers to the intensity of competition between firms in an industry.

Micro Environment
The middle layer of elements in a firm's external environment, primarily concerned with a firm's industry situation.

New Entrants
One of Porter's Five Forces, the threat of new entrants assesses the potential that a new firm will start operations in an industry.

Porter's Five Forces
A tool used to examine different micro-environmental groups in order to understand the impact each group has on a firm in an industry.

Substitute
One of Porter's Five Forces; products or services outside a firm's industry that can satisfy the same customer needs as industry products or services can.

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Supplier Power

One of Porter's Five Forces; describes the balance of power in the relationship between firms in an industry and their suppliers.

Switching Costs

Penalty, financial or otherwise, that a consumer bears when giving up the use of a product currently being used to select a competing product or service.

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The Internal Environment

by Sophia

WHAT'S COVERED

In this lesson, you will learn about the relevance of a firm's competitive environment for strategic decision-making. You will also learn how and why managers conduct internal analysis of their firms. Specifically, this lesson will cover:

1. Internal Environment
2. Resources and Capabilities
3. The Value Chain
4. Using Resources and Capabilities to Build an Advantage Over Rivals
    a. Using VRIO

1. Internal Environment

A firm's internal environment is illustrated in the diagram below by the innermost circle. The**internal environment** consists of members of the firm itself, investors in the firm, and the assets a firm has. Employees and managers are good examples; they are firm members who have skills and knowledge that are valuable assets to their firms. Evaluating a firm's internal environment is not just a matter of counting heads, however. Successful firms have a wide range of resources and capabilities that they can use to maintain their success and grow into new ventures. A thorough analysis of a firm's internal situation provides a manager with an understanding of the resources available to pursue new initiatives, innovate, and plan for future success.

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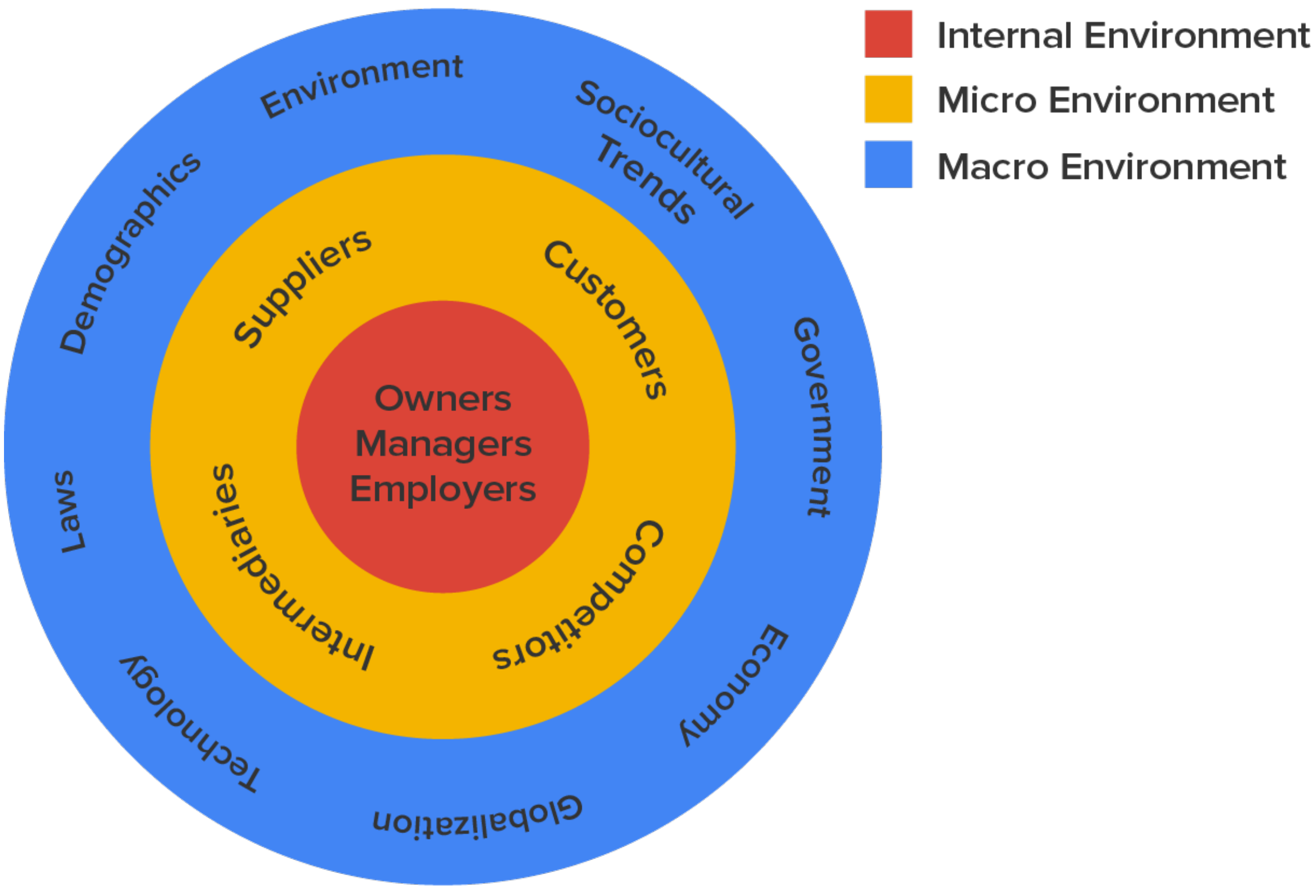

TERM TO KNOW

Internal Environment
Innermost layer of a firm's competitive environment, including members of the firm itself (such as employees and managers), investors in the firm, and the resources and capabilities of a firm.

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2. Resources and Capabilities

A firm's resources and capabilities are the unique skills and assets it possesses.**Resources** are things a firm has to work with, such as equipment, facilities, raw materials, employees, and cash. **Capabilities** are things a firm can do, such as deliver good customer service or develop innovative products to create value. Both are the building blocks of a firm's plans and activities, and both are required if a firm is going to compete successfully against its rivals. Firms use their resources and leverage their capabilities to create products and services that have some advantage over competitors' products.

EXAMPLE A firm might offer its customers a product with higher quality, better features, or lower prices.

Not all resources and capabilities are equally helpful in creating success, though. Internal analysis identifies exactly which assets bring the most value to the firm.

TERMS TO KNOW

Resources
Things a firm has, such as cash and skilled employees, that it can use to create products or services.

Capabilities

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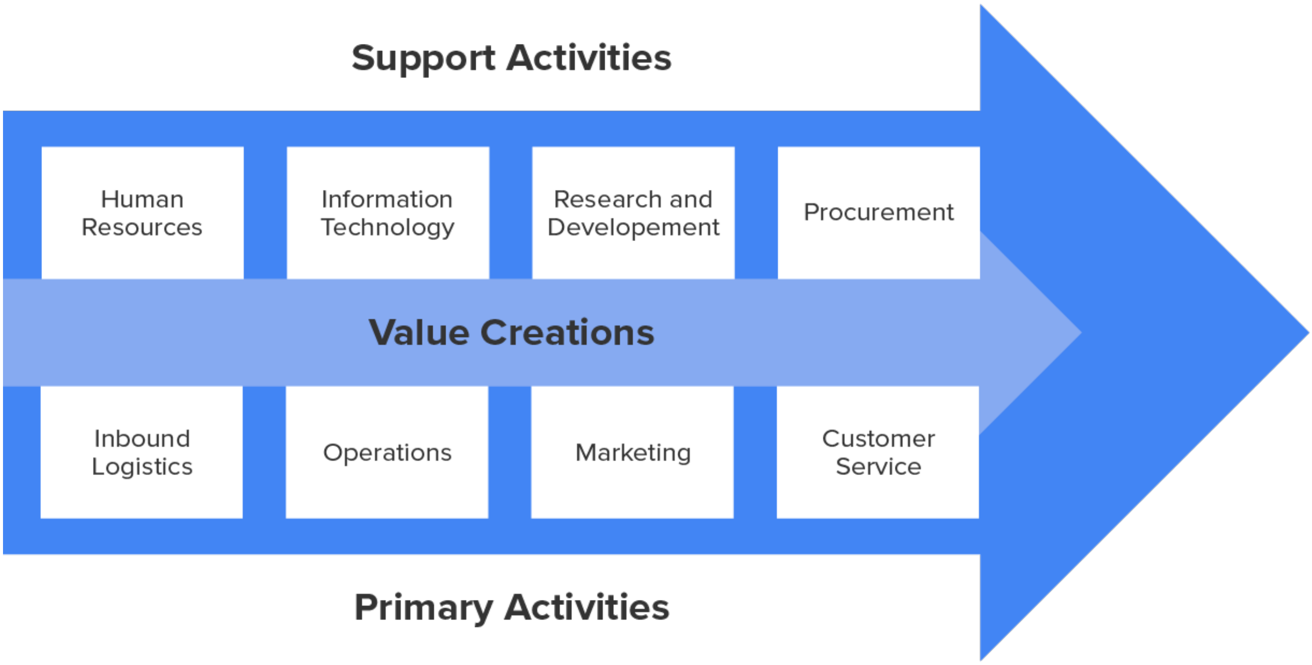
Capabilities

A firm’s skill at coordinating and leveraging resources to create value.

3. The Value Chain

Before examining the role of resources and capabilities in firm success, let’s take a look at the importance of how a firm uses those factors in its operations. A firm’s **value chain** is the progression of activities it undertakes to create a product or service that consumers will pay for. A firm should be adding value at each of the chain of steps it follows to create its product. The goal is for the firm to add enough value so that its customers will believe that the product is worth buying for a price that is higher than the costs the firm incurs in making it. As an example, the diagram below illustrates a hypothetical value chain for some of Walmart’s activities.



In this example, note that value increases from left to right as Walmart performs more activities. If an activity adds enough value through its efforts, it will profit when it finally sells its services to customers. If Walmart determines an activity doesn't add enough value they could consider outsourcing the activity to another company. By working with product suppliers (procurement), getting those products to store locations efficiently (inbound logistics), and automatically keeping track of sales and inventory (information technology), Walmart is able to offer its customers a wide variety of products in one store at low prices, a service customers value. **Primary activities**, the ones across the bottom half of the diagram, are the actions a firm takes to directly provide a product or service to customers. **Support activities**, the ones across the top of the diagram, are actions required to sustain the firm that are not directly part of product or service creation.

TERMS TO KNOW

Value Chain

Sequence of activities that firms perform to turn inputs (parts or supplies) into outputs (goods or services).

Primary Activities

Firm activities on the value chain that are directly responsible for creating, selling, or servicing a product or service, such as manufacturing and marketing.

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Support Activities

Value chain activities that a firm performs to sustain itself; they do not directly create a product or service but are necessary to support the firm's existence, such as accounting and human resources.

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4. Using Resources and Capabilities to Build an Advantage Over Rivals

A firm's resources and capabilities are not just a list of equipment and things it can do. Instead, resources and capabilities are the distinctive assets and activities that separate firms from each other. Firms that can amass critical resources and develop superior capabilities will succeed in competition over rivals in their industry. Strategists evaluate firm resources and capabilities to determine if they are sufficiently unique to help the firm succeed in a competitive industry.

4a. Using VRIO

An analytical tool sometimes used to assess resources and capabilities is called**VRIO**. As usual, this is an acronym developed to remind managers of the questions to ask when evaluating their firms' resources and capabilities. The four questions of VRIO, which focus on value, rarity, imitation, and organization, are described in the table below.

Component of VRIO	Question
Valuable	Does the resource or capability generate value for the firm?
Rare	Is the resource or capability rare among firms in the industry?
Imitation	Would it be difficult or expensive for other firms to imitate the resource or capability?
Organization	Is the firm effectively organized to capture the value that this resource or capability generates?

If each question can be answered with a "yes," then the resource or capability being evaluated can be a source of competitive advantage for the firm.

IN CONTEXT

Technology and Innovation: Uber, Lyft, and the Self-Driving Car: The Transportation of the Future Is Coming Soon

Although the ride-sharing industry is still relatively new, it has seen explosive growth, and its two main rivals, Uber and Lyft, are looking for ways to increase their capacity to serve riders. Both firms, and rivals like them, operate in basically the same way. A person needing a ride uses a smartphone app to alert a nearby person with a car of their location. The driver, usually an independent contractor for the service (meaning they are just a person with a car that has signed up to provide rides in exchange for a portion of the fare the customer pays), picks up the customer and drives them to their destination. Paying for the ride is also handled through the app, and the driver receives about 75–80% of the fare, with Uber or Lyft keeping the balance (Ridester, 2017).

The popularity of ride-sharing services has soared, and both companies are constantly recruiting more drivers. However, both companies have also explored alternatives to independent drivers: self-driving cars. Uber and Lyft have taken different paths to develop this capability. Uber has worked to internally develop its own software technology and self-driving car technology, while Lyft has focused on software interfaces that can accommodate other companies' self-driving cars (Bensinger, 2017). Lyft's partnerships with firms such as Google and GM that are already developing self-driving cars has put it ahead of Uber in the race to get driverless vehicles into its ride-sharing network, and it was able to test self-driving cars in Boston by partnering with NuTonomy in 2017 (Edelstein, 2017). Lyft offered a demonstration to journalists at the Consumer Electronics Show in Las Vegas in 2018, offering rides in self-driving cars developed by Aptiv (O'Kane, 2018). Uber had been testing similar technology in Pittsburgh but suspended its self-driving car program after a fatal pedestrian accident in Arizona (Korosec, 2018).

BRAINSTORM

1. What resource or capability challenges have Uber and Lyft faced because of their fast company growth?
2. What PESTEL factors do you think are contributing to the popularity of ride-sharing services?
3. What industry challenges (think of Porter's Five Forces) does the use of self-driving cars address?

REFLECT

1. What are firm resources and capabilities?
2. Describe a value chain and what the activities in the chain represent.
3. What is VRIO? What questions do the letters stand for, and how does using VRIO help a manager make decisions?

TERM TO KNOW

VRIO

Analytical tool that evaluates a firm's resources and capabilities to determine whether or not it can support an advantage for the firm in the competitive environment: value, rarity, imitation, and organization.

SUMMARY

In this lesson, you learned about the relevance of a firm's competitive **internal environment** for strategic decision-making, providing a manager with an understanding of the resources available to pursue new initiatives, innovate, and plan for future success. The internal environment represents the innermost layer of a firm's competitive environment, including members of the firm itself (such as employees and managers), investors in the firm, and the **resources and capabilities** of a firm. You learned that resources comprise things a firm has, such as cash and skilled employees, that it can use to create products or services, while capabilities are things a firm can do to create value. You also learned that a firm should be adding value at each step of its **value chain** that it follows to create its product. Lastly, you learned about the importance of a firm **using resources and capabilities to build**

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an advantage over rivals, and that managers can conduct an internal analysis of these assets**using VRIO**, an analytical tool that focuses on value, rarity, imitation, and organization.

Best of luck in your learning!

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TERMS TO KNOW

Capabilities
A firm's skill at coordinating and leveraging resources to create value.

Primary Activities
Firm activities on the value chain that are directly responsible for creating, selling, or servicing a product or service, such as manufacturing and marketing.

Resources
Things a firm has, such as cash and skilled employees, that it can use to create products or services.

Support Activites
Value chain activities that a firm performs to sustain itself; they do not directly create a product or service but are necessary to support the firm's existence, such as accounting and human resources.

VRIO
Analytical tool that evaluates a firm's resources and capabilities to determine whether or not it can support an advantage for the firm in the competitive environment: value, rarity, imitation, and organization.

Value Chain
Sequence of activities that firms perform to turn inputs (parts or supplies) into outputs (goods or services).

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Competition, Strategy, and Competitive Advantage

by Sophia

WHAT'S COVERED

In this lesson, you will learn the nature of competition and the generic strategies a firm can implement to gain advantage over its rivals. Specifically, this lesson will cover:

1. Introduction to Competition, Strategy, and Competitive Advantage
2. Competition
3. Generic Business-Level Competitive Strategies
    a. Cost Leadership
    b. Differentiation
    c. Focus
4. Strategic Groups

1. Introduction to Competition, Strategy, and Competitive Advantage

Now that you understand more about the environment that organizations operate in, let's take a deeper look at exactly how they operate. Businesses exist to make profits by offering goods and services in the marketplace at prices that are higher than the costs they incurred creating those goods and services. Businesses rarely exist alone in an industry; **competition** is usually a key part of any marketplace. This means that businesses must find ways to attract customers to their products and away from competitors' products. **Strategy** is the process of planning and implementing actions that will lead to success in competition.

The analytical tools we discuss here are part of the strategic planning process. Managers cannot successfully plan to compete in an industry if they don't understand its competitive landscape. It is also unlikely that a firm that is planning to launch a new product that they are not equipped to make will be successful.

HINT

You will conduct an internal and external analysis of the organization and add information about their strategy to the presentation you create for the Touchstone assignment.

TERMS TO KNOW

Competition
Business actions a firm undertakes to attract customers to its products and away from competitors' products.

Strategy

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Process of planning and implementing actions that will lead to success in competition.

2. Competition

Porter's Five Forces model is centered around rivalry, a synonym for competition. In any industry, multiple firms compete against each other for customers by offering better or cheaper products than their rivals. Firms use PESTEL to understand what consumers are interested in and use VRIO to evaluate their own resources and capabilities so that they can figure out how to offer products and services that match those consumer interests and that are better in quality and price than the products offered by their competitors.

A firm is described as having a **competitive advantage** when it successfully attracts more customers, earns more profit, or returns more value to its shareholders than rival firms do. A firm achieves a competitive advantage by adding value to its products and services or reducing its own costs more effectively than its rivals in the industry.

TERM TO KNOW

Competitive Advantage
When a firm successfully attracts more customers, earns more profit, or returns more value to its shareholders than rival firms do.

3. Generic Business-Level Competitive Strategies

When discussing business strategy, a business is a firm or a unit of a firm that centers its activities around one primary type of product or service line. Business-level strategy is the general way that a business organizes its activities to compete against rivals in its product's industry. Michael Porter (the same Harvard professor who developed the Five Forces Model) defined three **generic business-level strategies** that outline the basic methods of organizing to compete in a product market. He called the strategies "generic" because these ways of organizing can be used by any firm in any industry.

TERM TO KNOW

Generic Business-Level Strategies
Basic methods of organizing firm value chain activities to compete in a product market that can be used by any firm in any industry.

3a. Cost Leadership

When pursuing a **cost-leadership strategy**, a firm offers customers its product or service at a lower price than its rivals can. To achieve a competitive advantage over rivals in the industry, the successful cost leader tightly controls costs throughout its value chain activities. Supplier relationships are managed to guarantee the lowest prices for parts, manufacturing is conducted in the least expensive labor markets, and operations may be automated for maximum efficiency. A cost leader must spend as little as possible producing a product or providing a service so that it will still be profitable when selling that product or service at the lowest price.

EXAMPLE Walmart is the master of cost leadership, offering a wide variety of products at lower prices than competitors because it does not spend money on fancy stores, it extracts low prices from its suppliers, and it pays its employees relatively low wages.

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TERM TO KNOW

Cost-leadership Strategy

A generic business-level strategy in which a firm tightly controls costs throughout its value chain activities in order to offer customers low-priced goods and services at a profit.

3b. Differentiation

Not all products or services in the marketplace are offered at low prices, of course. A **differentiation strategy** is exactly the opposite of a cost-leadership strategy. While firms do not look to spend as much as possible to produce their output, firms that differentiate try to add value to their products and services so they can attract customers who are willing to pay a higher price. At each step in the value chain, the differentiator increases the quality, features, and overall attractiveness of its products or services. Research and development efforts focus on innovation, customer service is excellent, and marketing bolsters the value of the firm brand. These efforts guarantee that the successful differentiator can still profit even though its production costs are higher than a cost leader's.

EXAMPLE Starbucks is a good example of a differentiator: it makes coffee, but its customers are willing to pay premium prices for a cup of Starbucks coffee because they value the restaurant atmosphere, customer service, product quality, and brand.

Porter's typology assumes that firms can succeed through either cost leadership or differentiation. Trying to combine these two, Porter suggests, can lead to a firm being stuck in the middle—an undesirable, unsustainable, and ineffective place to be.

TERM TO KNOW

Differentiation Strategy

A generic business-level strategy in which firms add value to their products and services in order to attract customers who are willing to pay a higher price.

3c. Focus

Porter's third generic competitive strategy, **focus**, is a little different from the other two. A firm that focuses still must choose one of the other strategies to organize its activities. It will still strive to lower costs or add value. The difference here is that a firm choosing to implement a focused strategy will concentrate its marketing and selling efforts on a smaller market than a broad cost leader or differentiator. A firm following a focus-differentiation strategy, for example, will add value to its product or service that a few customers will value highly, either because the product is specifically suited to a particular use or because it is a luxury product that few can afford.

TERM TO KNOW

Focus Strategy

A generic business-level competitive strategy that firms use in combination with either a cost-leadership or differentiation strategy in order to target a smaller demographic or geographic market with specialized products or services.

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4. Strategic Groups

When managers analyze their competitive environment and examine rivalry within their industry, they are not confronted by an infinite variety of competitors. Although there are millions of businesses of all sizes around

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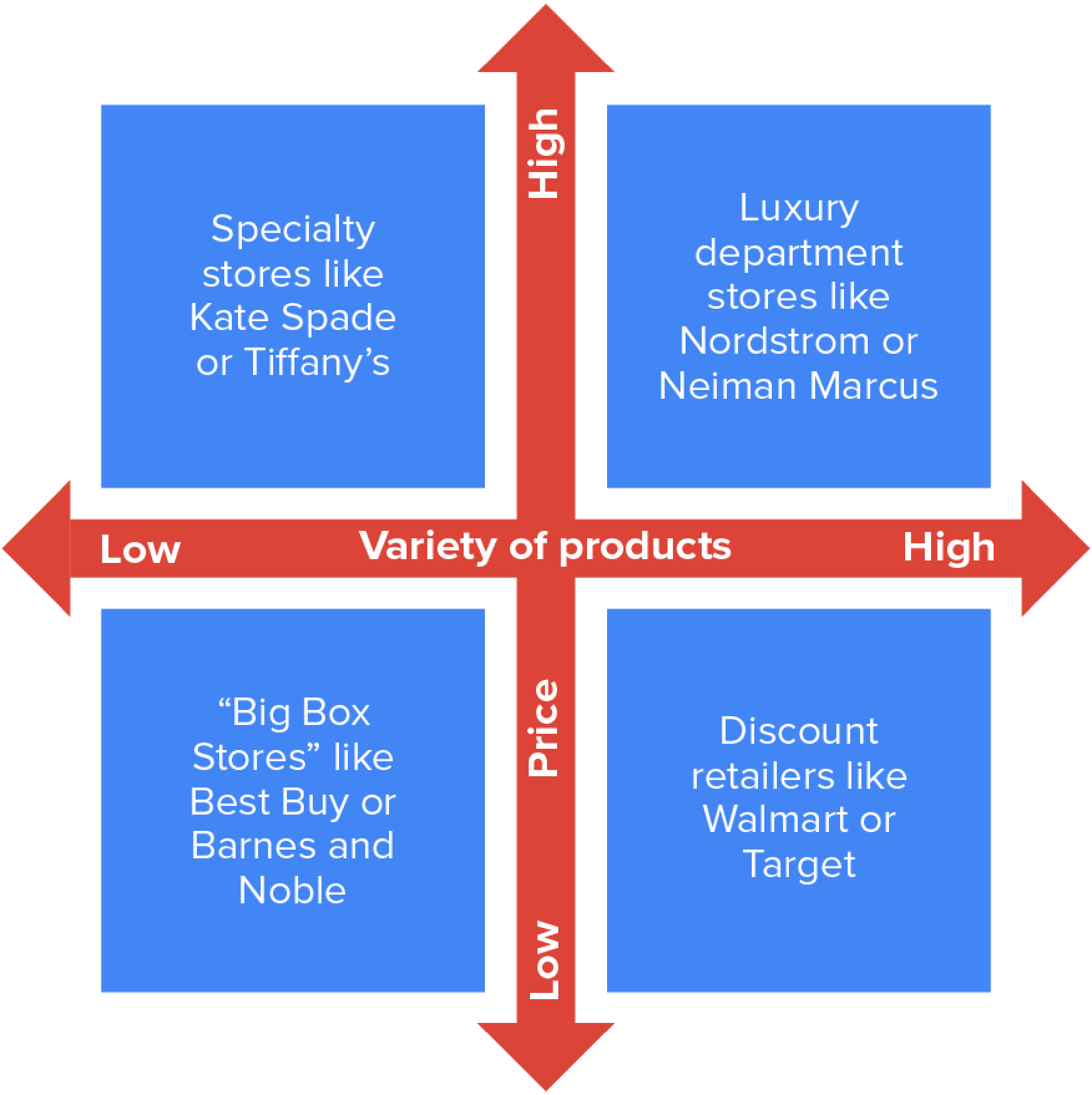
the globe, a single business usually competes mainly against other businesses offering similar products or services and following the same generic competitive strategy. Groups of businesses that follow similar strategies in the same industry are called **strategic groups**, and it is important that a manager knows the other firms in their strategic group. Rivalry is fiercest within a strategic group, and the actions of one firm in a group will elicit responses from other group members who don't want to lose market share in the industry. Take a look at the diagram below: although all of the firms shown are in the retail industry, they don't all compete directly against one another.



Although some cross-competition can occur (for example, you could buy a Kate Spade wallet at Nordstrom), firms in different strategic groups tend to compete more with each other than against firms outside their group.

Although Walmart and Neiman Marcus both offer a wide variety of products, the two firms do not cater to the same customers, and their managers do not lose sleep at night wondering what each might do next.

DID YOU KNOW

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A Walmart manager would be concerned with the products or prices offered at Target; if laundry detergent is on sale at Target, the Walmart manager might lose sales from customers who buy it at Target instead, and so the Walmart manager might respond to Target's sale price by discounting the same detergent at Walmart.

REFLECT

1. What is competition, and what is the role of strategy in competition?
2. When does a firm have a competitive advantage over its rivals?
3. Explain the differences between the three business-level generic competitive strategies.

HINT

This is where the rubber meets the road. Some firms lack strategic direction or attempt to pursue two strategies simultaneously, which often has dire consequences (e.g., low cost + differentiation rarely succeeds). For your Touchstone assignment, you need to identify which of Porter's three generic strategies you feel the organization is pursuing and why, and/or whether they should consider a different generic strategy and why. Sometimes it is not always clear. One thing that can help is to compare your organization to a competitor to gain a clearer understanding. For example, Target pursues a differentiation strategy; whereas, Walmart pursues a low-cost strategy

TERM TO KNOW

Strategic Group
Businesses offering similar products or services and following the same generic competitive strategy.

SUMMARY

In this lesson, you explored an **introduction to competition, strategy, and competitive advantage**. You learned about the nature of **competition**—business action a firm undertakes to attract customers to their products and away from competitors' products—and the **generic business-level competitive strategies** a firm can implement to gain a competitive advantage over its rivals. These strategies are labelled "generic" because they can be used by any firm in any industry, and they include a **cost leadership** strategy to lower costs, a **differentiation** strategy to add value, and a **focus** strategy, which is used in combination with either of the other two strategies in order to target a smaller demographic or geographic market with specialized products or services. Lastly, you learned about **strategic groups**, which are groups of businesses that follow similar strategies in the same industry and among whom rivalry is fiercest.

Best of luck in your learning!

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TERMS TO KNOW

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Competition
Business actions a firm undertakes to attract customers to its products and away from competitors' products.

Competitive Advantage
When a firm successfully attracts more customers, earns more profit, or returns more value to its shareholders than rival firms do.

Cost-leadership Strategy
A generic business-level strategy in which a firm tightly controls costs throughout its value chain activities in order to offer customers low-priced goods and services at a profit.

Differentiation Strategy
A generic business-level strategy in which firms add value to their products and services in order to attract customers who are willing to pay a higher price.

Focus Strategy
A generic business-level competitive strategy that firms use in combination with either a cost-leadership or differentiation strategy in order to target a smaller demographic or geographic market with specialized products or services.

Generic Business-Level Strategies
Basic methods of organizing firm value chain activities to compete in a product market that can be used by any firm in any industry.

Strategic Group
Businesses offering similar products or services and following the same generic competitive strategy.

Strategy
Process of planning and implementing actions that will lead to success in competition.

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Strategic Management

by Sophia

WHAT'S COVERED

In this lesson, you will learn to explain the strategic management process. Specifically, this lesson will cover:

1. The Strategic Management Process

1. The Strategic Management Process

In the previous lesson, we focused on analyzing and understanding a firm's competitive environment. In this lesson, we see how the information strategic analysis provides gets put to work. The **strategic management process** is the set of activities that firm managers undertake in order to try to put their firms in the best possible position to compete successfully in the marketplace. Strategic management is made up of several distinct activities, shown in the diagram below. This challenge will detail the role each activity plays in developing and sustaining a successful competitive position.

This diagram presents strategic management as an orderly process. However, most top managers deal with all of the steps simultaneously; they engage in environmental scanning to update their analytical view of the firm, they are executing strategies formulated in the past, they are formulating strategies to execute in the future, and so on. While it is useful to discuss the strategic management process in a stepwise fashion, it's important to point out that the cycle occurs such that everything is being done at once.

REFLECT

What activities make up the strategic management process?

TERM TO KNOW

Strategic Management Process

The set of activities that firm managers undertake in order to try to put their firms in the best possible position to compete successfully in the marketplace.

SUMMARY

In this lesson, you learned about **the strategic management process**, the set of activities that firm managers undertake in order to try to put their firms in the best possible position to compete successfully in the marketplace. These activities include defining the firm's vision and mission, strategic analysis, developing objectives, creating and choosing strategies, implementing strategies, and measuring and evaluating performance. It is important to note that top managers often deal with all of the steps simultaneously, rather than linearly.

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TERMS TO KNOW

Strategic Management Process

The set of activities that firm managers undertake in order to try to put their firms in the best possible position to compete successfully in the marketplace.

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Firm Vision and Mission

by Sophia

WHAT'S COVERED

In this lesson, you will learn how to interpret the difference between a firm's vision and its mission. Specifically, this lesson will cover:

1. Firm's Vision Statement
2. Firm's Mission Statement
3. Differences

1. Firm's Vision Statement

The first step in the process of developing a successful strategic position should be part of the founding of the firm itself. When entrepreneurs decide to start a business, they usually have a reason for starting it, a reason that answers the question "What is the point of this business?" Even if an entrepreneur initially thinks of starting a business in order to be their own boss, they must also have an idea about what their business will do. Overall, entrepreneurs start businesses for a variety of reasons. A **vision statement** is an expression of what a business's founders want that business to accomplish. The vision statement is usually very broad, and it does not even have to mention a product or service. The vision statement does not describe the strategy a firm will use to follow its vision—it is simply a sentence or two that states why the business exists.

TERM TO KNOW

Vision Statement
A broad expression of what a business's founders want that business to accomplish.

---

2. Firm's Mission Statement

While a firm's vision statement is a general statement about why it exists, a firm's**mission statement** is more specific. The mission statement takes the *why* of a vision statement and gives a broad description of *how* the firm will try to make its vision a reality. A mission statement is still not exactly a strategy, but it focuses on describing the products a firm plans to offer or the target markets it plans to serve.

TERM TO KNOW

Mission Statement
A general description of how the firm will try to accomplish the firm's vision.

---

3. Differences

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The table below gives examples of vision and mission statements for the Walt Disney Company and for Ikea. Notice that in both cases the vision statement is very broad and is not something a business could use as a strategy because there's simply not enough information to illustrate what kind of businesses they might be. The mission statements, on the other hand, describe the products and services each company plans to offer and the customers each company plans to serve in order to fulfill their visions.

Vision → Mission		
	Broad: ***Why do we exist?***	**Focused:** ***How will we accomplish our vision?***
Disney	"To make people happy."	"The mission of the Walt Disney Company is to be one of the world's leading producers and providers of entertainment and information. Using our portfolio of brands to differentiate our content, services, and consumer products, we seek to develop the most creative, innovative, and profitable entertainment experiences and related products in the world."
Ikea	"To create a better everyday life for the many people."	"We shall offer a wide range of well-designed, functional home furnishing products at prices so low that as many people as possible will be able to afford them."

An interesting thing to note about vision and mission statements is that many companies confuse them, calling a very broad statement their mission.

> EXAMPLE Microsoft says that its mission is "to help people around the world realize their full potential" (The Marketing Blender, 2017). By the description above, this would be a good vision statement. However, Microsoft's official vision statement is to "empower people through great software anytime, anyplace, and on any device" (The Marketing Blender, 2017).

Although the second statement is also quite broad, it does say how Microsoft wants to achieve the first statement, which makes it a better mission statement than a vision statement.

BRAINSTORM

Why are vision and mission statements important to a firm's strategy for developing a competitive advantage?

To put it simply, you can't make a plan or strategy unless you know what you want to accomplish.

BIG IDEA

Vision and mission statements together are the first building blocks in defining why a firm exists and in developing a plan to accomplish what the firm wants to accomplish.

REFLECT

1. What does a mission statement explain about a firm that a vision statement does not?
2. What are the similarities and differences between vision and mission?

SUMMARY

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In this lesson, you learned how to interpret the difference between a firm's vision and its mission. A **firm's vision statement** is a general statement about why it exists—an expression of what the founders want that business to accomplish. A **firm's mission statement**, on the other hand, is more specific and describes how the firm will try to accomplish the firm's vision. You learned that while neither a vision statement or mission statement describe a strategy, there are notable **differences** between the two: a vision statement is a broad statement about why a firm exists, whereas a mission statement is a more specific statement describing the products a firm plans to offer or the target markets it plans to serve.

Best of luck in your learning!

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TERMS TO KNOW

Mission Statement
A general description of how the firm will try to accomplish the firm's vision.

Vision Statement
A broad expression of what a business's founders want that business to accomplish.

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The Role of Strategic Analysis in Formulating a Strategy

by Sophia

WHAT'S COVERED

In this lesson, you will learn to indicate why strategic analysis is important for strategy formulation. Specifically, this lesson will cover:

1. Why Strategic Analysis Is Important to Strategy Formulation

1. Why Strategic Analysis Is Important to Strategy Formulation

In the previous lesson, you read about the various levels of analysis that a manager carries out in order to understand their firm's competitive environment. A **strategic analysis** of a firm's external environment (e.g., the world, competitors) and internal environment (e.g., firm capabilities and resources) gives its managers a clear picture of what they have to work with and also what needs to be addressed when developing a plan for the firm's success. Analysis comes early in the strategic process because the information a manager gets from the analysis informs the decision-making that follows. The information is so critical that entrepreneurs writing business plans (before the business even exists) do this analysis to understand if their business idea is feasible, and to understand how to position their business relative to existing competitors or potential customers in order to maximize their odds of success. The table below outlines just a few of the questions that strategic analysis tools can help answer.

PESTEL	Porter's Five Forces	Resources and Capabilities
• What technological opportunities exist for my business? • What sociocultural trends provide opportunities for my business? • Are there laws or regulations that affect what I can sell or how I can make my product?	• Are other firms in the industry competing based on prices or on differentiation? • Are new firms coming into this market? • Do buyers have attractive substitute options for my offerings? • Are suppliers available for the supplies I need?	• Do we have any special resources or capabilities that our competitors don't? • Do we need any resources or capabilities in order to compete with other firms in the industry?

As an example of how the strategic tools help inform decisions, look back at the Walt Disney mission and vision in the previous section. Imagine if you were Mr. Walt Disney today, and you wanted to start a company

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with a vision of making people happy in the 21st century. A PESTEL analysis would tell you that technology is an important part of entertainment and that sociocultural trends include people's preference for on-demand entertainment, to be convenient and compatible with their busy schedules.

BRAINSTORM

- Disney's mission statement is broad enough about products and services to include a wide variety of offerings (they are thinking about the future too!), but if you were starting this company today, where would you start?
- What products or services would you plan to offer?
- Would you make movies for movie theaters, or develop a way to offer video entertainment online?
- Would you make console video games or phone apps?
- Who would your competition be, and what do they offer?
- How could you offer something better or cheaper?

Managers learn about the conditions that their business will have to operate in by doing strategic analysis, and understanding those conditions is required in order to develop the plans and actions that will lead to success.

REFLECT

1. What strategic analysis tools from the previous challenge would a manager use when planning a strategy for an existing business?
2. What tools would be most helpful for a start-up business?

TERM TO KNOW

Strategic Analysis
The systematic examination of a firm's internal and external situation that informs managerial decision-making.

SUMMARY

In this lesson, you learned **why strategic analysis is important for strategy formulation**. You learned that strategic analysis of a firm's external and internal environment comes early in the strategic process and provides its managers a clear picture of what they have to work with and what needs to be addressed when developing a plan for success. As a reminder, managers can utilize strategic analysis tools like PESTEL, Porter's Five Forces, and resources and capabilities analysis to help answer critical questions about the world at large, competitors, and the firm's unique skills and assets to inform their decision-making.

Best of luck in your learning!

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TERMS TO KNOW

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Strategic Analysis

The systematic examination of a firm's internal and external situation that informs managerial decision-making.

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Strategic Objectives and Levels of Strategy

by Sophia

WHAT'S COVERED

In this lesson, you will learn about strategic objectives, levels of strategy, and grand strategy. You will also learn how they are related. Specifically, this lesson will cover:

1. Strategic Objectives
2. Levels of Strategies
3. The Grand Strategy
   a. Operationalizing a Grand Strategy

BEFORE YOU START

Once a strategic analysis has been completed, the next step in the strategy process is to establish strategic objectives. At this point, the manager has decided why the company exists and how it will try to fulfill its mission. Strategic analysis has provided information about customer preferences, competitors, and the firm's resources and capabilities. Now it is time to start planning for success.

1. Strategic Objectives

Strategic objectives are the big-picture goals for an organization. They describe what the company will do to fulfill its mission. Strategic objectives are usually some sort of performance goal—for example, to launch a new product, increase profitability, or grow market share for the company's product.

The diagram below shows what might be some strategic objectives for Disney. To make people happy (Disney's vision), Disney focuses on entertainment (its mission). Top executives then decide each year what entertainment products the company will offer. Because Disney is a large corporation, it has a variety of resources available to create entertainment products to offer. For example, they may decide to release three movies this year, as well as build a new theme park and create five new shows for their television network. In reality, the strategic objectives at Disney are much more complex than this, because some of these choices involve long-term efforts (e.g., they cannot build a theme park in one year).

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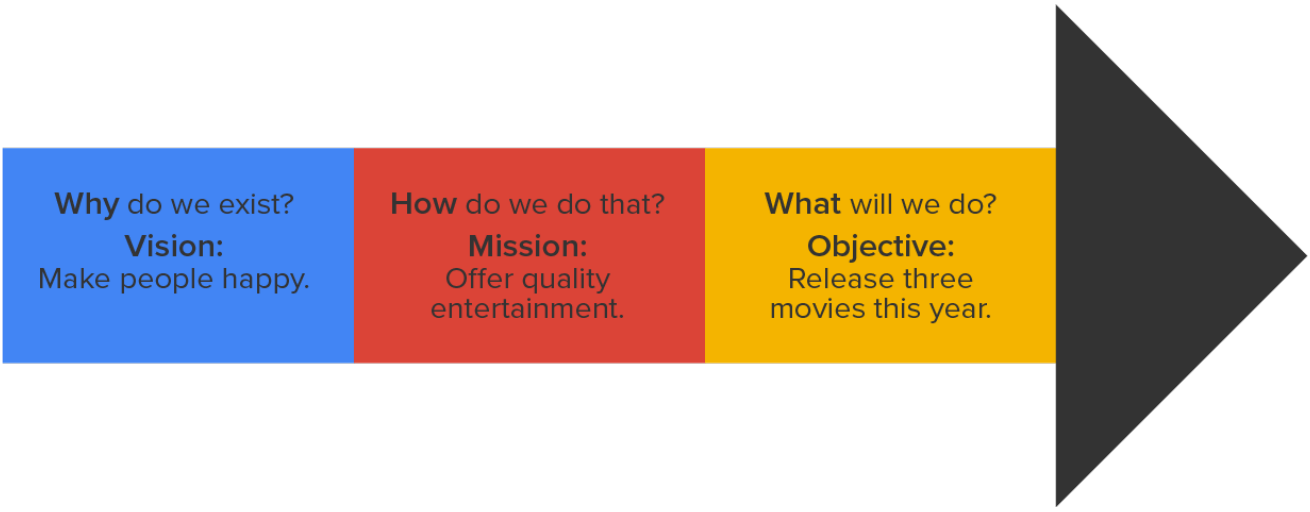

TERM TO KNOW

Strategic Objectives
The big-picture goals for the company: what the company will do to try to fulfill its mission.

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2. Levels of Strategies

Once a firm has set its objectives, it then must turn to the question of how it will achieve them. A **business-level strategy** is the framework a firm uses to organize its activities, and it is developed by the firm's top managers. Examples of business-level strategies include cost leadership and differentiation. These strategies are pursued by businesses with a single product or a range of products.

THINK ABOUT IT

Imagine that you own a coffee shop. You aren't Starbucks—you are a local shop in your neighborhood, and you run it yourself. You have employees, but you are the manager, owner, and all-around decision maker. While developing your vision and mission statements, you have already made some basic decisions about how your shop will operate. For example, you have chosen to either offer quick, inexpensive coffee (cost leadership) or a full-service coffee experience (differentiation). That decision impacts whether or not you choose premium or discount suppliers, how your shop is decorated, and how many employees you must have to serve customers.

A business-level strategy guides a company in how they approach the activities in the value chain. Operations, for example, would focus on efficiency for a cost leader and focus on adding value for a differentiator.

When you develop strategic objectives for your shop, you will decide whether or not you want to try to attract more customers (grow), maintain your business at its current level, or shrink your business (perhaps you feel you don't have enough time to spend with your family). If you decide that your objective is to grow, for example, you should set a specific target, say, to grow revenue by 10%. Once you set that specific objective, you can determine exactly what business-level actions you will need to take to reach that target.

Even if a business is much larger than a local coffee shop, the strategic objectives pursued by these larger companies are not significantly different in concept. Large companies like Nike or Apple, which have many different business units, develop strategies at several levels. Each individual business unit (say Nike Basketball) will have a manager who decides the objectives for that unit, just as in the coffee shop example. However, the company as a whole will have a chief executive officer (the top manager for the company) who

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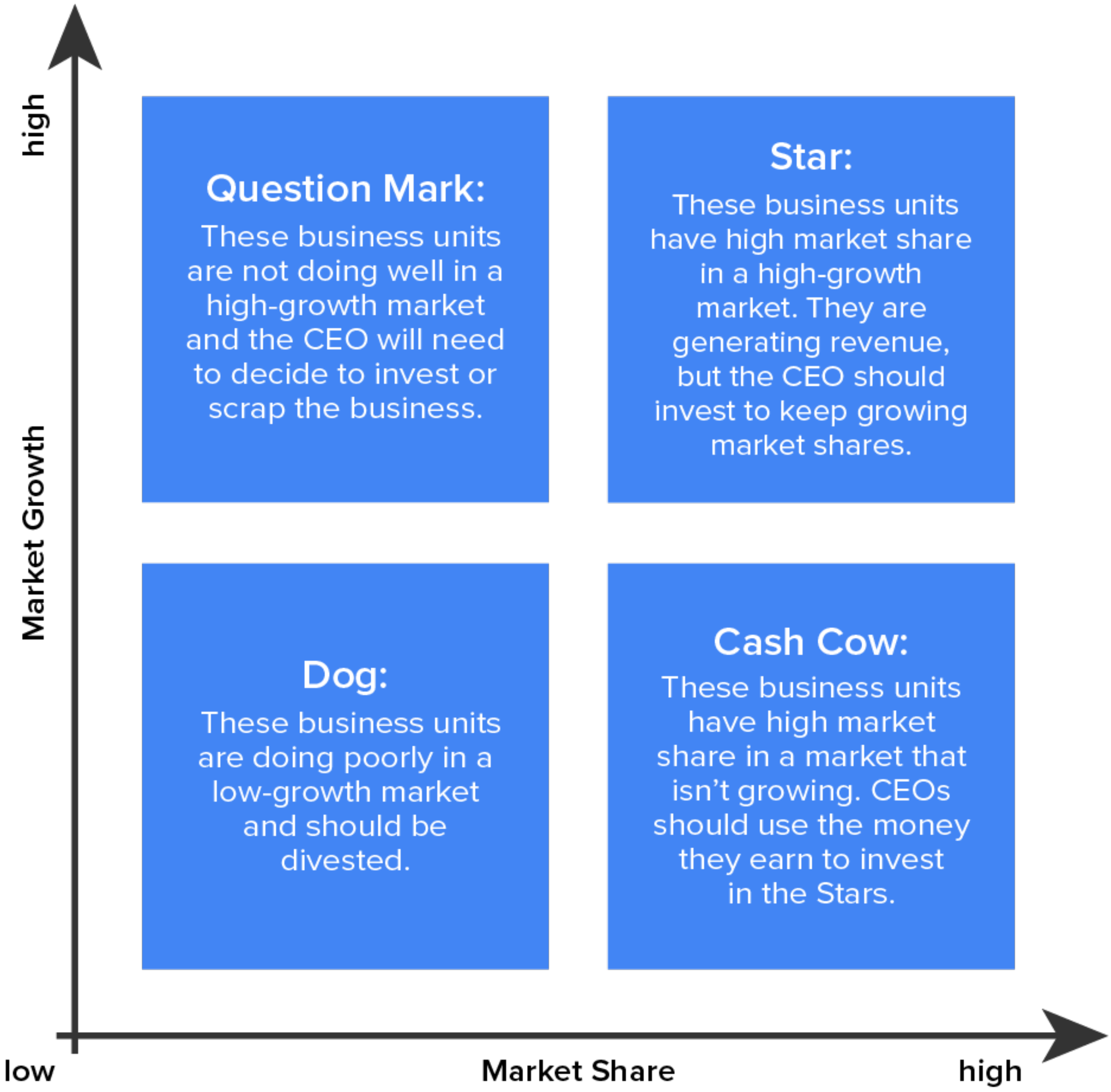
develops strategy for the entire corporation. **Corporate strategy** is the broadest level of strategy, and is concerned with decisions about growing, maintaining, or shrinking very large companies. At this level, business-level strategy activities, such as an advertising campaign to attract new customers for a single product line, are not going to be enough to significantly impact the company as a whole.

The corporate CEO essentially manages a group of businesses (unless the firm operates as one business unit) and develops strategies to create success for the overall group. Think of the group of businesses as an investment portfolio: investors try to have a diverse set of investments to spread risk and maximize the performance of the overall portfolio. On any given day, an investment that isn't doing so well should be offset by one that is doing well. Corporate strategy tries to achieve the same thing, and CEOs have to weigh the pros and cons of each business unit and how it is contributing to the success of the overall corporation.

> ↪ EXAMPLE A company that has business units that do well in the winter (ski resorts) will try to also have business units that will perform in the summer (swimming pools) to reduce the risk of having periods of low revenue.

One tool that corporate strategists use to understand how each of their businesses contributes to the corporation as a whole is the BCG Matrix, illustrated in the diagram below.



The **BCG Matrix** gives managers a quick picture of which business units are doing well and which are not. The tool has recommendations for businesses in each quadrant—for example, a business in the dog quadrant should be sold or closed. Cash cows provide income to the corporation, and stars provide growth. A CEO is always trying to balance the group of business units throughout the quadrants to maximize overall corporate performance. Note that the BCG Matrix is not applicable for firms that operate in one business unit.

In order to achieve the scale of growth necessary to meet corporate strategic objectives, a CEO may have to find ways to develop entirely new business units or reach brand-new markets. CEOs have several ways of growing their companies, as shown in the following table that describes how grand strategies are translated into objectives and actions.

Level of Strategy	Grand Strategy	Strategic Objective	Potential Action
Business-Level Strategy	Growth	Increase business revenue by 25%	• Introduce a new product • Expand to a new location
Corporate-Level Strategy	Growth	Increase corporate revenue by 10%	• Acquire a competitor • Expand to a new country • Develop a business in a new industry
International Strategy	Growth	Attract 10% overall market share in a new country	• Export products to that country • Acquire a local company in that country to gain their customers

International strategy is similar to corporate strategy because it is concerned with the large-scale actions involved in entering a brand-new geographic market. For companies operating internationally, strategic questions focus on how to successfully enter and compete in a foreign market. International strategy can combine with business-level or corporate-level strategies because a growth strategy at either scale can involve entering new markets in order to reach new customers.

TERMS TO KNOW

Business-level Strategy
Ways that single-product firms organize their activities to succeed against rivals; at this level, include cost leadership and differentiation.

Corporate Strategy
The broadest level of strategy, concerned with decisions about growing, maintaining, or shrinking very large companies.

BCG Matrix
A tool used to evaluate the various business units in a corporation.

International Strategy
The level of strategy concerned with the large-scale actions involved in entering a brand-new geographic market.

3. The Grand Strategy

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At all three levels, companies choose a **grand strategy** in response to the first question they should ask themselves: does the firm want to grow, strive for stability, or take a defensive position in the marketplace? Often, the choice of a grand strategy is based on conditions in the business environment because firms generally want to grow unless something (like a recession) makes that difficult. Note that a grand strategy and a corporate strategy can overlap significantly.

- A **growth strategy** involves developing plans to increase the size of the firm in terms of revenue, market share, or geographic reach (often a combination of these, as they can overlap significantly).
- A **stability strategy** is a strategy for a company to maintain its current income, market share, or geographic reach. A firm usually works to maintain a stable position when the alternative is to lose ground in one of those categories—for example, because of competition or economic factors. In today's business environment, publicly held firms rarely aim solely to maintain the status quo, because shareholders and the stock market reward firm growth.
- Firms pursue **defensive strategies** in the face of challenges. A company that is struggling may decide to shrink its operations to reduce costs in order to survive, for example. A company facing strong new competition may have to radically rethink its product offerings or pricing in order not to lose too much market share to the newcomer. A technological innovation may make a company's products obsolete (or at least less attractive), forcing it to work to catch up to the new technology. Ford made a defensive decision when it recently decided to stop selling sedans in the United States because of slow sales compared to trucks and SUVs.

TERMS TO KNOW

Grand Strategy
Overall business strategy of an organization.

Growth Strategy
A grand strategy to increase the size of the firm in terms of revenue, market share, geographic reach, or a combination of these elements.

Stability Strategy
A grand strategy for a company that wants to maintain its current income, market share, or geographic reach.

Defensive Strategy
A grand strategy pursued by companies facing challenges.

3a. Operationalizing a Grand Strategy

A firm operationalizes its choice of a grand strategy differently at each level of strategy (business, corporate, international). At the business level, a growth strategy means that the manager will have to develop ways to grow the business by developing new products or expanding the customer base for existing products, either at home or abroad. Expanding a company can take a wider variety of forms. The CEO can develop new businesses, expand to new countries, acquire or merge with competitors, or perform previously outsourced activities. International expansion can be accomplished by exporting goods to another country or by acquiring a similar firm in another country to establish the company's presence in that country. In all three of these cases, the grand strategy would be growth, and the strategic objectives could be expressed in terms of revenue growth, profit growth, market share growth, or even share price growth. The table in the previous section outlines how a grand strategy can be used to develop specific company actions.

REFLECT

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1. What is the difference between strategic objectives and a strategy?
2. Describe the three levels of strategy and what a manager developing strategy at each level is concerned with.
3. What is a grand strategy, and how does it relate to strategic objectives and the three levels of strategy?
4. What are the three grand strategies, and why would firms pursue each of them?

SUMMARY

In this lesson, you learned about strategic objectives, levels of strategy, and grand strategy, as well as how they are related. You learned that **strategic objectives** are the big-picture goals—usually some sort of performance goal—for an organization, describing what the company will do to fulfill its mission. Once a firm has set its objectives, it may use different **levels of strategies** to achieve them, such as a business-level strategy, which guides a company in how they approach the activities in the value chain; a corporate strategy, which is concerned with decisions about growing, maintaining, or shrinking very large companies; or an international strategy, which is concerned with the large-scale actions involved in entering a brand-new geographic market. Corporations with multiple business units can use a tool called the BCG Matrix to evaluate which are doing well and which are not. Lastly, you learned that at all three levels, companies choose a **grand strategy** in response to whether they want to grow, strive for stability, or take a defensive position in the marketplace. A firm will **operationalize its grand strategy** differently at each level of strategy (business, corporate, international).

Best of luck in your learning!

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TERMS TO KNOW

BCG Matrix
A tool used to evaluate the various business units in a corporation.

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Ways that single-product firms organize their activities to succeed against rivals; at this level, include cost leadership and differentiation.

Defensive Strategies
A grand strategy pursued by companies facing challenges.

Grand Strategy
Overall business strategy of an organization.

Growth Strategy
A grand strategy to increase the size of the firm in terms of revenue, market share, geographic reach, or a combination of these elements.

International Strategy

The level of strategy concerned with the large-scale actions involved in entering a brand-new geographic market.

Stability Strategy

A grand strategy for a company that wants to maintain its current income, market share, or geographic reach.

Strategic Objectives

The big-picture goals for the company: what the company will do to try to fulfill its mission.

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Planning Firm Actions to Implement Strategies

by Sophia

WHAT'S COVERED

In this lesson you will learn how and why managers plan. Specifically, this lesson will cover:

1. Planning Actions
2. Goal Setting
    a. Setting Good Goals: The SMART Framework
3. The Planning Process
4. Implementing Plans for Different Levels of Firm Activity and Time Horizons
5. Scale Levels of Planning
6. Implementing Planned Strategies

1. Planning Actions

When managers create strategies, they are making plans for how their firm will compete in the marketplace and what actions the firm will have to undertake to compete. A **plan** is a decision to carry out a particular action in order to achieve a specific goal. A plan includes decisions about when and how actions should be accomplished and what resources will be required to complete the actions. Because planning is one of the basic functions of management, a good manager should have good goal-setting skills, technical knowledge about the tasks necessary to reach goals, time management skills, and the organizational skills required to arrange company resources to be available to complete the planned tasks. Planning is a combination of deciding what needs to be done, figuring out how to do it, assigning roles to people and providing them the resources to complete their tasks, and overseeing the work to make sure it gets done correctly and in a timely manner.

TERM TO KNOW

Plan
A decision to carry out a particular action in order to achieve a specific goal, including decisions about when and how the action should be accomplished and what resources will be required to carry out the action.

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2. Goal Setting

To examine the planning process, we need to start by understanding what the planning is for. A **goal** is something that you are trying to accomplish, and any firm will have many items on its list of things to accomplish.

EXAMPLE Consider the situation of a Walmart store in a college town. When it's time for students to arrive back to school in the fall, the store needs to be ready with all the products students need when they move in. The Walmart store manager will plan months in advance and use information learned from the previous year's sales to decide what products to order and how many, and when to have extra staff in the store to efficiently check out increased numbers of shoppers.

The manager's plans will take into account the lead time for ordering products to make sure that mini-refrigerators and twin XL sheets arrive and can be stocked in the store in time for the back-to-school rush. Preparing for the back-to-school season may involve reducing prices on other items to get them out of the way to make room for all those small refrigerators, and hiring and training additional employees so that there will be enough associates to help students and their parents. The manager's ultimate goal is to have a successful back-to-school sales season, but achieving that goal will involve completing tasks such as making product selection decisions, meeting ordering deadlines, and setting intermediate goals for hiring and training additional employees.

TERM TO KNOW

Goal

Something that a firm is trying to accomplish; can also be called an objective.

2a. Setting Good Goals: The SMART Framework

Good goals have a few common characteristics, and the table below presents a framework for creating good goals.

Characteristic	Description
Specific	The goal should be specific and understandable.
Measurable	The goal should be measurable so that you can tell if you are achieving it.
Achievable	The goal should be achievable and reasonable, not impossible.
Relevant	The goal should be relevant to your overall objective and help you advance toward it.
Time-Bound	The goal must have a time limit so that there is a sense of urgency to accomplishing it.

The **SMART framework** can be applied to business or personal goals. A good goal should be**s**pecific, **m**easurable, **a**chievable, **r**elevant, and **t**ime-bound.

TERM TO KNOW

SMART Framework

An acronym for the characteristics of good goals: specific, measurable, achievable, relevant, and time-bound.

3. The Planning Process

The diagram below illustrates the planning cycle. It looks a lot like the strategy cycle shown in an earlier lesson because they have a lot in common. In fact, the planning process is an integral part of the strategy cycle, since developing objectives, creating strategies, and implementing firm-wide activities all require extensive planning.

The first step in planning is to set a goal to be accomplished. Making sure that the goal checks off all of the SMART criteria will help make the planning process easier and more likely to be successful, so be sure to spend some time developing a good goal.

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Once you've figured out your goal, the next step is to design the plan. Designing the plan involves several distinct activities, so let's break it down into what needs to happen. Think of planning as a problem-solving exercise. A plan is a set of actions developed to accomplish a goal, and planning is essentially figuring out what those actions should be. The goal is the end point, and the plan answers the question, "How do we get there?"

When designing a plan, a manager may think of many ways to achieve a goal. He or she can have a group of employees brainstorm to come up with ideas. Not all of the potential ideas are likely to be feasible, however. Part of the manager's task in designing a plan is to coordinate various ideas with a firm's resources and capabilities and its time constraints. When does the goal need to be accomplished? What other resources does the firm need to complete the project?

The following diagram illustrates coordination between different elements in effective planning.

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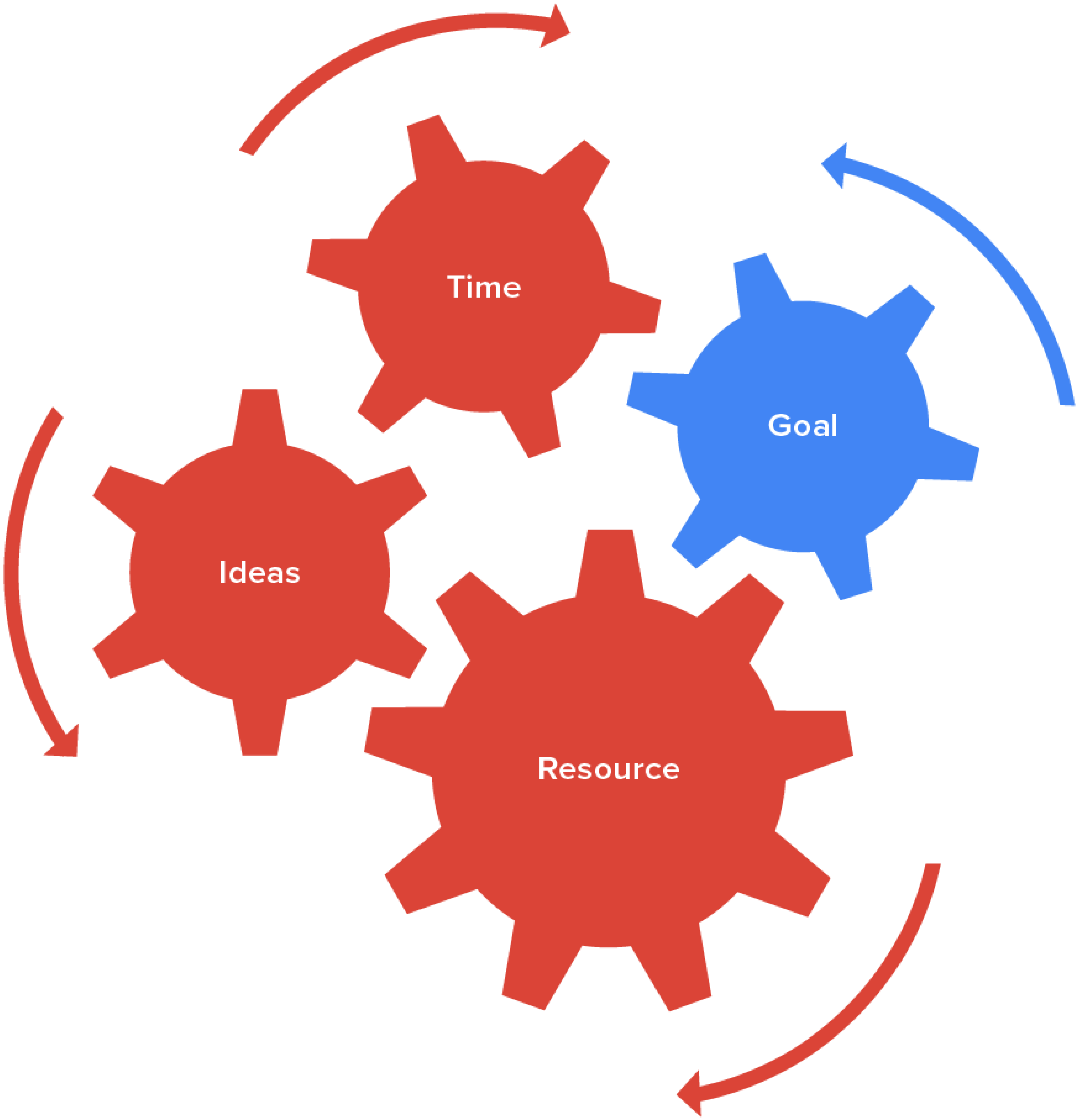

Designing the plan becomes a puzzle of figuring out what is the best way to reach a goal with the resources the firm has or can reasonably get in the time available. There is no prescription for this, and the best way to learn how to plan is to practice. Fortunately, you probably have a pretty good amount of practice already, because you've been planning in one form or another for a long time. You have planned study time, team practices, club events, and even meals. Strategic planning uses the same skills in a new context. Planning a product launch may sound complicated, but so is planning a wedding. The scale and scope of the things a manager must coordinate in order to reach company goals may be larger than what you are used to, but the specific skills are likely not new at all.

For example, let's take a look at the challenge Tesla is currently facing.

IN CONTEXT

Tesla has developed a mass market car and has a line of about half a million customers waiting to buy one. Until now, Tesla has been more of a boutique car maker, manufacturing small numbers of

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cars that they are able to sell at high prices. The Model 3, however, has been specifically conceived as an affordable car that almost anyone can buy. The brand and reputation Tesla has built with its premium cars has generated a lot of enthusiasm and demand for this new model. So Elon Musk, CEO of Tesla, is planning to make cars in larger numbers and more quickly than ever before.

What's Tesla's goal? Manufacture cars at a rate of 500,000 per year in order to meet demand. Is this a SMART goal? Analysts around the world are arguing over this (is it achievable?), but it's the goal that Tesla is focusing on, so Musk has to design a plan to reach that goal. What resources does Tesla need in order to reach this level of production? They developed a car that is easy to manufacture, because they knew that they would want to build it in large numbers. Still, they need manufacturing facilities, parts, and production employees. To get these resources, they need money. Elon Musk is a spectacular fundraiser, but they need billions of dollars to develop manufacturing capabilities on this scale. So while Tesla builds the world's largest factory in Nevada, called the Gigafactory, Musk continues to raise funds.

Components (specifically the batteries) are also an issue for the Model 3, and Musk has built his giant factory in part to manufacture the hundreds of thousands of batteries needed to power the Model 3. Tesla's planning involves many interrelated activities, and figuring out what the activities are, what resources Tesla needs to perform the activities, and how to obtain resources that they need but don't have yet are the challenges Elon Musk is tackling. Tesla is a fascinating company that is multifaceted. There have been serious questions raised about their ability to produce enough cars and an examination of more recent commentary is encouraged.

4. Implementing Plans for Different Levels of Firm Activity and Time Horizons

Developing plans happens simultaneously at multiple levels in any company. Plans often require different steps in order to achieve a large-scale objective. If a firm decides on growth as a grand strategy, actions at every level of firm activity should contribute to firm growth, and managers at all of those levels should develop plans so that their part of the firm is working to implement the growth strategy. A grand strategy cascades throughout the company, becoming more and more specific, until frontline employees are working on specific tasks that support the grand strategy.

Time is an important consideration when top managers develop company goals and the plans to achieve them. In general, firms have two time spans that they plan for: short term and long term. A **short-term strategic plan** is one that can be accomplished in a year or sooner. A**long-term strategic plan** is developed when an objective cannot be accomplished in less than a year. Companies generally have both scales of plans in place at any given time: short-term plans might involve quarterly sales goals, for example, but a firm might have a longer-term goal of establishing operations in another country or building a new facility.

EXAMPLE Tesla's Gigafactory and Apple's new headquarters at Apple Park in Cupertino, California, are both multiyear, multibillion dollar projects, and so would be good examples of long-term plans. In Tesla's case, the Gigafactory was initially planned many years ago when the company knew that it wanted to mass-produce cars at the scale required for the Model 3 (Tesla, 2017).

TERMS TO KNOW

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Short-Term Strategic Plan

Company actions to achieve an objective in a time frame of a year or less.

Long-Term Strategic Plan

Company actions to achieve an objective that will take a year or longer to accomplish.

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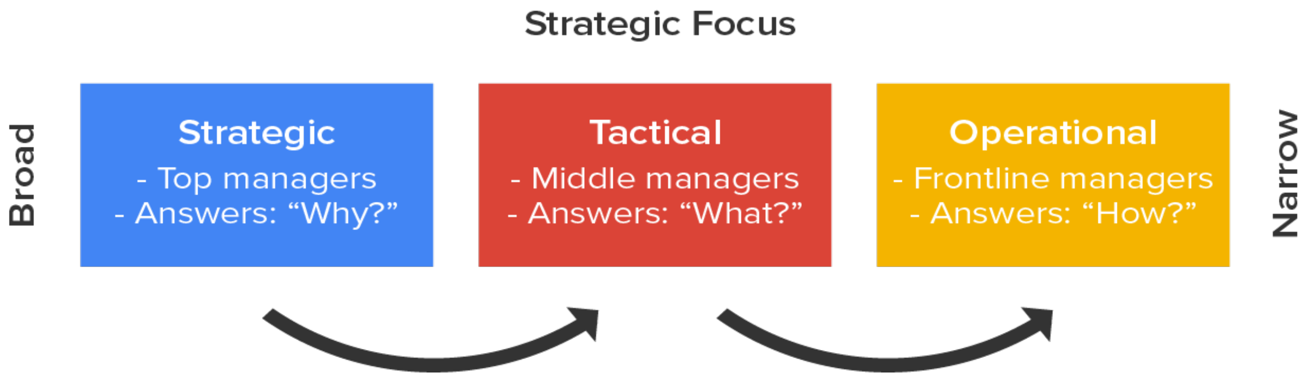
5. Scale Levels of Planning

Another dimension that impacts strategic planning is scale. We have already looked at some large-scale planning concepts, such as business-level and grand strategies. However, the day-to-day planning that managers do to take steps toward those bigger objectives is key to achieving success. The following diagram shows the typical levels of planning going on in a company at any given time.



Notice that if you compare this diagram to the possible strategic path for Disney, the "what" and "how" are switched. The switch is a scale switch. Vision and mission are both conceived at the broadest scale, and so even the "how" of the mission is a large-scale idea. In contrast, when managers are planning, the "how" of operational planning lays out precise actions and steps to follow to achieve a specific objective. Let's look at the levels one by one.

1. **Strategic planning** is what we've been discussing so far. It's the high-level planning performed by company executives in order to set the overall direction of the company. Grand strategies are part of strategic planning, as are business-level strategies such as cost leadership. Strategic planning connects the company's actions back to its vision and mission statements (the "why does this company exist" question).
2. **Tactical planning** is mid-level planning that consists of broad ideas of what the company should do to pursue its mission. This is the sort of planning done by division managers. For example, Walmart division managers carry out the company's growth and cost-leadership strategies by finding ways for the company to grow and continue to be able to offer low prices. They may decide where to locate distribution centers to maximize store-stocking efficiency, which manufacturers of goods they can buy inventory from at low prices, and where to build new stores to attract more customers.
3. **Operational planning** lays out the frontline activities that each employee in the company will do to advance the tactical plans. A McDonald's restaurant manager develops operational plans, but you might recognize them more as employee schedules or promotional plans. Operational plans are the daily activities required for the company to function, including ordering inventory or supplies, scheduling workers and defining their work tasks, and developing sales goals and promotions to help achieve those goals. At McDonald's, as at other companies that pursue a cost-leadership strategy, scheduling enough employees to work in the restaurant at specific times to keep the store functioning smoothly without

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scheduling more than you need (and incurring excess labor costs) is a critical task for the manager, and doing that task successfully is how the manager contributes to the company's larger cost-leadership strategy.

TERMS TO KNOW

Strategic Planning
Connects the company's actions back to its vision and mission statements.

Tactical Planning
Mid-level strategic planning consisting of broad ideas of what a company should do to pursue its mission.

Operational Planning
First-line strategic planning consisting of specific daily and short-term actions that employees will perform to make the company function.

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6. Implementing Planned Strategies

Implementation of planned strategies refers to the execution of a strategy by assigning tasks for people to carry out to accomplish the company's strategic goals. Although a manager may talk about "implementing a differentiation strategy," the real implementation of a strategy happens at the bottom of not just the strategy hierarchy, but the organizational hierarchy, in the actions of operational employees who carry out planned tasks that add value to the company's product. Such tasks include research and development to add unique features, monitoring manufacturing to ensure company products meet high quality standards, and marketing the product to add brand value in the eyes of consumers.

REFLECT

1. What are the three levels of planning, and what kinds of plans do managers develop at each level?
2. Why is strategic implementation most commonly carried out at the operational level?

TERM TO KNOW

Implementation
The execution of a strategy by planning and assigning actions to employees to carry out in order to accomplish the company's strategic objectives.

SUMMARY

In this lesson, you learned how and why managers plan. You learned that creating a plan—a decision to carry out a particular action in order to achieve a specific goal—is one of the basic functions of management. **Planning actions** include deciding what needs to be done, how to do it, assigning roles to people and providing them the resources to complete their tasks, and overseeing the work to make sure it gets done correctly and in a timely manner. You learned that planning begins with an understanding of what the plan is for; therefore, **goal setting**, or determining what you are trying to accomplish, is a critical component of planning. **The SMART framework** can be applied to business goals to ensure managers are **setting good goals**, given that a good goal should be specific, measurable, achievable, relevant, and time-bound. You also learned about the four steps in **the**

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planning process: set goals, design plan, implement plan, and review results. Since plan development happens simultaneously at multiple levels in any company, managers at each level will be **implementing plans for different levels of firm activity** as well as different **time horizons**—the short term (a year or less) or the long term (over a year). You learned that another dimension that impacts strategic planning is **scale**, with the typical **levels of planning** occurring in a company at any given time outlined as strategic, tactical, and operational. Lastly, you learned that **implementing planned strategies** refers to the execution of a strategy by assigning tasks for people to carry out to accomplish the company's strategic goals.

Best of luck in your learning!

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REFERENCES

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TERMS TO KNOW

Goal
Something that a firm is trying to accomplish; can also be called an objective.

Implementation
The execution of a strategy by planning and assigning actions to employees to carry out in order to accomplish the company's strategic objectives.

Long-Term Strategic Plan
Company actions to achieve an objective that will take a year or longer to accomplish.

Operational Planning
First-line strategic planning consisting of specific daily and short-term actions that employees will perform to make the company function.

Plan
A decision to carry out a particular action in order to achieve a specific goal, including decisions about when and how the action should be accomplished and what resources will be required to carry out the action.

SMART Framework
An acronym for the characteristics of good goals: specific, measurable, achievable, relevant, and time-bound.

Short-Term Strategic Plan
Company actions to achieve an objective in a time frame of a year or less.

Strategic Planning
Connects the company's actions back to its vision and mission statements.

Tactical Planning
Mid-level strategic planning consisting of broad ideas of what a company should do to pursue its

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mission.

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Measuring and Evaluating Strategic Performance

by Sophia

WHAT'S COVERED

In this lesson, you will learn how managers evaluate the effectiveness of strategic plans. Specifically, this lesson will cover:

1. Measuring and Evaluating Performance

1. Measuring and Evaluating Performance

The last step in the strategy cycle is measuring and evaluating performance. The “M” in SMART goals is also about measurement. A company’s actions need to be measured so that managers can understand if the firm’s strategic plans are working. Any action in a plan should be designed so that the people performing the action and the manager who is supervising employees can understand whether or not the action is accomplishing what it was designed to.

HINT

You have been living in this sort of framework all of your life. For many life goals, standards exist to measure achievements.

EXAMPLE Students are given standardized tests to see if they are learning what they are expected to, and the results are used to assess the effectiveness of education at all levels.

In businesses, measurement is also a fact of life. Investors decide whether or not to invest in a particular company based on its performance, and publicly held companies are required to disclose their financial performance so investors can make informed decisions. So the overall performance of a business is often defined by its financial measures, but how do they make sure their financial performance will make investors happy? Strategy. Firms make strategic plans in order to be successful. This challenge has explained the steps of making those plans, but a final step closes the circle of the strategy cycle. Checking to see if that success is happening is as important as making the plans in the first place.

Performance measurement comes in many forms, from financial reports to quality measures like defect rates. Any activity a firm can perform can have a performance measure developed to evaluate the success of that activity. The following table lists a few common firm objectives and how actions to achieve them might be evaluated. Evaluation involves setting a performance standard, measuring the results of firm activities, and comparing the results to the standard. One specific form of evaluation is called **benchmarking**, a process in which the performance standard is based on another firm’s superior performance.

EXAMPLE In the hospitality industry, for example, Disney theme park operations are used as standards for other companies in the theme park industry. Universal theme parks, for example, likely compare their customer satisfaction to Disney’s in order to evaluate whether or not they are also offering a superior park experience to their customers.

The table below describes three different actions to support a differentiation strategy and ways to measure results.

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Strategic Plan	Tactical Plan	Operational Plan	Performance Measure
Product differentiation	Innovation	Hire three engineers to develop new products	Number of new products launched
	Increase customer satisfaction	Improve customer service with hiring and training program for customer service associates	Customer complaints per 10,000 products sold
	Quality improvement	Reduce defective products by improving manufacturing process accuracy	Defect rate per 10,000 units produced

Performance evaluation closes the strategy cycle because of what managers do with the feedback they get in the evaluation process. When a manager compares performance to a standard, he/she is deciding whether or not the performance is acceptable or needs to be improved. The strategy cycle is a process managers use to achieve an advantage in the marketplace, and the measurement and evaluation stage tells managers whether the advantage is being achieved. If firm performance meets or exceeds objectives, then the manager reports the success to middle and upper-level managers. The company CEO may develop more ambitious objectives based on that success, and the strategy cycle starts over. If performance fails to meet objectives, the operational manager must develop new actions to try to meet the objectives or report to higher-level managers that the objectives cannot be met. In this case, a new round of operational planning begins, or upper managers examine their strategic plan to see if they need to make adjustments.

BIG IDEA

The strategy process is a continuous cycle. Performance feedback becomes part of the strategic analysis of the firm's capabilities and resources, and firm leadership uses the information to help develop better strategies for firm success.

REFLECT

1. Why is performance evaluation critical in strategic planning?
2. How does the strategic planning process inform itself?

TERMS TO KNOW

Benchmarking
A performance evaluation technique where the standard for a firm's performance is based on another firm's superior performance.

Performance Measurement
The evaluation of firm activities to determine the success of the activities in helping the firm reach its strategic objectives.

SUMMARY

In this lesson, you learned about the last step in the continuous strategy cycle: **measuring and evaluating performance**. It is important to measure a company's actions so that managers can understand if the firm's strategic plans are working. You learned that performance measurement comes in many forms; any activity a firm can perform can have a performance measure developed to

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evaluate the success of that activity, such as benchmarking. Performance evaluation closes the strategy cycle with managers deciding whether or not the performance is acceptable or needs to be improved. This performance feedback is used to help develop better strategies for firm success.

Best of luck in your learning!

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TERMS TO KNOW

Benchmarking
A performance evaluation technique where the standard for a firm's performance is based on another firm's superior performance.

Performance Measurement
The evaluation of firm activities to determine the success of that activity in helping the firm reach its strategic objectives.

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Terms to Know

BCG Matrix

A tool used to evaluate the various business units in a corporation.

Barriers to Entry

Industry factors (such as high start-up costs) that can prevent new firms from successfully launching new operations in that industry.

Benchmarking

A performance evaluation technique where the standard for a firm's performance is based on another firm's superior performance.

Bounded Rationality

The idea that for complex issues we cannot be completely rational because we cannot fully grasp all the possible alternatives, nor can we understand all the implications of every possible alternative.

Brainstorming

A process of generating as many solutions or options as possible, a popular technique associated with group decision-making.

Business-level Strategy

Ways that single-product firms organize their activities to succeed against rivals; at this level, include cost leadership and differentiation.

Buyer Power

In the relationship between a firm and its customers, buyers with high power can negotiate product price or features, while buyers with low power cannot.

Capabilities

A firm's skill at coordinating and leveraging resources to create value.

Competition

Business actions a firm undertakes to attract customers to its products and away from competitors' products.

Competitive Advantage

When a firm successfully attracts more customers, earns more profit, or returns more value to its shareholders than rival firms do.

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Competitive Environment

Includes components inside the firm and outside the firm that may impact the firm’s success.

Confirmation Bias

A shortcoming where people tend to pay more attention to information that confirms their existing beliefs and less attention to information that is contrary to their beliefs.

Cost-leadership Strategy

A generic business-level strategy in which a firm tightly controls costs throughout its value chain activities in order to offer customers low-priced goods and services at a profit.

Creativity

The generation of new or original ideas.

Critical Thinking

A disciplined process of evaluating the quality of information to determine whether the source should be trusted or whether the argument is valid.

Decision-Making

The action or process of thinking through possible options and selecting one.

Decision-making

The action or process of thinking through possible options and selecting one.

Decisional Role

One of three major roles identified in Mintzberg's seminal study of managers in which managers make decisions on behalf of both the organization and the organization's stakeholders.

Defensive Strategies

A grand strategy pursued by companies facing challenges.

Demographics

A subset of the sociocultural factors category; it includes facts about income, education levels, age groups, and the ethnic and racial composition of a population.

Devil's Advocate

Person who intentionally takes on the role of critic. Their job is to point out flawed logic, to challenge the group’s evaluations of various alternatives, and to identify weaknesses in proposed solutions.

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Differentiation Strategy

A generic business-level strategy in which firms add value to their products and services in order to attract customers who are willing to pay a higher price.

Economic Factors

Firms analyze economic indicators to make decisions about entering or exiting geographic markets, investing in expansion, and hiring or laying off employees.

Emotional Intelligence

The ability to understand and manage emotions in oneself and in others.

Environmental Factors

The physical environment, which provides natural resources for manufacturing and energy production.

Environmental Scanning

The systematic and intentional analysis of both a firm's internal state and its external, competitive environment.

Escalation of Commitment

The tendency of decision makers to remain committed to poor decision, even when doing so leads to increasingly negative outcomes.

Evidence-Based Decision-Making

An approach to decision-making that states that managers should systematically collect the best evidence available to help them make effective decisions.

Executive Managers

Generally, a team of individuals at the highest level of management of an organization.

External Environment

The world at large forms the external environment for businesses.

External Factors

Things in the global environment that may impact a firm's operations or success; examples are a rise in interest rates, or a natural disaster.

First-line Management

The level of management directly managing nonmanagerial employees.

Focus Strategy

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A generic business-level competitive strategy that firms use in combination with either a cost-leadership or differentiation strategy in order to target a smaller demographic or geographic market with specialized products or services.

Generic Business-Level Strategies

Basic methods of organizing firm value chain activities to compete in a product market that can be used by any firm in any industry.

Goal

Something that a firm is trying to accomplish; can also be called an objective.

Grand Strategy

Overall business strategy of an organization.

Groupthink

Group members choose not to voice their concerns or objections because they would rather keep the peace and not annoy or antagonize others.

Growth Strategy

A grand strategy to increase the size of the firm in terms of revenue, market share, geographic reach, or a combination of these elements.

Heuristics

Mental shortcuts to help reach a decision.

High-Involvement Decisions

Nonprogrammed decisions that don’t require greater involvement and thought on the part of the decision maker.

Implementation

The execution of a strategy by planning and assigning actions to employees to carry out in order to accomplish the company’s strategic objectives.

Industry

A group of firms all making similar products or offering similar services, for example automobile manufacturers or airlines.

Industry Rivalry

One of Porter’s Five Forces; refers to the intensity of competition between firms in an industry.

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Informational Role

One of three major roles identified in Mintzberg's seminal study of managers in which managers gather, collate, analyze, store, and disseminate many kinds of information both within and outside the organization.

Internal Factors

Characteristics of the firm itself including the physical, financial, and human resources it has, what it is good at, and how it is organized.

International Strategy

The level of strategy concerned with the large-scale actions involved in entering a brand-new geographic market.

Interpersonal Role

One of three major roles identified in Mintzberg's seminal study of managers in which managers form and maintain professional relationships both within and outside the organization.

Legal Factors

Laws and regulations that can impact business success. These factors commonly have deep political connections.

Long-Term Strategic Plan

Company actions to achieve an objective that will take a year or longer to accomplish.

Low-Involvement Decisions

Programmed decisions that don’t require in-depth mental processing to reach a decision.

Macro Environment

A firm’s macro environment contains elements that can impact the firm but are generally beyond its direct control. These elements are characteristics of the world at large and are factors that all businesses must contend with, regardless of the industry they are in or type of business they are.

Micro Environment

The middle layer of elements in a firm’s external environment, primarily concerned with a firm’s industry situation.

Middle Management

The managers in an organization at a level just below that of senior executives.

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Mission Statement

A general description of how the firm will try to accomplish the firm’s vision.

New Entrants

One of Porter’s Five Forces, the threat of new entrants assesses the potential that a new firm will start operations in an industry.

Nonprogrammed Decisions

Novel, unstructured decisions that are generally based on criteria that are not well-defined.

Operational Planning

First-line strategic planning consisting of specific daily and short-term actions that employees will perform to make the company function.

Opportunity

A potential external situation that a firm is equipped to take advantage of.

PESTEL

A tool that reminds managers to look at several distinct categories in the macro environment. PESTEL is an acronym with each letter representing categories to examine: political factors, economic factors, sociocultural factors, technological factors, environmental factors, and legal factors.

Performance Measurement

The evaluation of firm activities to determine the success of that activity in helping the firm reach its strategic objectives.

Plan

A decision to carry out a particular action in order to achieve a specific goal, including decisions about when and how the action should be accomplished and what resources will be required to carry out the action.

Political Factors

Include taxation, tariffs, trade agreements, labor regulations, and environmental regulations.

Porter's Five Forces

A tool used to examine different micro-environmental groups in order to understand the impact each group has on a firm in an industry.

Primary Activities

Firm activities on the value chain that are directly responsible for creating, selling, or

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servicing a product or service, such as manufacturing and marketing.

Process Conflict

Conflict about the best way to do something; conflict that is task-oriented and constructive, and not focused on the individuals involved.

Programmed Decisions

Decisions that are repeated over time and for which an existing set of rules can be developed to guide the process.

Reactive System

System of decision-making in the brain that is quick and intuitive.

Reflective System

System of decision-making in the brain that is logical, analytical, and methodical.

Relationship Conflict

Conflict between individuals that is more personal and involves attacks on a person rather than an idea.

Resources

Things a firm has, such as cash and skilled employees, that it can use to create products or services.

SMART Framework

An acronym for the characteristics of good goals: specific, measurable, achievable, relevant, and time-bound.

SWOT Analysis

An acronym for strengths, weaknesses, opportunities, and threats. Firms use SWOT analysis to get a general understanding of what they are good or bad at and what factors outside their doors might present chances for success or difficulty.

Satisficing

When a decision maker selects the first acceptable solution without engaging in additional effort to identify the best solution.

Short-Term Strategic Plan

Company actions to achieve an objective in a time frame of a year or less.

Sociocultural Factors

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This broad category encompasses everything from changing national demographics to fashion trends and many things in between.

Stability Strategy

A grand strategy for a company that wants to maintain its current income, market share, or geographic reach.

Stakeholders

All the individuals or groups that are affected by an organization (such as customers, employees, shareholders, etc.).

Strategic Analysis

The process that firms use to study and understand the many different layers and aspects of their competitive environment.

Strategic Group

Businesses offering similar products or services and following the same generic competitive strategy.

Strategic Management Process

The set of activities that firm managers undertake in order to try to put their firms in the best possible position to compete successfully in the marketplace.

Strategic Objectives

The big-picture goals for the company: what the company will do to try to fulfill its mission.

Strategic Planning

Connects the company's actions back to its vision and mission statements.

Strategy

Process of planning and implementing actions that will lead to success in competition.

Strengths

What a firm is good at.

Substitute

One of Porter's Five Forces; products or services outside a firm's industry that can satisfy the same customer needs as industry products or services can.

Supplier Power

One of Porter's Five Forces; describes the balance of power in the relationship between

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firms in an industry and their suppliers.

Support Activites

Value chain activities that a firm performs to sustain itself; they do not directly create a product or service but are necessary to support the firm's existence, such as accounting and human resources.

Suppression of Dissent

One individual in the group has more power or exerts more influence than others and discourages those with differing opinions from speaking up to ensure that only their own ideas are implemented.

Switching Costs

Penalty, financial or otherwise, that a consumer bears when giving up the use of a product currently being used to select a competing product or service.

Tactical Planning

Mid-level strategic planning consisting of broad ideas of what a company should do to pursue its mission.

Technological Factors

This category includes the Internet, automation, and consumer's increased access to information to make buying decisions.

Threat

Anything in the competitive environment that would make it harder for a firm to be successful.

VRIO

Analytical tool that evaluates a firm's resources and capabilities to determine whether or not it can support an advantage for the firm in the competitive environment: value, rarity, imitation, and organization.

Value Chain

Sequence of activities that firms perform to turn inputs (parts or supplies) into outputs (goods or services).

Vision Statement

A broad expression of what a business's founders want that business to accomplish.

Weaknesses

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What a firm is not good at—things that it does not have the capabilities to perform well.