A NOTE ON STRATEGIC PLANNING[i]

By John McMahan

The concept of strategic management has been studied for almost 50 years. Over this period, management consultants and business school faculty members have helped firms formulate and implement wide-ranging strategic plans to the point where strategic management is now widely accepted in America's general business community.

Strategic management involves positioning a firm in the marketplace through 1) planning and 2) implementation of the plan. It may involve changing a firm's relationship with its customers, competitors, employees, shareholders, and/or other stakeholders. It may represent a change in the total organization or some or most of its business lines or products/services. It may involve merging or dissolving the firm itself.

The strategic planning process provides the roadmap for strategic management and lays the groundwork for the action steps to follow.

THE STRATEGIC PLANNING ENVIRONMENT

Strategic planning is thinking in the future – about the world, the nation, the business environment – and how the firm can best compete in the markets in which it chooses to operate. Strategic planning is also anticipation of the impact of major trends in the drivers of change (e.g. technology, deregulation, changing customer needs, etc.). Since no vision of the future is 100% correct, however, planning most often focuses on a "most likely" scenario while minimizing risk and maximizing rewards of alternative scenarios.

Industry Influencing Factors

Characteristics of the firm's industry may influence the strategic planning process. Firms in *emerging industries* (growing faster than the overall economy) must deal with rapidly changing market characteristics, a high degree of technological innovation, shorter product cycles, and the emergence of new (often, unforeseen) competitors. The strategic planning process for these firms, by necessity, must consider a shorter time horizon and afford much higher levels of implementation flexibility.

Firms in *growth industries* (growing at the same rate as the overall economy) often utilize a strategy focused on a single or few products/services. Although this strategy can lead to a strong, perhaps unassailable, competitive advantage, the firm is vulnerable to major shifts in its markets through lifestyle changes, product substitution, and other forces. This is a particularly dangerous position for a firm during times of economic turmoil when changes in strategy (e.g. new products) may be difficult.

Firms in *mature industries* (growing slower than the overall economy or declining) have a different set of problems. Markets may be declining, with surplus capacity leading to thinner margins and intense levels of competition. Here the focus is usually on maintaining market share and increasing margins by reducing costs or eliminating competition through consolidation. The timing horizon is usually longer, with implementation less likely to be imperiled by unforeseen events.

The distribution of market share may prove critical to the planning process. Firms in *fragmented industries*, in which no firm has a significant market share, may wish to adopt a strategy of expanding market share through the acquisition of other firms. Firms in *concentrated industries,* in which one or a few other firms command a significant share, may be stifled in their attempts to increase market share and the best strategic decision may be to leave the industry.

The relationship between the firm and its external environment is important. Firms that are *external dependent*—on customers, suppliers, government, unions, etc.—have fewer strategic options and less flexibility in implementing their strategic plan.

The degree to which new firms can enter the marketplace also may have an impact on the planning process. Firms in industries with *barriers to entry* (e.g. large economies of scale, product differentiation, capital requirements, access to distribution channels, government policy, etc.) may be primarily concerned with maintaining or expanding these barriers. Firms in industries with few barriers may wish to discourage entry through branding, government regulation, etc.

Firm Influencing Factors

A firm's planning environment is influenced to a large extent by its own stage of evolution. New, smaller firms are in an *entrepreneurial mode* in which a few owner/managers make most of the decisions. Medium sized firms are usually in an *adaptive mode* where strategic decisions are more closely linked to the firm's existing strategy (*concentrated growth*). Larger firms with multiple business lines are most apt to be in a *planning mode* where strategic decisions are made through a comprehensive, formal process, which considers totally new initiatives. Larger firms can take more of a *portfolio approach* to planning, viewing each of the firm's business lines as elements in a total portfolio.

Planning may also be affected by the *company culture*—the mix of important assumptions shared by members of the firm; and the *company self-concept*—how the firm thinks about itself. The culture may be explicit or implicit, shaped by the business environment of the firm's industry, the prior experience of employees in other firms, professional relationships, community standards, and the experiences that the employees share in their everyday work environment within the firm.

Strategic Postures

In undertaking strategic planning, firms can adopt different postures regarding what they are trying to achieve from the planning process"

Shape the Future: The posture of the "market maker"— a firm with sufficient market share or resources, which, if successful, can largely dictate the rules of the game. Usually an *early entrant* or *pioneer* in the marketplace.

Adapt to the Future: The posture of the "market taker"— a firm with insufficient market share or resources to dominate a market but who can and will be a significant player.

Reserve the Right to Play: The posture of a *late entrant* that chooses to wait to enter a market until the players and outcomes are better defined but which wishes to keep abreast of key elements of entry (e.g. research, technology, distribution channels, etc.)

Working Assumptions

Strategic planning is based on several key assumptions:

- Strategic direction of business firms is at the heart of wealth creation
- Most firms are in competition
- The selection and implementation of strategic choices will heavily influence the success or failure of firms
- Strategic choices must be integrated, reinforcing one another
- Implementation of the plan must be monitored frequently with results measured against objectives on a continuing basis
- The future is fluid: the plan must be flexible enough to allow shifts in direction if circumstances change

At the heart of the planning process is the selection and integration of strategic choices.

Strategic Choices

What are the "strategic choices" that management[ii] can make through the strategic planning process? The first set of choices relate to the objectives that the firm is trying to achieve:

Selection of Goals: What goals does the company seek to achieve? What is the "mission" of the firm?

Market Positioning: Where is the firm currently? Where should it be to achieve its goals? How does it get there?

There are also choices related to changes in the scope and nature of the firm as a result of repositioning:

> **Selection of Products and Services:** What products/services should the firm offer in order to fulfill its obligations to its customers? How profitable are each of the lines and to what extent do they interact to support the firm's mission and achievement of its goals?
>
> **Level of Scope and Scale:** How large should the firm be to operate efficiently? What are the tradeoffs in reaching this level and how can they be overcome/mitigated?
>
> **Degree of Diversity:** How specialized should the firm be? What is the balance between corporate focus and risk diversification?
>
> **Organizational Structure:** How should the firm be organized to best achieve its goals and fulfill the strategic plan objectives?

Finally, there are questions related to implementation: how will the strategic plan be executed and managed? How will results be measured?

Targets of Strategic Planning

Strategic planning is directed at three major groups:

> **Customers:** Existing and prospective buyers of the firm's products/services as well as other firms in the distribution system (e.g. wholesalers, distributors, retailers, etc.)
>
> **Competitors:** Existing competitors; new entrants; substitute products.
>
> **Suppliers:** Other firms providing raw materials, labor, capital, services, etc.

Potential Successful Outcomes

If successful, the strategic planning process should result in certain *outcomes* for each of the firm's targets:

> **Differentiate Product/Service**: allows the firm to create sufficient differences in its products/services to improve the firm's image and support higher levels of customer loyalty; if successful, allows the firm to achieve higher margins and/or market share.

Capture Efficiencies: improved efficiencies in production, distribution, infrastructure, and capital costs; should result in lower costs and/or higher value to customers.

Innovate/Focus: utilizes greater levels of specialization/technology to secure higher margins, creates higher *switching costs* (customer's costs of changing suppliers) making it more difficult for competitors to enter/expand into the firm's markets.

Exhibit 1 matches successful outcomes with each of the targeted groups.

THE STRATEGIC PLANNING PROCESS

The strategic planning process, in its simplest terms, can be reduced to three fundamental questions:

1) Where are we today? What does the future hold?
2) What position in the marketplace will add the greatest value to the firm's customers, employees, and shareholders?
3) What actions do we take to achieve that position?

Put more simply, where are we now? Where do we want to go? How do we get there? (See Exhibit 2)

Entire professional competencies and theoretical constructs have grown up around answering each of these questions. The subject is too complex to address in detail here, but we can introduce some of the concepts and illustrate how they fit into the strategic planning process. Research activities undertaken in each area are described in the accompanying text boxes. Key words frequently used in the planning process are italicized. (See Exhibit 3)

Current and Future Situation

The first step in the strategic planning process is to assess the current position of the firm. This is not always an easy task since a wide variety of stakeholders—board members, management, employees, shareholders, suppliers, financiers, etc.—may not like the answers that are forthcoming and may use the material to promote personal agendas that may not be in the best interests of the firm. The research process, to be valuable, must be fair, accurate, and, above all, objective in its approach as well as the interpretation and dissemination of its findings.

RESEARCH

Current Business Valuation: Determination of where the firm is today in terms of the market viability and profitability of its core businesses and where the current strategy is expected to take it; usually measured in economic terms through metrics such as market share, profit contribution, EVA, etc. Provides a "baseline" scenario against which alternate scenarios can be measured.

A minimum threshold of success is the ability of a firm to *operate effectively* over the long-term in a highly competitive world. This means providing the customer with better performance by creating greater value or by delivering comparable value at a lower cost

Value Proposition: A critical element in developing operational effectiveness is a thorough understanding of and identification with the increasingly demanding customer. Finding out who the customer really is and isolating their needs, resources, and buying/use preferences is absolutely essential to a successful firm's operation.

Based on this understanding, a firm develops the mix of products and services that it will offer each customer, the prices that it will charge, and the terms by which it will perform its obligations to the customer. This is the *value proposition* that defines the relationship between the firm and its customers.

Core Competencies: In order to fulfill its value proposition, a firm develops certain *competencies* that provide the key to its' operational effectiveness. Hamel and Prahalad define a "competence" as "a bundle of skills and technologies rather than a single discrete skill or technology", representing "the sum of learning across individual skill sets and individual organizational units". [iii] In other words, competency is a standardized way (i.e. methodology) of doing the things that the firm is "good at".

Unfortunately, firms often spend vast sums of management time and money developing competencies that are largely irrelevant to the customer in making "buy" decisions and developing long-term relationships. Part of this mismatch may be due to customers not being aware of their own needs but, more likely, it is the result of firms proceeding to build competencies without fully understanding their role in fulfilling the value proposition.

Therefore, it's important to not just mindlessly build competencies but rather to focus on *core competencies* that are essential to the successful operation of the firm in fulfilling its value proposition with its customers. To be considered a core competence, the bundle of skills must make an important contribution to the value of the firm as perceived by the customer. In other words, it must satisfy the value proposition equation.

Core competency also must be "competitively unique" within the industry, although not necessarily unique to one firm. Finally, a core competency should be "extendable" to new products and services in the future, enhancing its value over time through continued development and use. [iv]

Customer Intimacy: How does a firm determine which competencies should be considered "core" and avoid a customer/competency mismatch? The answer, of course, is to *talk to the customer on an ongoing basis.* As simple as this sounds, it's amazing how many times strategic decisions are made without sufficiently understanding the person or organization making the buy decision and what's important to them. And this does not mean just doing a one-time consumer survey. While research surveys are a critical element, they are by no means the complete answer. What is required is *customer intimacy*—an in-depth understanding of and relationship with those who purchase the firms products and services.

> **RESEARCH**
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> **External Market Analysis:** examination of the *external environment*[v] and the forces that may influence the firm's future operation. General focus on economic trends, social and demographic trends, market growth, *technological substitution*, etc. Specific concentration on establishing the *competitive forces* affecting the firm including existing and potential customers, existing and potential competitors, new market entrants, possible substitute products, suppliers, etc. Involves determining *best practice* standards for industry and how the firm measures up on a *benchmark* basis.
>
> Research techniques may involve *customer surveys, focus groups, Delphi panels, multiple regression analysis, etc.* Forecasting techniques may include *trend extrapolation, product life cycle analysis, sales force estimates, time series models, econometric models, simulation techniques, situational analysis, sustainable growth models*, etc.

In building customer intimacy, the firm must establish a continuing dialogue with its' existing customers and with those it would like to have as customers. The purpose is to clarify known needs, identify unmet needs, and better understand attitudes toward the firm's current service or product offerings.

The first step in this process is to establish *customer knowledge*—who are the customers and what are their requirements? It is also important to know the depth of the customer base and how its size and activity patterns will change in the future. Is it vulnerable to new technology or business patterns? Is it vulnerable to demographic forces or lifestyle change?

In some situations, a firm may have a heterogeneous customer base where certain customers will perceive some but not all of the core competencies that the firm possesses. This forces the firm to segment its markets and focus its efforts on building core competencies that meet the needs of the majority of its customers and/or determining that smaller customer groups will grow sufficiently to support the maintenance of each competency. Without this *market segmentation*, the firm is diluting its efforts by building competencies that are not economically viable.

Establishing and maintaining customer intimacy is a multi-faceted, undertaking involving continuing surveys, in-depth discussions with key customers, continuous debriefing of sales personnel, and attending the customer's professional and trade functions to hear and talk about issues and concerns.

Unfortunately, this is a process that cannot be completely delegated. Senior management must be involved on a personal basis in establishing ongoing relationships with key customers and potential customers. Not only does this demonstrate to the customer that senior management is concerned with their well-being, but it also establishes a leadership model within the organization and eliminates any "noise" that might come from those with a personal stake in the outcome.

Technology can aid in implementing this process. By helping to define and track consumers, technology enables senior managers to gather information from sales force and other personnel that interact with customers in order to monitor attitudes towards the firm and its products/services. It also can help establish customer intimacy on a personal basis by allowing managers to respond more rapidly to problem situations with greater knowledge of the customer and his/her historical relationship with the firm.

Over time, customers' perception of the importance of specific core competencies can change. Competitors may adopt similar bundles of skills and technology to the point where there is a *competency convergence* with no one firm having a strategic advantage. In fact, a core competency may become an industry standard by which all firms are measured. In the customers' eyes, it is <u>expected.</u>

Competition: Defining the nature of the competition is closely related to and intertwined with understanding the customer. Who are the existing competitors and how does the firm compare in the minds and actions of the customer? Who are the likely new competitors and how will they change the competitive environment? How can the firm take industry leadership in defining and establishing new *competitive space* in which it can be dominant?

RESEARCH

Internal Analysis: Establishes the *company profile* describing the quality and quantity of a firm's human, physical, and financial resources. Evaluates strengths and weaknesses of the organization and management structure and company culture. Establishes core competencies of the firm. Compares firm's historical successes with current capabilities in order to determine a firm's future capabilities to execute a major repositioning effort.

Specific concerns are the firm's organizational structure, facilities location, and deployment of capital, technology, and financial/control systems. Attempts to establish the degree to which employee *learning curve* and *experience curve* can be utilized to improve firm productivity.

Research techniques frequently used include *one-off interviews, brainstorming sessions, dialectical inquiry, nominal group techniques,* etc.

Meaningful continuing analysis of the customer and the competition requires establishment of a *benchmarking* process by which data produced from the interview/analytical process can be continuously compared to a standard. This standard may be the average of the competitive universe in order to gain an idea of the firm's general market position. More useful is a determination of who the industry leaders are and what they are doing. Even more enlightening, in many cases, is benchmarking against other industries where processes are more advanced. When complete, benchmarking establishes a set of "*best practices*" against which the activities of the firm can be compared and measured.

The costs of developing and analyzing meaningful benchmark data and best practices can be high. The cost of not doing so, however, means managing in a vacuum, which ultimately may be the most costly decision of all. One thing is clear—the process must be continuous and iterative.

The research process involves a high degree of interaction between the work elements with findings in one area prompting additional research in another. Research should identify the optimal market position for the firm as well as the competitive advantages that it has or can establish. From this process, an understanding of a series of alternative courses of action begins to emerge.

Strategy Formulation

The next step is to begin consolidating courses of action into alternate strategies. This *strategic issue analysis* contrasts the company profile with its external environment to identify a range of possible strategic alternatives. Particular attention should be given to *critical success factors* reflecting areas in which high performance by the firm can result in an improved *competitive position*. Strategic alternatives are then screened against the firm's mission statement to determine courses of action that are consistent with the firm's overall goals and objectives.

Externally Focused Strategies: Strategic alternatives can be either externally or internally focused. Alternatives associated with external growth are generally directed at moving the firm to a more optimal competitive position, with a focus on revenue enhancement. This might include actions such as introducing new products/services, differentiating existing products/services, improving product distribution systems (*outbound logistics*), divesting existing operating units, acquiring new operating units, etc. Since competitive marketplaces are seldom calm, the analysis should also consider *competitive reaction* to alternative strategic initiatives.

Often a growth strategy involves a choice between integrating horizontally or vertically. *Horizontal integration* expands the firm through acquisition or internal growth without significantly changing its stage in the production/marketing processes. This strategy is utilized to enter new geographical markets or eliminate competition in existing markets. *Vertical integration*, on the other hand, involves adding functions forward or backward in the production/marketing process. *Forward integration*, a form of vertical integration, such as acquiring a distributor, could move the firm closer to the customer, thereby improving market share and potentially reducing costs to the point of sale.

Internally Focused Strategies: Internally focused growth strategies are usually associated with improving internal operations by lowering production costs, improving procurement policies (*inbound logistics*), or improving the firm's overall work environment. This may involve reorganizing the structure of the firm, re-engineering the way the firm undertakes certain activities, outsourcing non-core functions, re-capitalizing the balance sheet, etc. It may also involve external actions such as a merger or acquisition of another firm. *Backward integration*, such as acquiring a supplier, could reduce costs to the consumer and/or improve product/service quality.

Growth strategies may also reflect the presence or absence of synergies between consolidating firms. *Concentric diversification* reflects a strategy of acquiring firms which are similar to and synergistic with the acquiring firm in terms of markets, products, or technology. *Conglomerate diversification* is a strategy of acquiring firms for investment purposes with little or no anticipated synergy with the acquired firm.

Highly specialized firms are faced with the decision of whether to diversify or focus their operations even more. Diversification usually reduces the risk of a business being affected by a major adverse event (e.g. product replacement, market area deterioration, loss of key executives, etc.) but it may also lead to a decline in the firm's major business activity. Given this choice, firms may decide it is better to harden the silo by developing a *defensible niche* in which margins improve and future competitive entry is made more difficult.

For large firms, a *grand strategy* evolves which rationalizes and guides a series of *functional strategies* for each business unit with broader company objectives. This is an iterative process with corporate planning concerned with top-down strategic issues and business unit managers working with bottom-up, operating issues.

In most cases, strategic change is going to involve some change in the organization. This may range from fine tuning an already smoothly-functioning organization to radical re-structuring of all aspects of the firm's operation. The critical factor is that the organizational format is consistent with and supportive of the strategic objectives of the plan.

Dealing with Resource Constraints: The evaluation of strategic alternatives allows management to reject certain alternatives as being unfeasible or not of economic value to the firm, focusing on a final range of alternatives for consideration. The process of dropping alternatives, while important, must be undertaken with some caution. Too often, strategic planning focuses on what a firm *can't do* rather than what it *must do* to gain a competitive advantage. It is certainly necessary to consider existing resources, particularly core competencies, but they should be viewed as a foundation, not a limitation. When a manager says, "Let's be realistic," it usually means that the full range of *stretch thinking* essential to creative strategic planning has not been achieved. If it's the boss who says it, the firm's in trouble!

Effective strategic planning first establishes what the firm must do to establish competitive advantage and then concerns itself with the resources required to achieve the goal. It may turn out that the firm will, in fact, be limited by its resources but this assumption should be put to the most rigorous test imaginable because well managed, creative firms have usually been able to come up with the necessary resources, once they knew what was required.

Valuation of Strategic Alternatives

As alternative strategies emerge, it is important to test them quantitatively against the baseline standards established during the Current Business Evaluation research. This testing may utilize *activity ratios* such as asset turnover, sales to fixed assets, return on assets (ROA), return on investment (ROI), and Economic Value Added © (EVA). Each alternative should improve shareholder value and/or reduce downside risk when compared to the current strategic plan. If it does not, it should be rejected or modified to produce improved value. In some cases, a strategic alternative may have non-quantifiable characteristics that allow it to continue to be considered, but the costs of doing so must be fully understood.

As previously noted, strategic positioning means performing different activities than the competition or performing the same activities in a different way, requiring that strategic tradeoffs be made. Selecting between trade-off alternatives will limit what a company can do, because <u>no firm can be all things to all people</u>. This increases risk because the selected alternative may turn out to be wrong and, once discovered, it might be too late to go back and take a different route. But making the "right" strategic decision(s) is what good management and industry leadership is all about and, if correct, can distance the firm from its competitors and insure successful corporate growth and long-term profitability. The right decisions don't have to be optimal—they just have to be better than the competitor's decisions.

Formulation of the Strategic Plan

Once each of the strategic alternatives has been tested, management can begin the process of selecting desirable alternatives and formulating the final strategic plan. The plan should first state the *company goals* that it expects to attain through implementation of the strategic plan. Next, these goals should be translated into *company objectives*, projected over a multi-year period. This should include measurable objectives such as improvement in market share, profitability, return on investment, technology leadership, productivity improvements, employee relations, public responsibility, etc. In the early years, goal measurement should be tied to specific accomplishments in specific time periods (*annual goals*). Finally, *company policies* should be formulated reflecting broad guidelines which will influence the thinking, decisions, and actions of managers and subordinates as the plan is implemented.

There are several possible strategies for a firm to consider:

Elimination of Non-Core Activities: In order to force management to focus on establishing and maintaining core competencies, the plan can identify and reduce/eliminate non-core activities by divesting or outsourcing them to other organizations. It's tough enough for management to make critical decisions on the things that really matter without having to concentrate resources on those that are important but not essential. In many cases, management discovers that the non-core activities weren't needed in the first place or can be performed better and less expensively by others.

Maintaining/Reorienting Core Competencies: Dealing with customers' changing perception of core competencies requires continuing strategic planning and out-of-the-box thinking on the part of senior management. Given the high volatility of most markets and the rapid rate of industry change, maintenance and improvement of core competencies can be almost as difficult as establishing them in the first place.

Part of having an open mindset is being able to deal with changing reality—hard facts about customers, the effectiveness of the products and services the firm is offering, and the strength and nature of the competition.

Establishing and/or Enhancing Competitive Advantage: Once a firm is operating effectively, the next and most crucial step is to differentiate itself by adding value through products and services that give it a *strategic advantage* over the competition.[vi] A firm's long term profitability will depend, in large measure, upon the degree to which this strategic positioning can be achieved and sustained over time.

As opposed to operational effectiveness--performing the same task better, faster, or cheaper than the competition—competitive advantage means performing different activities than the competition or performing the same activities in a different way. This often requires that strategic tradeoffs be made, such as between greater value and lower cost, products offered, and customers served. Making these choices requires a high degree of personal and organizational discipline and integrity, clear lines of communication, and a willingness to say "no".[vii]

Firms may establish competitive advantage in a highly focused "niche" or across a broad range of products and services, depending upon size, resources, established market position, and level of operating effectiveness.

Weak competitive advantages result in contestable positions whether the scope of the advantage is narrow or broad. For firms attempting a broad reach, moderate competitive advantages will allow the firm to participate in rivalry with other major firms but not establish clear-cut industry domination. Niche firms with a moderate level of competitive advantage will be able to participate in one-off matches with other firms of comparable advantage. <u>It is only strong, sustainable competitive advantages that will lead to defensible niches or, for the firm with broad scope, industry domination.</u>

Competitive advantage can be established independent of the firm's core competencies, built on these competencies, or forged by creating an entirely new strategic initiative.

Independent of Core Competency: Some companies may gain strategic competitive advantage *without* developing core competencies through legal control of monopolies (e.g. patents, zoning); a market position as a result of a relationship with another firm (e.g. franchise; licensing agreement); or an inherited image from years of market share dominance (e.g. strong historical brand identity).

Building on Existing Core Competencies: More commonly, and of much more importance to most firms, is utilizing existing core competencies to build strategic competitive advantage.

Judging the sustainability of competitive advantages arising out of core competencies is not easy. As previously noted, customer perceptions of what is expected from firms can change over time. Competitors also may improve their core competencies to the point where there is little differentiation between firms.

It's generally a good idea to assume that, in today's highly competitive world, most strategic advantages arising from existing core competencies will not be sustainable over extended periods of time unless they are redirected or combined with an entirely new strategic initiative. Michael Porter, as an example, notes that operational effectiveness is necessary but is *not* strategy.

Porter argues that a firm can "outperform rivals only if it can establish a difference that it can preserve."[viii] (See Exhibit 4)

Establishing New Initiatives: Due to the time required to develop a competitive advantage, the rate of change in most industries, and corresponding competitor moves, it is often necessary to *leapfrog* the existing competitive environment. This may help to establish entirely new competitive space in which the firm is not only a leader but establishes most, if not all, of the standards by which all firms will be measured.

As previously noted, leapfrogging the competition requires a stretch in not only thinking about the future in terms of customer preferences but also in terms of the firm's resources. In essence, new initiatives require the firm to say "If we started from scratch, what would we do?" rather than be constrained by available resources. (See Exhibit 5)

Assets and Infrastructure

Each strategic alternative carries with it certain asset and infrastructure requirements. In some cases, the decision will be to reduce or eliminate assets and/or infrastructure, such as in the sale/leasing of real estate or outsourcing non-core competencies of the firm. More likely, new resources will be required to implement an alternative, as in the addition of plants, employees, and/or new technology.

Implementation

To be successful, a strategic plan must become an integral part of a firm's daily operations and culture. This is often the most difficult part of the strategic management process.

Institutionalization: Translating the plan into short-term action guidelines for all employees is one of the most difficult challenges facing management and it is not surprising this is where many strategic plans fail. The process requires the integration of a firm's structure, culture, leadership, and employee reward system. The seeds for success or failure may be sown in the planning process itself. A plan that is based on extensive management participation is more apt to receive the *buy-in* necessary for successful implementation.

Organization: Creating an organizational structure to support a strategic plan is a formidable problem. While firms may formulate a resourceful plan for their future, there is no single model for developing an organizational structure to successfully achieve the objectives of the plan. In many cases, the plan is forced onto an existing organizational structure, which may or may not be appropriate.

For many years American business primarily relied on *functional* organizational structures. The functional structure stresses improving productivity by encouraging specialization by functions (e.g. marketing, production, financial reporting, etc.). This structure can pose significant problems, however, which become even more apparent in a highly competitive environment.

By focusing internally, the customer is given less attention and numerous layers of costly middle management are created, increasing overhead and requiring higher levels of revenue to breakeven. It is also extremely difficult to establish responsibility for the success or failure of specific products or service lines.

As a result, several alternative organizational structures have begun to emerge. The *matrix* structure delegates power to independent operating units which then rely on centralized corporate facilities for functional support. Another approach is the *flat* corporation in which many middle management functions are eliminated. While this may reduce overhead and allow for more rapid decision making, information and communications are still largely centralized. (See Exhibit 6)

More recently, some firms have experimented with other forms of organization which are even less hierarchical in structure. Utilizing a *networked* structure, a firm is divided into units which operate independently of each other but within a framework which is consistent with broader corporate goals and objectives. Data and information is widely shared, largely through a telecommunication system linking all of the units to each other and to the corporate support group.

Unfortunately, the networked approach offers little opportunity to capture the benefits of economic scale and may lead to considerable duplication. It tends to work best in situations where local presence is critical and yet national information flow is needed to support local operations.

With a *virtual* organization, the firm performs internally only its core competencies (perhaps just marketing), while outsourcing all other activities (perhaps all production). Similar to the networked firm, heavy reliance is placed on a state-of-the-art telecommunication system linking individual units. The virtual organization also operates within an overall corporate strategic support structure although there may be no formal corporate "headquarters". This organizational structure is helpful in situations where being "small" assists in building customer intimacy, yet rapid access to other resources is required to perform larger tasks.

Some firms are also linking together a series of *work teams,* each dedicated to developing and marketing one or more new products and services. Members of each team can be internal or external to the firm, but who possess the necessary complementary skills to bring the new idea to market or determine that it is infeasible to do so. The life of any work team varies, depending upon the complexity of the task and the degree of market success. The work team approach represents the most focused attack on aligning work skills and motivation with customer requirements. The bad news is that this approach may require periodic, often wrenching, shifts in the organization and also be quite costly as a result of resource duplication.

Each of these approaches to organizing the work effort has its advantages and drawbacks. Firms will have to experiment with various mixes and blends until the right combination is discovered that works for their markets, core competencies, and company culture. The most important concern is that the organizational approach follows and is complementary with the strategic goals that the firm has set. Dropping a new strategic initiative on an inappropriate structure is doomed to fail from the start.

Transition: A key element in making a final determination regarding strategic direction is the way in which the firm chooses to grow or *migrate* to its desired market position. Usually, there are three choices:

Grow Internally: Most firms rely on internal resources to implement their strategic plan. This technique works well for firms that already have strong market share and significant resources. The advantage is that this approach is less disruptive to the firm's internal organization and, as a result, may be more lasting as it is implemented. Disadvantages include the wrong person is placed in a critical role, possible delay in implementation, and the possibility that insufficient organizational change will be achieved.

Consolidate with Another Firm: While getting bigger through consolidation is not an end in itself, mergers and acquisitions *do* have a place if they are well thought-out and accomplish one or more key objectives of a broader strategic plan focused on attaining competitive advantage. In fact, when the dust settles, it may be that the merged firm is not significantly larger than before, but better positioned to serve its customer base.

Key objectives may vary, depending upon the strategic plan. One goal may be to gain access to geographical markets not presently served. Another may be to add one or more product/service lines that will enhance the firm's value proposition with the firm's existing customer base. Still another may be to seek additional customers, spreading the same service/product mix over a larger base. In some cases, firms consolidate in order to obtain/enhance a strong management team.

Not all mergers are successful, particularly transactions involving weak firms. Without the resources to be an acquiring firm, the weak firm is truly adrift on the competitive seas. If it does nothing, it runs the risk of being scooped up by another firm and effectively dismantled for its remaining asset value. Needless to say, not too many managers are interested in this outcome so they often seek another weak firm as a merger partner, where management prerogatives can be preserved, at least temporarily. Usually, the result is simply a larger weak firm, perhaps with more problems than the firms had previously.

Partner with Another Firm: *Strategic alliances* between firms (*partnering)* is gaining momentum as firms seek to achieve strategic objectives without surrendering (or, in some cases, even sharing) operating control.

Partnering can take many forms. Firms may wish to expand into geographical markets or product/service lines where a single firm is dominant but doesn't wish to consolidate. Two or more firms may wish to enter a new, uncharted market in which no one firm has the necessary resources to be successful. Desiring to round out a product/service mix, a large firm may want to enter a highly specialized market where only small, boutique firms can operate successfully.

To be successful, alliances must achieve an important strategic objective for both (all) firms. In some cases, the objectives may be different, but complementary. It's important to clearly lay out in writing the goals of both firms and how the alliance will further these objectives. The plan should also establish how the alliance will operate on a day-to-day basis, including a clear indication of management responsibilities and financial arrangements.

Although usually underestimated, successful alliances require a lot of management involvement. It is generally a sound idea for each (all) of the firms to dedicate (or hire) a senior management person to be responsible for the alliance's activities. These individuals must be able to work together if the alliance is to succeed. Progress should be measured on a periodic basis, including benchmarking data similar to what management receives from their internal operations. Customer response to alliances may be negative and require a change in direction or termination.

It should be noted that a broad-based strategy might involve more than one implementation technique.

Monitoring

An on-going *control and evaluation system* is important in assessing the success of the repositioning effort and to establish a change in direction, if required. *Milestone reviews* are established on the basis of time, critical events, or the use of predetermined amount of resources. Properly defined goals and performance measures, such as the *balanced scorecard* approach, can keep management apprised of the strategy's success or failure in an ongoing manner.

Maintaining Flexibility

In an increasingly complex and rapidly changing business environment, it is critical that the strategic plan be continually reviewed in terms of its continuing relevance. A *premise control system* systematically determines if the premises on which a strategy is based are still valid. *Contingency plans* can be developed to become activated if certain *trigger points* are reached (e.g. a competitor takes a predicted action). During both planning and implementation, g*ame theory* can be useful in predicting the impact of certain changes on major premises and in making changes to the strategy as new information becomes available (e.g. a competitor's response to your actions).

SUMMARY

To summarize, operating effectiveness is having the requisite skills necessary to provide a successful value proposition to its customers.

The successful firm's approach to providing this value to customers and improving it over time is to develop and maintain a number of core competencies, each representing a bundle of skills and technology which transcend any one product or service, and in fact, provide a platform for launching successful new products and services.

Generally, the goal is to produce this invaluable product/service as efficiently as possible. In order to maintain and expand their core competencies, successful companies will continually benchmark their performance against that of the competition and perform to best practice levels for their industry. In order to concentrate firm resources on establishing and maintaining core competencies, non-core activities should be eliminated or outsourced to others.

In today's highly competitive world, achieving operating effectiveness is equivalent to putting up the "table stakes" necessary to stay in the game. In fact, as more firms build core competencies, the competitive advantage enjoyed by early pioneers in an industry may largely evaporate.

To achieve the "winning hand" of long-term profitability, a firm must establish sustainable competitive advantage. Competitive advantage may be based on an extension and redirection of existing core competencies or created entirely from whole cloth, based on a reading of future trends and customer preferences. Selecting between strategic alternatives requires an assessment of the assets and infrastructure required to implement the alternative and may involve trade-offs between objectives as well as pose substantial risk to the firm.

A key consideration in the ultimate success of any strategic plan is implementation. The first, and often most critical, implementation issue is the form of the organizational structure that the firm will utilize and its compatibility with the strategic plan. Transition plans are also important, involving consideration of a variety of techniques including internal growth, consolidation, and/or partnering with other firms. Implementation must also involve some form of continual monitoring to determine to what extent the repositioning effort is succeeding and, if not, whether a change in direction would be desirable. Above all, the implementation process must be flexible and responsive to changes in major premises upon which the plan is based.

While by no means perfect, strategic plans may be the best (and perhaps only) approach to reaching a firm's growth objectives and, in some cases, its economic survival.

Endnotes

[ii] For the purposes of discussion, "management" is defined as including the Board of Directors, the Chief Executive Officer, and the members of senior management (e.g. CFO, COO, Director of Strategic Planning, and heads of the major operating units).
[iii] Gary Hamel & C.K. Prahalad *Competing for the Future*, Harvard Business School Press, 1994
[iv] Hamel & Prahalad, *ibid*.
[v] Also called *competitive environment* and *operating environment*.
[vi] In *de nova* situations, establishing a strategy for gaining competitive advantage precedes building core competencies.
[vii] Michael E. Porter, *What is Strategy*?, Harvard Business Review, November-December, 1996
[viii] Porter, *ibid.*