Chapter 1

The strategy process

Chapter learning objectives:

Lead	Component	Indicative syllabus content
A.1 Explain the purpose of strategy.	(a) Define strategy (b) Explain the purpose of strategy	• Different definitions of strategy • Essential features and characteristics of strategy
A.2 Discuss the types and levels strategy.	Discuss (a) Types of strategy (b) Levels of strategy	• Intended and emergent strategy • Corporate, business and functional strategies
A.3 Outline the strategy process.	(a) Outline the rational and emergent processes of arriving at strategy.	• Analysis of organisational ecosystem • • Generating options • • Strategic choice • • Strategic control

1. What is ecosystem

> An organisation's **ecosystem** is made up of a network of organisations involved in the delivery of a product or service. This includes customers, suppliers, distributors, competitors, government agencies etc.

- The interaction within the ecosystem can be via cooperation or via competition.
- The idea is that all components of an ecosystem impact on each other, creating a relationship that is constantly evolving and within which each organisation must be flexible and adaptable to survive.
- The concept of a business ecosystem is thought to help organisations consider how to succeed in an environment which is changing constantly and at great speed.

2. What is strategy

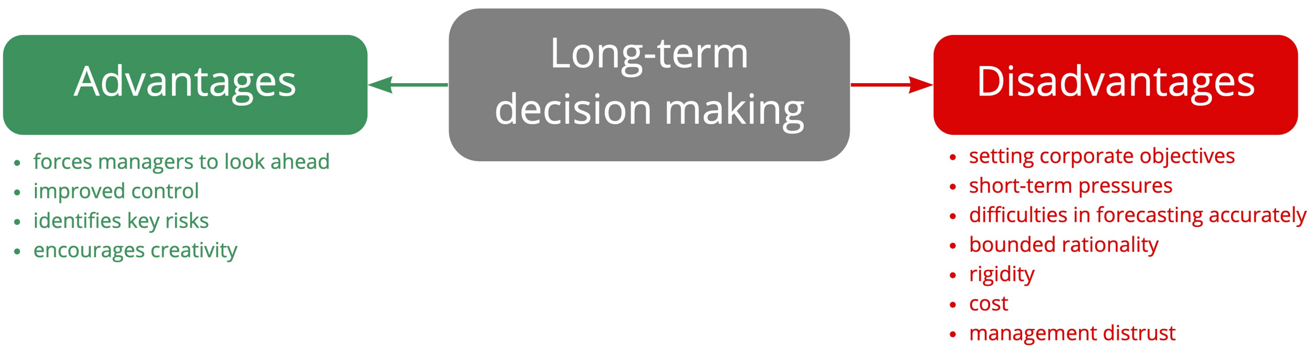
> A course of action, including the specification of resources required, to achieve a specific objective. - ***CIMA***

> Strategy is the direction and scope of an organisation over the long term, which achieves advantage for the organisation through its configuration of resources within a changing environment, to meet the needs for markets and to fulfill stakeholders' expectations. - ***Johnson, Scholes and Whittington (Exploring Corporate Strategy)***

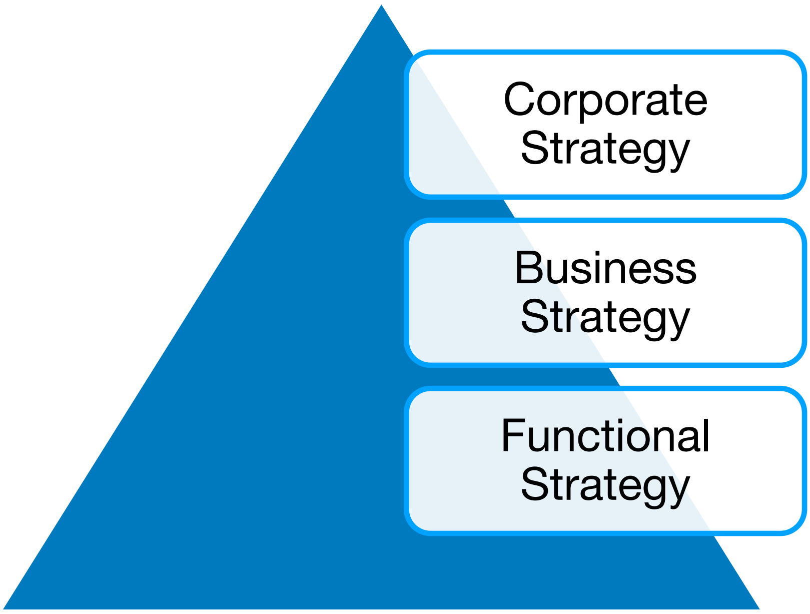
The characteristics of strategic decisions:

Johns, Scholes and Whittington defined the following characteristics of strategic decisions:

- Strategic decisions are likely to be affected by the scope of an organisation's activities.
- Strategy involves the matching of the activities of an organisation to its environment.
- Strategies need to be considered in terms of the extent to which resources can be obtained, allocated and controlled to develop a strategy for the future.
- Operational decisions will be affected by the strategic decisions.
- Strategic decisions are apt to affect the long-term direction of the organisation.



3. Levels of strategy



Corporate or strategic level (which)

- It raises the question of which businesses and markets should we be in?
- It involves considering acquisition and diversification and will see an organisation being in more than one business.
- Corporate Strategy is concerned with:
- Entering new industries
- Leaving new industries

Business or management level (how)

- Once selected the market, the organisation must develop a plan to be successful in the market.
- The aim is to compete successfully in the individual markets that the company chooses to operate in.
- Business strategy is concerned with:
- Achieving advantage over competitors.
- Avoiding competitive advantage.

Corporate strategy affects the organisation as a whole while business strategy will focus upon Strategic Business Units (SBUs).

A SBU will be a unit within an organisation for which there is an external market for products distinct from other units.

Functional or operational level (day-to-day)

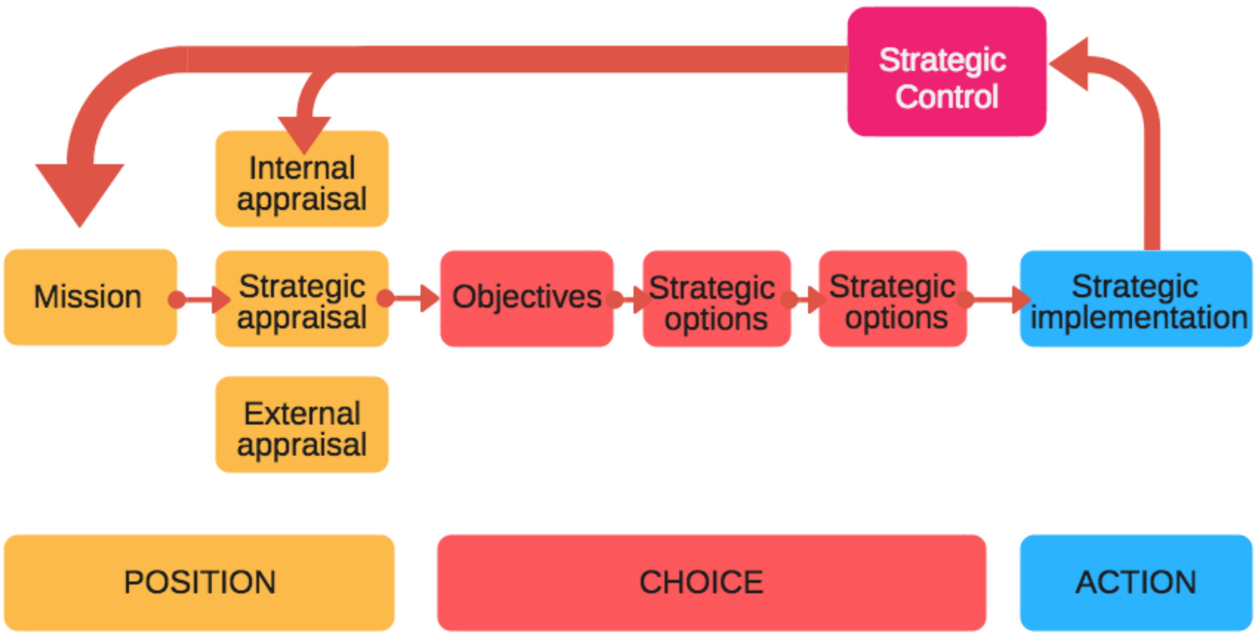
It is concerned with:

- Human resource strategy
- Marketing strategy
- Information systems and technology strategy
- Operations strategy

4. The strategic planning process

RATIONAL MODEL:

- It is a logical step-by-step approach.
- It requires organisation to analyse its existing circumstances.
- It requires the organisation to generate possible strategies.



Johnson, Scholes and Whittington Model:

They took the stages from the rational model and grouped them into three main stages:

1

STRATEGIC ANALYSIS

- External analysis to identify opportunities and threats
- Internal analysis to identify strengths and weaknesses
- Stakeholders analysis to identify key objectives and to assess power and interests of different groups
- GAP analysis to identify the difference between desired and expected performance

2

STRATEGIC CHOICE

- Required to close the gap
- Competitive strategy for each business unit
- Directions for growth
- Whether expansion should be achieved by organic growth/ acquisition or some form of joint arrangement

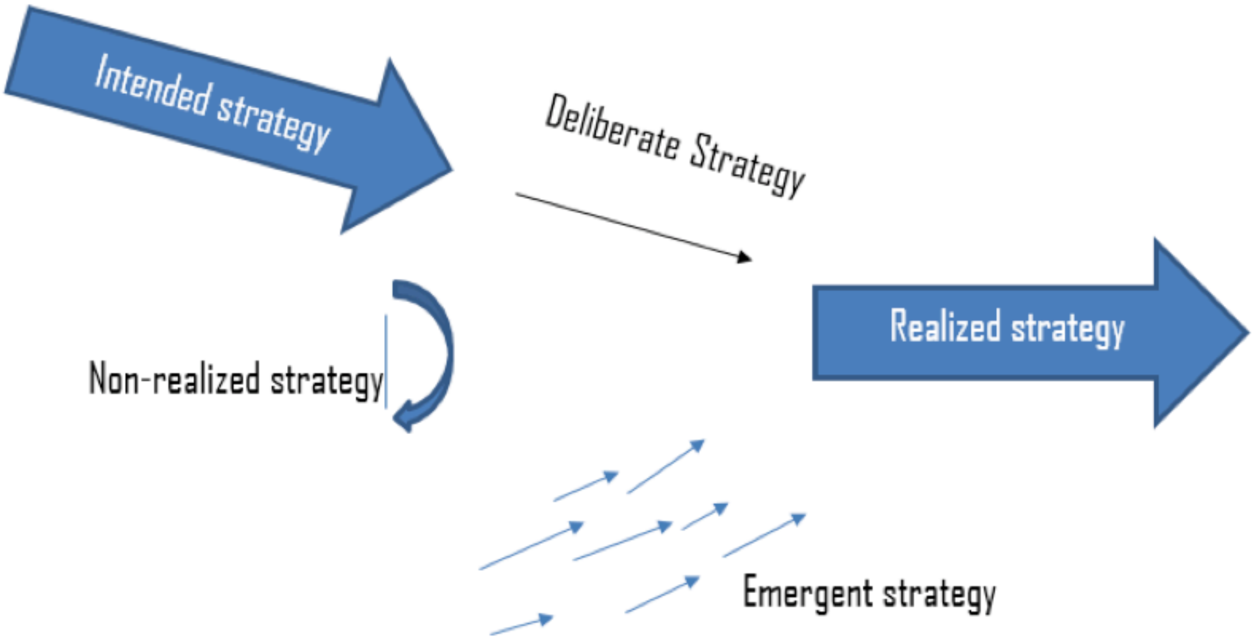
3

STRATEGIC IMPLEMENTATION

- Formulation of detailed plan and budget
- Target setting for KPIs
- Monitoring and control

EMERGENT APPROACH (MITZBERG)

- Rational model quickly becomes outdated.
- Strategy tends to evolve rather than results from a logical, formal process.
- An emergent approach is evolving, continuous and incremental.



LESS FORMAL APPROACHES TO STRATEGY:

Incrementalism (Lindblom)

- Strategic managers do not evaluate all the possible options open to them but choose between relatively few alternatives.
- It does not normally involve an autonomous strategic planning team that impartially sifts alternatives options before choosing the best.
- Strategy-making tends to involve small scale extensions of past policy.

Freewheeling opportunism

- Freewheeling opportunists do not like planning.
- They prefer to see and take opportunities as they arise.
- It is probable that the approach is adopted more for psychological reasons.
- Some people simply do not like planning.

Problems with lack of formal planning

- Failure to identify risks.
- The organization may not have an overall plan for future.
- Difficulty in raising finance.
- High level management skills are required.

The three Es approach of Audit Commission

- **Effectiveness** – looks at the output.
- **Efficiency** – looks at the link between outputs and inputs.
- **Economy** – looks solely at the level of inputs.

5. Perspectives to strategic planning

A traditional approach – stakeholders:

- It starts by looking at the shareholders and their objectives.
- The emphasize is on formulating plans to achieve these objectives.
- This approach is flawed because the objectives are set in isolation from market consideration and are unrealistic.
- This approach is useful for not-for-profit organizations, where a discussion of mission and objectives is a key.

A market-led or positioning approach:

- It starts with an analysis of markets and competitors' actions before objectives are set and strategies developed.
- The essence of strategic planning is to ensure that the firm has a good fit with its environment.
- The idea is to be able to predict the changes sufficiently far in advance to control change rather than always have to react to it.
- The main problem with this approach lies in predicting the future, since some markets are so volatile that it is impossible to estimate to further ahead than the immediate short term.

A resource-based or competence led approach:

- Many firms who have found anticipating the environment to be difficult have switched to a competence or resource-based approach, where the emphasis of a strategy is to look at what the firm is good at – its core competences.
- Ideally these correlate to the areas that the firm has to be good at in the order to succeed in its chosen markets.

6. The role of the management accountant

> Strategic management accounting is a form of management accounting in which emphasis is placed on information which relates to the factors external to the entity, as well as non-financial information and internally generated information. - ***CIMA Official Terminology***

This indicates some key differences between the strategic and traditional management accountants.

External focus:

Traditional management accountants tend to focus on internal company issues; this is because their role is:

- To aid in the creation of operational strategies for the business
- To safeguard company assets
- To measure and report both financial and non-financial performance to the managers
- To ensure efficient use of assets and resources

Forward looking:

- A large part of a traditional management accountant's role is to do with the measurement of historic performance of a business and its division.
- Strategic management accountants need to be more forward-looking.

Information provided by strategic management accountants:

- Competitors' analysis.
- Customer profitability.
- Pricing decision.
- Portfolio analysis.
- Corporate decision support.

Value for strategic management information:

- More effective strategic planning.
- Increased awareness of the business and its environment.
- Increased control over business performance.
- Better decision-making.

8. Chapter summary