

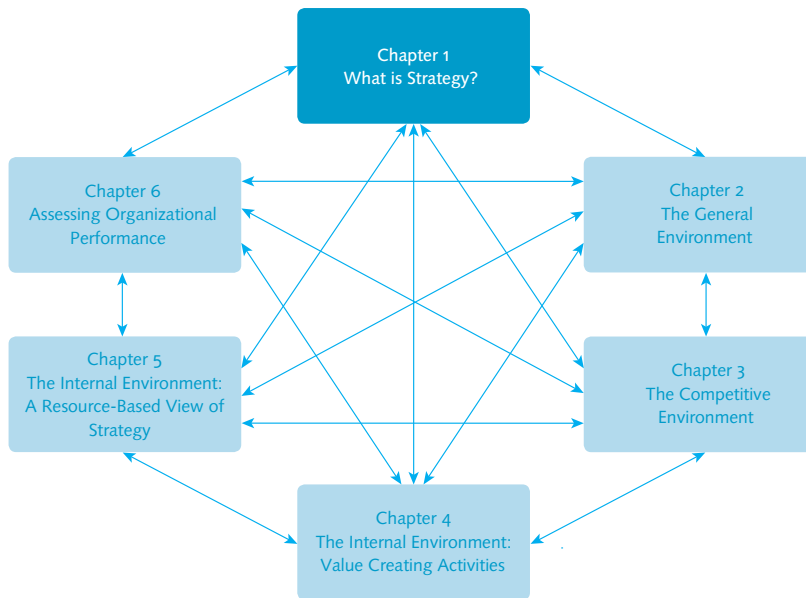
PART 1

What is Strategy?

1 What is Strategy?



1 What is Strategy?



Learning Objectives

After completing this chapter you should be able to:

- Explain what is meant by strategy
- Describe a strategic management process
- Discuss the role of values, vision, and mission statements
- Explain what is meant by a theory of business
- Evaluate different perspectives on strategy formulation
- Explain the linkages between an organization's strategy and its external and internal environment



1.1 Introduction

What is strategy? How is strategy formulated and implemented? Are values important in determining which markets organizations seek to compete in? These are some of the questions that will be discussed in this first chapter. We start the chapter with a discussion of what strategy is. There is general agreement that the purpose of strategy is to help organizations achieve a sustainable competitive advantage. Where this consensus begins to break down is when we discuss *how* this should be achieved. We can identify two broad perspectives that we can call the *rationalist* or *positioning* approach, and the *resource-based view* of strategy. Each of these perspectives will be evaluated in greater detail in subsequent chapters. For now, we will simply introduce these perspectives and some of their chief protagonists when we address different approaches to strategy formulation.

This chapter also looks at a strategic management process which includes strategy analysis, formulation, and implementation. We note that this essentially linear framework is very useful for exposition but has limitations when seeking to explain strategy in practice. The role of an organization's values, vision, and mission is explained as we discuss their importance in setting strategic goals, and the role of strategy in achieving these goals. We address an organization's assumptions about its competitive environment or its theory of business and discuss how this can lead to organizational failure. We end the chapter with a discussion of a strategic management framework which will be useful for navigating subsequent chapters.

- Section 1.2 explains what strategy is and discusses some of its military antecedents.
- Section 1.3 deals with the strategic management process which explains strategy analysis, strategy formulation, and strategy implementation.
- In Section 1.4 we discuss the impact of an organization's values, vision, and mission in guiding decision making and employees' behaviour. A theory of business is also discussed.
- Section 1.5 briefly discusses different types of strategy. These include corporate strategy, business strategy, and functional strategy
- In Section 1.6 we look at the different approaches to strategic management and the changes that have taken place
- Section 1.7 evaluates two different perspectives on strategy formulation: the positioning or design school, and the learning school.

- The chapter concludes with a strategic management framework which explains the linkages between an organization's internal and external environment, its strategy, and its stakeholders.

1.2 What is Strategy?

The use of strategy has existed for many centuries although its use in management has a more recent history, dating back about 40 years. Strategy was borne out of military conflicts and the use of a superior strategy enabled one warring party to defeat another. Von Clausewitz, writing in the nineteenth century, states that the decision to wage war ought to be *rational*, that is, based on estimates of what can be gained and the costs incurred by the war (von Clausewitz 1982). War should also be *instrumental*, that is, waged to achieve some specific goal, never for its own sake, and that strategy should be directed to achieve one end, in this case, victory. While policy makers may be unsure about what they expect from modern military engagements, military personnel from commanders down to foot soldier all know to ask one question: what is our objective in committing to a particular course of action? If the goal or objective is unclear they can expect the formulation of strategy to be disjointed and its implementation to be unsuccessful.

In *The Art of War*, the Chinese philosopher and insightful military strategist Sun Tzu wrote:

the one who figures on victory at headquarters before even doing battle is the one who has the most strategic factors on his side. The one who figures on inability to prevail at headquarters before doing battle is the one with the least strategic factors on his side . . . Observing the matter in this way, I can see who will win and who will lose. (see Hawkins and Rajagopal 2005)

We need to exercise caution in drawing military analogies. Unlike military conflicts where might, power, and strength of numbers often determine the outcome, strategy is more subtle. As Sun Tzu notes, battles are often won in the mind long before enemy forces engage. In the modern business arena organizations are increasingly aware of the benefits of cooperation as well as competition.

There is agreement that the role of strategy is to achieve *competitive advantage* for an organization. Competitive advantage may usefully be thought of as that which allows an organization to meet consumers' needs better than its rivals. Its source may derive from a number of factors including its products or services, its culture, its technological know-how, and its processes. To be sustainable, however, the competitive advantage must be difficult for competitors to imitate. As Henderson (1989) astutely

points out, 'Your most dangerous competitors are those that are most like you. The difference between you and your competitors are the basis of your advantage'.

The use of strategy in decision-making is the primary way in which managers take account of a constantly changing external environment. An effective strategy allows them to use their organization's resources and capabilities to exploit opportunities and limit threats in the external environment. A debate arises when we try to pin down *what is strategy* and, importantly, *how is strategy formulated*? This discussion has continued unabated for decades and is rooted in a desire for managers to undertake better strategic thinking and therefore better strategic decisions.

Strategy can be defined in a number of different ways. We should be aware that any definition is likely to be rooted within the different perspectives adopted by its authors. For this reason a definition of strategy, which is accepted by everyone, is not as straightforward as might first appear. As individuals we all devise strategies to help us achieve certain goals or objectives. For instance, consider a couple on a long journey with two young children under five in the back of the car. Do they set off early because this will beat the traffic congestions and make sense because the toddlers rise early? Or do they leave in the evening at the children's bedtime when they will hopefully sleep for the entire journey, giving mum and dad a much-needed break! Do they take the main roads in the hope of cutting the journey time but with the downside of congestion, or take less travelled roads which avoid traffic jams but may take longer? What this emphasizes is that strategy is all about choice. At the organizational level the choices are far more complex.

In an article entitled 'What is strategy?', Porter (1996) asserts that 'competitive strategy is about being different. It means deliberately choosing a different set of activities to deliver a unique mix of value'. Markides (1999a) argues that the essence of strategy is for an organization to select one strategic position that it can claim as its own. A strategic position represents a company's answers to the following questions.

- *Who* should the company target as customers?
- *What* products or services should the company offer the targeted customers?
- *How* can the company do this efficiently?

In this way a company can achieve success by choosing a strategic position which differs from the competitors in its industry. Kay (1993) sees the strategy of an organization as '... the match between its internal capabilities and its external relationships', i.e. the match between what an organization is particularly capable of doing and its relationships with its stakeholders: employees, customers, shareholders, and suppliers. Strategy is about the firm using analytical techniques to help it understand, and therefore influence, its position in the market.

The organization is faced with a constantly changing external environment and needs to ensure that its own internal resources and capabilities are more than sufficient to meet the needs of the external environment. Organizations do not exist simply to survive in the marketplace but want to grow and prosper in a competitive environment. In order to make sense of what is going on around them, firms must undertake an analysis of their external and internal environment.

An organization's external environment comprises the general environment and the competitive environment. The general or macro-environment consists of factors which may not have an immediate impact on the firm but has the capacity to change the industry in which the firm competes and even create new industries. The competitive environment deals with the industry in which the firm competes. For an organization to prosper it needs to achieve a competitive advantage over its competitors in the industry. Changes within an organization's competitive environment, such as an increase in the number of competitors, will have a far more immediate impact on the organization. The tools of analysis for analysing the external environments are considered in detail in **Chapters 2** and **3**. In contrast, the internal environment of the organization deals with the organization itself. It includes its values, goals, resources and capabilities, and internal structure. The values that the firm embodies will guide its choice and implementation of strategic goals, and how it deals with crises (see Strategy Focus on Johnson & Johnson). We will consider some tools of analysis for analysing the internal environment of the organization in **Chapters 4** and **5**. For a discussion of strategy and its interdependent elements, see Case Study: What is Strategy?



CASE STUDY 1.1

What is Strategy?

Strategy is, very simply, an outline of how a business intends to achieve its goals. The goals are the objective; the strategy sets out the route to that objective. In the early stages, business objectives are usually fairly simple: to survive, and to achieve growth targets. Strategies are correspondingly simple as well, and are often not even committed to paper; it is enough that everyone in the company understands where it is going and how it will get there. But as the business grows, so does the need for coordination. Accordingly, there is a need for a mutually agreed and accepted strategy for the business.

Some theorists, such as Alfred Chandler, the business historian, would say that this is the wrong way to go about it. A strategy should be developed first, and then the organization tailored to meet the requirements of the strategy. But this is easier said than done. Strategy is also constrained by the company's capabilities.

Where are we going and how will we get there? Strategy sets out the route a business intends to take to achieve its goals.



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Following privatization in the 1990s, several British gas and electricity companies branched out into retail operations, selling domestic appliances in high-street shops. Most of these shops quickly closed when it transpired that the companies had no experience or expertise in retailing. This was not a matter of organization, but of the wrong companies doing the wrong things.

Strategy, then, is the art of the possible, and needs to take account of time and resources available. Many managers like to have a formal strategy: a written document to which managers and staff sign up and which sets out everyone's responsibilities in meeting the company's goals. This formal approach has its critics, notably the Canadian guru Henry Mintzberg, who believes that most companies evolve their strategy as they go along. 'Emergent' strategy adapts continuously to changing circumstances and environment.

Another possibility is that managers adopt a mixture of both methods, with a formal strategy document creating a framework within which managers respond to events as they arise and make ad hoc decisions.

There is an old adage that 'everything in strategy is very simple, but nothing in strategy is very easy'. One of the first things the novice manager learns is that strategic plans are almost never executed as intended.

No matter how careful the planning process has been, there will always be unknown factors and unforeseen events. Known in the jargon as 'turbulence' or 'friction', these build up until they threaten to derail the original plan. This usually means that the original plan must be adapted or, in extreme cases, scrapped and a new plan developed instead. Flexibility is key to good strategic thinking. Is it better to go through obstacles, or round them?

There is a perception in some quarters that strategy is somehow the preserve of senior managers, who carry it out while everyone else puts their heads down and gets on with the job. This is a mistake. Everyone in the business contributes to the execution of the strategy in some way, even if only indirectly. Every department has

its role to play—even the cleaning staff and the post room help to contribute to the success of the strategy by ensuring that offices are clean and communications keep flowing, leading to greater efficiency. If there is a group or department that is not contributing to the strategy, then it is wasting resources and should be dispensed with.

Once the company's goals have been established, every ounce of energy should be devoted to carrying out the strategy to reach those goals. This does not mean that the strategy, and indeed the goals themselves, will not change. Change ebbs and flows, and it takes quick and creative thinking to recognize the need for it and adapt the existing strategy accordingly. Ultimately, strategy is not a matter of formal documents and plans, but a way of thinking.

Source: 'Plan to think strategically.' *Financial Times*, 9 August 2004

■ Questions

1. What is strategy?
2. What is the importance of strategy to individuals within an organization?

1.3 Strategic Management

If a strategy allows an organization to match its resources and capabilities to the needs of the external environment in order to achieve competitive advantage, the process of bringing about the strategy is strategic management. All organizations set goals they want to achieve. Strategic management is about analysing the situation facing the firm, and on the basis of this analysis formulating a strategy and finally implementing that strategy. The end result is for the organization to achieve competitive advantage over its rivals in the industry. A point worth noting is that these elements are co-dependent, i.e. in formulating a strategy an organization must also consider how that strategy will be implemented. Failure to consider these issues in tandem will decrease the likelihood of success. We might also note that this neat sequential pattern may not resemble how a given organization might undertake strategic management. Figure 1.1 illustrates that each part of the strategic management process is interdependent. Analysis, formulation, and implementation all need to be considered if the organization's strategy is to meet the needs of its environment effectively.

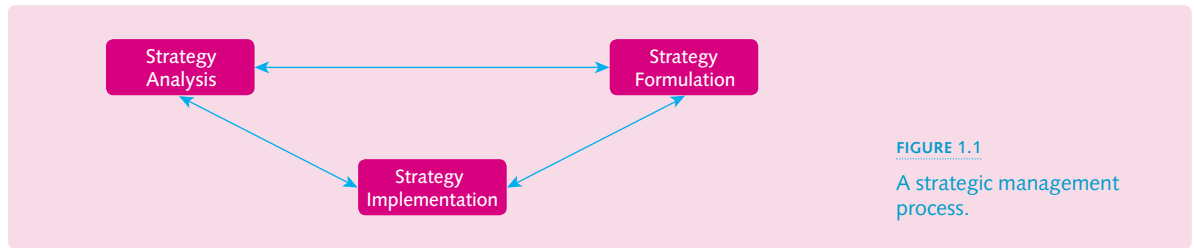


FIGURE 1.1
A strategic management process.

For example, some organizations might actually implement a strategy without fully analysing their current situation. This may be because events in their industry are changing so fast that they feel they simply do not have the luxury of undertaking detailed analysis. An organization's leader might take a series of decisions based on experience or intuition. In reality, without the use of some analysis the organization will never know if its strategy succeeds, and why it succeeds. It will not fully understand how it meets the industry's **key success factors**. Key success factors are those elements in the industry that keep customers loyal and allow the organization to compete successfully. By analysing what consumers want and the basis of competition in the industry, an organization is able to ascertain the key success factors for its industry. For instance, it might ask: which elements of its resources and capabilities brought it success? What was the role played by its internal structure and organizational culture? What factors drive competition in this industry? In short, without analysis its success will likely be short-lived and difficult to repeat.

KEY SUCCESS FACTORS

elements in the industry which keep customers loyal and allow the organization to compete successfully

1.3.1 Strategy Analysis

This is also referred to as situation analysis. Whilst bearing in mind that the strategic management process is co-dependent, the undertaking of strategy analysis by the organization is a useful starting point. As we shall see in **Chapters 2** and **3**, this involves an analysis of the general environment and the competitive environment. Strategy analysis also deals with the organization's internal environment. It allows the organization to evaluate how well it is positioned to exploit the opportunities in its external environment.

1.3.2 Strategy Formulation

A careful analysis of the firm's internal environment and the needs of the external environment will allow the firm to assess where it can best achieve a strategic fit between the two. Without some form of analysis decisions can only be based on experience. Experience alone may have been fine in the stable industries of the 1960s, but in today's turbulent environments an organization cannot expect to follow today's

patterns tomorrow. Mintzberg (1994) reminds us that strategy formulation also occurs as a creative and, at times, subconscious act which synthesizes experiences to form a novel strategy. Ohmae (1984) accepts that strategic thinking starts with analysis but stresses creative insight in the formulating of great strategies. Such insight does not form part of any conscious analysis.

Markides (1999b) argues that 'effective strategic design is a process of continuously asking questions . . . correctly formulating the questions is often more important than finding a solution.' Ohmae (1984) makes a similar point. He states that a vital part of strategic thinking is to formulate questions in a way that will help find a solution. A key part of strategy formulation is strategy evaluation which recognizes that an organization is seldom faced with one strategy but requires a criterion to judge competing strategies. We will return to some of these points later when we evaluate different perspectives on strategy formulation. Strategy formulation primarily takes place at two different levels within the organization: the *business level* and the *corporate level*. The different types of strategy are briefly discussed in **Chapter 5**, Section 5.1. Business and corporate level strategies are addressed in detail in **Chapters 7** and **8**. For now we can say that business level strategy deals with *how* an organization competes in its chosen markets, whereas corporate strategy deals with the fundamental question of *what* business (or businesses) we want to be in.

1.3.3 Strategy Implementation

The best formulated strategy in the world will amount to nothing if it is poorly communicated throughout the organization and incorrectly implemented. Effective implementation of strategies requires the organization to be sufficiently flexible in its organizational structure and design. Strategies need to be communicated, understood, and properly coordinated with stakeholders inside and outside the organization. In an age of collaboration, this may involve discussions with suppliers and partners. Although the leader of an organization will ultimately be responsible for a strategy's success or failure, their role should be to encourage and create an organizational culture which empowers managers to respond to opportunities. In this way each employee will be confident to try out new ideas and innovate without fear of reprisals. The values of an organization will be important here.

At a fundamental level we can ask: What is the purpose of any organization? Why does it exist? The question is relevant irrespective of whether an organization operates in the private or public sector since all organizations must have a clear sense of direction based upon agreed objectives if they are to understand what they are seeking to achieve. If, for example, organizations in the private sector seek to maximize returns to shareholders whilst taking account of stakeholder expectations, and likewise firms in the public sector seek to utilize their resources in an optimal manner, strategy is simply the way in which an organization bridges the gap between its stated goals and

how it intends to achieve them. Often purpose and goals are used interchangeably, but this misses an important distinction between the two; the goals that an organization sets derive from its purpose. This will become clearer as we look at the purpose or *raison d'être* of organizations and how this has guided their strategy.

1.4 Values, Visions, and Mission Statements

A **vision** is often associated with the founder of an organization and represents a desired state which the organization aspires to achieve in the future. In contrast with goals and objectives, a vision does not change over time. A vision must tap into the personal goals and values of the organization's employees if it is to be internalized by them. When it bears little resemblance to reality, disregards the capabilities of the organization, and the problems of the organization, it will be rejected by employees. Employees will also reject a vision where they see a credibility gap between managers' rhetoric and their actions. The prerequisite for producing a vision is not great intellect but imagination, intuition, and an ability to synthesize disparate information. A vision may or may not find its expression in a *vision statement* (Lipton 1996). The length and complexity of vision statements differ between organizations, but clearly they must be easy to understand and remember.

VISION

this is often associated with the founder of an organization and represents a desired state that the organization aspires to achieve in the future

An organization's **mission** seeks to answer the question as to why an organization exists. A *mission statement* can be defined as a way in which the organization communicates the business it is in to the outside world. Drucker (1995) argues that a mission statement is the same as asking the question: What business are we in? A mission statement needs to appeal to a broad spectrum of stakeholders if all these stakeholders are to accept it. In this respect, a mission statement which simply exhorts the need to maximize shareholder value will be unlikely to motivate employees. It is not unusual, particularly in the public sector, for organizations to have mission statements at different levels ranging from a department all the way down to individual teams. If these statements are to guide employee behaviour, then it would seem that two conditions are necessary: (1) such statements are communicated clearly to all employees; (2) those employees internalize these statements and use them to direct their behaviour. The use of these statements may constitute a necessary but not sufficient condition for organizational success. At some point we might ask what actually is being accomplished as a result of vision and mission statements.

MISSION

seeks to answer the question why an organization exists

Campbell *et al.* (1990) make a distinction between an organization's *mission* and its *sense of mission*. They see a mission as an intellectual concept that can be used to guide the policies of an organization. However, a sense of mission is an emotional commitment that employees feel towards the organization. It occurs when employees

feel that there is match between the values of an organization and those of the individual. The key point is that individuals with a sense of mission are emotionally committed to the organization, what it stands for, and what it is trying to achieve.

In their quest for what makes a visionary organization, Collins and Porras (1994) describe a **core ideology** which is made up of **core values** and purpose. The core values are an organization's essential and enduring tenets which will not be compromised for financial expediency and short-term gains. They do not shift as competitive conditions change but remain largely inviolate. It is what members are expected to endorse and internalize as part of working for such organizations. More than that, it is what attracts individuals to these types of organizations in the first place. IBM's former chief executive officer, Thomas J. Watson Jr, put it this way:

... I firmly believe that any organization, in order to survive and achieve success, must have a sound set of beliefs on which it premises all its policies and actions . . . the most important single factor in corporate success is faithful adherence to those beliefs . . . Beliefs must always come before policies, practices, and goals. The latter must always be altered if they are seen to violate fundamental beliefs. (Collins and Porras 1994, p. 74)

CORE IDEOLOGY

is made up of core values and purpose

CORE VALUES

are an organization's essential and enduring tenets which will not be compromised for financial expediency and short-term gains



STRATEGY FOCUS

Core Purpose at Tesco



Courtesy of Tesco PLC

Tesco is the UK's most profitable supermarket retailer. It continues to expand beyond its core business into new markets such as non-food, and services such as telecoms. It expects its employees to internalize the following core values:

Our Core Purpose is to create value for customers to earn their lifetime loyalty.

Surprisingly simple. Refreshingly honest. And yet incredibly powerful. Everything we do, every innovation we bring to market, every business decision we take, is driven by our customers.

We believe that we continually demonstrate that we're good at getting things done, good at 'what' we do, and we take pride in being good at the way in which we achieve it too, the 'how' we do it. We believe that by living by our Values, we will encourage and demonstrate behaviour that will help us achieve our Core Purpose and set us apart from our competitors.

Values enable us to build a common way of working. We want people in our business who feel comfortable with these Values and feel they can genuinely demonstrate them. They aren't about being soft and lovely, but about being rigorous and single minded about how we achieve our goals.

Some of the values which Tesco says make it what it is today and what it will be in the future are:

- Be energetic, be innovative, and be first for customers
- Look after our people so they can look after our customers
- Treat people how we like to be treated
- Ask more than tell, and share knowledge so that it can be used
- Trust and respect each other
- Strive to do our very best
- Enjoy work, celebrate success, and learn from experience

Source: From recruitment pages at www.tesco.com

A similar point was made by the founder of Johnson & Johnson, Robert Wood Johnson, when he wrote the organization's *credo* or set of beliefs in 1943. Unusually for this time Johnson explicitly recognized the importance of meeting stakeholder needs. Stakeholders are those individuals and groups upon whom the organization depends to achieve its goals. Stakeholders, in turn, have an interest in and can influence the success of the organization. They include customers, suppliers, shareholders, employees, and the local community, among others. Robert Wood Johnson codified that service to their customers should always come first, service to the organization's employees and management should be second, the local community third, and lastly service to shareholders. It is only when this chronology of events occurs that

the shareholders will receive a *fair return*. See Strategy Focus: Organizational Values which illustrates how Johnson and Johnson's credo guided their executive management decisions some forty years later when they were faced with a crisis.



STRATEGY FOCUS

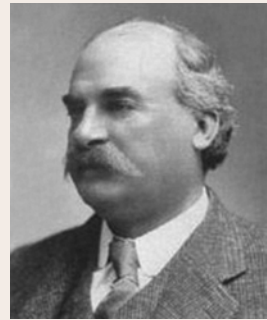
Organizational Values

Johnson & Johnson: How their Credo Guides their Strategy

General Robert Wood Johnson guided Johnson & Johnson from a small, family-owned business to a worldwide enterprise. In doing so he had an enlightened view of a corporation's responsibilities beyond the manufacturing and marketing of products. In 1935, in a pamphlet titled *Try Reality*, he urged his fellow industrialists to embrace 'a new industrial philosophy'. Johnson defined this as the corporation's responsibility to customers, employees, the community, and stockholders.

Eight years later, in 1943, Johnson wrote and first published the Johnson & Johnson *Credo*, a one-page document outlining these responsibilities in greater detail. Putting customers first and stockholders last was a refreshing approach to the management of a business. However, Johnson was a practical businessman. He believed that by putting the customer first the business would be well served, and it was. Johnson saw to it that his company embraced the Credo, and he urged his management to apply it as part of their everyday business philosophy.

In 1982 Johnson & Johnson faced a crisis when its drug Tylenol was altered and cyanide placed in the capsule form of the product resulting in seven deaths. Johnson & Johnson's strategic response was inspired by the philosophy embodied in the Credo. The product was voluntarily recalled and destroyed, even though subsequent testing found the remaining capsules to be safe. Johnson & Johnson took a \$100 million charge against earnings. In 1986, as a result of a second tampering incident and another fatality, Johnson & Johnson took the decision to discontinue the sale of Tylenol in capsule form. The company reintroduced Tylenol in tamper-proof packaging and regained its leading share of the analgesic market. Faced with the loss of millions of dollars, the values that are embodied in Johnson & Johnson's Credo guided its strategic response and ensured its quick and honest handling of the crisis preserved the company's reputation.



General Robert Wood Johnson: the man who guided Johnson & Johnson from a small, family-owned business to a worldwide enterprise.

Courtesy of Johnson & Johnson

When Robert Wood Johnson wrote and then institutionalized the Credo within Johnson & Johnson, he never suggested that it guaranteed perfection. But its principles have become a constant goal, as well as a source of inspiration, for all who are part of the Johnson & Johnson Family of Companies.

Source: adapted from www.johnson&johnson.com

Johnson & Johnson provides a classic example of how an organization's values (credo) guide its behaviour with its stakeholders. The example of Johnson & Johnson demonstrates the importance of values in guiding how an organization decides and implements its strategy. It is values that form and shape the corporate culture over time and provide signposts for acceptable behaviour of internal and external stakeholders. For example, as organizations continue to outsource activities overseas in search of cheap production economies, they must ensure that employee conditions conform to their own organizational values. The use of child labour in some countries has forced organizations to face up to and bridge a credibility gap between their rhetoric and their deeds. The more robust the values in an organization are, the greater the clarity this provides for setting goals and therefore strategic direction and action. The more ambiguous the values within an organization are, the greater the opportunity for conflicting goals and for decisions to go unchallenged. A discussion of values is dealt with in greater detail in **Chapter 10**.

Purpose represents the reasons an organization exists beyond making a profit. The **purpose** of an organization is distinct from its goals and strategies. Its primary function is to guide and inspire individuals. A purpose should be broad, fundamental, and enduring in its composition. It should be capable of being stated succinctly. A purpose is comparable to a vision in that organizations never achieve their purpose; it is an ongoing journey. For example, Walt Disney stated, 'Disneyland will never be completed, as long as there is imagination in the world' (Collins and Porras 1994, p. 77). The American pharmaceutical company Merck has its stated purpose as: 'We are in business of preserving and improving human life. All our actions must be measured by our success in achieving this' (Collins and Porras 1991). In an address to members of Hewlett Packard, its co-founder, David Packard, outlined his company's purpose as follows:

I want to discuss why a company exists in the first place. In other words, why are we here? I think many people assume, wrongly, that a company exists simply to make money. While this is an important result of a company's existence, we have to go deeper and find the real reasons for our being . . . The real reason for our existence is that we provide something which is unique [that makes a contribution]. (Collins and Porras 1994, p. 56)

PURPOSE

the reasons an organization exists beyond making a profit

A purpose need not be unique, but it must be sincerely held. Other corporations might endorse a similar purpose to Merck and Hewlett Packard, for example, but the key difference is the authenticity. How is that purpose worked out in the daily lives of corporate employees? This shows the difference between an organization's rhetoric and reality. An organization's core purpose does not prevent change; it simply provides a compass by which organizations can steer as they exploit new business opportunities.

The challenge for organizations is how to preserve what is their very essence but still respond to a changing competitive environment. Collins and Porras (1994) suggest the use of BHAGs to stimulate progress. BHAGs are Big Hairy Audacious Goals. A BHAG is clear and compelling, and it serves as a rallying cry to all employees as to where their energies should be focused. It has a finite time span so that everyone knows when it is achieved. Such goals include President John F. Kennedy's commitment in 1961 to landing a man on the Moon and returning him safely to Earth before the decade was out. BHAGs are easy to understand, and no matter how many different ways they may be put, they are still understood by everyone. In 1907, Henry Ford proclaimed that he wanted to democratize the automobile and '... build a car for the great multitude . . . so low in price that no man making a good salary will be unable to own one . . .' (Collins and Porras 1994, p. 97). At that time Ford was one of over 30 car companies competing in this emerging market. It succeeded but its success was short-lived. This highlights a couple of important points to bear in mind with BHAGs. First, they must fit with an organization's core ideology; this was the case with Ford. Second, once achieved they need replacing. Ford achieved its BHAG but did not set another. This allowed General Motors to supplant its dominant position in the automobile industry.

1.4.1 The Theory of Business

Drucker (1995) argues that organizations encounter difficulties when the assumptions on which they are built and the basis on which they are being run no longer fit reality. These assumptions affect an organization's behaviour and its decisions about what and what not to do, and determine what an organization thinks are meaningful results. They include assumptions about markets, customers, competitors, and the organization's strengths and weaknesses. Drucker refers to this as a company's **theory of business**. Every organization has a theory of business regardless of whether it operates in the public, private, or not-for-profit sector. The reason many large corporations are no longer successful is that their theory of business no longer works. For example, when the computer was in its infancy IBM's theory of business suggested that the future of computing was in mainframes. Around this time the first personal computer was developed by enthusiasts. At the same time as *serious* computer makers were *reminding* themselves that there was absolutely no reason for personal computers, the Apple and the Macintosh went on sale, starting the PC revolution.

An organization's theory of business has four characteristics. First, the assumptions about the environment, mission, and core competencies must fit reality. Simon Marks,

THEORY OF BUSINESS

the assumptions that affect an organization's behaviour, its decisions about what and what not to do, and determine what an organization thinks are meaningful results

the co-founder of Marks & Spencer, realized that continued success in his business meant that he as merchant should develop new core competencies. He would design products based on his customer knowledge, and find manufacturers to make them to his costs. This went against the established practice of manufacturers producing products *they* thought the consumer might buy. Second, the assumptions in all three areas have to fit one another. Third, the theory of business must be known and understood throughout the organization. This is relatively easy when an organization is founded, but as it grows it must be reinforced if the organization is not to pursue what is expedient rather than what is right. Fourth, the theory of business has to be continually tested. In effect, the theory of business has to have the ability to change to meet changing conditions. See Strategy Focus: Theory of Business for the challenges facing Dell as its business model continues to be tested.



STRATEGY FOCUS

Theory of Business

RETURNING founders have form. Since Charles Schwab got back in harness in 2004, the stockbroker's shares have doubled. Steve Jobs's return 10 years ago has triggered a 15-fold rise in Apple's stock. Can Michael Dell, who has ousted his hand-picked successor from the top job after less than three years, weave the same magic on the computer business he founded in his college bedroom in 1984? He's got his work cut out. Dell's problems have mounted in the past year, with missed profit forecasts and the slowest sales growth in years. An expensive bid to rebuild bridges with disgruntled customers has taken the gloss off the former PC market leader. It still faces a government investigation into its accounts. Dell's consumer business lacks the pizzazz of Apple but its low-margin business model won't let the company beef up research spending to compete with rivals on level terms.

Winning back individual buyers might require a move away from direct-sales but a retail presence would be ruinously costly. Its corporate business isn't much healthier. It's losing share here too. The initial spike in Dell's share price yesterday was a short-lived vote of confidence in the company's founder. The reassessment was unsurprising because the prodigal son never really went away. When he handed over the reins to Kevin Rollins in 2004, Dell (the man) shared an office with the former Bain management consultant and pointedly reminded anyone who asked that the two of them ran Dell (the company) together.

There can't be any bigger motivation to succeed than having your name on the box, but creating Dell 2.0 is going to be no quick fix. The stock market has taken the prudent view that the company needs a new strategy, not just its old boss.

Source: 'Michael Dell's personal rescue mission looks tricky' *Daily Telegraph*, 2 February 2007

Drucker argues that every theory of business will eventually become obsolete and no longer meet the needs of the organization. However, there are two preventive measures. The first is *abandonment*. Drucker suggests that every three years an organization might look at its markets, products, and policies and ask itself: if we were not already in it, would we still want to be in it now? This forces managers in organizations to question the assumptions on which their business is based—their theory of business. The second is to study what is happening outside the business, especially with non-customers. This is because fundamental change rarely happens within your own industry or with your own customers. This type of change invariably first manifests itself with your non-customers. We will say much more on detecting changes that might impact one's competitive environment in **Chapter 2**.

A theory of business becomes obsolete when an organization has achieved its original objectives. As with the example earlier of Ford democratizing the automobile, the achievement of the objective may point to the need for new thinking rather than be a cause for celebration. As Sam Walton, the founder of the American retailer Wal-Mart noted:

You can't just keep doing what works one time, because everything around you is always changing. To succeed you have to stay out in front of that change. (Collins and Porras 1994, p. 81)

Thomas J. Watson Jr argued that an organization's basic beliefs should remain inviolate:

If an organization is to meet the challenges of a changing world, it must be prepared to change everything about itself except its basic beliefs . . . The only scared cow in an organization should be its basic philosophy of doing business. (Collins and Porras 1994, p. 81)

1.5 Types of Strategy

There are three basic forms of strategy that interest organizations. These are corporate strategy, business strategy, and functional strategy. In reality, most organizations are concerned with business level strategy and corporate strategy. These are described below.

Corporate Strategy

Corporate strategy is concerned with the broader issues of what industries the organization wants to compete in. It deals with mergers and acquisitions, and allocates resources between the organization's strategic business units (SBUs). The Royal Bank

CORPORATE STRATEGY

is concerned with what industries the organization wants to compete in

of Scotland's takeover of National Westminster Bank was part of their corporate strategy, as was Intel's move away from memory chips and towards microprocessors. Corporate strategy is often seen as the preserve of the most senior management within an organization.

Business Strategy

Business strategy, sometimes called competitive strategy, deals with how an organization is going to compete within a particular industry or market. It is concerned with how the organization will achieve a competitive advantage over its rivals. In contrast with corporate strategies, managers of SBUs, who are usually given substantial autonomy, formulate business strategies. Business strategy is dealt with in **Chapter 3**, when we assess the competitive environment.

BUSINESS STRATEGY

deals with how an organization is going to compete within a particular industry or market

Functional Strategy

We might note that there is a third category, functional strategy. This deals with decisions according to functional lines such as R&D, marketing, and finance. These functions will be involved in the support of the business strategy. Therefore we will subsume this within business strategy in our discussions.

1.6 Changes in the Approach to Strategic Management

We have seen that strategic management is concerned with how firms achieve and sustain competitive advantage. However, a major disagreement arises when we look at *how* competitive advantage is achieved by the firm. The true test of how organizations achieve and sustain competitive advantage is ultimately decided in the marketplace. Therefore one might expect research to help provide an answer. Again, there is controversy here as research findings are both accepted and contested.

The changes in strategic management as a discipline reflect the changing dynamics of modern economies. For example, during the 1950s and 1960s firms could rely on stable and expanding market conditions with a customer emphasis on price. Under such conditions it was natural that organizations would engage in corporate planning. It was not unusual for major corporations to have a corporate planning function or department which annually developed long-term plans for the next 5 years, and even longer in some instances. These were primarily finance-based budgetary control systems, giving the assurance that there was some scientific basis to this kind of planning. In times of relative stability, which in turn provides for some degree of predictability, this type of corporate planning was the norm.

In the 1960s and 1970s the corporate landscape was beating the drum of diversification, in particular how to increase market share by capturing new markets. Ansoff's growth vector matrix explains how organizations can engage in related and unrelated diversification to increase their market shares (Ansoff 1965). Diversification works well as long as synergies ensue resulting in increased profitability and an increase in the capital value of the firm. It also presupposes that management has sufficient skills and capabilities to run business operating in markets of which they may have little or no knowledge.

In the 1980s, the work of Porter (1980, 1985) on industry analysis shifted the emphasis to firms analysing the competitive forces inherent within their industry as a means of gaining competitive advantage. Porter argued that firms should position themselves favourably against adversarial forces within their industry and adopt a strategy that would enable them to compete effectively. In the 1980s corporations had also begun to focus on the core elements of their businesses. This was a period in corporate history in which managers sought to *stick to the knitting*, as exemplified in the best-selling book *In Search of Excellence* (Peters and Waterman 1982).

This continued throughout the 1990s as new management techniques taught corporate leaders about downsizing, outsourcing, delayering, total quality management, economic value analysis, benchmarking, and re-engineering. Organizations were outsourcing all but the essential elements or the core competencies of the organization. In contrast with Porter's work the resource-based view (RBV) of the firm, exemplified by the work of Grant (1991), Kay (1993), and Prahalad and Hamel (Pralhad and Hamel 1990, Hamel and Prahalad 1994), exalts the organization to look within itself at its own resources and core competencies, and use these as a basis for competitive advantage. Amit and Schoemaker (1993) see the resource-based view of the firm as a complement to the industry analysis framework of Porter since industry analysis views the sources of profitability to be the characteristics of the industry and the firm's position within the industry, while the resource view sees the determinants of profitability as the firm's resources and capabilities.

D'Aveni (1994) coined the term *hypercompetition* to describe the new competitive situation where firms must continually innovate, developing new products or services for the customer. For D'Aveni, sustainable competitive advantage now requires firms to constantly develop new products to provide customers with increased functionality and performance. Microsoft is a classic example of a hypercompetitive firm (see **Chapter 3** for a discussion of hypercompetition). However, not everyone is convinced that hypercompetition represents a new framework for understanding competition. For example, Porter (1996) argues that hypercompetition can be seen as an excuse for a lack of managerial ability and poor strategic thinking. Mintzberg (1994) argues that turbulence, inasmuch as it exists at all, is an opportunity for organizations to learn from a changing environment, as the Japanese have done. Mintzberg is not denying turbulence *per se*; he is simply pointing out that there is a tendency in strategic

management to characterize the previous decades as stable, and our current decade as turbulent. Research by McNamara *et al.* (2003) seems to support Mintzberg, as they suggest that 'hypercompetition perspectives are important but no more so now than they were in recent years . . .'.

In the 1990s organizations began to see the benefits of collaboration, cooperation, and joint alliances. 'Networking' between corporations became the new buzzword. Supplier relationships were seen as a source of competitive advantage and not as one of competition. Brandenburger and Nalebuff (1996) refer to this détente as *co-competition*, i.e. a blend of competition and cooperation existing simultaneously, in effect a non-zero sum game. This is discussed in detail in **Chapter 3**.

1.7 Different Perspectives on Strategy Formulation

The issue of how strategy is actually formulated has led to claims and counter-claims about the merits of different schools of thought within strategic management. This ongoing debate has been largely implicit in strategic management books, but waged more explicitly in the various strategic management journals (Mintzberg 1990, Ansoff 1991). There are numerous perspectives on strategy formulation which in many respects overlap and branch off from each other (see Mintzberg and Lampel (1999) for an identification of 10 different schools of strategic thought and whether these are fundamentally different ways of making strategy or different parts of the same process). We can identify two broad perspectives of strategy management which at first reading may appear to be polar opposites: the *design school* and the *learning school*.

1.7.1 The Design School

The design school is associated with the work of Andrews (1971) and Ansoff (1965). According to Andrews, an organization needs to match its strengths and weaknesses (which are internal to the firm, and derive from its resources and competencies) with the needs of its competitive environment. The competitive environment comprises both threats and opportunities. This provides the familiar SWOT analysis of strengths, weaknesses, opportunities, and threats. An external analysis is used to identify the opportunities and threats facing the firm, while an internal analysis of the organization identifies its strengths and weaknesses.

For the design school, the match between these elements will lead to the creation of a number of different strategies, each of which can be evaluated and the best strategy

then implemented. In the 1960s organizations had planning departments which created strategies for managers to implement. The role of top management was to choose the most appropriate strategy. Ansoff's product matrix was an attempt to help organizations understand the relationship between their existing products and new products, and how these fitted with the organization's competencies. An awareness of this relationship allows the organization to assess more clearly its strategy, and therefore reduce its risks. For the past quarter of a century Porter, more than any other, has exemplified this rationalist approach to strategy formulation using *generic* strategies.

1.7.2 The Learning School

In contrast with the design school, Mintzberg (1990) argues that a rational approach to strategy fails to take account of how strategy making occurs in reality. Mintzberg and Waters (1985) suggest three approaches to strategy making: intended, realized, and emergent strategies. An **intended strategy** is one that the organization has deliberately chosen to pursue and will therefore have been worked out in detail. A **realized strategy** is the strategy that the organization actually carries out. For a variety of reasons, for example a change in consumer preferences, the intended strategy may no longer be relevant to market conditions and therefore is not implemented. Mintzberg and Waters refer to this as an unrealized strategy. In such a case managers will use their experience and learning to develop an **emergent strategy** which meets the needs of the external environment. When this emergent strategy is implemented it becomes the realized strategy. They argue that strategy formulation is far more likely to be a result of emergent strategies rather than based on any detailed intentions. This process is shown in Figure 1.2.

INTENDED STRATEGY

the strategy that the organization has deliberately chosen to pursue

REALIZED STRATEGY

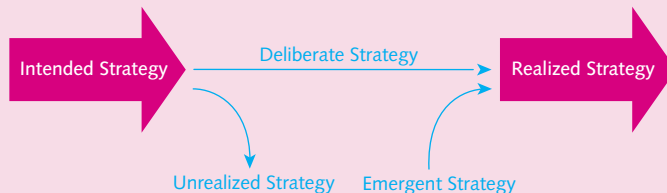
the strategy that the organization actually carries out

EMERGENT STRATEGY

where managers use their experience and learning to develop a strategy that meets the needs of the external environment

FIGURE 1.2

Types of strategies. 'Types of Strategies, Deliberate & Emergent'. Mintzberg, H. and Waters, J.A. 1985 © John Wiley & Sons Ltd. Reproduced with permission.



Mintzberg (1994) points out that '... strategy is an immensely complex process, which involves the most sophisticated, subtle, and, at times subconscious elements of human thinking . . . strategies can develop inadvertently, without the conscious intention of senior management, often through a process of learning'. However, Mintzberg does allow '... that all viable strategies have emergent and deliberate qualities, since

all must combine some degree of flexible learning with some degree of cerebral control.' See Case Study: Deliberate and Emergent Strategies which shows competing perspectives on Honda's success and ultimate domination of the US motorcycle industry. The design school or rationalists see Honda's success as part of a deliberate strategy. Mintzberg, in contrast, argues that it results from an emergent strategy.

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For a greater understanding of the debate surrounding Honda's domination of the US motorcycle industry go to the Online Resource Centre and see the Key Work feature.



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CASE STUDY 1.2

Deliberate and Emergent Strategies



Courtesy of Honda UK

The Honda Cub, which has sold more than 40 million units since 1958.

Honda and the Supercub is probably the best known and most debated case in business strategy. In the 1950s, motor cycles were sold through specialist outlets welcoming only testosterone-loaded young men. Bikes were powerful and noisy, and the riders' leather clothes smelt of leaking oil. Honda entered the US market in 1959 and changed everything. Five years later the company made one in two bikes sold in the US. Their best selling machine was the 50cc Super Cub. The company's advertising slogan was 'You meet the nicest people on a Honda'.

The story benefits from deconstruction. One school of explanation derives from the original Harvard Business School case study. That case is based on a 1975 report by the Boston Consulting Group for the British government that described these events as the archetype of an orchestrated attack on Western markets by Japanese manufacturers of consumer goods. Having established large economies of scale in the domestic market, Honda was able to exploit its cost advantage globally.

A quite different history was given by Richard Pascale, who went to Tokyo to interview the elderly Japanese who had managed Honda's first steps in the US. These executives explained that Honda had never imagined that small bikes, popular in Japan, would find a market in the wide open spaces of the US. They had focused on large machines, planning to compete with US manufacturers. Mr Honda, they said, was especially confident of success with these products because the shape of the handlebars looked like the eyebrows of Buddha.

But the eyebrows of Buddha were not appealing in the world of Marlon Brando and James Dean. The Japanese hawked their wares around the western US, to dealers 'who treated us discourteously and gave the impression of being motorcycle enthusiasts who, secondarily, were in business'. The few machines they sold, ridden more aggressively than was possible in Japan, leaked even more oil than their US counterparts.

Dispirited and short of foreign currency, the Honda executives imported some Super Cubs to ease their own progress around the asphalt jungle of Los Angeles. Passers by expressed interest, and eventually a Sears buyer approached them. And the 'nicest people' slogan? That was invented by a University of California undergraduate on summer assignment. Only the naive will believe either account.

Successful business strategy is a mixture of luck and judgment, opportunism and design, and even with hindsight the relative contributions of each cannot be disentangled. Mr Honda was an irascible genius who made inspired intuitive decisions—with assistance from the meticulous market analysis of his colleagues and the intense discipline of Honda's production line operations. It is a mistake to believe the ultimate truth about Honda can be established through diligent research and debate. The Harvard account, although paranoid, is right to emphasize Honda's operational capabilities. Mr Pascale correctly stresses the human factors but his interviewees must have laughed as he wrote down the story of the eyebrows of Buddha.

The Boston Consulting Group naturally saw the experience curve at work and later, when peddling a different panacea, realized it was an example of time-based competition. Gary Hamel and C.K. Prahalad perceived the development of Honda's 'core competence' in engine manufacture. Henry Mintzberg seized on Mr Pascale's account as an instance of emergent strategy. But there is no true story and no point in debating what it might be.

The lesson of Honda is that a business with a distinctive capability that develops innovative products to exploit that capability and recognizes the appropriate

distribution channels for such innovations can take the world by storm. And that lesson is valid whether Honda's achievement was the result of careful planning or serendipity.

Source: 'Driving through the spin on Honda's big success' *Financial Times*, 16 November 2004

■ Questions

1. To what extent can Honda's strategy said to have emerged?
2. What difference does it makes whether Honda's success was as a result of a *deliberate or emergent strategy*?

We argued at the start of this section on different perspectives that the truth often lies somewhere between competing positions and drawn battle lines. The question is not whether some approaches to strategic management are overly rational and analytical, failing to take account of more complex processes within strategy making. Perhaps the real question is how does strategic management as a discipline move forward and ultimately benefit the performance of organizations, and in so doing increase society's net benefit. There is a danger that emanates from having battle lines and positions too clearly demarcated, which is that common ground can often be overlooked. However, as is often the case, the truth lies somewhere between these two perspectives. Successful strategy formulation will inevitably involve both analytical techniques and a creative process: '... it's a complicated world out there. We all know we shall get nowhere without emergent learning alongside deliberate planning' (Mintzberg 1996).

1.8 A Strategic Management Framework

A framework is useful to help us to structure our thoughts and navigate around the different aspects of strategic management. If the purpose of strategy is to enable an organization to achieve a sustainable competitive advantage, then any framework needs to address the process necessary for this. In Figure 1.3 we outline a framework which includes an analysis of the organization's external environment and its internal resources and capabilities. However, as we saw in the Strategy Focus on Johnson & Johnson, all organizations needs a clear sense of direction and this is provided by its values (or credo), which in turn will direct the goals it sets and therefore the strategy necessary to achieve them. It is in this respect that strategy can be seen as a means to an end. It is the lynchpin between an organization's internal and external environment.

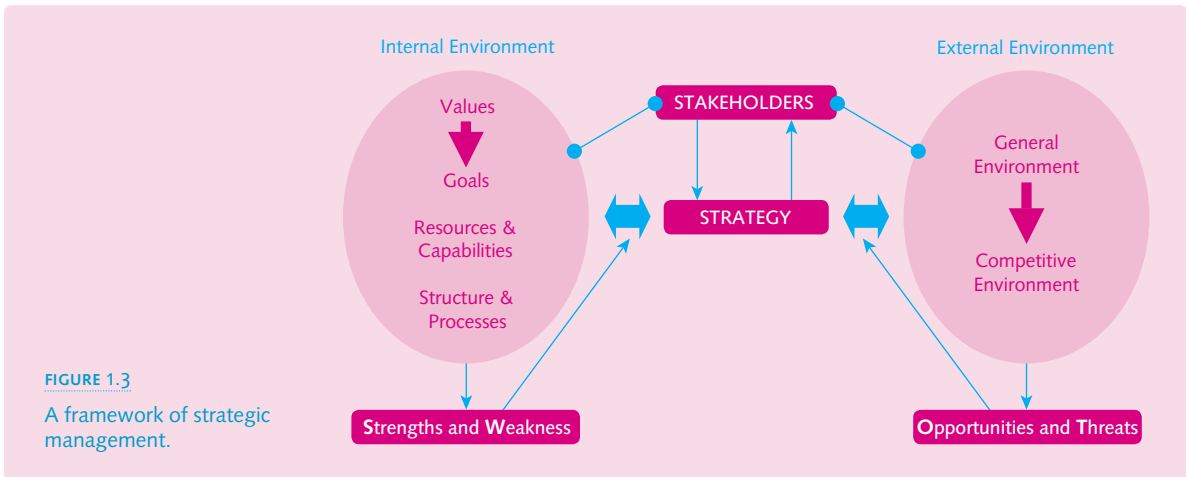


FIGURE 1.3

A framework of strategic management.

Figure 1.3 shows the importance of values in the strategy-making process. Hence the arrow emanating from *values* which determine the *goals* the organization sets, the *resources and capabilities* it requires, and the *structures and processes* necessary to achieve those goals. Goals need to be clearly defined throughout the organization as they provide the direction and motivation for individuals within the firm. The more clearly the goals are stated and imbued within the organization, the greater the understanding by the organization's participants of their role in achieving these goals. An organization's goals will reflect its internal *strengths and weaknesses* and the *opportunities and threats* within its external environment. Values and goals will also determine the types of resources the organization accumulates. How the organization is structured and the processes it utilizes will again reflect the organization's goals and what it sees as important—its values. An organization's values will also determine the relationship with its stakeholders.

Stakeholders are those individuals and groups who are impacted by the behaviour of the organization, and whose own behaviour can, in turn, have an impact on the organization's strategy. This is shown in the framework by arrows which emanate from stakeholders to strategy, and strategy to stakeholders. Stakeholders occur within the internal and external environment, as shown by the linkages in the diagram. For example, managers and employees are internal stakeholders, while suppliers, shareholders, and the local community are external stakeholders. The dichotomy between internal and external stakeholders is not always this simple, since a shareholder may also be an employee of the firm.

Figure 1.3 links strategy and the internal environment since each new strategy adopted must meet the organization's values and goals. Similarly there is a link between the firm and its external environment since its values will determine the types of markets

it will and will not operate within. This is perhaps most clearly seen in the strategies being pursued by ethical investment fund managers. The two-way arrows positioned between an organization's strategy and its internal and external environments provide feedback on the appropriateness of the intended strategy. As we have seen, the intended strategy may not be implemented, perhaps because of a change in market conditions, and an emergent strategy then becomes the realized strategy. The arrow emanating from the general environment to the competitive environment draws our attention to the fact that changes in the general environment may have their greatest impact on the competitive environment. For example, a change in technology in the general environment resulted in the destruction of the typewriter industry.

Do organizations analyse their internal and external environments and then develop a strategy based upon this analysis and in line with their values? Or do they develop a strategy based upon experience and resources contained within the firm and then seek to exploit or leverage this within their external environment? This is an interesting question that has provoked much debate within strategic management. On the one hand is the positioning school (Henderson 1989), which is characterized by the work of Harvard professor Michael Porter. This is often referred to as strategic fit or an 'outside-in' approach to strategic management. On the other hand is the resource-based view that has come to be associated with Gary Hamel and C.K. Prahalad. This debate will be addressed in detail in **Chapters 3 and 5**.



Summary

In addressing what strategy is, we have looked at different perspectives and a number of different authors. These different perspectives will be evaluated more fully as we assess differential firm performance in later chapters. The strategic management process covers strategy analysis, formulation, and implementation. However, we might reiterate that this linear approach, although highly useful in explaining the discipline of strategy, may not fully capture how strategy occurs in reality. This is not to demean its usefulness since all organizations need to undertake analysis before they are ready to take decisions. It is more to open up thinking about the different ways in which strategy formulation occurs; whether deliberately or emerging.

A vision is often associated with the leader of an organization and represents a desired state that the organization aspires to achieve in the future. In contrast with goals and objectives, a vision does not change over time. To be effective, a vision should tap into the personal values of employees. A mission seeks to answer the question as to why an organization exists. A mission statement is a way in which the organization communicates the business it is in to the outside world. A mission statement needs to appeal to a broad spectrum of stakeholders if all these stakeholders are to accept it. The

research of Collins and Porras into visionary organizations shows the importance of an organization's core ideology. This comprises core values and purpose. Core values are an organization's essential and enduring tenets which will not be compromised for financial expediency and short-term gains. Purpose represents the reasons an organization exists beyond making a profit.

Organizations encounter difficulties when the assumptions on which they are built and the basis on which they are being run no longer fit reality. Drucker refers to this as a company's *theory of business*. The reason many large corporations are no longer successful is that their theory of business no longer works.

This chapter has introduced the reader to some of the complexities that emanate from a study of strategic management. There are conflicting and competing definitions. There is disagreement over how strategy is formulated, which gives rise to competing perspectives. This should not be seen as an insurmountable issue since any discipline as young as strategic management will inevitably be concerned with the exactitude of its terminology and the rigour of its modus operandi. What we have tried to show is that, in and amongst all this ambiguity, there is common ground and clarity of thought and expression. The fact that different perspectives exist at all is simply part of the dynamic nature of strategic management.

The purpose of organizations has also been discussed. This will be more fully evaluated in **Chapter 12** on corporate governance.

Review Questions

1. How might knowledge of deliberate and emergent strategies help managers when thinking about strategy?
2. Comment on Drucker's assertion that many large organizations are failing because their theory of business does not fit with reality.

Discussion Question

Vision and mission statements are a passing fad with no real links with an organization's strategy. Discuss.

Research Topic

Identify organizations whose success seems to derive from emergent strategies rather than a conscious effort on the part of their senior managers.

Recommended Reading

- **Porter, M.E.** (1996). What is strategy? *Harvard Business Review*, **74**(6), 61–78.

For an insight into the debate on deliberate and emergent strategies see:

- **Pascale, R.T.** (1984). Perspectives on strategy: the real story behind Honda's success. *California Management Review*, **26**(3), 47–72.
- **Mintzberg, H.** (1990). The design school: reconsidering the basic premises of strategic management. *Strategic Management Journal*, **11**(3), 171–95.
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- **Mintzberg, H.** (1996). Learning 1, Planning 0. *California Management Review*, **38**(4), 92–3.

For a discussion of the importance of core ideology to visionary organizations and the place of BHAGs in stimulating progress see:

- **Collins, J.** and **Porras, J.I.** (1994). *Built to Last: Successful Habit of Visionary Companies*. Harper, New York.

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Test your understanding of this chapter with online questions and answers, explore the subject further through web exercises, and use the weblinks and journal abstracts to provide a quick resource for further research.



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PART 1 CASE STUDY

Laura Ashley



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Laura Ashley's folksy, flowery patterns sum up 1970s English fashion.

Last week, Laura Ashley, the retailer whose folksy, flowery patterns sum up 1970s English fashion, reported one of the strongest Christmas trading performances in the retail sector. At a time when traditional retailers are supposed to be suffering at the hands of supermarkets and internet retailers, Laura Ashley is a rare success story. It really shouldn't be like this. The quintessentially British company has been through 11 chief executives in the last 14 years, it is majority-owned by a Malaysian conglomerate, and the billowy iconic style it is best known for went out of favour decades ago.

However, somehow Laura Ashley has transformed itself. Shares have doubled since early 2006, and profits for the year to the end of this month are expected to be double the £6 million reported last year. Last week the company paid its first interim dividend since 1996. Like-for-like sales for the year to date are up 8.7 per cent. It is boom time at Laura Ashley. Analysts think its success is here to stay. 'I don't think it is a flash in the pan. The strategy they are employing is a good one', says Rob Brent, an analyst at Peel Hunt.

It has been a long and rocky journey for Laura Ashley, whose eponymous founder was a mixture between Beatrix Potter and Marjorie Scardino, the chief executive of Pearson. The company was a British success story for decades, until tragedy, management arrogance, and changing trends nearly wiped it out completely. 'It was, up until the 1980s, a family-run niche retailer with a good culture, it was iconic and pretty focused. It was really very effective, but then success went to its head and it tried to play on a bigger stage than it should', says a former board member. For the first half of its existence, Laura Ashley was the ultimate cottage industry made good.

In the 1950s, Laura Ashley and husband Bernard started to produce headscarves, tablemats, and napkins on the kitchen table of their flat in Pimlico. The breakthrough came in 1966, when Laura Ashley produced its first dress for social occasions rather than for work around the house. Between 1970 and 1975 annual sales grew from £300 000 to £5 million and the company opened stores across the UK. It also opened concessions in department stores in Australia, Canada, and Japan, and outlets in Paris and San Francisco. By 1979 sales were £25 million.

In the early 1980s, Laura Ashley peaked as the epitome of cosy Britishness. 'Laura Ashley started from such an honest beginning and remained true for a long time. It was English kitchen table. In the 1980s it tapped right into that Sloane Ranger scene, where the whole British scene was about pretty prints and soft romance, on the back of the Lady Diana wave. It just hit it right with fashion', says Tamasin Doe, fashion director of *In Style*, the fashion magazine. But just as the business was about to make a major step change in its growth, disaster struck. While staying at the Cotswolds home of one of her children on her 60th birthday in 1985, Laura fell down the stairs. She fell into a coma and died 10 days later in a Coventry hospital.

Despite the tragedy Bernard ploughed on. Two months after Laura's death the company floated in London with a value of around £200 million. But it was shortly after this that problems set in—problems that would beset the company for the best part of 20 years. Fashions were changing; the formality of the previous decade was replaced by a new casualness. 'Laura Ashley was completely left behind. It didn't adapt. It did what many companies do in those circumstances and seized up. It became more and more classic until it was so classic that it became an octogenarian style', says Doe. Hopes that Laura Ashley's woes could be fixed were given a boost in 1995 by the appointment of Ann Iverson, a feisty American with a reputation for shooting from the hip, as chief executive.

Iverson should have retrenched Laura Ashley and returned it to its roots. But she did the exact opposite. She expanded Laura Ashley overseas and tried to appeal to younger customers in the UK. The most ambitious part of her strategy was launching 30 huge flagship stores in the US. The trouble was, there was not enough product to fill them. 'The US was Ann's big folly. She rolled out a bunch of 25 000 sq ft stores with high rents. The stores themselves were five times too big for the product catalogue', says a former senior director. Iverson was sacked in 1997 and a rescue team put in. This team, which included a finance director called Richard Pennycook, now FD of the supermarket William Morrison, had the tricky brief of sorting the chain out. 'It was a mess. When Ann left this was a business with £350 million of turnover but was operating in 30 countries. It was manufacturing, retailing, franchising, licensing. A total mess', says a former executive.

It was at this time that Laura Ashley was thrown a lifeline by its current largest shareholder, Malayan United Industries (MUI), the Malaysian conglomerate chaired by Dr Khoo Kay Peng. The company bought 40 per cent of the chain. Dr Khoo also bought a large stake personally through a company called Bonham Industries. As part of its purchase MUI appointed four new board directors. The following year Laura Ashley sold its 100 US stores to their management for \$1. MUI gave the company the stability that it desperately needed. It also started to implement a sensible long-term strategy for the chain. However, there has been a revolving door of management along the way.

David Cook, Laura Ashley's finance director, declines to comment on the 11 CEOs over the last 14 years. 'I'd really rather focus on driving the business forward', he says. Executives talk of an inevitable clash of cultures when a Far Eastern conglomerate takes over a slightly twee English chain. However, Laura Ashley is now firing on all cylinders. The biggest move over recent years has been the huge growth of the homewares and furniture business, and the relative shrinking of the clothing side. In the UK, where Laura Ashley has 180 stores, home-related products now account for 80 per cent of sales, while clothing accounts for just 20 per cent. Just five years ago, clothing accounted for more than 50 per cent of the sales. This move has been applauded. 'The demand for Laura Ashley home furnishings is there. It is good quality middle-market product, and that area of the market is devoid of good quality household goods. Marks & Spencer largely pulled out of it, so where do you go? Big department stores are the only option', says Peel Hunt's Brent.

Interiors experts say that Laura Ashley has the 'shabby chic' appeal that is fashionable now. Its chandeliers are one of this season's must-have items among London's media fashionistas. Cook says that elements of the market do not appreciate that the company is now much more of a homeware retailer than a fashion one. 'The perception is that Laura Ashley is very much a fashion brand and within that we focus very much on florals. It is very hard to change those perceptions that people have', says Cook.

Laura Ashley has also relocated its poorer performing stores from prime sites on high streets to larger off-pitch stores. The move is part of a deliberate strategy to

save money and make Laura Ashley a 'destination' store. It seems to be working. 'We have a very loyal customer base who are well aware of what we do. The challenge is building on it', says Cook, who promises an 'aggressive' store opening programme. The company also has a strong overseas following through 200 franchised stores. Blogs from foreign customers view the chain as a nostalgic slice of England. Some bloggers talk about 'the smell from long-ago Europe' that apparently infuses every store. It is no surprise that 70 per cent of sales overseas come from the fashion, rather than the homeware ranges.

In Style's Doe says that the retailer's current fashion ranges have plundered its rich heritage. 'They are absolutely straight back to the 1960s and 1970s. It is back to the kitchen table with Laura Ashley, which taps into the current fashion. It is very on trend', she says. The retro English print look is also evident by the success of upmarket designers such as Cath Kidston. Through folky beginnings, tragedy, failed attempts at global domination, and incongruous owners, Laura Ashley has become one of the most unlikely business success stories of 2007.

Source: 'Not just a pretty dress' *Sunday Telegraph*, 21 January 2007

Questions

1. To what extent did Laura Ashley's *theory of business* under Ann Iverson represent a fit with reality?
2. Comment on whether Laura Ashley's strategy in the past has been more emergent than deliberate.
3. How is Laura Ashley's theory of business being continually tested?