Session 10

5.4. Strategy and Policies

Because business policy research has primarily been a series of inductive generalizations of case studies; theories have been typically ambiguous and untested, and have not progressed swiftly. Deductive theorizing, by contrast, yields clear, often non-obvious conclusions that can be debated effectively and generalized slowly; so realism of current models can be sacrificed for progress towards realistic future models. Deductive theorizing, with more attention to a game-theoretic definition of equilibrium and to recent ideas from economics, should be one new direction for policy research. Of course, these deductive models will inevitably draw their inspiration from the richness of careful observation and exhaustive checklist-making that are the hallmarks of induction. Specific avenues for new research are described, and the importance of teaching non-obvious theories is defended.

Businesses need to implement sound strategies to succeed. Those strategies form part of an overall management and business policy that guides the business in connecting with customers, generating profits and managing resources. The related concepts of strategic management and business policy are keys to help small business owners manage their responsibilities and set clear objectives.

Strategic Management

Strategic management represents a theoretical concept first introduced by Peter Drucker in the mid-20th century. The idea behind strategic management is that organizations will be better equipped to meet their goals and objectives if the owners and managers adopt a clear business philosophy. For many businesses, that philosophy will be to increase their share of the market. For others, it might be about making a difference in the community or about developing new products. Sometimes, a combination of motives drives the management's strategy. In any case, strategic management helps the business to keep its sights set on what matters most and to not get distracted by ancillary concerns.

Business Policy

The generic term business policy refers to all of an organization's processes and procedures. This can range from human resources policies to the company's marketing agenda and its plans for growth and development. Business policy is closely related to strategic management because the policies are essentially the strategies put into action. If the strategy calls for an increased market share, for instance, the business policies would be constructed to match this strategy. The two terms are so closely intertwined that they are often use interchangeably. Policies become strategies and vice versa. The important thing for a business owner to keep clear is that strategic management is a mind-set or philosophy for doing business, but business policies are the specific methods for running the organization on a day-to-day business.

Setting Objectives

Strategic management and business policy both rely on the basic notion of setting objectives that are "SMART" -- an acronym representing specific, measurable, attainable, realistic and time-bound goals. In the context of owning a business, setting SMART goals means specifically detailing what the goals are about and what they are intended to do. For example, a goal to "sell more products" means little unless details are added to the goal statement. A goal might be: "sell 25 percent more of the product within the next 30 days by targeting new customers." This goal is clear and concise and it helps the business owner to manage all of the policies and strategies necessary to enact that objective.

Following Through

Goals and objectives mean little in the organization if there is no follow-through. Effective strategic management and coherent business policy depends on the enactment of objectives in a timely and responsible manner. This involves, above all else, clear communication of those objectives to all the concerned parties. If the business has decided to increase revenue by 5 percent during the next quarter, for instance, it needs to clearly delineate to its staff and managers how this goal will be accomplished and what is required of them in order to accomplish it. This sets the bar for excellence in the organization and gives business owners a benchmark against which to judge performance.

5.5. From competitive advantage to corporate strategy

Corporate strategy, the overall plan for a diversified company, is both the darling and the stepchild of contemporary management practice—the darling because CEOs have been obsessed with diversification since the early 1960s, the stepchild because almost no consensus exists about what corporate strategy is, much less about how a company should formulate it.

A diversified company has two levels of strategy: business unit (or competitive) strategy and corporate (or companywide) strategy. Competitive strategy concerns how to create competitive advantage in each of the businesses in which a company competes. Corporate strategy concerns two different questions: what businesses the corporation should be in and how the corporate office should manage the array of business units.

Corporate strategy is what makes the corporate whole add up to more than the sum of its business unit parts. The track record of corporate strategies has been dismal. I studied the diversification records of 33 large, prestigious U.S. companies over the 1950–1986 periods and found that most of them had divested many more acquisitions than they had kept. The corporate strategies of most companies have dissipated instead of created shareholder value.

The need to rethink corporate strategy could hardly be more urgent. By taking over companies and breaking them up, corporate raiders thrive on failed corporate strategy. Fueled by junk bond financing and growing acceptability, raiders can expose any company to takeover, no matter how large or blue chip.

Recognizing past diversification mistakes, some companies have initiated large-scale restructuring programs. Others have done nothing at all. Whatever the response, the strategic questions persist. Those who have restructured must decide what to do next to avoid repeating the past; those who have done nothing must awake to their vulnerability. To survive, companies must understand what good corporate strategy is.

5.6. The 5 factors of a strategy alliance

Share on email Email Share on twitter Share on Twitter Share on Facebook Post to Facebook Share on LinkedIn Share on LinkedIn Share on delicious Save to Delicious Share on instapaperSave to Instapaper “Strategic” may be one of the most over-used words in business today. This observation is especially valid in the world of alliances, where managers must distinguish between those alliances that are merely conventional and those that are truly strategic. This author outlines the five factors that make an alliance “strategic.”

As companies gain experience in building alliances, they often find their portfolios ballooning with partnerships. While these partnerships may contribute value to the firm, not all alliances are in fact strategic to an organization. This is a critical point, since, as this article will explain, those alliances that are truly strategic must be identified clearly and managed differently than more conventional business relationships.

Due to the levels of organizational commitment and investment required, not all partner relationships can be given the same degree of attention as truly strategic alliances. The impact of mismanaging a strategic alliance or permitting it to fall apart can materially impact the firm’s ability to achieve its core business objectives.

What is it that makes an alliance truly strategic to a particular company? Is it possible for an alliance to be strategic to only one of the parties in a relationship? Many alliances default to some form of revenue generation—which is certainly important— but revenue alone may not be truly strategic to the objectives of the business. There are five general criteria that differentiate strategic alliances from conventional alliances. An alliance meeting any one of these criteria is strategic and should be managed accordingly.

1. Critical to the success of a core business goal or objective.

2. Critical to the development or maintenance of a core competency or other source of competitive advantage.

3. Blocks a competitive threat.

4. Creates or maintains strategic choices for the firm.

5. Mitigates a significant risk to the business.

The essential issue when developing a strategic alliance is to understand which of these criteria the other party views as strategic. If either partner misunderstands the other’s expectation of the alliance, it is likely to fall apart. For example, if one partner believes the other is looking for revenue generation to achieve a core business goal, when in reality the objective is to keep a strategic option open, the alliance is not likely to survive.

Examining each of the five strategic criteria in depth provides insight into how the strategic value of alliances can be leveraged.

1. Critical to a business objective

While the most common type of alliance generates revenue through a joint go-to-market approach, not every alliance that produces revenue is strategic. For example, consider the impact on revenue objectives if the relationship were terminated? Clearly, a truly strategic relationship would have a great bearing on the prospects for achieving revenue growth targets.

In addition to a single strategic alliance, related groupings of alliances—networks or constellations—may also be critical to a business objective. Sun Microsystems has established a group of integrator alliances that function as an effective marketing channel and drive significant revenues for the company each quarter.

This category also includes alliances with high potential, such as alliances that have large but unrealized revenue opportunity. Consider the impact of new industry standards that make it possible for products from different manufacturers to work together. This can unlock customer value and boost the revenue potential of new, technology-based products. From writable DVD formats to next-generation wireless technologies, technical standards are democratically determined in consortiums of interested industry participants. With product development racing in parallel, the first mover's advantage can be substantial, and hence alliance development and lobbying within an industry become paramount to financial success.

Cost reduction may also be a core business objective of the alliance, particularly among supply-side partners. By investing together in new processes, technologies and standards, alliance partners can obtain substantial cost savings in their internal operations. Again, however, a cost-saving alliance is not truly strategic unless it has an underlying business objective, such as "to achieve an industry-leading cost structure."

2. Critical to the development or maintenance of a core competency or other source of competitive advantage.

Another way in which an alliance can prove to be strategic is to play a key role in developing or protecting a firm's competitive advantage or core competency. Learning alliances are the most common form of competitive/competency strategic alliances. An organization's need to build incremental skills in an area of importance is often accelerated with the help of an experienced partner. In some cases, the learning objective of the relationship is openly agreed between the partners; however, this is not always the case. Learning alliances work best when:

a) The objectives are openly shared

b) There is little chance of future competition (such as when the partners are in adjacent industries)

c) The cultures of the organizations are similar enough to enable process and methods to be leveraged, and

d) The governance structure of the alliances is established to promote learning at the executive, managerial and operational levels.

3. Blocking a competitive threat

An alliance can be strategic even when it falls short of establishing a competitive advantage. Consider the case of an alliance that blocks a competitive threat. It is strategic to bring competitive parity to a secondary segment of a market in which the firm competes, when the absence of parity creates a competitive disadvantage in the related primary segments of that market. For example, competing in the high and medium price range of a market with a premium product may leave the firm vulnerable to a low-priced entry. If the firm's manufacturing processes do not permit the creation of a low-priced product entry, a strategic alliance with a volume partner in an adjacent market can successfully block the competitive threat.

Another example of strategic alliances that block competitive threats is the airline alliances that permit route-sharing among carriers. The two primary determinants of customer flight selection are routing and cost. Therefore, the adoption of route-sharing alliances by the airlines blocks the competitive threat of preferential routing in the specific markets in which the airline chooses to compete. In essence, strategic alliances within the airline industry ensure competitive parity with respect to routing and force other factors such as on-time departures and customer service to become the bases for competitive differentiation.

4. Creates or maintains strategic choices for the firm

From a longer-term perspective, an alliance that is not fundamental to achieving a business objective today could become critical in the future. For example, in 1984, a U.S. consumer products company needed to expand distribution beyond the Midwestern states. Faced with the prospect of European competition at some point in the future, the firm made a strategic decision to invest in an alliance with a distribution and support services company that had incremental distribution capacity in the U.S. and a similar presence in Europe, rather than invest in expanding its own local distribution capabilities. With the option to expand into European distribution at any point, the firm could work to sew up the U.S. market before expanding too quickly internationally.

5. Mitigates a significant risk to the business.

When an alliance is driven by intent to mitigate significant risk to an underlying business objective, the nature of the risk and its potential impact on the underlying business objective are the key determinants of whether or not it is truly strategic. Dual sourcing strategies for critical production components or processes are excellent examples of how risk mitigation can become the context for supply-side strategic alliances.

As process manufacturing companies advance the yield of their operations, suppliers often collaborate with the manufacturer to ensure their new products fit within its new operations. The benefits of such an alliance are cost savings to the manufacturer and accelerated product development for the supplier. In situations where the supplier's product is critical to the manufacturer's operation, it may be necessary for the manufacturer to have strategic alliances with two competing suppliers in order to mitigate such risks as unilateral cost increases or degradation in quality of service.

Joint ventures and minority equity investments

Among relationship commitments, joint ventures and equity investments are closest to the strategic end of the spectrum. However, investing a large sum of money in a partner does not automatically make the relationship strategic. One needs only to survey the wreckage of the dot-com era for proof of failed minority equity investments in alliances. It may be economically sound to invest $1 million in a distribution relationship that is projected to return $1.5 million in incremental sales the following year. This would not necessarily be strategic to a firm with $800 million in annual sales, unless the alliance also served an alternate purpose that met one of the five strategic criteria. For example, if the achievement of a core business objective, such as access to a new market, were enabled by the investment, then it would be strategic to the firm.

Management

How, then, should strategic alliances be managed differently than traditional alliances? There are countless lists of reasons why alliances fail. However, aside from ensuring “sound strategic alignment” between the partners, most determinants of failure are less than strategic in nature.

Lack of executive sponsorship is often a source of alliance failure. With strategic alliances, the key to effective executive sponsorship is visibility and accountability. Since failed alliances can directly impact a business in a meaningful way, or even have adverse implications for the executive’s own financial bonus or prestige, he has a strong incentive to consider the strategic alliance as important as his other primary responsibilities.

Metrics determine just how the alliance and accountable executives are kept on track. While clear metrics are required of any alliance, shared metrics between the partners are absolutely critical to the success of a strategic alliance. Shared metrics bring immediate alignment of focus between the parties, and when executive sponsors are held accountable for the shared metrics, the two firms become aligned as one.

Poor alliance governance structures are another common source of alliance failure. Strategic alliances are best served by formalized governance structures with clear mandates that are directly linked to the shared metrics underpinning the partnership. At Hewlett-Packard we often create strategic alliance executive committees using an “N by N” mapping of key HP executives to their counterparts at the alliance partner. The number ("N") and position of the executives participating in the review meetings—usually on a quarterly basis—is tailored to the specifics of each strategic alliance. The attending executives represent the business unit(s) and core functions that are critical to execution of the strategic alliance.

Regular meetings of executives from the partner companies continue the relationship building that begins while formulating and negotiating the terms of the strategic alliance. Trust is perhaps the foundation of a strategic alliance and these relationships are the building blocks for establishing trust amongst the individuals who represent the two parties in the strategic alliance.

The real reason that most alliances fail is the constant change in the business environment. Trust allows the parties in a strategic alliance to have the difficult discussions that will transform the alliance over time and give it longevity. When corporate strategies change as a result of a changing business environment, the assumptions upon which the strategic alliance was originally based also change. What was once a strategic investment may no longer remain strategic without modification to the terms of the alliance? In the most extreme cases, the trust built between the two companies enables the adaptability—even renegotiation of the financial terms—to accommodate changes in market or other conditions that impact one of the partners.

Strategic alliance organizations are feeling increased pressure. As critical personnel become stretched and financial resources become scarce, strategic alliance organizations must allocate their resources in the most efficient manner possible so that truly strategic alliances can support and accelerate the strategy of the business. The five strategic criteria outlined in this article are primary determinants of the strategic value of an alliance. Using these criteria to identify genuine strategic alliances in the portfolio today and as a guide for developing future strategic alliances are the first steps to improving the impact of an alliance organization. The management principles, also described above, are the next steps towards improving the effectiveness of the strategic alliances themselves.