Unit 12 Strategic Options

Concepts of Strategic Options:

Strategic options are creative alternative action-oriented responses to the external situation that an organization (or group of organizations) faces. Strategic options take advantage of facts and actors, trends, opportunities and threat of the outside world.

Strategic options can be identified after an institutional assessment, keeping in mind the aspirations (basic question) of an organization. The tool ‘Strategic options’ helps to identify and make a preliminary screening of alternative strategic options or perspectives.

Corporate level strategy:

Strategic Alternative at Corporate Level (Grand Strategies): Corporate or Grand strategies are the decisions or choices of long term plans from available alternatives. Grand strategies also called as master or corporate strategy. It is based on analysis of internal and external environment. This directs the organization towards achievement of overall long term objectives (strategic intent).

Corporate level strategy is concerned with overall purpose and scope of an organization and how value will be added to the different parts (business units) of the organization. (Johnson and Scholes).

Corporate level strategy addresses the question as “what business are we in? It is related to the acquisition of new business, addition or divestments of business units, plants or product lines and joint ventures with other companies in new areas etc.

Strategic Alternatives at Corporate level: The different strategic options/alternatives at corporate level are as follows:

1. **Stability Strategy**: Keeping the organization where it is……..

2. **Growth Strategy**: Moving the organization ahead ………

3. **Retrenchment Strategy**: Reversing the organization’s weaknesses or decline………. 
1. **Stability Strategy**: A strategy where the organization maintains its current size and current level of business operations. Stability strategy does not mean do nothing nor are goals such as profit growth abandoned. It means, to increase profit through improving efficiency in current operations.

**When stability strategy is suitable to adopt:**

a. This strategy is pursued in a relatively stable environment.

b. Organization is the market leader.

c. The product is at the maturity stage in the product life cycle.

d. Its main strategic decision focus on incremental improvement of functional performance.

e. Industry is facing slow or no growth opportunities.

f. When product is in maturity stage.

**Types of strategic alternatives/options under stability strategy:**

i. Pause/Proceed with caution strategy: This strategy is taken as a rest before continuing a growth or retrenchment strategy. It is a deliberate attempt to make only incremental improvements until a particular environmental situation changes.

ii. No change Strategy: This strategy is adopted when environment is perceived as stable, with few threats to cause problems or few opportunities the firm wishes to take advantage.

iii. Profit Strategy: This is an attempt to artificially support profits when a company’s sales are declining by reducing investment and short-term discretionary expenditures.

**Advantages and disadvantages of Stability Strategy:**

**Advantages:**

i. It is less risky.

ii. Implementation is relatively simple, since it does not demand fundamental change.

iii. It aims to bring efficiency to maintain current profit and growth.
iv. Suitable if growth strategy is risky to pursue.

**Disadvantages:**

i. Organization may lose opportunities created by change in external environment.

ii. May not able to address the expectation of the shareholder.

iii. Market share may decline due to expansion of competitors.

2. **Growth Strategy:** It involves the attainment of specific growth objectives by increasing the level of a firm’s operations. An organization can grow internally expanding its operations or it can grow externally through merger, acquisitions and strategic alliances.

**Purposes behind Growth Strategy:**

- Increase in sales revenues
- Increase in earnings or profits
- Other performance measures
- Increasing clients served or patrons attracted
- Broadening the geographic area
- Increasing programs offered

**Types of Strategic options under growth Strategy:**

i. **Concentration Strategy:** A growth strategy where the firm concentrates on its primary line of business. It looks for ways to meet its growth objectives through increasing its level of operation in this primary business. It directs all its resources to the profitable growth of a single product, in a single market with a single dominant technology. Two basic concentration strategies are vertical integration and horizontal integration.

   - **Vertical Integration:** When a company expands its business into areas that are at different points on the same production path, such as when a manufacturer owns its supplier (Backward integration) and/or distributor (Forward Integration).
     
     Vertical integration can help companies reduce costs and improve efficiency by decreasing transportation expenses and reducing turnaround time, among other advantages. However, sometimes it is more effective for a company to rely on the expertise and economies of scale of other vendors rather than be vertically integrated.

   - **Horizontal Integration:** The acquisition of additional business activities that are at the same level of the value chain in similar or different industries. This can be achieved by internal or
external expansion. Because the different firms are involved in the same stage of production, horizontal integration allows them to share resources at that level. Expanding the firm's operations through combining with competitors operating in the same industry & doing the same things.

ii. Diversification Strategy: A risk reduction strategy that involves adding product, services, location, customers and market to company’s portfolio.
   - Concentric (Related) Diversification: concentric diversification strategy allows a company to add similar products to an already successful line of business. For example, a computer manufacturer that produces personal computers begins to produce laptop computers. The technical knowledge necessary to accomplish the new task comes from its current field of skilled employees.
   - Conglomerate (unrelated) Diversification: It is related to Diversifying into completely different industry from the firm’s current operations. When companies engage in conglomerate diversification strategies, they are often looking to enter a previously untapped market. Companies can do this by purchasing or merging with another company in the desired industry. Moving into a totally unrelated industry is often highly dangerous; as the company’s current management is unfamiliar with the new industry.

Advantages and Disadvantages of Growth Strategy:

Advantages:

i. Market power of the organization increase due to growth of product and market.

ii. It ensures strategic advantage to the organization through high production and long experience.

iii. High degree of profit potential from the untapped market.

iv. Suitable for highly competitive and dynamic markets.

Disadvantages:

i. Focusing other product lines and market may deplete the current product lines productivity.
ii. In absence of knowledge of product market, growth strategy may be high risky.

iii. May not fulfill growth requirement from current available resources and competencies.

3. **Retrenchment Strategy:** Retrenchment strategy is a strategy used by corporate in order to reduce the diversity or to cut the overall size of the operations of the company. This strategy is often used to cut down expenses with the goal of becoming more financially stable business. Typically the strategy involves withdrawing from certain markets or the discontinuation of selling certain products or services in order to make a beneficial turn around.

**Types of Strategic options under retrenchment strategy:**

i. **Turnaround strategy:** This strategy focuses on regrouping and restructuring the organizational functioning to reduce cost & asset to reverse declining sales.

ii. **Divesture:** The partial or full disposal of a business unit through sale, exchange, closure or bankruptcy. Divestiture may result from a management decision to no longer operate a business unit because it is not part of a core competency. It may also occur if a business unit is deemed redundant (unnecessary) after a merger or acquisition.

iii. **Liquidation:** A liquidation strategy involves selling a company, in its entirety or in parts, for the value of its assets. Many small business owners exit their businesses through liquidation. This strategy is mostly adopted by companies in distress. To make any money with such an exit strategy, the business should have valuable assets to sell, such as land or expensive equipment, and profits from selling assets have to go to pay creditors first. The selling under this strategy is not as a going concern but in salvage value to escape further hardship.

**Advantages and Disadvantages of retrenchment strategy:**

**Advantages:**

i. Suitable for highly uncertain business environment.

ii. It is helpful in securing the organization from deep crisis.

iii. Restructuring under retrenchment may revitalize the organization and may lead to achieving higher productivity.

**Disadvantages:**

i. Gives the organization a sense of failure.

ii. Ineffective to meet the customer demands.

iii. Employees and management may fear of losing jobs and may not show expected behaviors in the jobs.
iv. Depreciate public image

4. **Combination strategy:** Combination grand strategy is followed when an organization adopts a mixture of stability, expansion and retrenchment, either at the same time, in its different business or at the different time in the same business with the aim of improving its performances. The organization has several strategy business units (SBU). It simultaneously uses combinations of stability, expansion and retrenchment strategies to different parts of the organization. Old products, markets and functions are continued, dropped and expanded. Product lifecycles are in different stages. The aim is to improve performance. The combination can be simultaneous sequential or both.

**Business Level Strategy:** Business level strategy attempts to gain competitive advantage by exploiting core competences in specific product market. The main objectives of business strategies are:

- To fulfill customer needs and attract them.
- To reduce competitive pressure
- To enhance market position by increasing market share.

The different strategic alternatives available at business level may be studied in two ways.

1. Porter’s Competitive Strategies
2. Strategic Clock Oriented Market based Generic Strategies.

1. **Porter’s Generic/Competitive Strategies:** Porter’s Generic Strategies is a frameworks used to outline the three major strategic options open to organizations that wish to achieve a sustainable competitive advantage. Each of the three options needs to be considered within the context of two aspects of the competitive environment. Firstly, the sources of competitive advantage which establish whether the products are differentiated in any way, or if they are the lowest cost producer in the industry. Secondly, the competitive scope of the market determines if the company targets a wide market or if it focuses on a very narrow niche market.

a. **Low Cost Strategy:** In cost leadership, a firm sets out to become the low cost producer in its industry. The sources of cost advantage are varied and depend on the structure of the industry. They may include the pursuit of economies of scale, proprietary technology, preferential access to raw materials and other factors. A low cost producer must find and exploit all sources of cost advantage. If a firm can achieve and sustain overall cost
leadership, then it will be an above average performer in its industry, provided it can command prices at or near the industry average.

**Ways of Reducing Costs: There are two ways to reduce cost**

i. **Controlling Cost Drivers**
   - Economics of scale
   - Experience
   - Cost key resources (strong bargaining power)
   - Resource sharing
   - Outsourcing
   - Capacity utilization
   - Being first mover (introducing new product)
   - Integration (forward and backward)

ii. **Revamping (improving) Value Chain:**
   - Make greater use of Internet technology application.
   - Use direct-to-end-user sales marketing methods.
   - Simplify product design
   - Offer basic, no frills (unnecessary) product/services
   - Shift to a simpler, less capital-intensive or more flexible technological process
   - Find the way to bypass use of high-cost raw materials
   - Relocate facilities closer to suppliers or customers.
   - Drop “something for everyone” approach and focus on a limited product/service.

**Conditions for the best use of low cost strategies:**

- High price competition
- Identical products and sufficient suppliers
- Price sensitive customers
- Low switching cost
- Most buyers use the product in the same way
- Bargaining power of buyer
- New entrants with low introductory price

b. **Differentiation Strategy:** In a differentiation strategy a firm seeks to be unique in its industry along some dimensions that are widely valued by buyers. It selects one or more attributes that many buyers in an industry perceive as important, and uniquely positions it-self to meet those needs. It is rewarded for its uniqueness with a premium price. *The downside to this*
strategy is that these unique features will eventually be copied by the competition or customers could change their tastes and options, so there is a constant pressure to innovate and continuously improve.

Basis of Differentiation

- **Product parameters**: Size, shape, design, quality performance
- **Services back-up**: delivery, installation, repairs, training etc.
- **Personnel**: Better and experienced personnel to serve customers.
- **Promotion**: Differentiating claims in promotion appeals.
- **Image**: Projecting organization or brand

Conditions for the best use of differentiation strategies:

i. Diverse buyers’ needs

ii. Different ways to differentiate

iii. Different approach followed by few rivals

iv. Fast technological change

v. Buyers’ are less price sensitive

c. **Focus Strategy**: The focus strategy applies to a narrow segment of a total market. Usually companies using this strategy have a reduced size, focus all their resources and efforts on a narrow and well defined segment of market, and have the advantage of a high degree of customer loyalty. They can therefore pass higher costs on to their customers because close substitute products or services are less likely to exist. Beauty Parlors, local bakeries & retail boutique are the examples of enterprises that serve narrow or local customer segments.

**The niche can be defined by:**

- Demographic characteristics (particular group of customers based on age, occupation, income etc.
- Geographical Uniqueness. (Tarai, Himal etc. people)
- Specialized requirements.
- Special product attributes

**The focus strategy has two variants.**

- In cost focus a firm seeks a cost advantage in its target segment,
- Differentiation focus a firm seeks differentiation in its target segment. *(Cost focus exploits differences in cost behavior in some...*
segments, while differentiation focus exploits the special needs of buyers in certain segments.)

**Conditions for the best use of focused strategies:**

- The customers are based in terms of unique tastes & preference and specialized requirements.
- The customers are willing to pay higher price or upscale (Higher class) buyers.
- Major competitors do not see the presence of niche as crucial to their own success.
- Target market for niche is big enough to be profitable.

**Strategic Clock Oriented Market based Strategies**

Bowman's Strategy Clock analyzes the competitive position of a company in comparison to the offerings of competitors. It was developed by Cliff Bowman and David Faulkner as an elaboration of the three Porter generic strategies.

It is important to understand how companies compete in the market place. It is a diagrammatic representation which shows the relationship between customer value and prices.
**Position 1: Low Price/Low Value**

Firms do not usually choose to compete in this category. This is the "bargain basement" bin and not a lot of companies want to be in this position. Rather it's a position they find themselves forced to compete in because their product lacks differentiated value. The only way to "make it" here is through cost effectively selling volume, and by continually attracting new customers. You won't be winning any customer loyalty contests, but you may be able to sustain yourself as long as you stay one step ahead of the consumer (we're not going to mention any names here!) Products are inferior but the prices are attractive enough to convince consumers to try them once.

**Position 2: Low Price**

Companies competing in this category are the low cost leaders. These are the companies that drive prices down to bare minimums, and they balance very low margins with very high volume. If low cost leaders have large enough volume or strong strategic reasons for their position, they can sustain this approach and become a powerful force in the market. If they don't, they can trigger price wars that only benefit consumers, as the prices are unsustainable over anything but the shortest of terms. Wal-Mart is a key example of a low price competitor that persuades suppliers to enter the low price arena with the promise of extremely high volumes.

**Position 3: Hybrid (moderate price/moderate differentiation)**

Hybrids are interesting companies. They offer products at a low cost, but offer products with a higher perceived value than those of other low cost competitors. Volume is an issue here but these companies build a reputation of offering fair prices for reasonable goods. Good examples of companies that pursue this strategy are discount department stores. The quality and value is good and the consumer is assured of reasonable prices. This combination builds customer loyalty.

**Position 4: Differentiation**

Companies that differentiate offer their customers high perceived-value. To be able to afford to do this they either increase their price and sustain themselves through higher margins, or they keep their prices low and seek greater market share.
Branding is important with differentiation strategies as it allows a company to become synonymous with quality as well as a price point. Nike is known for high quality and premium prices; Reebok is also a strong brand but it provides high value with a lower premium.

**Position 5: Focused Differentiation**

These are your designer products: High perceived value and high prices. Consumers will buy in this category based on perceived value alone. The product does not necessarily have to have any more real value, but the perception of value is enough to charge very large premiums. Think Gucci, Armani, Rolls Royce. clothes either cover you or they don't, and a car either gets you around the block or it doesn't. If you believe pulling up in your Rolls Royce Silver Shadow is worth 25 times more than in an economy Ford then you will pay the premium. Highly targeted markets and high margins are the ways these companies survive.

**Position 6: Increased Price/Standard Product**

Sometimes companies take a gamble and simply increase their prices without any increase to the value side of the equation. When the price increase is accepted, they enjoy higher profitability. When it isn't, their share of the market plummets, until they make an adjustment to their price or value. This strategy may work in the short term, but it is not a long-term proposition as an unjustified price premium will soon be discovered in a competitive market.

**Position 7: High Price/Low Value**

This is classic monopoly pricing, in a market where only one company offers the goods or service. As a monopolist, you don't have to be concerned about adding value because, if customers need what you offer, they will pay the price you set, period. Fortunately for consumers in a market economy, monopolies do not last very long, if they ever get started, and companies are forced to compete on a more level playing field.

**Position 8: Low Value/Standard Price**

Any company that pursues this type of strategy will lose market share. If you have a low value product, the only way you will sell it is on price. You can't sell day-old
bread at fresh prices. Mark it down a few cents, and suddenly you have a viable product. That is the nature of consumer behavior, and you will not get around it, no matter how hard you try.

*Positions 6, 7, and 8 are not viable competitive strategies in truly competitive marketplaces. Whenever price is greater than perceived value you have an uphill battle on your hands. There will always be competitors offering better quality products at lower prices so you have to have your value and price aligned correctly.*

**Direction for Strategy Development**

The BOD and planning division at the top provide direction for the development of corporate and other strategies. Top level management and other executives especially from the planning division are involved in developing strategic options. The bases for formulating long-term strategies are mainly dependent on the capability of a firm to build competencies, increase market share in new and existing markets with existing and new products etc.
1. **Protect and Build**: With this direction a firm has to compete in the market protecting or building on the current position. This is also known as stability or “no change” strategy through which a firm decides to make no deviation from the current level of activities and remain in the existing product and market. Different strategic options under this category are:
   i. **Consolidation**: It is concerned with protecting and strengthening the organization’s position in existing market with existing product. Under consolidation company could decide to combine its operation as a result of corporate restructuring.
   ii. **Market Penetration**: This is another strategy to gain a competitive advantage in existing market with existing products. It is possible through aggressive marketing tactics like trade discount, advertising, price reduction and package improvement.

2. **Product Development**: Product development strategy attempts to offer modified or new products in the existing market. It requires core competencies and research and development efforts.

3. **Market Development**: With this strategy a firm enters into the new market segment, territories using its competence in its existing products. This is one of the less risky and least costly grand strategies. A firm select market development strategy with a view to achieving growth in sales, profit etc by expanding its activities in national, regional and international markets.

4. **Diversification**: It refers to the strategy which takes the organization away from its present markets and its present products at the same time. It attempts to extend its current range of product offering or area of activity.

**Methods of Strategy Development**

1. **Internal Development**: The strategies are developed by building up an organization own resources and competencies. It is also called organic development. It is a slow process. It consists of developing internal strategic factors for strategic success. It is a strategy other than mergers, acquisitions, joint development and alliances. All these are the external approach to expansion whereas internal development strategy is an approach of internal expansion. Internal development has a number of particular advantages over acquisition or joint development. This strategy is quite appropriate for small companies which may not have the resources available for major investment. There are so many problems that are faced by the companies which are entering into external developments. Such as inability to find suitable company for mergers and acquisitions, and other organizational cultural and tradition problems. The company will develop and retain the core competencies upon
which the growth is based. Some of the types of internal development strategy are:

- Stable, Growth, Combination and Retrenchment strategies under corporate strategy
- Overall cost leadership, differentiation and focus strategies of organization under business level strategy

Consideration of internal development usually commences with an estimate of the best growth rate that the company can achieve. Value creating activities can be brought and there is no need to buy another company.

2. **Merger and Acquisition:** Merger and acquisition involve permanent ownership ties. Merger and acquisitions take the form of amalgamation or absorption. The need to keep up with the changing environment necessitate merger and acquisitions.

   i. **Merger:** It is own organization merging with another. It is combination of two or more than two organization into one. Negotiations are usually friendly because the merger is believed to be mutually beneficial. It can take the following forms:
      - **Horizontal Merger:** It is a combination of 2 or more similar firms engaged in similar types of production and marketing processes. (e.g. merger of 2 banks.)
      - **Vertical merger:** It is the combination of two or more firms which engaged to produce the complementary products (e.g. merger of sports shoe co. and leather shoe co.)
      - **Concentric merger:** It is the combination of two or more firms that are related to each other in terms of customer functions or customer groups (e.g. merger of noodles co. and biscuit co.)
      - **Conglomerate merger:** It is the combination of two or more firms that are unrelated to each other (e.g. merger of biscuit co. and textile co.)

   ii. **Acquisition:** It is one organization taking over another through purchase of shares or ownerships. The acquired organization generally keeps its separate identity.

      The reason behind the development of merger and acquisitions can be explained as: it allows the company to enter into the new product or market areas, since the rapid change in this area cannot meet the internal development. When a company lacks the resources or competencies to develop a strategy internally, the merger or acquisition takes place.

3. **Joint Development and Strategic Alliances:** Joint development is where two or more organization share resources and activities to develop a strategy. This
is a cooperative approach to strategy development. It is time bound and of a temporary nature. It takes the form of strategic alliances. Strategic alliance is a partnership tie up agreement between two or more organization to jointly achieve mutually beneficial strategic objectives. Resources capabilities and core competencies are combined to pursue mutual interests. It can be to develop/manufacture/distribute products. Strategic alliances have a limited life span.