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Formulation of Functional Strategy

Learning Objectives

- ◆ Understand how functional strategies are formulated.
- ◆ To have a fair idea about the role of marketing strategy in implementation.
- ◆ Learn different aspects of financial strategy.
- ◆ Know how to formulate production, logistics, human resource and other important functional strategies.

Most of the time, strategists should not be formulating strategy at all; they should be getting on with implementing strategies they already have.

Henry Mintzberg

1. Introduction

Once higher level corporate and business strategies are developed, management need to formulate and implement strategies for each functional area. Strategy of one functional area cannot be looked at in isolation. Different functional tasks of the business are interwoven together and how a strategy is synergised with other areas determines its effectiveness.

For effective implementation, strategists have to provide direction to functional managers regarding the plans and policies to be adopted. In fact, the effectiveness of strategic management depends critically on the manner in which strategies are implemented. Functional strategies provide details to business strategy & governs as to how key activities of the business are to be managed.

Functional strategies play two important roles. *Firstly*, they provide support to the overall business strategy. *Secondly*, they spell out as to how functional managers will work so as to ensure better performance in their respective functional areas.

Functional area strategy such as marketing, financial, production and human resource management are based on the functional capabilities of an organisation. For each functional area, first the major sub areas are identified and then for each of these sub functional areas,

content of functional strategies, important factors, and their importance in the process of strategy implementation are identified.

In terms of the levels of strategy formulation, functional strategies operate below the SBU or business-level strategies. Within functional strategies there might be several sub-functional areas. Functional strategies are made within the higher level strategies and guidelines therein that are set at higher levels of an organization. Functional managers need guidance from the business strategy in order to make decisions. Operational plans tell the functional managers what has to be done while policies state how the plans are to be implemented.

Major strategies need to be translated to lower levels to give holistic strategic direction to an organization. The reasons why functional strategies are needed can be enumerated as follows:

- ◆ The development of functional strategies is aimed at making the strategies-formulated at the top management level-practically feasible at the functional level.
- ◆ Functional strategies facilitate flow of strategic decisions to the different parts of an organization.
- ◆ They act as basis for controlling activities in the different functional areas of business.
- ◆ The time spent by functional managers in decision-making is reduced as plans lay down clearly what is to be done and policies provide the discretionary framework within which decisions need to be taken.
- ◆ Functional strategies help in bringing harmony and coordination as they remain part of major strategies.
- ◆ Similar situations occurring in different functional areas are handled in a consistent manner by the functional managers.

Thus, strategies need to be segregated into viable functional plans and policies that are compatible with each other. In this way, strategies can be implemented by the functional managers. Environmental factors relevant to each functional area have an impact on the choice of functional strategies. Organizational strategies affect the choice of functional strategies. However, the actual process of choice is influenced by objective as well as subjective factors. Functional strategies affect, and are affected by, the resource allocation decisions.

2. Marketing Strategy Formulation

Marketing is a social and managerial process by which individuals and groups obtain what they need and want through creating, offering and exchanging products of value with others.

Philip Kotler

Ordinary marketing is an activity performed by business organizations. However, it is not necessarily confined only to business enterprises. It is an activity that creates and sustains exchange relationships among those who are willing and able to buy and sell products,

5.3 Strategic Management

services, satisfaction and even ideas. In the present day for business, it is considered to be the activities related to identifying the needs of customers and taking such actions to satisfy them in return of some consideration. In marketing it is more important to do what is strategically right than what is immediately profitable.

The term marketing constitutes different processes, functions, exchanges and activities that create perceived value by satisfying needs of individuals. Marketing induces or helps in moving people closer to making a decision to purchase and facilitate a sale.

Marketing in recent decades has gained a lot of importance. It is an immediate cause and effect of rapid economic growth, globalization, technological upgradation, development of ever-increasing human needs and wants and increasing purchasing power.

A business organization faces countless marketing variables that affect the success or failure of strategy implementation. Some examples of marketing decisions that may require special attention are as follows:

1. The kind of distribution network to be used. Whether to use exclusive dealerships or multiple channels of distribution.
2. The amount and the extent of advertising. Whether to use heavy or light advertising. What should be the amount of advertising in print media, television or internet?
3. Whether to limit or enhance the share of business done with a single or a few customers?
4. Whether to be a price leader or a price follower?
5. Whether to offer a complete or limited warranty?
6. Whether to reward salespeople based on straight salary, straight commission, or on a combination of salary/commission?

2.1 Delivering value to Customer

Marketing alone cannot produce superior value for the consumer. It needs to work in coordination with other departments to accomplish this. Marketing acts as part of the organizational chain of activities. Marketers are challenged to find ways to get all departments to think with focus on customer. In its search for competitive advantage, the firm needs to look beyond its own chain of activities and into the chains of its suppliers, distributors, and ultimately customers. This "partnering" will produce a value delivery network.



Figure 5.1: Value Delivery Network

Connecting with consumers: To succeed in today's competitive marketplace, companies must be customer centred. They must win customers from competitors and keep them by delivering greater value. Since companies cannot satisfy all consumers in a given market, they must divide up the total market (**market segmentation**), choose the best segments (**market targeting**), and design strategies for profitably serving chosen segments better than the competition (**market positioning**).

2.2 The Marketing Process

- ◆ Once the strategic plan has defined the company's overall mission and objectives, marketing plays a role in carrying out these objectives.
- ◆ The **marketing process** is the process of analyzing market opportunities, selecting target markets, developing the marketing mix, and managing the marketing effort.
- ◆ Target customers stand at the centre of the marketing process.

2.3 Marketing Mix

Marketing mix forms an important part of overall competitive marketing strategy. The marketing mix is the set of controllable marketing variables that the firm blends to produce the response it wants in the target market. The marketing mix consists of everything that the firm can do to influence the demand for its product. These variables are often referred to as the "4 Ps." The 4 Ps stand for product, price, place and promotion. An effective marketing program blends all of the marketing mix elements into a coordinated program designed to achieve the company's marketing objectives by delivering value to consumers. The 4 Ps are from a marketer's angle. When translated to the perspective of buyers, they may be termed as 4 Cs. Product may be referred as customer solution, price as customer cost, place as convenience and promotion as communication.

- ◆ **Product** stands for the "goods-and-service" combination the company offers to the target market. Strategies are needed for managing existing product over time adding new ones and dropping failed products. Strategic decisions must also be made regarding branding, packaging and other product features such as warranties.

Products and markets are infinitely dynamic. An organization has to capture such dynamics through a set of policies and strategies. Some products have consistent customer demand over long period of time while others have short and fleeting life spans. There are products that have wide range of quality and workmanship and these also change over time. There are industrial or consumer products, essentials or luxury products, durables or perishables.

Products can be differentiated on the basis of size, shape, colour, packaging, brand names, after-sales service and so on. Organizations seek to hammer into customers' minds that their products are different from others. It does not matter whether the differentiation is real or imaginary. Quite often the differentiation is psychological rather than physical. It is enough if customers are persuaded to believe that the marketers product is different from others.

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Organizations formalize product differentiation through christening 'brand names' to their respective products. These are generally reinforced with legal sanction and protection. Brands enable customers to identify the product and the organization behind it. The products' and even firms' image is built around brand through advertising and other promotional strategies. Customers tend to develop strong brand loyalty for a particular product over a period of time.

- ◆ **Price** stands for the amount of money customers have to pay to obtain the product. Necessary strategies pertain to the location of the customers, price flexibility, related items within a product line and terms of sale. The price of a product is its composite expression of its value and utility to the customer, its demand, quality, reliability, safety, the competition it faces, the desired profit and so on.

In an industry there would be organizations with low cost products and other organizations with high costs. The low cost organizations may adopt aggressive pricing strategy as they enjoy more freedom of action in respect of their prices. They may also afford selective increase in costs to push their sales.

Theoretically, organizations may also adopt cost plus pricing wherein a margin is added to the cost of the product to determine its price. However, in the competitive environment such an approach may not be feasible. More and more companies of today have to accept the market price with minor deviations and work towards their costs. They reduce their cost in order to maintain their profitability.

For a new product pricing strategies for entering a market needs to be designed. In pricing a really new product at least three objectives must be kept in mind.

- (a) Making the product acceptable to the customers.
- (b) Producing a reasonable margin over cost.
- (c) Achieving a market that helps in developing market share.

For a new product an organization may either choose to skim or penetrate the market. In *skimming* prices are set at a very high level. The product is directed to those buyers who are relatively price insensitive but sensitive to the novelty of the new product. For example call rates of mobile telephony were set very high initially. Even the incoming calls were charged. Since the initial off take of the product is low, high price, in a way, helps in rationing of supply in favour of those who can afford it. In *penetration* firm keeps a temptingly low price for a new product which itself is selling point. A very large number of the potential consumer may be able to afford and willing to try the product.

- ◆ **Place** stands for company activities that make the product available to target consumers. One of the most basic marketing decision is choosing the most appropriate marketing channel. Strategies should be taken for the management of channel(s) by which ownership of product is transferred from producers to customers and in many cases, the system(s) by which goods are moved from where they are produced from they are purchases by the final customers. Strategies applicable to the middleman such as wholesalers and retails must be designed.

The distribution policies of a company are important determinants of the functions of marketing. The decision to utilize a particular marketing channel or channels sets the pattern of operations of sales force. We will learn more about place when we study logistics later in this chapter.

- ◆ **Promotion** stands for activities that communicate the merits of the product and persuade target consumers to buy it. Strategies are needed to combine individual methods such as advertising, personal selling, and sales promotion into a coordinated campaign. In addition promotional strategies must be adjusted as a product move from an earlier stage from a later stage of its life.

Modern marketing is highly promotional oriented. Organizations strive to push their sales and market standing on a sustained basis and in a profitable manner under conditions of complex direct and indirect competitive situations. Promotion also acts as an impetus to marketing. It is simultaneously a communication, persuasion and conditioning process. There are at least four major direct promotional methods or tools – personal selling, advertising, publicity and sales promotion. They are briefly explained as follows:

- (i) *Personal selling*: Personal selling is one of the oldest forms of promotion. It involves face-to-face interaction of sales force with the prospective customers and provides a high degree of personal attention to them. In personal selling, oral communication is made with potential buyers of a product with the intention of making a sale. It may initially focus on developing a relationship with the potential buyer, but end up with efforts for making a sale. Personal selling suffers from a very high costs as sales personnel are expensive. They can physically attend only one customer at a time. Thus it is not a cost-effective way of reaching a large number of people. However, as it is a highly effective method to persuade a potential customer into making a purchase, the personal selling is used in all kind of industries for all products.
- (ii) *Advertising*: Advertising is a non-personal, highly flexible and dynamic promotional method. The media for advertisings are several such as pamphlets, brochures, newspapers, magazines, hoardings, display boards, radio, television and internet. Choice of appropriate media is important for effectiveness of the message. The media may be local, regional, or national. The type of the message, copy, and illustration are a matter of choice and creativity. Advertising may be directed towards consumers, middlemen or opinion leaders. Advertising is likely to succeed in promoting the sales of an organization but its effectiveness in respect to the expenditure can not be directly measured. A sale is a function of several variables out of which advertising is only one.
- (iii) *Publicity*: Publicity is also a non-personal form of promotion similar to advertising. However, no payments are made to the media as in case of advertising. Organizations skilfully seek to promote themselves and their product without payment. Publicity is communication of a product, brand or business by placing information about it in the media without paying for the time or media space directly. Thus it is way of reaching customers with negligible cost. Basic tools for publicity are

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press releases, press conferences, reports, stories, and internet releases. These releases must be of interest to the public.

- (iv) *Sales promotion*: Sales promotion is an omnibus term that includes all activities that are undertaken to promote the business but are not specifically included under personal selling, advertising or publicity. Activities like discounts, contests, money refunds, instalments, kiosks, exhibitions and fairs constitute sales promotion. All these are meant to give a boost to the sales. Sales promotion done periodically may help in getting a larger market share to an organization.

Expanded Marketing Mix: Typically, all organizations use a combination of 4 Ps in some form or the other. However, the above elements of marketing mix are not exhaustive. It is pertinent to discuss a few more elements that may form part of an organizational marketing mix strategy. They have got more currency in recent years. Growth of services has its own share for the inclusion of newer elements in marketing. A few new Ps are as follows:

- ◆ **People**: all human actors who play a part in delivery of the market offering and thus influence the buyer's perception, namely the firm's personnel and the customer.
- ◆ **Physical evidence**: the environment in which the market offering is delivered and where the firm and customer interact.
- ◆ **Process**: the actual procedures, mechanisms and flow of activities by which the product / service is delivered.

2.4 Marketing Analysis

Marketing analysis involves a complete analysis of the company's situation. A company performs analysis by identifying environmental opportunities and threats. It also analyzes its strengths and weaknesses to determine which opportunities the company can best pursue. Marketing Analysis has three components as planning, implementation and control. Through analyses organization feed information and other inputs to each of the other marketing management functions.

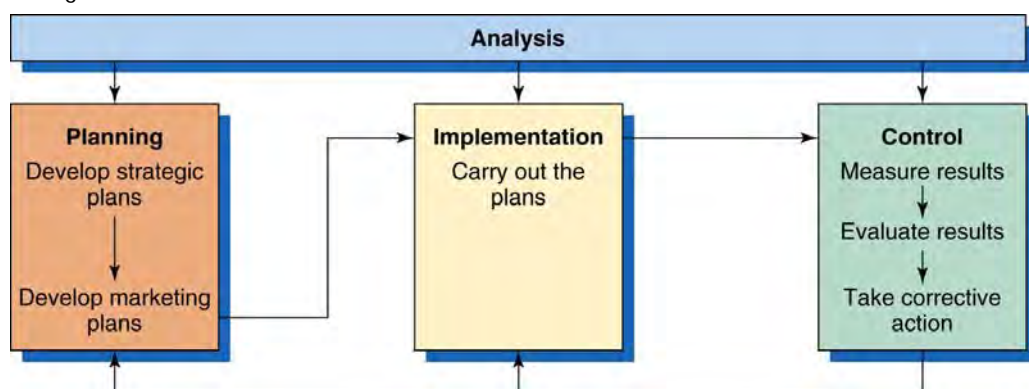


Figure: Managing the marketing effort

Marketing Planning: Marketing planning involves deciding on marketing strategies that will help the company attain its overall strategic objectives. A detailed plan is needed for each business, product, or brand. A product or brand plan may contain different sections: executive summary, current marketing situation, threats and opportunity analysis, objectives and issues, marketing strategies, action programs, budgets, and controls.

- ◆ The executive summary is a short summary of the main goals and recommendations to be presented in the plan.
- ◆ The current marketing situation is the section of a marketing plan that describes the target market and the company's position in it. Important sections include:
 - A market description.
 - A product review.
 - Analysis of the competition.
 - A section on distribution.
- ◆ In the threats and opportunities section, managers are forced to anticipate important developments that can have an impact, either positive or negative, on the firm.
- ◆ Having studied the product's threats and opportunities, the manager can set objectives and consider issues that will affect them. The objectives should be stated as goals that the company would like to attain during the plan's term.
- ◆ Marketing strategy is the marketing logic by which the business unit hopes to achieve its marketing objectives. Strategies should be created for all marketing mix components.
- ◆ The marketing budget is a section of the marketing plan that shows projected revenues, costs, and profits.
- ◆ The last section of the marketing plan outlines the controls that will be used to monitor progress. This allows for progress checks and corrective action.

Dealing with the Marketing Environment: A company must carefully analyze its environment in order to avoid the threats and take advantage of the opportunities. Areas to be analyzed in the environment normally include:

- ◆ Forces close to the company such as its ability to serve customers, other company departments, channel members, suppliers, competitors, and publics.
- ◆ Broader forces such as demographic and economic forces, political and legal forces, technological and ecological forces, and social and cultural forces.

Marketing Strategy Techniques

- ◆ **Social Marketing:** It refers to the design, implementation, and control of programs seeking to increase the acceptability of a social idea, cause, or practice among a

target group. For instance, the publicity campaign for prohibition of smoking in Delhi explained the place where one can and can't smoke in Delhi.

- ◆ **Augmented Marketing.** It is provision of additional customer services and benefits built around the core and actual products that relate to introduction of hi-tech services like movies on demand, on-line computer repair services, secretarial services, etc. Such innovative offerings provide a set of benefits that promise to elevate customer service to unprecedented levels.
- ◆ **Direct Marketing:** Marketing through various advertising media that interact directly with consumers, generally calling for the consumer to make a direct response. Direct marketing includes catalogue selling, mail, telecomputing, electronic marketing, shopping, and TV shopping.
- ◆ **Relationship Marketing:** The process of creating, maintaining, and enhancing strong, value-laden relationships with customers and other stakeholder. For example, Airlines offer special lounges at major airports for frequent flyers. Thus, providing special benefits to select customers to strength bonds. It will go a long way in building relationships.
- ◆ **Services Marketing:** It is applying the concepts, tools, and techniques, of marketing to services. Services is any activity or benefit that one party can offer to another that is essentially intangible and does not result in the banking, savings, retailing, educational or utilities.
- ◆ **Person Marketing:** People are also marketed. Person marketing consists of activities undertaken to create, maintain or change attitudes or behaviour towards particular people. For example, politicians, sports stars, film stars, professional i.e., market themselves to get votes, or to promote their careers and income.
- ◆ **Organization Marketing:** It consists of activities undertaken to create, maintain, or change attitudes and behaviour of target audiences towards an organization. Both profit and non-profit organizations practice organization marketing.
- ◆ **Place Marketing:** Place marketing involves activities undertaken to create, maintain, or change attitudes and behaviour towards particular places say, business sites marketing, tourism marketing.
- ◆ **Enlightened Marketing:** A marketing philosophy holding that a company's marketing should support the best long-run performance of the marketing system; its five principles include customer-oriented marketing, innovative marketing, value marketing, sense-of-mission marketing, and societal marketing.
- ◆ **Differential Marketing:** A market-coverage strategy in which a firm decides to target several market segments and designs separate offer for each. For example, Hindustan Unilever Limited has Lifebuoy, Lux and Rexona in popular segment and Dove and Pears in premium segment.

- ◆ **Synchro-marketing:** When the demand for the product is irregular due to season, some parts of the day, or on hour basis, causing idle capacity or overworked capacities, synchro-marketing can be used to find ways to alter the same pattern of demand through flexible pricing, promotion, and other incentives. For example, products such as movie tickets can be sold at lower price over week days to generate demand.
- ◆ **Concentrated Marketing:** A market-coverage strategy in which a firm goes after a large share of one or few sub-markets.
- ◆ **Demarketing:** Marketing strategies to reduce demand temporarily or permanently-the aim is not to destroy demand, but only to reduce or shift it. This happens when there is overfull demand. For example, buses are overloaded in the morning and evening, roads are busy for most of times, zoological parks are over-crowded on Saturdays, Sundays and holidays. Here demarketing can be applied to regulate demand.

3. Financial Strategy Formulation

The financial strategies of an organization are related to several finance/accounting concepts considered to be central to strategy implementation. These are: acquiring needed capital/sources of fund, developing projected financial statements/budgets, management/usage of funds, and evaluating the worth of a business. Strategists need to formulate strategies in these areas so that they are implemented. Some examples of decisions that may require finance/accounting policies are:

1. To raise capital with short-term debt, long-term debt, preferred stock, or common stock.
2. To lease or buy fixed assets.
3. To determine an appropriate dividend payout ratio.
4. To extend the time of accounts receivable.
5. To establish a certain percentage discount on accounts within a specified period of time.
6. To determine the amount of cash that should be kept on hand.

Acquiring capital to implement strategies / sources of funds: Successful strategy implementation often requires additional capital. Besides net profit from operations and the sale of assets, two basic sources of capital for an organization are debt and equity. Determining an appropriate mix of debt and equity in a firm's capital structure can be vital to successful strategy implementation. Theoretically, an enterprise should have enough debt in its capital structure to boost its return on investment by applying debt to products and projects earning more than the cost of the debt. In low earning periods, too much debt in the capital structure of an organization can endanger stockholders' return and jeopardize company survival. Fixed debt obligations generally must be met, regardless of circumstances. This does not mean that stock issuances are always better than debt for raising capital. Some special stock is issued to finance strategy implementation; ownership and control of the enterprise are diluted. This can be a serious concern in today's business environment of hostile takeovers, mergers, and acquisitions.

5.11 Strategic Management

The major factors regarding which strategies have to be made are: capital structure; procurement of capital and working capital borrowings; reserves and surplus as sources of funds; and relationship with lenders, banks and financial institutions. Strategies related to the sources of funds are important since they determine how financial resources will be made available for the implementation of strategies. Organizations have a range of alternatives regarding the sources of funds. While one company may rely on external borrowings, another may follow a policy of internal financing.

Projected financial statements / budgets: Projected (pro forma) financial statement analysis is a central strategy-implementation technique because it allows an organization to examine the expected results of various actions and approaches. This type of analysis can be used to forecast the impact of various implementation decisions (for example, to increase promotion expenditures by 50 percent to support a market-development strategy, to increase salaries by 25 percent to support a market-penetration strategy, to increase research and development expenditures by 70 percent to support product development, or to sell common stock to raise capital for diversification). Nearly all financial institutions require a projected financial statement whenever a business seeks capital. A pro forma income statement and balance sheet allow an organization to compute projected financial ratios under various strategy-implementation scenarios. When compared to prior years and to industry averages, financial ratios provide valuable insights into the feasibility of various strategy-implementation approaches.

Primarily as a result of the Enron collapse and accounting scandal, companies today are being much more diligent in preparing projected financial statements to "reasonably rather than too optimistically" project future expenses and earnings.

A financial budget is also a document that details how funds will be obtained and spent for a specified period of time. Annual budgets are most common, although the period of time for a budget can range from one day to more than ten years. Fundamentally, financial budgeting is a method for specifying what must be done to complete strategy implementation successfully. Financial budgeting should not be thought of as a tool for limiting expenditures but rather as a method for obtaining the most productive and profitable use of an organization's resources. Financial budgets can be viewed as the planned allocation of a firm's resources based on forecasts of the future.

There are almost as many different types of financial budgets as there are types of organizations. Some common types of budgets include cash budgets, operating budgets, sales budgets, profit budgets, factory budgets, capital budgets, expense budgets, divisional budgets, variable budgets, flexible budgets, and fixed budgets. When an organization is experiencing financial difficulties, budgets are especially important in guiding strategy implementation.

Financial budgets have some limitations. First, budgetary programs can become so detailed that they are cumbersome and overly expensive. Over budgeting or under budgeting can cause problems. Second, financial budgets can become a substitute for objectives. A budget

is a tool and not an end in itself. Third, budgets can hide inefficiencies if based solely on precedent rather than on periodic evaluation of circumstances and standards. Finally, budgets are sometimes used as instruments of tyranny that result in frustration, resentment, absenteeism, and high turnover. To minimize the effect of this last concern, managers should increase the participation of subordinates in preparing budgets.

Management / usage of funds: Plans and policies for the usage of funds deal with investment or asset-mix decisions. The important factors regarding which plans and policies are to be made are: capital investment; fixed asset acquisition; current assets; loans and advances; dividend decisions; and relationship with shareholders. Usage of funds is important since it relates to the efficiency and effectiveness of resource utilization in the process of strategy implementation.

Implementation of projects in pursuance of expansion strategies typically results in increase in capital work in progress and current assets. If plans and policies are not clear, the usage of funds is inefficient, leading to less than an optimum utilization of resources. An example is of Modi Cement, which followed a deliberate policy of generous capital investment in setting up its plant based on the latest technology. As compared to its competitor Jaypee Rewa's plant, which cost Rs 120 crore, Modi's plant had an investment of Rs 153 crore. The result was high interest liability and depreciation, causing a serious dent in profitability in the initial years. Other factors of usage of funds are also considered by companies to attract and retain shareholders' interest. Payout policies for dividends and bonus distribution play an important role in the usage of funds.

The management of funds is an important area of financial strategies. It basically deals with decisions related to the systemic aspects of financial management. The major factors regarding which plans and policies related to the management of funds have to be made are: the systems of finance, accounting, and budgeting; management control system; cash, credit, and risk management; cost control and reduction; and tax planning and advantages.

The management of funds can play a pivotal role in strategy implementation as it aims at the conservation and optimum utilization of funds objectives which are central to any strategic action. Organizations that implement strategies of stability, growth or retrenchment cannot escape the rigours of a proper management of funds. In fact, good management of funds often creates the difference between a strategically successful and unsuccessful company. For instance, Gujarat Ambuja Cements, currently a highly profitable cement company in the country, has achieved tremendous financial success primarily on the basis of its policies of cost control. This company has been particularly successful in maintaining a low cost for power, which is a major input in cement manufacturing.

Financial plans and policies, however, present a dilemma before management. The priorities of management may often conflict with those of shareholders. It is the responsibility of the strategists to minimize the conflict of interest between the management and the shareholders.

Evaluating the worth of a business: Evaluating the worth of a business is central to strategy implementation because integrative, intensive, and diversification strategies are often

implemented by acquiring other firms. Other strategies, such as retrenchment may result in the sale of a division of an organization or of the firm itself. Thousands of transactions occur each year in which businesses are bought or sold in the United States. In all these cases, it is necessary to establish the financial worth or cash value of a business to successfully implement strategies.

All the various methods for determining a business's worth can be grouped into three main approaches:

- ◆ The first approach in evaluating the worth of a business is determining its net worth or stockholders' equity. Net worth represents the sum of common stock, additional paid-in capital, and retained earnings. After calculating net worth, add or subtract an appropriate amount for goodwill and overvalued or undervalued assets. This total provides a reasonable estimate of a firm's monetary value. If a firm has goodwill, it will be listed on the balance sheet, perhaps as "intangibles".
- ◆ The second approach to measuring the value of a firm grows out of the belief that the worth of any business should be based largely on the future benefits its owners may derive through net profits. A conservative rule of thumb is to establish a business's worth as five times the firm's current annual profit. A five-year average profit level could also be used. When using the approach, remember that firms normally suppress earnings in their financial statements to minimize taxes.
- ◆ The third approach, letting the market determine a business's worth, involves three methods. First, base the firm's worth on the selling price of a similar company. A potential problem, however, is that sometimes comparable figures are not easy to locate, even though substantial information on firms that buy or sell to other firms is available in major libraries. The second approach is called the price-earnings ratio method. To use this method, divide the market price of the firm's common stock by the annual earnings per share and multiply this number by the firm's average net income for the past five years. The third approach can be called the outstanding shares method. To use this method, simply multiply the number of shares outstanding by the market price per share and add a premium. The premium is simply a per-share amount that a person or firm is willing to pay to control (acquire) the other company. As indicated in the Global Perspective, European firms aggressively are acquiring American firms, using these and perhaps other methods for evaluating the worth of their target companies.

4. Production Strategy Formulation

The strategy for production is related to the production system, operational planning and control, and research and development (R&D). The strategy adopted affects the nature of product/service, the markets to be served, and the manner in which the markets are to be served. All these collectively influence the operations system structure and objectives which are used to determine the operations plans and policies. Thus, a strategy of expansion

through related diversification, for instance, will affect what products are offered to which market and how these markets are served. The operations system structure, which is concerned with the manufacturing/ service and supply/delivery system, and operations system objectives, which are related to customer service and resource utilisation, both determine what operations, plans and policies are set.

Production System: The production system is concerned with the capacity, location, layout, product or service design, work systems, degree of automation, extent of vertical integration, and such factors. Strategies related to production system are significant as they deal with vital issues affecting the capability of the organisation to achieve its objectives.

Strategy implementation would have to take into account the production system factors as they involve decisions which are long-term in nature and influence not only the operations capability of an organisation but also its ability to implement strategies and achieve objectives. For example, Excel Industries, a pioneering company in the area of industrial and agro chemicals, adopts a policy of successive vertical integration for import substitution. It starts with the end product and then integrates backward to make raw materials for it. Another example is of Lakshmi Machine Works, where operations policy related to the product range is aimed at the successive enlargement of its textile machinery range. This is done through a policy of mastering the process of production by absorption of technology, indigenisation, and adaptation to customer needs.

Operations Planning and Control: Strategies related to operations planning and control are concerned with aggregate production planning; materials supply; inventory, cost, and quality management; and maintenance of plant and equipment. Here, the aim of strategy implementation is to see how efficiently resources are utilized and in what manner the day-to-day operations can be managed in the light of long-term objectives.

Operations planning and control provides an example of an organizational activity that is aimed at translating the objectives into reality. For instance, Instrumentation Ltd is a public sector company engaged in the business of process control and automation and is currently following a strategy of expansion and diversification. Operations planning and control at this company is based on the policy of ancillarisation. There are about 259 ancillary units that supply sub-assemblies and components. The company's centralized production is at Kota in Rajasthan and its operations plans are based on the plans of its ancillary units. The centralized production provides all the basic inputs to ancillaries and performs the functions of testing, standardizing, and fabricating the equipment.

Some companies use quality as a strategic tool. The operations policies at KSB Pumps Ltd lay a great emphasis on quality aspects. In implementing its strategy of stable growth, KSB Pumps has built a solid reputation for its quality products. Structurally, it has a separate department of quality assurance having two groups of quality inspection and quality engineering. Thus, quality is a consideration not only at the inspection stage but is built into the design itself.

5. Logistics Strategy

Management of logistics is a process which integrates the flow of supplies into, through and out of an organization to achieve a level of service which ensures that the right materials are available at the right place, at the right time, of the right quality, and at the right cost. Organizations try to keep the cost of transporting materials as low as possible consistent with safe and reliable delivery.

Supply chain management helps in logistics and enables a company to have constant contact with its distribution team, which could consist of trucks, trains, or any other mode of transportation. Given the changes that affect logistics operations such as emerging technologies and industry initiatives, developing and using a formal logistics strategy is very important. For a business organization effective logistic strategy will involve raising and finding solutions to the following questions:

- ◆ Which sources of raw materials and components are available?
- ◆ How many manufacturing locations are there?
- ◆ What products are being made at each manufacturing location?
- ◆ What modes of transportation should be used for various products.
- ◆ What is the nature of distribution facilities?
- ◆ What is the nature of materials handling equipment possessed? Is it ideal?
- ◆ What is the method for deploying inventory in the logistics network?
- ◆ Should the business organization own the transport vehicles?

Improvement in logistics can results in savings in cost of doing business. These savings can also reveal in the profits of the company. Some examples of how logistics can help a business are as follows:

- ◆ Cost savings
- ◆ Reduced inventory
- ◆ Improved delivery time
- ◆ Customer satisfaction
- ◆ Competitive advantage

5.1 Supply Chain Management

The way businesses were conducted in the yesteryears is entirely different as they are conducted now. Today, organisations work in highly turbulent environment. There are several changes in business environment that have contributed to the development of supply chain networks. The technology has made impact on all spheres of business activities. Organisational systems have improved. Even the available infrastructure is improving. Technological changes and reduction in information communication costs with increase in its

speed has led to changes in coordination among the members of the supply chain network. Availability of newer technologies have resulted in creation of innovative products with shorter product life cycles.

Traditionally companies have been managing themselves by taking orders, buying supplies, manufacturing products and shipping them from their warehouses. Such organisations may lose out the businesses that strongly lay their focus on key areas of marketing, branding and delivering value to the customer and outsourcing the rest. Today organisations and individual customers have become more demanding. They desire customised products that are made according to their needs. They also aspire that these should be available at lower costs.

5.2 What is Supply Chain Management?

The term supply chain refers to the linkages between suppliers, manufacturers and customers. Supply chains involve all activities like sourcing and procurement of material, conversion, and logistics. Planning and control of supply chains are important components of its management. Naturally, management of supply chains include closely working with channel partners – suppliers, intermediaries, other service providers and customers.

Supply chain management is defined as the process of planning, implementing, and controlling the supply chain operations. It is a cross-functional approach to managing the movement of raw materials into an organization and the movement of finished goods out of the organization toward the end-consumer who are to be satisfied as efficiently as possible. It encompasses all movement and storage of raw materials, work-in-process inventory, and finished goods from point-of-origin to point-of-consumption. Organizations are finding that they must rely on the chain to successfully compete in the global market.

Modern organizations are striving to focus on core competencies and reduce their ownership of sources of raw materials and distribution channels. These functions can be outsourced to other business organizations that specialize in those activities and can perform in better and cost effective manner. In a way organizations in the supply chain do tasks according to their core-competencies. Working in the supply chain improve trust and collaboration amongst partners and thus improve flow and management of inventory.

5.3 Is logistic management same as supply chain management?

Supply chain management is an extension of logistic management. However, there is difference between the two. Logistical activities typically include management of inbound and outbound goods, transportation, warehousing, handling of material, fulfilment of orders, inventory management, supply/demand planning. Although these activities also form part of Supply chain management, the latter has different components. Logistic management can be termed as one of its part that is related to planning, implementing, and controlling the movement and storage of goods, services and related information between the point of origin and the point of consumption.

Supply chain management includes more aspects apart from the logistics function. It is a tool of business transformation and involves delivering the right product at the right time to the right place and at the right price. It reduces costs of organizations and enhances customer service.

5.4 Implementing Supply Chain Management Systems

A successful implementing supply management system requires a change from managing individual functions to integrating activities into key supply chain processes. It involves collaborative work between buyers and suppliers, joint product development, common systems and shared information. A key requirement for successfully implementing supply chain will be network of information sharing and management. The partners need to link together to share information through electronic data interchange and take decisions in timely manner.

Implementing and successfully running supply chain management system will involve:

1. **Product development:** Customers and suppliers must work together in the product development process. Right from the start the partners will have knowledge of all. Involving all partners will help in shortening the life cycles. Products are developed and launched in shorter time and help organizations to remain competitive.
2. **Procurement:** Procurement requires careful resource planning, quality issues, identifying sources, negotiation, order placement, inbound transportation and storage. Organizations have to coordinate with suppliers in scheduling without interruptions. Suppliers are involved in planning the manufacturing process.
3. **Manufacturing:** Flexible manufacturing processes must be in place to respond to market changes. They should be adaptive to accommodate customization and changes in the taste and preferences. Manufacturing should be done on the basis of just-in-time (JIT) and minimum lot sizes. Changes in the manufacturing process be made to reduce manufacturing cycle.
4. **Physical distribution:** Delivery of final products to customers is the last position in a marketing channel. Availability of the products at the right place at right time is important for each channel participant. Through physical distribution processes serving the customer become an integral part of marketing. Thus supply chain management links a marketing channel with customers.
5. **Outsourcing:** Outsourcing is not limited to the procurement of materials and components, but also includes outsourcing of services that traditionally have been provided within an organization. The company will be able to focus on those activities where it has competency and everything else will be outsourced.
6. **Customer services:** Organizations through interfaces with the company's production and distribution operations develop customer relationships so as to satisfy them. They work with customer to determine mutually satisfying goals, establish and maintain relationships. This in turn helps in producing positive feelings in the organization and the customers

7. **Performance measurement:** There is a strong relationship between the supplier, customer and organisation. Supplier capabilities and customer relationships can be correlated with a firm performance. Performance is measured in different parameters such as costs, customer service, productivity and quality.

6. Research and Development

Research and development (R&D) personnel can play an integral part in strategy implementation. These individuals are generally charged with developing new products and improving old products in a way that will allow effective strategy implementation. R&D employees and managers perform tasks that include transferring complex technology, adjusting processes to local raw materials, adapting processes to local markets, and altering products to particular tastes and specifications. Strategies such as product development, market penetration, and concentric diversification require that new products be successfully developed and that old products be significantly improved. But the level of management support for R&D is often constrained by resource availability.

Technological improvements that affect consumer and industrial products and services shorten product life cycles. Companies in virtually, every industry are relying on the development of new products and services to fuel profitability and growth. Surveys suggest that the most successful organizations use an R&D strategy that ties external opportunities to internal strengths and is linked with objectives. Well formulated R&D policies match market opportunities with internal capabilities. R&D policies can enhance strategy implementation efforts to:

- ◆ Emphasize product or process improvements.
- ◆ Stress basic or applied research.
- ◆ Be leaders or followers in R&D.
- ◆ Develop robotics or manual-type processes.
- ◆ Spend a high, average, or low amount of money on R&D.
- ◆ Perform R&D within the firm or to contract R&D to outside firms.
- ◆ Use university researchers or private sector researchers.

There must be effective interactions between R&D departments and other functional departments in implementing different types of generic business strategies. Conflicts between marketing, finance/accounting, R&D, and information systems departments can be minimized with clear policies and objectives.

Many firms wrestle with the decision to acquire R&D expertise from external firms and develop R&D expertise internally. The following guidelines can be used to help make this decision:

- ◆ If the rate of technical progress *is* slow, the rate of market growth *is* moderate, and

there are significant barriers to possible new entrants, then in-house R&D is the preferred solution. The reason is that R&D, if successful, will result in a temporary product or process monopoly that the company can exploit.

- ◆ If technology is changing rapidly and the market is growing slowly, then a major effort in R&D may be very risky, because it may lead to the development of an ultimately obsolete technology or one for which there is no market.
- ◆ If technology is changing slowly but the market is growing quickly, there generally is not enough time for in-house development. The prescribed approach is to obtain R&D expertise on an exclusive or nonexclusive basis from an outside firm.
- ◆ If both technical progress and market growth are fast, R&D expertise should be obtained through acquisition of a well-established firm in the industry?

There are at least three major R&D approaches for implementing strategies. The first strategy is to be the first firm to market new technological products. This is a glamorous and exciting strategy but also a dangerous one. Firms such as 3M and General Electric have been successful with this approach, but many other pioneering firms have fallen, with rival firms seizing the initiative.

A second R&D approach is to be an innovative imitator of successful products, thus minimizing the risks and costs of start up. This approach entails allowing a pioneer firm to develop the first version of the new product and to demonstrate that a market exists. Then, laggard firms develop a similar product. This strategy requires excellent R&D personnel and an excellent marketing department.

A third R&D strategy is to be a low-cost producer by mass-producing products similar to but less expensive than products recently introduced. As a new product accepted by customers, price becomes increasingly important in the buying decision. Also, mass marketing replaces personal selling as the dominant selling strategy. This R&D strategy requires substantial investment in plant and equipment, but fewer expenditures in R&D than the two approaches described earlier.

7. Human Resource Strategy Formulation

The job of human resource manager is changing rapidly as there companies that downsize and reorganize. Strategic responsibilities of the human resource manager include assessing the staffing needs and costs for alternative strategies proposed during Strategy formulation and developing a staffing plan for effectively implementing strategies. The plan must also include how to motivate employees and managers.

The human resource department must develop performance incentives that clearly link performance and pay to strategies. The process of empowering managers and employees through their involvement in strategic management activities yields the greatest benefits when all organizational members understand clearly how they will benefit personally if the firm does well. Linking company and personal benefits is a major new strategic responsibility of human

resource managers. Other new responsibilities for human resource managers may include establishing and administering an employee stock ownership plan (ESOP), instituting an effective childcare policy, and providing leadership for managers and employees in a way that allows them to balance work and family.

A well-designed strategic-management system can fail if insufficient attention is given to the human resource dimension. Human resource problems that arise when business implement strategies can usually be traced to one of three causes: (1) disruption of Social and political structures, (2) failure to match individuals' aptitudes with implementation tasks, and (3) inadequate top management support for implementation activities.

Strategy implementation poses a threat to many managers and employees in an organization. New power and status relationships are anticipated and realized. New formal and informal groups' values, beliefs, and priorities may be largely unknown. Managers and employees may become engaged in resistance behaviour as their roles, prerogatives, and power in the firm change. Disruption of social and political structures that accompany strategy execution must be anticipated and considered during strategy formulation and managed during strategy implementation.

A concern in matching managers with strategy is that jobs have specific and relatively static responsibilities, although people are dynamic in their personal development. Commonly used methods that match managers with strategies to be implemented include transferring managers, developing leadership workshops, offering career development activities, promotions, job enlargement, and job enrichment.

A number of other guidelines can help ensure that human relationships facilitate rather than disrupt strategy-implementation efforts. Specifically, managers should do a form of chatting and informal questioning to stay abreast of how things are progressing and to know when to intervene. Managers can build support for strategy-implementation efforts by giving few orders, announcing few decisions, depending heavily on informal questioning, and seeking to probe and clarify until a consensus emerges. Key thrusts that needed should be rewarded generously and visibly.

It is surprising that so often during strategy formulation, individual values, skills, and abilities needed for successful strategy implementation are not considered. It is rare that a firm selecting new strategies or significantly altering existing strategies possesses the right line and staff personnel in the tight positions for successful strategy implementation. The need to match individual aptitudes with strategy-implementation tasks should be considered in strategy choice.

Inadequate support from strategists for implementation activities often undermines organizational success. Chief executive officers, small business owners, and government agency heads must be personally committed to strategy implementation and express this commitment in highly visible ways. Strategists' formal statements about the Importance of strategic management must be consistent with actual support and rewards given for activities completed and objectives reached. Otherwise, stress created by inconsistency can cause uncertainty among managers and employees at all levels.

5.21 Strategic Management

Perhaps the best method for preventing and overcoming human resource problems in strategic management is to actively involve many managers and employees' as possible in the process. Although time-consuming, this approach builds understanding, trust, commitment and ownership and reduces resentment and hostility. The true potential of strategy formulation and implementation resides in people.

The firm's external opportunities and threats on the one hand and its internal strengths and weaknesses on the other. In Human Resource Strategic management, the strategist tries to achieve a competitive advantage for his organization. The competitive advantage may be in the form of low cost relationship in the industry or being unique in the industry along dimensions that are widely valued by the customers in particular and the society at large. And so that they can obtain a competitive edge by becoming a low-cost leader or a differentiator puts a heavy premium on having a highly competent and committed team for human resources. To quote Charles Greer,

In a growing number of organizations, human resources are now viewed as a source of competitive advantage. There is greater recognition that distinctive competencies are obtained through highly developed employee skills, distinctive organizational cultures, management processes and systems.

The role of human resources in enabling the organization to effectively deal with the external environmental challenges, the human resource management function has been accepted as a strategic partner in the formulation of organization's strategies and in the implementation of such strategies through human resource planning, employment, training, appraisal and rewarding of personnel. An organization's recruitment, selection, training, performance appraisal, and compensation practices can have a strong influence on employee competence is very important. The following points should be kept in mind:

1. *Recruitment and selection:* The workforce will be more competent if a firm can successfully identify, attract, and select the most competent applicants.
2. *Training:* The workforce will be more competent if employees are well trained to perform their jobs properly.
3. *Appraisal of performance:* The performance appraisal is to identify any performance deficiencies experienced by employees due to lack of competence. Such deficiencies, once identified, can often be solved through counselling, coaching or training.
4. *Compensation:* A firm can usually increase the competency of its workforce by offering pay and benefit packages that are more attractive than those of their competitors. This practice enables organizations to attract and retain the most capable people.

Strategy and Human Resource Management: The human resource strategy of business should reflect and support the corporate strategy. An effective human resource strategy includes the way in which the organization plans to develop its employees and provide them suitable opportunities and better working conditions so that their optimal contribution is ensured. This implies selecting the best available personnel, ensuring a 'fit' between the

employee and the job and retaining, motivating and empowering employees to perform well in direction of corporate objectives.

Strategic human resource management may be defined as the linking of human resource management with strategic goals and objectives to improve business performance and develop organizational culture that fosters innovation and flexibility. The success of an organization depends on its human resources. This means how they are acquired, developed, motivated and retained organization play an important role in organizational success. This presupposes an integrated approach towards human resource functions and overall business functions of an organization.

The Human Resource Management practices of an organization may be an important source of competitive advantage. For this strategic focus should be given in the following points:

- ◆ Pre-selection practices including human resource planning and job analysis.
- ◆ Selection practices meant to staff various positions in the organization. Both recruitment and selection policies and procedures should be designed keeping in view the mission and the purpose of the organization.
- ◆ Post-selection practices to maintain and improve the workers job performance levels. Human Resources decisions related to training and development, performance appraisal, compensation and motivation should be based on corporate strategy of the organization.

Strategic Role of Human Resource Management: The prominent areas where the human resource manager can play strategic role are as follows:

1. **Providing purposeful direction:** The human resource management must be able to lead people and the organization towards the desired direction involving people right from the beginning. The most important tasks of a professional management is to ensure that the object of an organization has been internalized by each individual working in the organization. Goals of an organization state the very purpose and justification of its existence.

The management have to ensure that the objects of an organization become the object of each person working in the organization and the objectives are set to fulfill the same. Objectives are specific aims which must be in the line with the goal of the organization and the all actions of each person must be consistent with the objectives defined.
2. **Creating competitive atmosphere:** Present's globalized market maintaining a competitive gain is the object of any organization. There are two important ways of business can achieve a competitive advantages over the others. The first is cost leadership which means the firm aims to become a low cost leader in the industry. The second competitive strategy is differentiation under which the firm seeks to be unique in the industry in terms of dimensions that are highly valued by the customers. Putting these strategies into effect carries a heavy premium on having a highly committed and competent workforce.
3. **Facilitation of change:** The Human resource will be more concerned with substance

rather than form, accomplishments rather than activities, and practice rather than theory. The personnel function will be responsible for furthering the organization not just maintaining it. Human resource management will have to devote more time to promote changes than to maintain the status quo.

4. **Diversion of workforce:** In the modern organization management of diverse workforce is a great challenge. Workforce diversity can be observed in terms of male and female workers, young and old workers, educated and uneducated workers, unskilled and professional employee, etc. Moreover, many organizations also have people of different castes, religious and nationalities. The workforce in future will comprise more of educated and self conscious workers. They will ask for higher degree of participation and avenues for fulfilment. Money will no longer be the sole motivating force for majority of the workers. Non-financial incentives will also play an important role in motivating the workforce.
5. **Empowerment of human resources:** Empowerment means authorizing every member of a society or organization to take of his/her own destiny realizing his/her full potential. It involves giving more power to those who, at present, have little control what they do and little ability to influence the decisions being made around them.
6. **Building core competency:** The human resource manager has a great role to play in developing core competency by the firm. A core competence is a unique strength of an organization which may not be shared by others. This may be in the form of human resources, marketing, capability, or technological capability. If the business is organized on the basis of core competency, it is likely to generate competitive advantage. Because of this reason, many organizations have restructured their businesses by divesting those businesses which do not match core competence. Organization of business around core competence implies leveraging the limited resources of a firm. It needs creative, courageous and dynamic leadership having faith in organization's human resources.
6. **Development of works ethics and culture:** Greater efforts will be needed to achieve cohesiveness because workers will have transient commitment to groups. As changing work ethic requires increasing emphasis on individuals, jobs will have to be redesigned to provide challenge. Flexible starting and quitting times for employees may be necessary. Focus will shift from extrinsic to intrinsic motivation. A vibrant work culture will have to be developed in the organizations to create an atmosphere of trust among people and to encourage creative ideas by the people. Far reaching changes with the help of technical knowledge will be required for this purpose.

Summary

Overall strategies are to be divided and sub-divided into different functional areas to govern as to how key activities of the business are to be managed. Functional strategies play two important roles – to provide support to the overall business strategy and spell out as to how functional managers will work. Functional strategies facilitate flow of strategic decisions to the different parts of an organization.

This chapter covers different categories of functional level strategies, viz., marketing, production, finance and human resources. The functional strategy related to the marketing area deals with different aspects of marketing process and marketing mix – product, price, place and promotion. The chapter also elucidates financial strategy formulation - acquiring capital to implement strategies, projected financial statements, management of funds and evaluating the worth of a business.

Strategies related to production system are significant as they deal with vital issues affecting the capability of the organization to achieve its objectives. For a business organization effective logistics strategy will involve to solve certain problems with the help of supply chain management. Supply chain refers to the linkages between suppliers, manufacturers and customers. Implementing and successfully running supply chain management system will involve synergistical mix of product development, material procurement, manufacturing, physical distribution, outsourcing, customer services and performance measurement.

Research and Development personnel can play an important and integral role in strategic implementation. There must be effective interactions between R & D departments and other functional departments in implementing different types of business strategies.

Human resource management function has been accepted as a strategic partner in the formulation and implementation of organizational strategies. The strategic role of human resource management is also explained in the chapter.