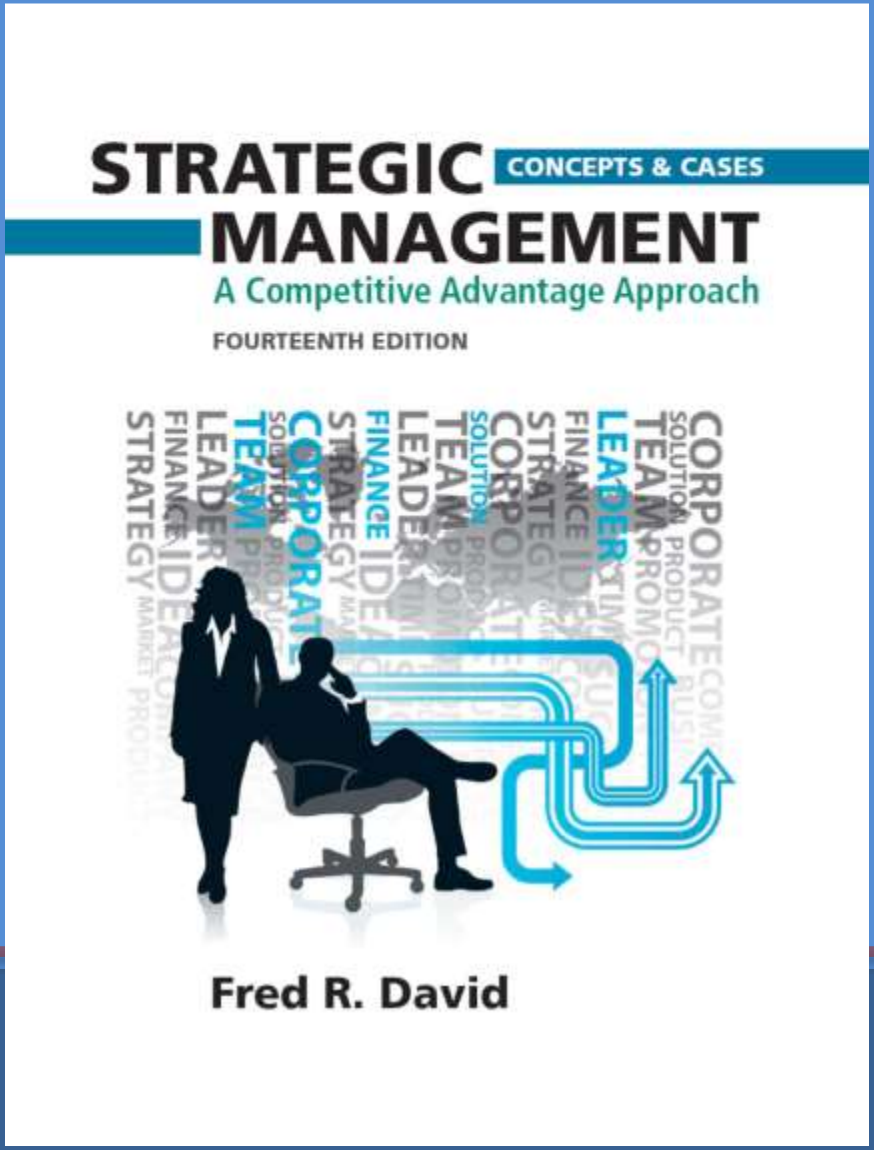


Strategy Review, Evaluation, and Control

Chapter Nine

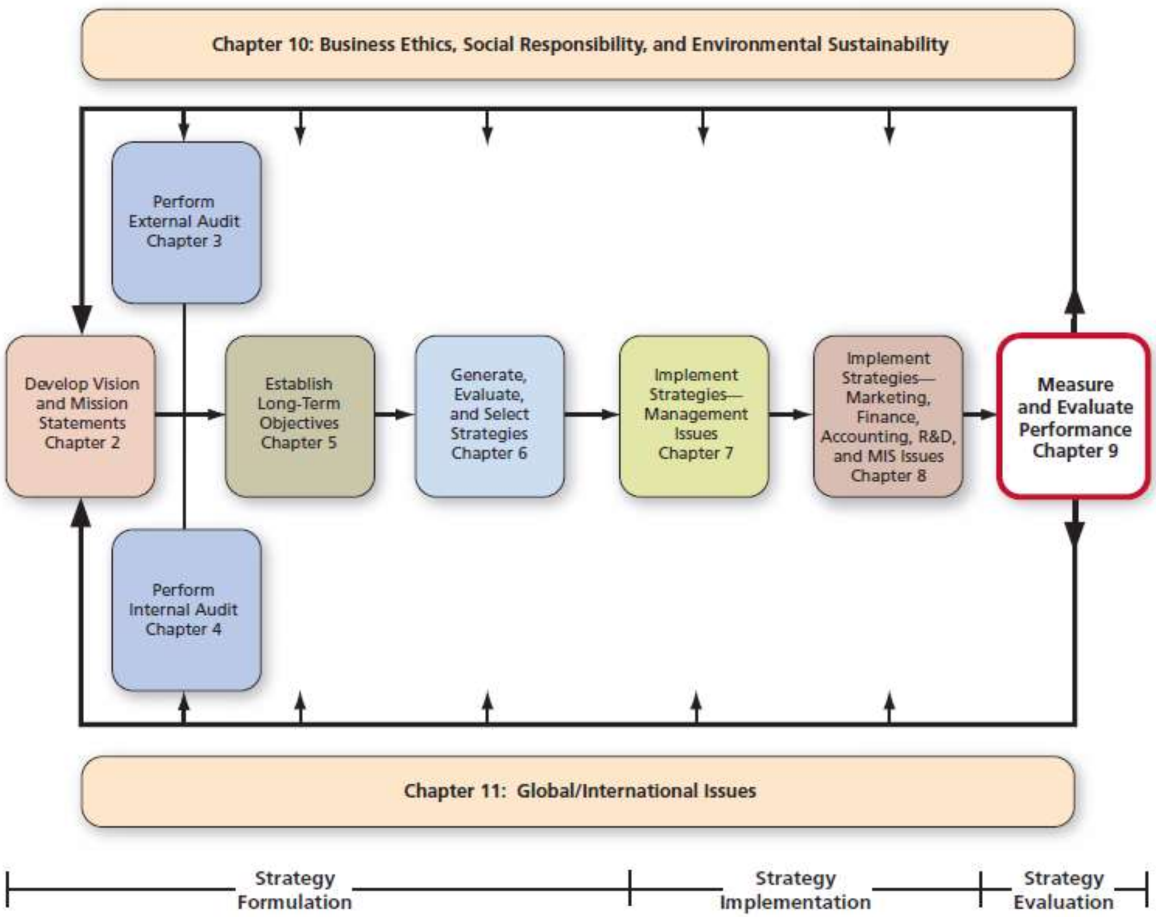
Chapter Objectives

1. Describe a practical framework for evaluating strategies.
2. Explain why strategy evaluation is complex, sensitive, and yet essential for organizational success.
3. Discuss the importance of contingency planning in strategy evaluation.
4. Discuss the role of auditing in strategy evaluation.
5. Discuss the Balanced Scorecard.
6. Discuss three twenty-first-century challenges in strategic management.

A Comprehensive Strategic-Management Model

FIGURE 9-1

A Comprehensive Strategic-Management Model



The Nature of Strategy Evaluation

Strategy evaluation includes three basic activities:

1. examining the underlying bases of a firm's strategy
2. comparing expected results with actual results
3. taking corrective actions to ensure that performance conforms to plans

The Nature of Strategy Evaluation

- Consonance and advantage are mostly based on a firm's external assessment
- Consistency and feasibility are largely based on an internal assessment

Rumelt's Criteria for Evaluating Strategies

TABLE 9-1 Rumelt's Criteria for Evaluating Strategies

Consistency

A strategy should not present inconsistent goals and policies. Organizational conflict and interdepartmental bickering are often symptoms of managerial disorder, but these problems may also be a sign of strategic inconsistency. Three guidelines help determine if organizational problems are due to inconsistencies in strategy:

- If managerial problems continue despite changes in personnel and if they tend to be issue-based rather than people-based, then strategies may be inconsistent.
- If success for one organizational department means, or is interpreted to mean, failure for another department, then strategies may be inconsistent.
- If policy problems and issues continue to be brought to the top for resolution, then strategies may be inconsistent.

Consonance

Consonance refers to the need for strategists to examine *sets of trends*, as well as individual trends, in evaluating strategies. A strategy must represent an adaptive response to the external environment and to the critical changes occurring within it. One difficulty in matching a firm's key internal and external factors in the formulation of strategy is that most trends are the result of interactions among other trends. For example, the day-care explosion came about as a combined result of many trends that included a rise in the average level of education, increased inflation, and an increase in women in the workforce. Although single economic or demographic trends might appear steady for many years, there are waves of change going on at the interaction level.

Rumelt's Criteria for Evaluating Strategies

Feasibility

A strategy must neither overtax available resources nor create unsolvable subproblems. The final broad test of strategy is its feasibility; that is, can the strategy be attempted within the physical, human, and financial resources of the enterprise? The financial resources of a business are the easiest to quantify and are normally the first limitation against which strategy is evaluated. It is sometimes forgotten, however, that innovative approaches to financing are often possible. Devices, such as captive subsidiaries, sale-leaseback arrangements, and tying plant mortgages to long-term contracts, have all been used effectively to help win key positions in suddenly expanding industries. A less quantifiable, but actually more rigid, limitation on strategic choice is that imposed by individual and organizational capabilities. In evaluating a strategy, it is important to examine whether an organization has demonstrated in the past that it possesses the abilities, competencies, skills, and talents needed to carry out a given strategy.

Advantage

A strategy must provide for the creation and/or maintenance of a competitive advantage in a selected area of activity. Competitive advantages normally are the result of superiority in one of three areas: (1) resources, (2) skills, or (3) position. The idea that the positioning of one's resources can enhance their combined effectiveness is familiar to military theorists, chess players, and diplomats. Position can also play a crucial role in an organization's strategy. Once gained, a good position is defensible—meaning that it is so costly to capture that rivals are deterred from full-scale attacks. Positional advantage tends to be self-sustaining as long as the key internal and environmental factors that underlie it remain stable. This is why entrenched firms can be almost impossible to unseat, even if their raw skill levels are only average. Although not all positional advantages are associated with size, it is true that larger organizations tend to operate in markets and use procedures that turn their size into advantage, while smaller firms seek product/market positions that exploit other types of advantage. The principal characteristic of good position is that it permits the firm to obtain advantage from policies that would not similarly benefit rivals without the same position. Therefore, in evaluating strategy, organizations should examine the nature of positional advantages associated with a given strategy.

A Few Big Company Household Names That Disappeared Over Past Years

TABLE 9-3 A Few Big Company Household Names That Disappeared Over Past Years

Compaq	Compaq was one of the largest sellers of PCs in the world until, under duress, the company was acquired by Hewlett-Packard and their name dissolved.
E.F. Hutton	"When E.F. Hutton speaks, people listen," claimed the well-known slogan from the 1970s and 1980s. But money laundering and fraud scandals caused people to stop listening. What barely remains of the once proud firm is today part of Citigroup.
PaineWebber	Founded in 1880 by William Alfred Paine and Wallace G. Webber, PaineWebber by 1990 had 200 brokerage branch offices in 42 states and six offices in Asia and Europe. But in 2000, it merged with UBS AG to become UBS PaineWebber. Then in 2003, "PaineWebber" was dropped and replaced with UBS Wealth Management USA.
Eastern Airlines	Eastern Airlines once dominated much of the domestic travel industry along the profitable East Coast U.S. corridor, but deteriorating labor relations forced the firm into bankruptcy, and it ceased operations in 1991.
Woolworth's	Founded in 1879, Woolworth's became the model for five-and-dime stores throughout the United States. The rise of Wal-Mart and K-mart ended Woolworth's reign.
Arthur Andersen	Arthur Andersen was once a member of the "Big 8" accounting firms, which later became the "Big 5." Andersen's downfall was its role as Enron's auditor, whereby it had approved a whole host of illegal accounting.
TransWorld Airlines (TWA)	Founded in 1930, TWA once dominated airline travel in the United States but eventually declared bankruptcy and was absorbed into American Airlines in 2001.

Why Strategy Evaluation is More Difficult Today

1. A dramatic increase in the environment's complexity
2. The increasing difficulty of predicting the future with accuracy
3. The increasing number of variables
4. The rapid rate of obsolescence of even the best plans

Why Strategy Evaluation is More Difficult Today

5. The increase in the number of both domestic and world events affecting organizations
6. The decreasing time span for which planning can be done with any degree of certainty

The Process of Evaluating Strategies

- Strategy evaluation should initiate managerial questioning of expectations and assumptions, should trigger a review of objectives and values, and should stimulate creativity in generating alternatives and formulating criteria of evaluation

The Process of Evaluating Strategies

- Evaluating strategies on a continuous rather than on a periodic basis allows benchmarks of progress to be established and more effectively monitored
- Successful strategies combine patience with a willingness to promptly take corrective actions when necessary

Reviewing Bases of Strategy

- How have competitors reacted to our strategies?
- How have competitors' strategies changed?
- Have major competitors' strengths and weaknesses changed?
- Why are competitors making certain strategic changes?

Reviewing Bases of Strategy

- Why are some competitors' strategies more successful than others?
- How satisfied are our competitors with their present market positions and profitability?
- How far can our major competitors be pushed before retaliating?
- How could we more effectively cooperate with our competitors?

Key Questions to Address in Evaluating Strategies

1. Are our internal strengths still strengths?
2. Have we added other internal strengths? If so, what are they?
3. Are our internal weaknesses still weaknesses?
4. Do we now have other internal weaknesses? If so, what are they?

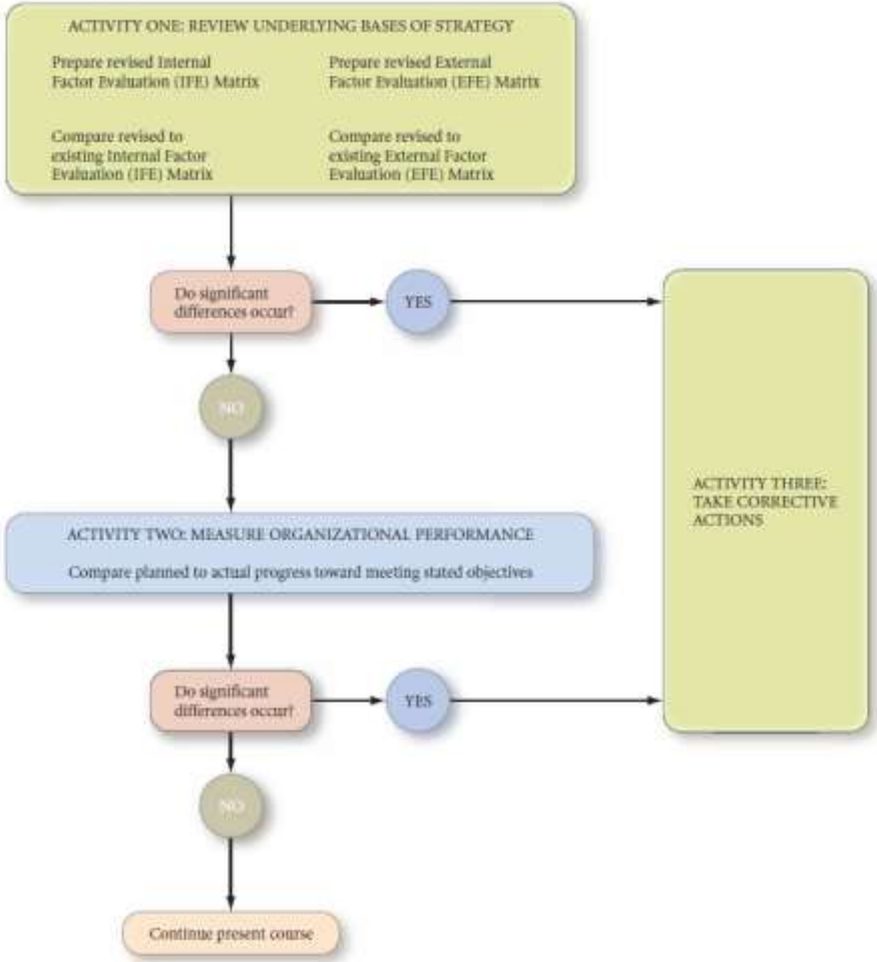
Key Questions to Address in Evaluating Strategies

5. Are our external opportunities still opportunities?
6. Are there now other external opportunities? If so, what are they?
7. Are our external threats still threats?
8. Are there now other external threats? If so, what are they?
9. Are we vulnerable to a hostile takeover?

A Strategy-Evaluation Framework

FIGURE 9-2

A Strategy-Evaluation Framework



Measuring Organizational Performance

Strategists use common quantitative criteria to make **three critical comparisons**:

- Comparing the firm's performance over different time periods
- Comparing the firm's performance to competitors'
- Comparing the firm's performance to industry averages

Problems with Quantitative Criteria

- Most quantitative criteria are geared to annual objectives rather than long-term objectives
- Different accounting methods can provide different results on many quantitative criteria
- Intuitive judgments are almost always involved in deriving quantitative criteria

Additional Key Questions

- How good is the firm's balance of investments between high-risk and low-risk projects?
- How good is the firm's balance of investments between long-term and short-term projects?
- How good is the firm's balance of investments between slow-growing markets and fast-growing markets?

Additional Key Questions

- How good is the firm's balance of investments among different divisions?
- To what extent are the firm's alternative strategies socially responsible?
- What are the relationships among the firm's key internal and external strategic factors?
- How are major competitors likely to respond to particular strategies?

Corrective Actions

TABLE 9-6 Corrective Actions Possibly Needed to Correct Unfavorable Variances

1. Alter the firm's structure
2. Replace one or more key individuals
3. Divest a division
4. Alter the firm's vision and/or mission
5. Revise objectives
6. Alter strategies
7. Devise new policies
8. Install new performance incentives
9. Raise capital with stock or debt
10. Add or terminate salespersons, employees, or managers
11. Allocate resources differently
12. Outsource (or rein in) business functions

The Balanced Scorecard

1. How well is the firm continually improving and creating value along measures such as innovation, technological leadership, product quality, operational process efficiencies, and so on?

The Balanced Scorecard

2. How well is the firm sustaining and even improving upon its core competencies and competitive advantages?
3. How satisfied are the firm’s customers?

The Balanced Scorecard

- The Balanced Scorecard approach to strategy evaluation aims to balance long-term with short-term concerns, to balance financial with nonfinancial concerns, and to balance internal with external concerns.

An Example Balanced Scorecard

TABLE 9-7 An Example Balanced Scorecard

Area of Objectives	Measure or Target	Time Expectation	Primary Responsibility
Customers			
1.			
2.			
3.			
4.			
Managers/Employees			
1.			
2.			
3.			
4.			
Operations/Processes			
1.			
2.			
3.			
4.			
Community/Social Responsibility			
1.			
2.			
3.			
4.			
Business Ethics/Natural Environment			
1.			
2.			
3.			
4.			
Financial			
1.			
2.			
3.			
4.			

Characteristics of an Effective Evaluation System

- Strategy evaluation activities must be economical
  - too much information can be just as bad as too little information
  - too many controls can do more harm than good
- Activities should be meaningful
  - should specifically relate to a firm's objectives

Characteristics of an Effective Evaluation System

- Activities should provide timely information
- Activities should be designed to provide a true picture of what is happening
- Activities should not dominate decisions
  - should foster mutual understanding, trust, and common sense

Contingency Planning

- If a major competitor withdraws from particular markets as intelligence reports indicate, what actions should our firm take?
- If our sales objectives are not reached, what actions should our firm take to avoid profit losses?

Contingency Planning

- If demand for our new product exceeds plans, what actions should our firm take to meet the higher demand?
- If certain disasters occur, what actions should our firm take?
- If a new technological advancement makes our new product obsolete sooner than expected, what actions should our firm take?

Effective Contingency Planning

1. Identify both beneficial and unfavorable events that could possibly derail the strategy or strategies.
2. Specify trigger points.
3. Assess the impact of each contingent event.
4. Develop contingency plans.

Effective Contingency Planning

5. Assess the counter-impact of each contingency plan.
6. Determine early warning signals for key contingent events.
7. For contingent events with reliable early warning signals, develop advance action plans to take advantage of the available lead time.

Auditing

- **Auditing**
  - “a systematic process of objectively obtaining and evaluating evidence regarding assertions about economic actions and events to ascertain the degree of correspondence between these assertions and established criteria, and communicating the results to interested users”

Twenty-First-Century Challenges in Strategic Management

- Deciding whether the process should be more an art or a science
- Deciding whether strategies should be visible or hidden from stakeholders
- Deciding whether the process should be more top-down or bottom-up in their firm