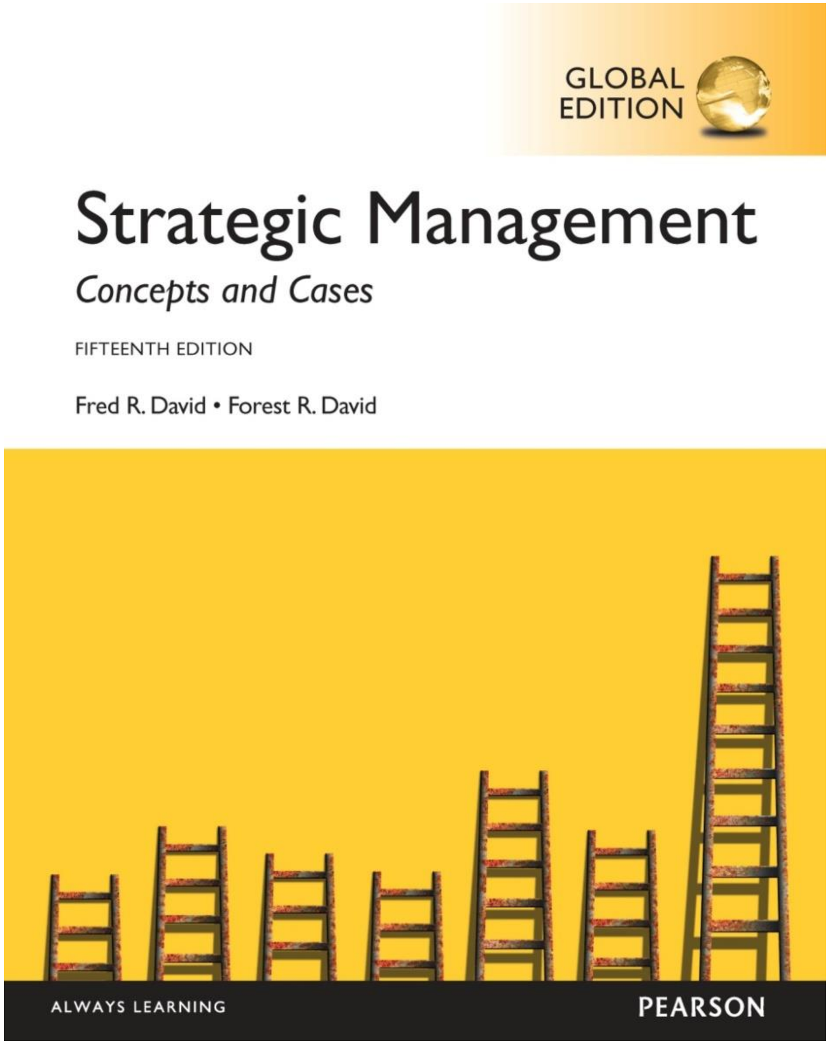


Strategy GENERATION and SELECTION

Chapter Eight

The Process of Generating and Selecting Strategies

- A manageable set of the most attractive alternative strategies must be developed
- The advantages, disadvantages, trade-offs, costs, and benefits of these strategies should be determined

The Process of Generating and Selecting Strategies

- Identifying and evaluating alternative strategies should involve many of the managers and employees who earlier assembled the organizational vision and mission statements, performed the external audit, and conducted the internal audit.

The Process of Generating and Selecting Strategies

- Alternative strategies proposed by participants should be considered and discussed in a series of meetings.
- Proposed strategies should be listed in writing.
- When all feasible strategies identified by participants are given and understood, the strategies should be ranked in order of attractiveness.

The Strategy-Formulation Analytical Framework

STAGE 1: THE INPUT STAGE

External Factor Evaluation (EFE) Matrix	Competitive Profile Matrix (CPM)	Internal Factor Evaluation (IFE) Matrix

STAGE 2: THE MATCHING STAGE

Strengths-Weaknesses-Opportunities-Threats (SWOT) Matrix	Strategic Position and Action Evaluation (SPACE) Matrix	Boston Consulting Group (BCG) Matrix	Internal-External (IE) Matrix	Grand Strategy Matrix

STAGE 3: THE DECISION STAGE

Quantitative Strategic Planning Matrix (QSPM)

FIGURE 8-2

The Strategy-Formulation Analytical Framework

A Comprehensive Strategy-Formulation Framework

- **Stage 1 - Input Stage**
  - summarizes the basic input information needed to formulate strategies
  - consists of the EFE Matrix, the IFE Matrix, and the Competitive Profile Matrix (CPM)

A Comprehensive Strategy-Formulation Framework

- **Stage 2 - Matching Stage**
  - focuses on generating feasible alternative strategies by aligning key external and internal factors
  - techniques include the Strengths-Weaknesses-Opportunities-Threats (SWOT) Matrix, the Strategic Position and Action Evaluation (SPACE) Matrix, the Boston Consulting Group (BCG) Matrix, the Internal-External (IE) Matrix, and the Grand Strategy Matrix

A Comprehensive Strategy-Formulation Framework

- **Stage 3 - Decision Stage**
  - involves the Quantitative Strategic Planning Matrix (QSPM)
  - reveals the relative attractiveness of alternative strategies and thus provides objective basis for selecting specific strategies

Matching Key External and Internal Factors to Formulate Alternative Strategies

TABLE 8-1 Matching Key External and Internal Factors to Formulate Alternative Strategies

Key Internal Factor	Key External Factor	Resultant Strategy
Excess working capital (an internal strength)	+ 20 percent annual growth in the cell phone industry (an external opportunity)	= Acquire Cellfone, Inc.
Insufficient capacity (an internal weakness)	+ Exit of two major foreign competitors from the industry (an external opportunity)	= Pursue horizontal integration by buying competitors' facilities
Strong research and development expertise (an internal strength)	+ Decreasing numbers of younger adults (an external threat)	= Develop new products for older adults
Poor employee morale (an internal weakness)	+ Rising health-care costs (an external threat)	= Develop a new wellness program

The Matching Stage

- The **Strengths-Weaknesses-Opportunities-Threats (SWOT) Matrix** helps managers develop four types of strategies:
  - SO (strengths-opportunities) Strategies
  - WO (weaknesses-opportunities) Strategies
  - ST (strengths-threats) Strategies
  - WT (weaknesses-threats) Strategies

The Matching Stage

- ***SO* Strategies**
  - use a firm’s internal strengths to take advantage of external opportunities

- ***WO* Strategies**
  - aim at improving internal weaknesses by taking advantage of external opportunities

The Matching Stage

- ***ST* Strategies**
  - use a firm's strengths to avoid or reduce the impact of external threats
- ***WT* Strategies**
  - defensive tactics directed at reducing internal weakness and avoiding external threats

SWOT Matrix

1. List the firm's key external opportunities
2. List the firm's key external threats
3. List the firm's key internal strengths
4. List the firm's key internal weaknesses
5. Match internal strengths with external opportunities

SWOT Matrix (cont.)

6. Match internal weaknesses with external opportunities, and record the resultant WO Strategies

7. Match internal strengths with external threats, and record the resultant ST Strategies

8. Match internal weaknesses with external threats, and record the resultant WT Strategies

A SWOT Matrix for a Retail Computer Store

	Strengths	Weaknesses
	1. Inventory turnover up 5.8 to 6.7	1. Software revenues in store down 12 percent
	2. Average customer purchase up \$97 to \$128	2. Location of store hurt by new Hwy 34
	3. Employee morale is excellent	3. Carpet and paint in store in disrepair
	4. In-store promotions = 20 percent increase in sales	4. Bathroom in store needs refurbishing
	5. Newspaper advertising expenditures down 10 percent	5. Total store revenues down 8 percent
	6. Revenues from repair and service in store up 16 percent	6. Store has no website
	7. In-store technical support persons have MIS degrees	7. Supplier on-time-delivery up to 2.4 days
	8. Store's debt-to-total-assets ratio down 34 percent	8. Customer checkout process too slow
		9. Revenues per employee up 19 percent

FIGURE 8-3
A SWOT Matrix for a Retail Computer Store

A SWOT Matrix for a Retail Computer Store

Opportunities	SO Strategies	WO Strategies
1. Population of city growing 10 percent 2. Rival computer store opening one mile away 3. Vehicle traffic passing store up 12 percent 4. Vendors average six new products a year 5. Senior citizen use of computers up 8 percent 6. Small business growth in area up 10 percent 7. Desire for websites up 18 percent by realtors 8. Desire for websites up 12 percent by small firms	1. Add four new in-store promotions monthly (S4, O3) 2. Add two new repair and service persons (S6, O5) 3. Send flyer to all seniors over age 55 (S5, O5)	1. Purchase land to build new store (W2, O2) 2. Install new carpet, paint, and bath (W3, W4, O1) 3. Up website services by 50 percent (W6, O7, O8) 4. Launch mailout to all realtors in city (W5, O7)
Threats	**ST Strategies**	**WT Strategies**
1. Best Buy opening new store in one year nearby 2. Local university offers computer repair 3. New bypass Hwy 34 in 1 year will divert traffic 4. New mall being built nearby 5. Gas prices up 14 percent 6. Vendors raising prices 8 percent	1. Hire two more repair persons and market these new services (S6, S7, T1) 2. Purchase land to build new store (S8, T3) 3. Raise out-of-store service calls from $60 to $80 (S6, T5)	1. Hire two new cashiers (W8, T1, T4) 2. Install new carpet, paint, and bath (W3, W4, T1)

FIGURE 8-3
A SWOT Matrix for a Retail Computer Store

The SPACE Matrix

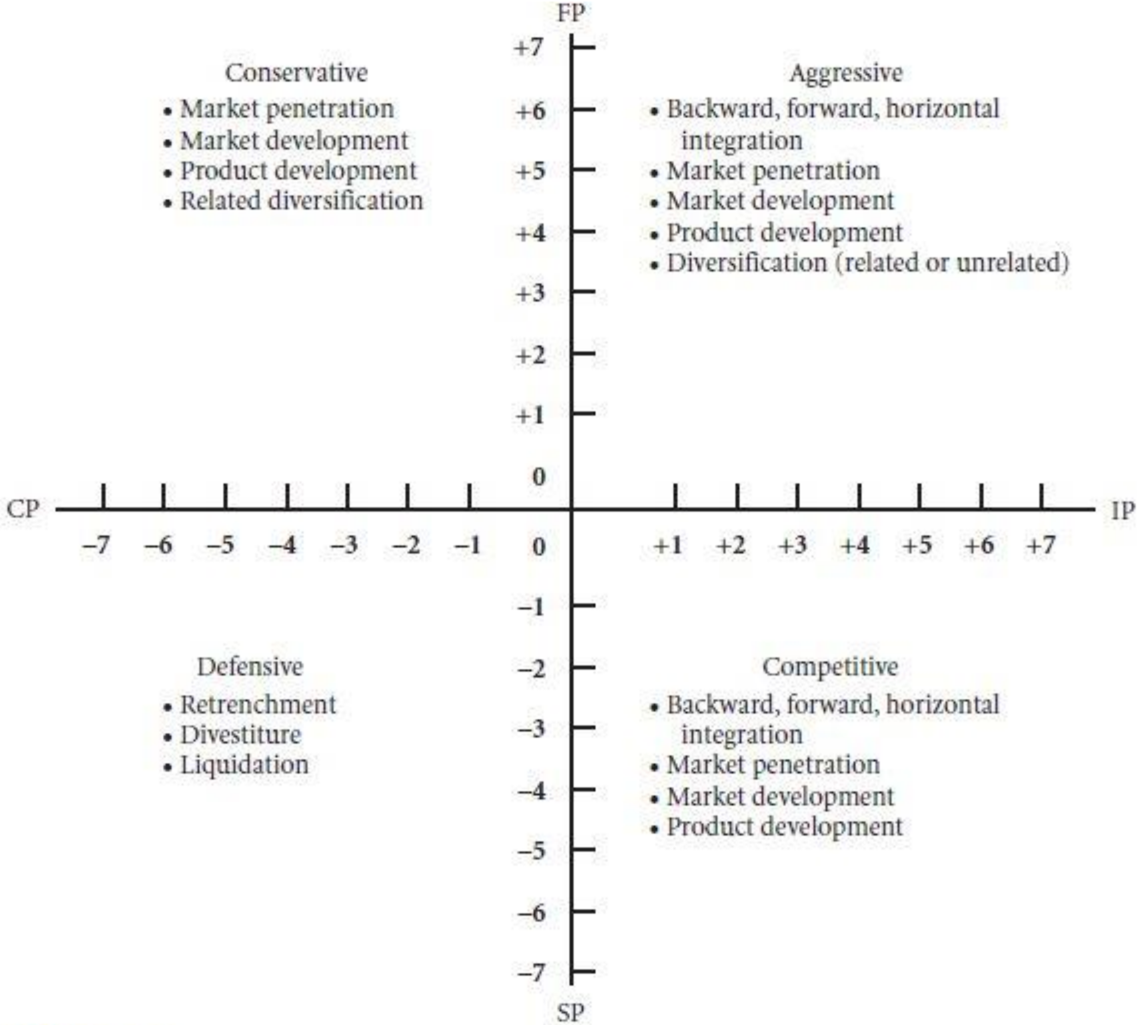


FIGURE 8-4

The SPACE Matrix

The Strategic Position and Action Evaluation (SPACE) Matrix

- **Strategic Position and Action Evaluation (SPACE) Matrix**
  - four-quadrant framework indicates whether aggressive, conservative, defensive, or competitive strategies are most appropriate for a given organization

The Strategic Position and Action Evaluation (SPACE) Matrix

- Two internal dimensions (financial position [FP] and competitive position [CP])
- Two external dimensions (stability position [SP] and industry position [IP])
- Most important determinants of an organization's overall strategic position

Factors That Make Up the SPACE Matrix Axes

TABLE 8-2 Example Factors That Make Up the SPACE Matrix Axes

Internal Strategic Position	External Strategic Position
Financial Position (FP)	*Stability Position (SP)*
Return on investment	Technological changes
Leverage	Rate of inflation
Liquidity	Demand variability
Working capital	Price range of competing products
Cash flow	Barriers to entry into market
Inventory turnover	Competitive pressure
Earnings per share	Ease of exit from market
Price earnings ratio	Price elasticity of demand
	Risk involved in business
Competitive Position (CP)	*Industry Position (IP)*
Market share	Growth potential
Product quality	Profit potential
Product life cycle	Financial stability
Customer loyalty	Extent leveraged
Capacity utilization	Resource utilization
Technological know-how	Ease of entry into market
Control over suppliers and distributors	Productivity, capacity utilization

Steps to Develop a SPACE Matrix

1. Select a set of variables to define financial position (FP), competitive position (CP), stability position (SP), and industry position (IP).

Steps to Develop a SPACE Matrix

2. Assign a numerical value ranging from +1 (worst) to +7 (best) to each of the variables that make up the FP and IP dimensions. Assign a numerical value ranging from –1 (best) to –7 (worst) to each of the variables that make up the SP and CP dimensions.

Steps to Develop a SPACE Matrix

3. Compute an average score for FP, CP, IP, and SP.

4. Plot the average scores for FP, IP, SP, and CP on the appropriate axis in the SPACE Matrix.

5. Add the two scores on the *x*-axis and plot the resultant point on *X.* Add the two scores on the *y*-axis and plot the resultant point on *Y.* Plot the intersection of the new *xy* point.

Steps to Develop a SPACE Matrix

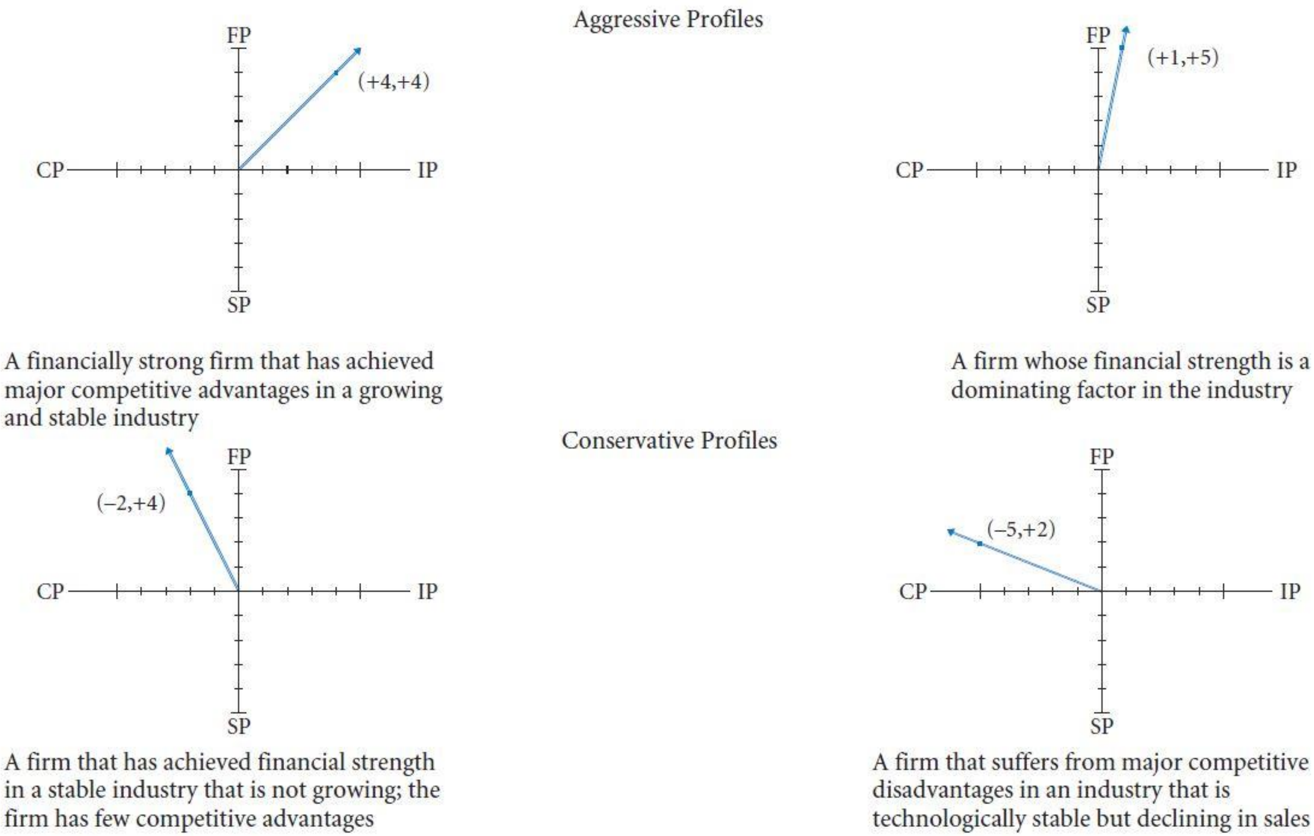
6. Draw a *directional vector* from the origin of the SPACE Matrix through the new intersection point.

- This vector reveals the type of strategies recommended for the organization: aggressive, competitive, defensive, or conservative

Example Strategy Profiles

FIGURE 8-5

Example Strategy Profiles



Example Strategy Profiles

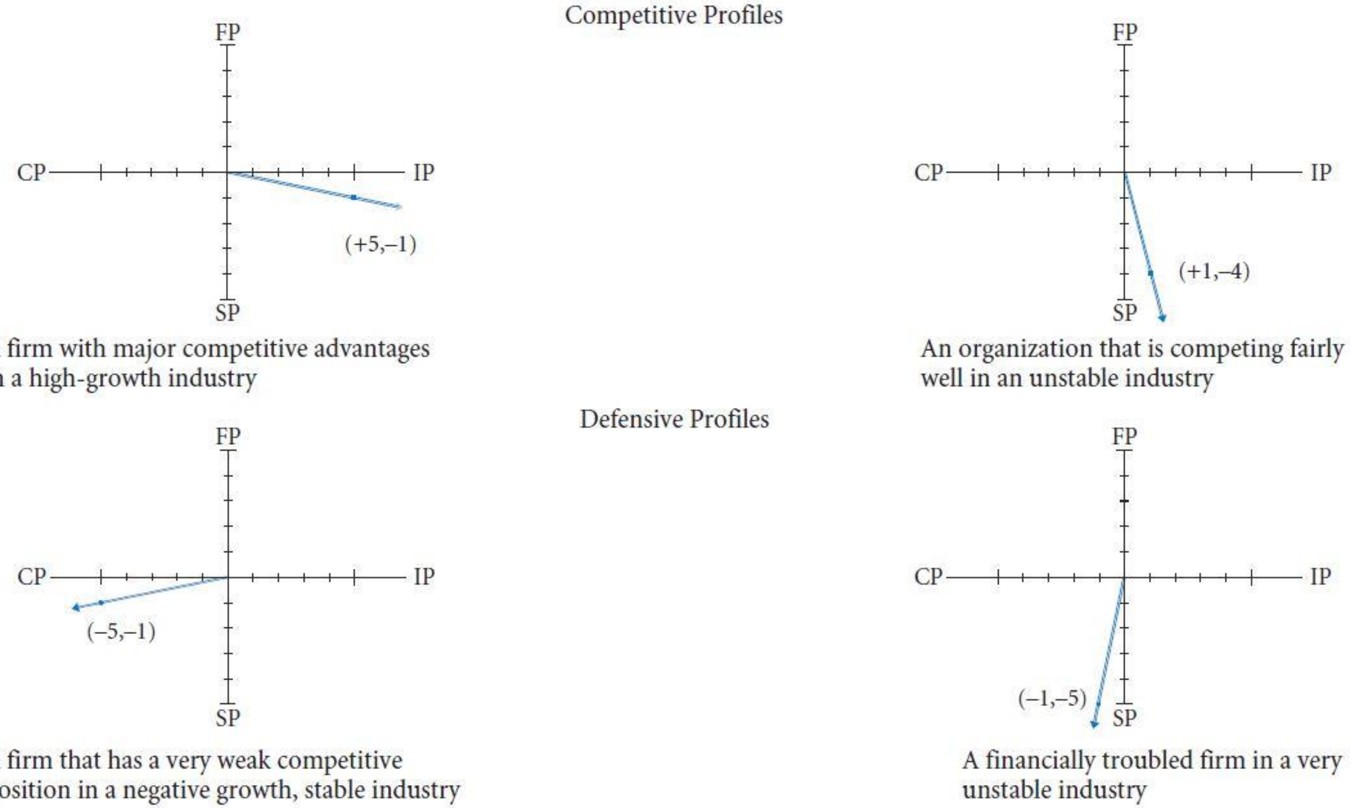


FIGURE 8-5

Example Strategy Profiles

The Boston Consulting Group (BCG) Matrix

- **BCG Matrix**
  - graphically portrays differences among divisions in terms of relative market share position and industry growth rate
  - allows a multidivisional organization to manage its portfolio of businesses by examining the relative market share position and the industry growth rate of each division relative to all other divisions in the organization

The BCG Matrix

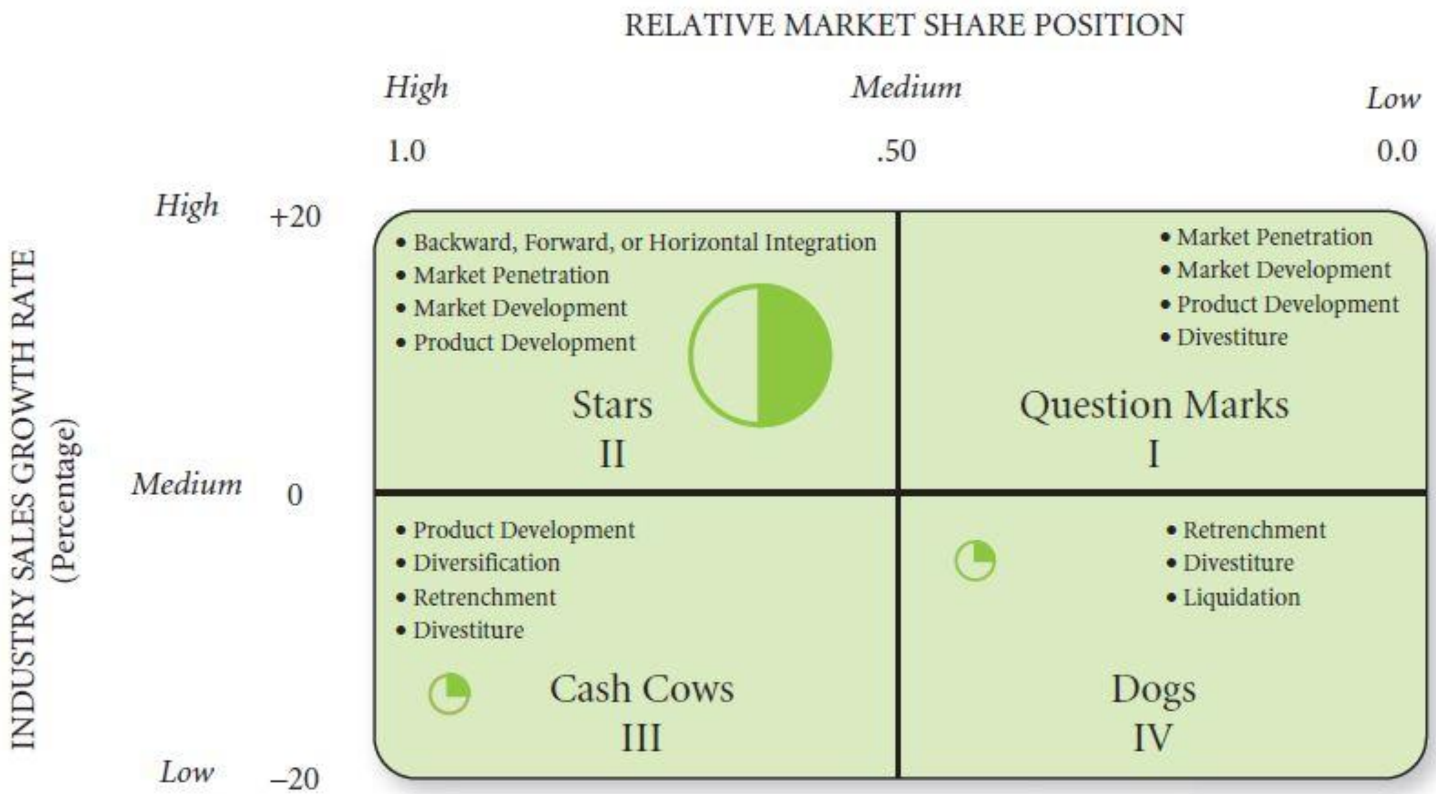


FIGURE 8-7

The BCG Matrix

The BCG Matrix

- **Question marks – Quadrant I**
  - Organization must decide whether to strengthen them by pursuing an intensive strategy (market penetration, market development, or product development) or to sell them
- **Stars – Quadrant II**
  - represent the organization’s best long-run opportunities for growth and profitability

The BCG Matrix

- **Cash Cows – Quadrant III**
  - generate cash in excess of their needs
  - should be managed to maintain their strong position for as long as possible
- **Dogs – Quadrant IV**
  - compete in a slow- or no-market-growth industry
  - businesses are often liquidated, divested, or trimmed down through retrenchment

The BCG Matrix

- The major benefit of the BCG Matrix is that it draws attention to the cash flow, investment characteristics, and needs of an organization’s various divisions

The Internal-External (IE) Matrix

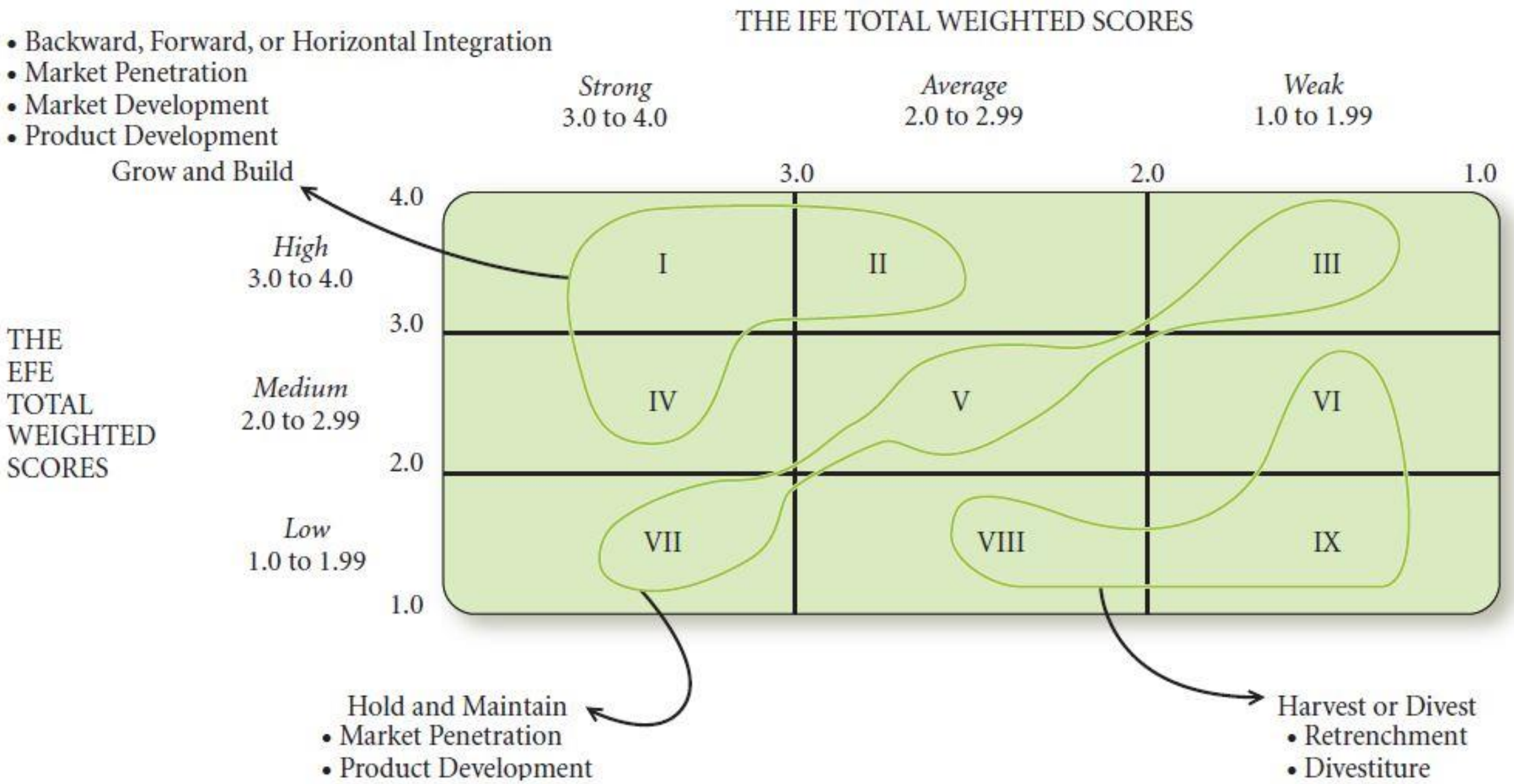


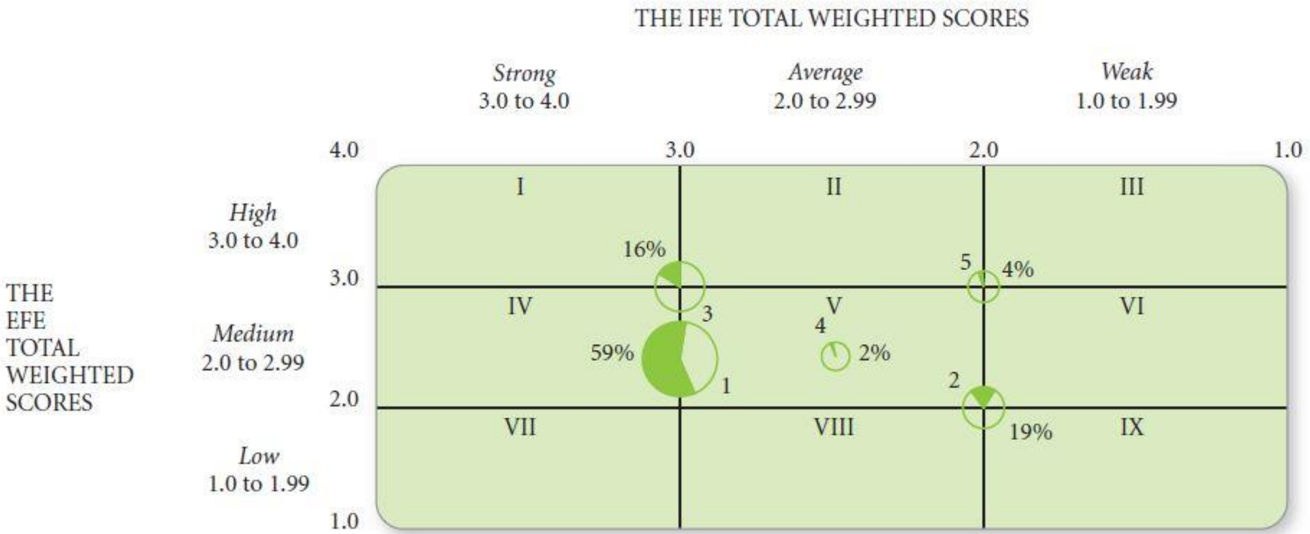
FIGURE 8-10

The Internal–External (IE) Matrix

The Internal-External (IE) Matrix

- The **IE Matrix** is based on two key dimensions: the IFE total weighted scores on the x-axis and the EFE total weighted scores on the y-axis
- **Three major regions**
  - Grow and build
  - Hold and maintain
  - Harvest or divest

The IE Matrix



Grow and Build

Segments	*$ Revenue*	*% Revenue*	*$ Profit*	*% Profit*	*EFE Scores*	*IFE Scores*
1.	$7,868	71.5%	$3,000	59%	2.5	3
2.	1,241	11.3%	1,000	19%	2	2
3.	1,578	14.3%	800	16%	3	3
4.	90	0.8%	100	2%	2.5	2.5
5.	223	2.1%	200	4%	3	2
Total	$11,000	100%	$5,100	100%	—	—

FIGURE 8-12
The IE Matrix

The Grand Strategy Matrix

- **Grand Strategy Matrix**
  - based on two evaluative dimensions: competitive position and market (industry) growth

The Grand Strategy Matrix

FIGURE 8-13
The Grand Strategy Matrix

The Grand Strategy Matrix

- **Quadrant I**
  - continued concentration on current markets (market penetration and market development) and products (product development) is an appropriate strategy
- **Quadrant II**
  - unable to compete effectively
  - need to determine why the firm’s current approach is ineffective and how the company can best change to improve its competitiveness

The Grand Strategy Matrix

- **Quadrant III**
  - must make some drastic changes quickly to avoid further decline and possible liquidation
  - Extensive cost and asset reduction (retrenchment) should be pursued first
- **Quadrant IV**
  - have characteristically high cash-flow levels and limited internal growth needs and often can pursue related or unrelated diversification successfully

The Quantitative Strategic Planning Matrix (QSPM)

- **Quantitative Strategic Planning Matrix (QSPM)**
  - objectively indicates which alternative strategies are best
  - uses input from Stage 1 analyses and matching results from Stage 2 analyses to decide objectively among alternative strategies

The Quantitative Strategic Planning Matrix (QSPM)

TABLE 8-7 The Quantitative Strategic Planning Matrix—QSPM

		Strategic Alternatives		
Key Factors	Weight	Strategy 1	Strategy 2	Strategy 3
Key External Factors				
Economy				
Political/Legal/Governmental				
Social/Cultural/Demographic/Environmental				
Technological				
Competitive				
Key Internal Factors				
Management				
Marketing				
Finance/Accounting				
Production/Operations				
Research and Development				
Management Information Systems				

Steps in a QSPM

1. Make a list of the firm's key external opportunities/threats and internal strengths/ weaknesses in the left column of the QSPM.

2. Assign weights to each key external and internal factor.

3. Examine the Stage 2 (matching) matrices, and identify alternative strategies that the organization should consider implementing.

Steps in a QSPM (cont.)

4. Determine the Attractiveness Scores (AS).

5. Compute the Total Attractiveness Scores.

6. Compute the Sum Total Attractiveness Score.

Positive Features of the QSPM

- Sets of strategies can be examined sequentially or simultaneously
- Requires strategists to integrate pertinent external and internal factors into the decision process
- Can be adapted for use by small and large for-profit and nonprofit organizations

Limitations of the QSPM

- Always requires intuitive judgments and educated assumptions
- Only as good as the prerequisite information and matching analyses upon which it is based

A QSPM for a Retail Computer Store

TABLE 8-8 **A QSPM for a Retail Computer Store**

		STRATEGIC ALTERNATIVES			
		1		2	
		Buy New Land and Build New Larger Store		Fully Renovate Existing Store	
Key Factors	*Weight*	*AS*	*TAS*	*AS*	*TAS*
Opportunities					
1. Population of city growing 10 percent	0.10	4	0.40	2	0.20
2. Rival computer store opening one mile away	0.10	2	0.20	4	0.40
3. Vehicle traffic passing store up 12 percent	0.08	1	0.08	4	0.32
4. Vendors average six new products/year	0.05	—		—	
5. Senior citizen use of computers up 8 percent	0.05	—		—	
6. Small business growth in area up 10 percent	0.10	—		—	
7. Desire for websites up 18 percent by realtors	0.06	—		—	
8. Desire for websites up 12 percent by small firms	0.06	—		—	
Threats					
1. Best Buy opening new store nearby in one year	0.15	4	0.60	3	0.45
2. Local university offers computer repair	0.08	—		—	
3. New bypass for Hwy 34 in one year will divert traffic	0.12	4	0.48	1	0.12
4. New mall being built nearby	0.08	2	0.16	4	0.32
5. Gas prices up 14 percent	0.04	—		—	
6. Vendors raising prices 8 percent	0.03	—		—	
Total	**1.00**				

A QSPM for a Retail Computer Store (cont.)

TABLE 8-8 A QSPM for a Retail Computer Store

		STRATEGIC ALTERNATIVES			
		1		2	
		Buy New Land and Build New Larger Store		Fully Renovate Existing Store	
Key Factors	*Weight*	*AS*	*TAS*	*AS*	*TAS*
Strengths					
1. Inventory turnover increased from 5.8 to 6.7	0.05	—		—	
2. Average customer purchase increased from $97 to $128	0.07	2	0.14	4	0.28
3. Employee morale is excellent	0.10	—		—	
4. In-store promotions resulted in 20 percent increase in sales	0.05	—		—	
5. Newspaper advertising expenditures increased 10 percent	0.02	—		—	
6. Revenues from repair/service segment of store up 16 percent	0.15	4	0.60	3	0.45
7. In-store technical support personnel have MIS college degrees	0.05	—		—	
8. Store's debt-to-total-assets ratio declined to 34 percent	0.03	4	0.12	2	0.06
9. Revenues per employee up 19 percent	0.02	—		—	
Weaknesses					
1. Revenues from software segment of store down 12 percent	0.10	—		—	
2. Location of store negatively impacted by new Hwy 34	0.15	4	0.60	1	0.15
3. Carpet and paint in store somewhat in disrepair	0.02	1	0.02	4	0.08
4. Bathroom in store needs refurbishing	0.02	1	0.02	4	0.08
5. Revenues from businesses down 8%	0.04	3	0.12	4	0.16
6. Store has no website	0.05	—		—	
7. Supplier on-time delivery increased to 2.4 days	0.03	—		—	
8. Often customers have to wait to check out	0.05	2	0.10	4	0.20
Total	**1.00**		**3.64**		**3.27**

The Politics of Strategy Choice

- Political maneuvering consumes valuable time, subverts organizational objectives, diverts human energy, and results in the loss of some valuable employees
- Political biases and personal preferences get unduly embedded in strategy choice decisions

The Politics of Strategy Choice

- The hierarchy of command in an organization, combined with the career aspirations of different people and the need to allocate scarce resources, guarantees the formation of coalitions of individuals who strive to take care of themselves first and the organization second, third, or fourth

Tactics to Aid Strategists

- Choose Methods That Afford Employee Commitment
- Achieve Satisfactory Results with a Popular Strategy
- Shift from Specific to General Issues
- Focus on Long-Term Issues and Concerns
- Involve Middle Level Managers in Decisions

Governance Issues

- **Board of directors**
  - a group of individuals who are elected by the ownership of a corporation to have oversight and guidance over management and who look out for shareholders’ interests

Board of Director Duties and Responsibilities

TABLE 8-10 Board of Director Duties and Responsibilities

1. CONTROL AND OVERSIGHT OVER MANAGEMENT
   a. Select the Chief Executive Officer (CEO).
   b. Sanction the CEO's team.
   c. Provide the CEO with a forum.
   d. Ensure managerial competency.
   e. Evaluate management's performance.
   f. Set management's salary levels, including fringe benefits.
   g. Guarantee managerial integrity through continuous auditing.
   h. Chart the corporate course.
   i. Devise and revise policies to be implemented by management.
2. ADHERENCE TO LEGAL PRESCRIPTIONS
   a. Keep abreast of new laws.
   b. Ensure the entire organization fulfills legal prescriptions.
   c. Pass bylaws and related resolutions.
   d. Select new directors.
   e. Approve capital budgets.
   f. Authorize borrowing, new stock issues, bonds, and so on.
3. CONSIDERATION OF STAKEHOLDERS' INTERESTS
   a. Monitor product quality.
   b. Facilitate upward progression in employee quality of work life.
   c. Review labor policies and practices.
   d. Improve the customer climate.
   e. Keep community relations at the highest level.
   f. Use influence to better governmental, professional association, and educational contacts.
   g. Maintain good public image.
4. ADVANCEMENT OF STOCKHOLDERS' RIGHTS
   a. Preserve stockholders' equity.
   b. Stimulate corporate growth so that the firm will survive and flourish.
   c. Guard against equity dilution.
   d. Ensure equitable stockholder representation.
   e. Inform stockholders through letters, reports, and meetings.
   f. Declare proper dividends.
   g. Guarantee corporate survival.

Principles of Good Governance

1. No more than two directors are current or former company executives.
2. The audit, compensation, and nominating committees are made up solely of outside directors.
3. Each director owns a large equity stake in the company, excluding stock options.

Principles of Good Governance

4. Each director attends at least 75 percent of all meetings.
5. The board meets regularly without management present and evaluates its own performance annually.
6. The CEO is not also the chairperson of the board.
7. There are no interlocking directorships (where a director or CEO sits on another director's board).