INTRODUCTION

It is useful to consider strategy formulation as part of a strategic management process that comprises three phases: diagnosis, formulation, and implementation. Strategic management is an ongoing process to develop and revise future-oriented strategies that allow an organization to achieve its objectives, considering its capabilities, constraints, and the environment in which it operates.

Diagnosis includes: (a) performing a situation analysis (analysis of the internal environment of the organization), including identification and evaluation of current mission, strategic objectives, strategies, and results, plus major strengths and weaknesses; (b) analyzing the organization's external environment, including major opportunities and threats; and (c) identifying the major *critical issues*, which are a small set, typically two to five, of major problems, threats, weaknesses, and/or opportunities that require particularly high priority attention by management.

Formulation, the second phase in the strategic management process, produces a clear set of recommendations, with supporting justification, that revise as necessary the mission and objectives of the organization, and supply the strategies for accomplishing them. In formulation, we are trying to modify the current objectives and strategies in ways to make the organization more successful. This includes trying to create "sustainable" competitive advantages -- although most competitive advantages are eroded steadily by the efforts of competitors.

A good recommendation should be: effective in solving the stated problem(s), practical (can be implemented in this situation, with the resources available), feasible within a reasonable time frame, cost-effective, not overly disruptive, and acceptable to key "stakeholders" in the organization. It is important to consider "fits" between resources plus competencies with opportunities, and also fits between risks and expectations.

There are four primary steps in this phase:

* Reviewing the current key objectives and strategies of the organization, which usually would have been identified and evaluated as part of the diagnosis

* Identifying a rich range of strategic alternatives to address the three levels of strategy formulation outlined below, including but not limited to dealing with the critical issues

* Doing a balanced evaluation of advantages and disadvantages of the alternatives relative to their feasibility plus expected effects on the issues and contributions to the success of the organization

* Deciding on the alternatives that should be implemented or recommended.

In organizations, and in the practice of strategic management, strategies must be *implemented* to achieve the intended results. The most wonderful strategy in the history of the world is useless if not implemented successfully.

This third and final stage in the strategic management process involves developing an implementation plan and then doing whatever it takes to make the new strategy operational and effective in achieving the organization's objectives.

The remainder of this chapter focuses on strategy formulation, and is organized into six sections:

Three Aspects of Strategy Formulation, Corporate-Level Strategy, Competitive Strategy, Functional Strategy, Choosing Strategies, and Troublesome Strategies.

THREE ASPECTS OF STRATEGY FORMULATION

The following three aspects or levels of strategy formulation, each with a different focus, need to be dealt with in the formulation phase of strategic management. The three sets of recommendations must be internally consistent and fit together in a mutually supportive manner that forms an integrated hierarchy of strategy, in the order given.

Corporate Level Strategy: In this aspect of strategy, we are concerned with broad decisions about the total organization's scope and direction. Basically, we consider what changes should be made in our growth objective and strategy for achieving it, the lines of business we are in, and how these lines of business fit together. It is useful to think of three components of corporate level strategy: (a) growth or directional strategy (what should be our growth objective, ranging from retrenchment through stability to varying degrees of growth - and how do we accomplish this), (b) portfolio strategy (what should be our portfolio of lines of business, which implicitly requires reconsidering how much concentration or diversification we should have), and (c) parenting strategy (how we allocate resources and manage capabilities and activities across the portfolio -- where do we put special emphasis, and how much do we integrate our various lines of business).

Competitive Strategy (often called Business Level Strategy): This involves deciding how the company will compete within each line of business (LOB) or strategic business unit (SBU).

Functional Strategy: These more localized and shorter-horizon strategies deal with how each functional area and unit will carry out its functional activities to be effective and maximize resource productivity.

CORPORATE LEVEL STRATEGY

This comprises the overall strategy elements for the corporation as a whole, the grand strategy, if you please. Corporate strategy involves four kinds of initiatives:

* Making the necessary moves to establish positions in different businesses and achieve an appropriate amount and kind of diversification. A key part of corporate strategy is making decisions on how many, what types, and which specific lines of business the company should be in. This may involve deciding to increase or decrease the amount and breadth of diversification. It may involve closing out some LOB's (lines of business), adding others, and/or changing emphasis among LOB's.

* Initiating actions to boost the combined performance of the businesses the company has diversified into: This may involve vigorously pursuing rapid-growth strategies in the most promising LOB's, keeping the other core businesses healthy, initiating turnaround efforts in weak-performing LOB's with promise, and dropping LOB's that are no longer attractive or don't fit into the corporation's overall plans. It also may involve supplying financial, managerial, and other resources, or acquiring and/or merging other companies with an existing LOB.

* Pursuing ways to capture valuable cross-business strategic fits and turn them into competitive advantages -- especially transferring and sharing related technology, procurement leverage, operating facilities, distribution channels, and/or customers.

* Establishing investment priorities and moving more corporate resources into the most attractive LOB's.

It is useful to organize the corporate level strategy considerations and initiatives into a framework with the following three main strategy components: growth, portfolio, and parenting. These are discussed in the next three sections.

What Should be Our Growth Objective and Strategies?

Growth objectives can range from drastic retrenchment through aggressive growth.

Organizational leaders need to revisit and make decisions about the growth objectives and the fundamental strategies the organization will use to achieve them. There are forces that tend to push top decision-makers toward a growth stance even when a company is in trouble and should not be trying to grow, for example bonuses, stock options, fame, ego. Leaders need to resist such temptations and select a growth strategy stance that is appropriate for the organization and its situation. Stability and retrenchment strategies are underutilized.

Some of the major strategic alternatives for each of the primary growth stances (retrenchment, stability, and growth) are summarized in the following three sub-sections.

Growth Strategies

All growth strategies can be classified into one of two fundamental categories: *concentration* within existing industries or *diversification* into other lines of business or industries. When a company's current industries are attractive, have good growth potential, and do not face serious threats, concentrating resources in the existing industries makes good sense. Diversification tends to have greater risks, but is an appropriate option when a company's current industries have little growth potential or are unattractive in other ways. When an industry consolidates and becomes mature, unless there are other markets to seek (for example other international markets), a company may have no choice for growth but diversification.

There are two basic concentration strategies, *vertical integration* and *horizontal growth*. Diversification strategies can be divided into *related* (or concentric) and *unrelated* (conglomerate) diversification. Each of the resulting four core categories of strategy alternatives can be achieved internally through investment and development, or externally through mergers, acquisitions, and/or strategic alliances -- thus producing eight major growth strategy categories.

Comments about each of the four core categories are outlined below, followed by some key points about mergers, acquisitions, and strategic alliances.

NOTES