EXPAND YOUR BUSINESS

Training Manual

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PREFACE

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Training **small to medium business owners** on expanding their business is one of the short and practical training courses developed under the ILO's global enterprise development programmes which cater for the business training needs of this target group which is often neglected by the average business schools and commercial training providers. ILO's global enterprise development programmes include the Generate Your Business Idea (GYBI), the Start Your Business programme (SYB), the Improve Your Business Programme and the Expand Your Business Programme (EYB). The Generate Your Business (GYB) and Start Your Business (SYB) courses enable individuals to pursue entrepreneurship as an employment generation strategy, and Improve Your Business (IYB) training assists them in consolidating this path. The Action My Business Growth (AMG) training helps entrepreneurs decide if they are ready to grow or not and the Expand Your Business (EYB) training seeks to enhance their capacity to grow in order to increase their income and employment generation potential.

This version of EYB is based on the concept of **sustainable enterprise** growth. This approach responds to the pressing need to integrate visions for economic growth with social progress and environmental concerns. It is based on the notion that a business is only sustainable if it responds to the needs of various stakeholder support networks which exist to make markets work, and that income and employment generation needs to ensure net wealth creation for the local community and society at large in which the enterprise is embedded.

This approach recognizes that non-financial objectives play an increasingly important role in shaping businesses, and profit may not be the most important driver for enterprise growth. As long as the financial bottom lines are being met, sustainable enterprises may choose to meet the needs of their various stakeholders. The distinction between for-profit and not-for-profit organizations thus is increasingly blurred, and **social equity and environmental sustainability** are becoming as important as shareholder value.

As a consequence, human resource management takes an increasingly important place in the implementation of growth strategies for small to medium businesses, no less important than marketing and operations management. Key elements in strategies to expand the business are people, processes, and learning.

The manual also pays attention to obstacles that limit growth of women-led enterprises and suggests strategies for women growth oriented entrepreneurs to deal with the issues. The manual particularly recognizes that growing an enterprise entails elevating women entrepreneur's powers and rights that have mainly been the preserve of men in society. The manual recognises the influence that societal and cultural norms have on access to resources, credit, education and decision making for growth oriented women entrepreneurs.

ACKNOWLEDGEMENTS

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This EYB training material has been reviewed, updated, and adapted for use by growth oriented entrepreneurs by Fine-Touch Consulting represented by Sibongile Sibanda. It is based on the core EYB Training manual developed by the SIYB China programme and initial materials developed for training growth oriented women entrepreneurs in Mozambique, Kenya and South Africa.

Diverse individuals and organizations provided useful comments and feedback, in particular The Chief Technical Advisor of the ILO's Women's Entrepreneurship Development and Gender Equality Project in Southern Africa, Grania Mackie; EYB Master Trainer, Jealous Chirove and the following EYB trainers in Kenya, Mozambique, South Africa and Zambia as listed below:

Kenya	Mozambique	South Africa	Zambia
Ben Mbai	Filomena Samussone Matimbe	Brett Giddy	Naomy Kanyemba Lintini
Francis Odiwour	Dieter Santos Savaio	Marina Clarke	
Jane Maigua	Thembile Maswera	Percy Mkhosi	
Benson Kimithi	Jude Ssebuliba	Nqobekile Dorah Manyoni	
	Grace Mungla		
	Rotafina Donco		

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LIST OF ABBREVIATIONS

AMG	Action My Business Growth
A/R	Accounts receivable
A/P	Accounts payable
BDS	Business Development Services
ESS	Employee Suggestion Systems
EYB	Expand Your Business
GYBI	Generate Your Business Idea
GOE	Growth Oriented Entrepreneur
HRM	Human resource management
ILO	International Labour Organization
ISO	International Organization for Standardization
IYB	Improve Your Business
KPI	Key performance indicator
KSF	Key success factor
M&E	Monitoring and evaluation
NPD	New product development
NPV	Net present value
QCC	Quality Control Circles
R&D	Research and development
ROA	Return on total assets
ROE	Return on equity
SIYB	Start and Improve Your Business
SME	Small and medium enterprise
STEEP	Socio-cultural, technological, economic, ecologic and political/ legal analysis
SYB	Start Your Business
TNA	Training Needs Analysis
WACC	Weighted average cost of capital

ABOUT THE EYB PROGRAMME

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The Expand Your Business (EYB) programme is a business management training package for growth oriented entrepreneurs who own or manage a business that has been in existence for at least 1 year and employs between 5 and 100 employees and seek strategic advice and planning support about how to expand their business.

The EYB programme was originally developed by the International Labour Organization (ILO), a specialized agency of the United Nations system. The objective of EYB training is to enable growth oriented entrepreneurs (GOEs) to successfully grow their business. By the end of the EYB training course, participants would have developed a feasible growth strategy, and adequately prepared to successfully steer the strategy implementation process.

EYB training is delivered through experts selected from private sector-led Business Development Service providers (BDS) that have been trained and certified by ILO. The ILO monitors the quality of training through the Programme Coordinators and thus ensures high service delivery standards.

EYB training is suitable for manufacturers as well as businesses involved in trade and services since it focuses on the facilitation of business growth irrespective of the nature of business.

The EYB training course helps entrepreneurs answer the following questions:

- Why am I in business?
- What is the growth potential of my business?
- How can I grow my business?
- How can I make my growth strategy actionable?

How to use the EYB Manual

The EYB manual presents a step by step process of developing a business growth strategy. It contains exercises that help you to complete a strategic plan for your own business. A separate booklet containing an in-depth case study about a fictional manufacturing company accompanies the manual and it enables you to study how another business has developed a growth strategy. In addition the EYB manual supports the training sessions with additional background information and serves as reference after the training course.

EYB Service Delivery Process

The EYB delivery process covers a number of steps. The **first** step of the service cycle is a product briefing to introduce you to our service offer, and to enable you to make an informed buying decision. The **second** step of the service cycle is a Training Needs

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Analysis (TNA) to enable the EYB trainer to group you with other prospective clients and to customize the training intervention in response to your training needs and wants. The **third** step of the service cycle is the training course, followed in the **fourth** step by individual counselling sessions.

After the training course, and at your request, your EYB trainer will link you up with other business development service providers and potential investors. Your EYB trainer will also systematically monitor and evaluate (M&E) your satisfaction with the service treatment and impact derived from participating in EYB activities. Your feedback will be further used to refine the service package. The EYB delivery road map is presented in figure 1.

EYB DELIVERY ROAD MAP

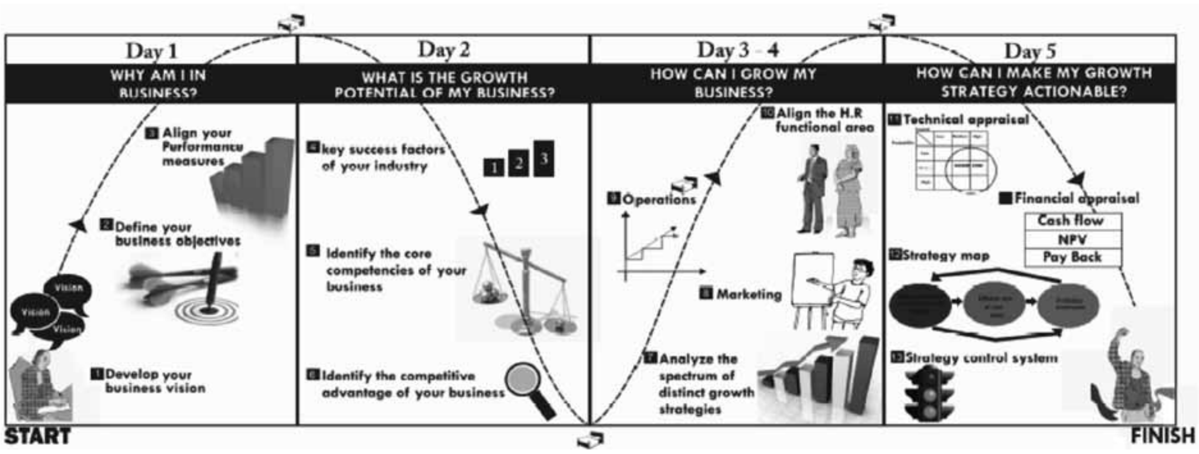

Figure 1: EYB Delivery Road Map

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CHAPTER 1: WHY AM I IN BUSINESS?

This chapter of the manual introduces detailed discussions on why you are in business. It helps you to define your business vision, the core purpose for your business existence and broad goals for your business future. The chapter also assists you to define your business objectives after considering a range of options as well as set your performance measurement standard.

1.1 Review your business vision

What is a business vision?

A business vision is an impression or picture of a desirable future for your company. It describes why your business exists, what product it offers, to whom, where it wants to go and which values will drive it along the way. It is important to consider your own personal dreams in relation to society and family as you develop your vision for the business. Personal dreams and special circumstances give true meaning to being in business. For example, there is recognition that women in particular start businesses out of frustration with the lack of flexibility in the traditional corporate world. Many growth oriented entrepreneurs have not taken time to develop a clear vision of what they want to achieve in business. This module helps you develop a vision for your business.

Why is a business vision important?

Setting a business vision helps you to:

- define the core of your business and ensure that its core competencies are preserved, strengthened or, where applicable, newly established
- inspire your employees and its core stakeholders by providing a purpose that is worthwhile and enabling
- give your business direction for your growth effort
- inspire you towards the realisation of your personal dreams and ambition
- assist you to identify personal development and growth areas that support your vision

As the business grows it places additional pressure on the entrepreneur's managerial, operational, marketing and financial management capabilities. Managing growth increases responsibility and requires the entrepreneur to focus on important roles of managing the business and providing strategic leadership. In articulating the vision, entrepreneurs need to also identify key hurdles they need to personally deal with in order to realise their dream. Growth oriented women entrepreneurs can face additional challenges compared to their male counterparts. This can be due to lower educational levels, limited business exposure, limited networks, the demands of family responsibilities and less access to information on market potential and market complexities. It is therefore important for growth oriented women entrepreneurs to be aware of these challenges and how they affect their business growth. It may even be the case that these factors may have an effect of limiting a business vision statement.

How to review your business vision

You will very likely already have a vision for your own business. You know "why you are doing what you are doing" and you might also have an idea about where you would like your business to be in the future. The main challenge is to structure these thoughts in the light of your growth ambition and to write down your vision statement. If your business already has a written vision statement, then the challenge is to review this statement in the light of your growth ambition.

The four pillars of a business vision are core purpose of your business existence, core values and a defined ambitious goal for your business as illustrated figure 1:

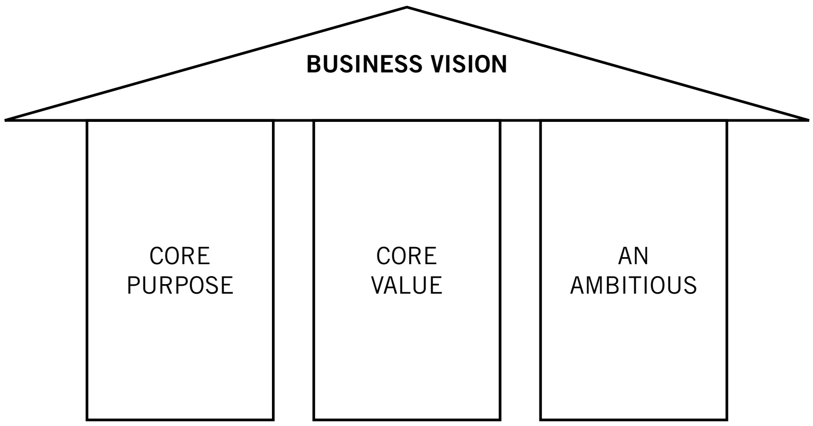

Figure 2: The Pillars of a business vision

Follow these steps to review the vision for your own business:
1. Define the core purpose of your business existence (Mission)
2. Define the core values of your business
3. Define an ambitious goal for your business
4. Consolidate the core purpose, core values and main goal of your business in a vision statement.

1. Define the core purpose or mission of your business

The core purpose or mission of your business is **the reason why your business exists**. It broadly outlines what business you are in, specifies the organization's future direction and how you will satisfy the needs of your customer. It specifies activities to pursue and the course management will engage in for the future. The mission provides the basis for the business goals in the mid-term future. The difference between the vision and mission is that the mission is relatively short term and more concrete, whereas the vision is longer term and visionary in nature.

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To define the core purpose of your business, you have to answer the following three questions:

Why am in business?
What is my business?
Who are my customers?

Why am I in business?

The first question you have to answer is what your ultimate business goals are. Are you in business to make money, to pursue a personal development goal, to pursue family and societal goals such as better livelihood for your family and society or for a combination of both reasons? Businesses in general pursue financial and non-financial goals:

Financial goals: In for-profit businesses, the financial goal of the investors will be to earn more than they could have earned from the best alternative investment opportunity available for them. In not-for-profit businesses, the financial goal will be to at least recoup the costs of business operations.

Non-financial goals: Businesses also have non-financial goals which relates to the interests in the social systems, the ecosystem and other stakeholders that the business is connected to. Every business constitutes a system that is inextricably connected with other systems. For example, businesses draw on labour from the community (the social system) and on raw materials from the environment (the ecosystem). All businesses have a vested interest in the sustainability of these external systems, as they have an influence on its own sustainability.

Accounting for and maintaining the supply of natural goods and services will make your business profitable in the long run and sustainable. While in the short run a 'slash-and-burn' strategy might lead to short term profits, only businesses which ensure the sustained provision of natural capital without compromising the environment will be economically successful in the long term. As a result all enterprises have obligations and a duty of care (often sanctioned in regulations) to safeguard against the destruction of the environment, and maintain value for shareholders in a sustainable way.

The natural environment, which is also often referred to as the ecosystem is providing four main services upon which all enterprises depend. It provides renewable goods (for example, wood, water and food) and non renewable goods (for example fuel and minerals) which are used in many production processes and businesses. Nature regulates the climate, purifies the water and controls the air quality and provides cultural identification and recreational sites which is important for enterprises working in tourism, marketing or branding of geographic local products and services. Finally, nature supports the whole process of soil formation, nutrition cycle and provides the natural space for making these services happen which is notably important to farmers and agro-processing firms.

It is important for a business to balance its financial and non-financial goals as it pursues growth and sustainability. For-profit businesses need to strive for the stability of the interconnected businesses and social and ecological systems in order to be able to pursue their financial goals. In turn, not-for-profit businesses need to secure stable income to be able to pursue their development goals. They can not ignore their finances if they want to survive and expand.

The link between the financial and non-financial goals of a business is illustrated in the chart below. Three ultimate business goals are distinguished, namely to maximize financial performance (shareholder value), to contribute to social development (social equity) and to protect the physical environment (environmental sustainability).

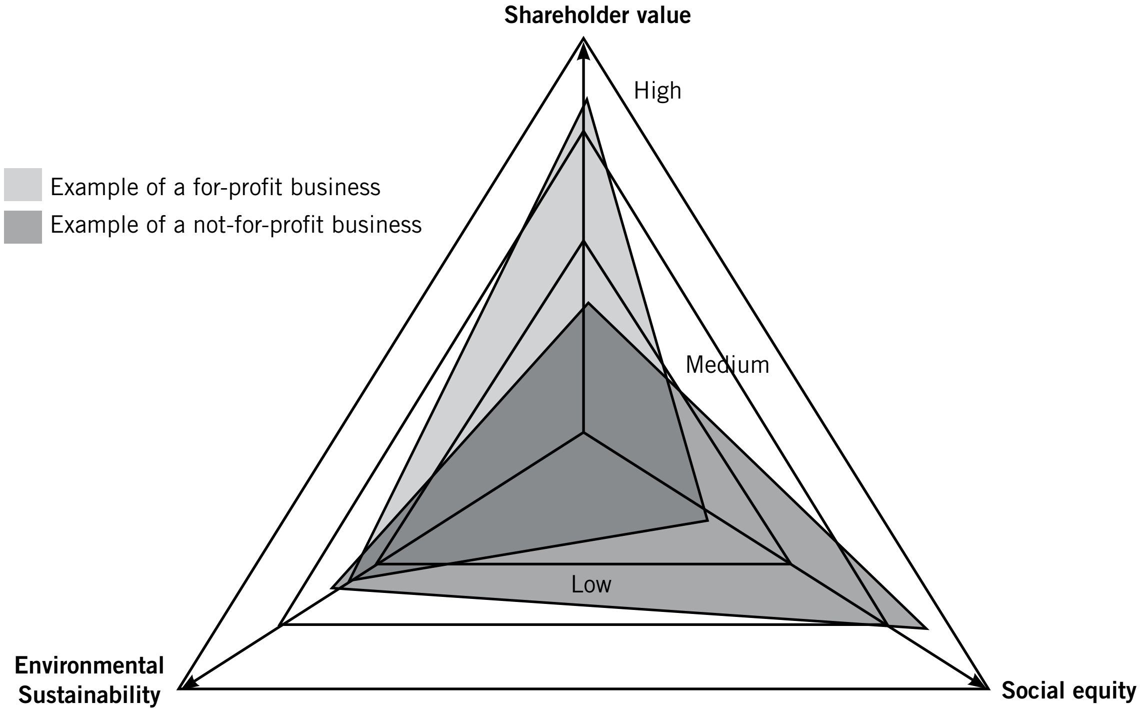

Figure 3: The three dimensions of systemic business competitiveness

These goals have been plotted on the axis of the chart, and the scaling from "low-high" indicates to what extent the aspect has been factored into the vision of the business. A business that has factored these three dimensions into its vision has laid the foundation for "systemic competitiveness", i.e. for business competitiveness that builds on an understanding of the external systems inextricably connected with the own enterprise.

As the two examples of a for-profit and a not-for-profit business mapped in the chart show, the emphasis on any of these three dimensions of systemic competitiveness will vary from case to case – the point is that none of the dimensions are ignored.

There are a number of cases where businesses have accepted the risk of system collapse for the sake of short-term profit maximization, or that might actually benefit from chaos in their own system environment. For example, a construction company might force its employees to work excessive hours and deprive them of basic occupational safety and health equipment to save on production costs and maximize returns.

However, in any of these cases, the risk to the longer-term survival of the business sharply increases. Businesses that continuously act against, or choose to ignore the interests of, the interconnected external systems undermine their prospect for sustained growth. In the case of the construction company above, productivity and ultimately competitiveness of the business might suffer because of high labour turnover, high number of workplace accidents and ultimately closure by the authorities. Businesses that ignore the systems structurally interlinked with their own business system ultimately face the prospect of sanctions or decline.

What is my business?

The next questions you have to answer are: *What does your business do?* What goods or services does it offer and which industry are you in? Are these the (only) products and services that you would like to offer in the future? Is this the industry you are in today the same industry as you would like to be in tomorrow?

At a first glance, the questions about the nature of your business seem trivial. For example, if you run a restaurant you might quickly respond that you operate in the local tourism industry and offer food and a range of alcoholic and non-alcoholic beverages. However, a closer inspection of your business can quickly unfold a complex picture, even in very small ventures. To stay with the example of the restaurant, do you specialize in certain types of dishes, such as vegetarian food or ethnic food; do you offer any enhancing services like live entertainment or home delivery? Do you specialize in lunches or dinners, or do you run a fast food outlet?

The picture becomes increasing complicated as a business has grown in size, offers a broader range of products and possibly has diversified in different lines of business. For example, a tourism agency might retail a broad range of tourism products offered by local tour operators, but sometimes also organize and sell its own excursion packages and also sell souvenirs and memorabilia in its shop. Other than in the tourism industry, which exact line is this business in: Is it a retailer for souvenirs, a service broker for tourism products, or a tour operator?

To further add to the complexity, the fact that you are currently offering a certain type of product in a given industry does not necessarily mean that you want your business to be there in the future. You might sense new or better business opportunities in other industries, or with other products. If you have the ambition to position new products in the same industry, or to exit the industry altogether in search of business opportunities related or unrelated to it, you need to reflect this ambition in your statement about the core purpose of your business.

Who are my customers?

The third question you have to answer is who your customers are and which specific needs of these customers you (intend to) satisfy with your products. The answer to this question can be complicated considering that businesses might serve a wide spectrum of clients and sometimes spread over more than one geographic market. For example, a business can have two locations one in a high-income and the other in a low-income neighbourhoods, two markets with clearly distinct features and needs. Also, a business might cater for both consumer markets and business markets, the two client groups have distinct needs.

As an entrepreneur you may need to reflect more on how gender differences impact on your business, for example, as you define your customers. Men and women have diverse needs to be derived from products. Businesses have come to appreciate that women make most of the consumer purchase decisions in the home and hence understanding their peculiar needs is vital for your business growth. There is also a rising female consumer power in terms of how different products affect women. Be sure to understand how your products are responding to the needs of women essentially making their lives easier. Consider the different groups of women in defining the needs your products will meet for your customers.

Often women are not the end user of your product but could be considered to be the customer as they make the purchasing decisions about that product. A business offers products intended for a particular end user but actually being paid for by an intermediary, like child toys paid by parents or business start-up training courses for the unemployed subsidized by local Government.

In addition to reflecting on your current customers, you also need to reflect on who your prospective customers could be in a desirable future. Your prospective customers are all customers with intrinsic demand for your products that currently buy from your competitors or do not buy at all. If you intend to develop new market segments in future, you should reflect this ambition in your vision statement.

2. Define the core values of your business

Core values are the timeless, guiding principles of your business. Core values underpin the "way you are doing business" and thus shape the corporate code of conduct. They reflect what makes your business special for yourself, for your customers, for your employees, for your investors and for other core stakeholders.

Core values of a business can include the following: customer satisfaction, quality, punctuality, reliability, honesty, fairness, innovation, employee satisfaction, compliance with environmental standards and compliance with (inter-) national production standards.

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The choice of core values will often draw inspiration from the core purpose of your business. For example, if you are in the business of delivering express mail, then your core values might be "speed" and "reliability".

When you define the core values of your own business, focus on the priority values. Your choice of priority will usually be determined by the values that are key for your customers. For example, your customers may value detailed information and honesty in what a product offers among others. Ask yourself: Which core values of my business would boost the product benefit/service experience for my customers? Answer this question by trying to look through the eyes of your customers and keep in mind that your own perception of product benefit can vary substantially from your customers' perception of product benefit. Evidence based research on product usage and customer perceptions are one way of identifying what customers value from your products and services. For example, you might manufacture wrist watches with built-in diving computers assuming that your customers appreciate the technology when in fact they rather appreciate the adventurer image depicted by its image (and might never actually go on a diving trip).

Furthermore, when you define the core values of your own business, keep the list short. An "all-inclusive" list of core values can quickly become meaningless. In fact, focusing on a single core value, like "zero product defects" or "total punctuality", can create the strongest impression on your customers.

3. Define an ambitious goal for your business

Ambitious goals provide a clear and compelling aspiration and challenge for your business. They provide your stakeholders with direction for the future to come and with a cause to rally around. Examples for ambitious business goals could be the quest to become the national, regional or global market leader, to realize double-digit annual sales growth rates or to pay dividends double the industry average.

By implication of its name, an ambitious goal sets a high threshold for your business. This is done on purpose. An ambitious goal is not to be confused with a concrete performance benchmark; it rather serves as a bright light on the line of the horizon. Having said this, an ambitious goal should not "over-stretch" that line of the horizon of a business. A totally unrealistic business goal can become meaningless or even turn into a source of ridicule for your business. Consider where your business is at the moment in defining your ambitious goal.

4. Consolidate your thoughts in a vision statement

In the last step of the process of formulating a draft vision for your business, you need to consolidate your thoughts about your business purpose, your business goals and your big business goals in a single statement.

The following tips can help you to compose a vision statement:

- **The vision statement should be brief**. For best impact on the audience, a vision statement should comprise not more than two short sentences.
- **The vision statement should be concise**. The products and the core values of your business should clearly relate to your business purpose and your customers. For example, a pre-school will likely need to emphasize childcare services and related products, target parents with young children and emphasize values like trust, care and reliability.
- **The vision statement should have a clear flow of thought**: The vision statement should first spell out your core business purpose and then describe your ambitious goal, your products, your customers and your core values. For example, a local event management company might state that the purpose of its business is "to enrich cultural life with modern music entertainment". It might continue saying that the goal of the business is to become the "biggest local organizer of rock and pop music concerts for the young urban crowd.
- **The vision statement should be easy to understand for the audience**. In the vision statement, avoid the use of highly technical language or abbreviations that might be misunderstood by your business stakeholders. Keep in mind that your employees might not be trained in the language of management and might simply not understand what you mean with "shareholder value" or "sustainable development".
- **The vision statement should be specific**. When you pull your thoughts together, avoid the temptation to compose an all-inclusive statement. The purpose, the driving values and the big goal need to come out loud and clearly.

IN-DEPTH CASE STUDY

Throughout the manual we will refer to a case study of a growth oriented entrepreneur who has developed a business growth strategy. In the case study Mega Juice Industries formulated their vision statement as:

"To become an internationally competitive company that meets the demand of consumers in Africa for high quality fruit juice and other processed fruit products while ensuring attractive returns for our shareholders. We acknowledge our social responsibility to the welfare of our employees, our society and our environmental, and responsibility to the communities with whom we are involved."

EXERCISE

1. Please specify the core purpose of your own business, by asking yourself
   - Why am I in business?
   - What exactly is my business about?
   - Would I like to stay in the same business in the future?
   - If not: What kind of business would I rather like to be in?

   Summarize your response in a brief statement:

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The core purpose or mission of my business is to….

___

___

___

___

2. Please specify up to five core values of your own business

The core values of my business are…

___

___

___

___

3. Please specify an ambitious goal for your own business:

The ambitious goal of my business is to….

___

___

___

___

4. Please refer back to the statements under 1-3 above and then consolidate your thoughts in a single statement about the vision of your business.

MY DRAFT COMPANY VISION IS TO…

___

___

___

___

1.2 Refine your business objectives

What is a business objective?

A business objective describes what exactly you need to achieve to fulfil your business vision. Business objectives draw inspiration from the business vision; they specify the priorities of your business and together form the building blocks of your business strategy.

All businesses have objectives that guide their daily operations, but you might not have written them down on paper yet. This section is about helping you to specify and, where applicable, review your business objectives in response to your overall growth ambition stated in your draft vision statement.

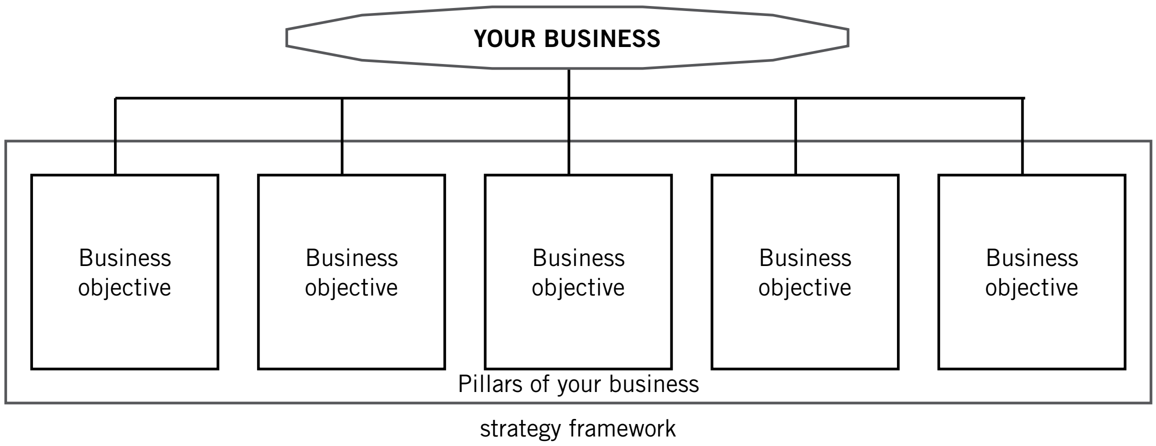

Figure 4: The link between business vision and business objectives

Why is it important to refine your business objectives?

It is important to refine your business objectives to ensure that the strategy framework defined by these objectives is firmly aligned with your business vision.

How to refine your business objectives

Follow these steps to refine your business objectives:
1. Screen the range of objectives frequently used by other businesses.
2. Set objectives that fit your own business vision.

1. Screen the range of objectives used by other businesses

The range of objectives set by businesses can be broadly classified into two groups: Objectives supporting the financial goals of a business and objectives supporting the non-financial goals of a business.

Objectives supporting the financial goals of a business make reference to strategic priorities critical for good financial performance, like “attractive returns” and “market share”. Whilst objectives supporting non-financial business goals make reference to strategic priorities related to the **people** that constitute the social system of the business and other structurally interlinked social or ecosystems, the **processes** implemented by these people to transform inputs drawn from the physical environment into business outputs, and **learning**, a cross-cutting dimension that refers to the (self-) adaptive capacity of the business to continuously refine internal communication and processes. Examples for objectives referring to non-financial goals of a business are “motivated staff” (people), “cleaner production” (processes) and “systematic knowledge management (learning).

The social system of your business needs to include issues relating to your family and welfare objectives. Your family is an interested party in the business and can positively or negatively affect the performance of your business. Be clear on how your business will contribute to your family’s wellbeing; build your own confidence and economic development. It is important for you to articulate measurable performance indicators in this area.

The link between financial and non-financial objectives is dialectic – each group of objectives relates to a separate strategic thrust of the business and at the same time these objectives are inextricably linked by circular cause-effect relationships. For example, good financial performance is a precondition to be able to (re-) invests in staff training and qualified staff is a key enabler for good financial performance.

The graph below illustrates the different groups of business objectives and provides examples for each group. It shows the circular interrelatedness between financial and non-financial business objectives. The graph also shows that in a way all objectives are inter-connected, that the system boundaries are permeable and that it is debatable where the system ends and begins (for example is the local community part of it?). Still, the main building blocks of a business strategy aiming at systemic competitiveness emerge from the picture.

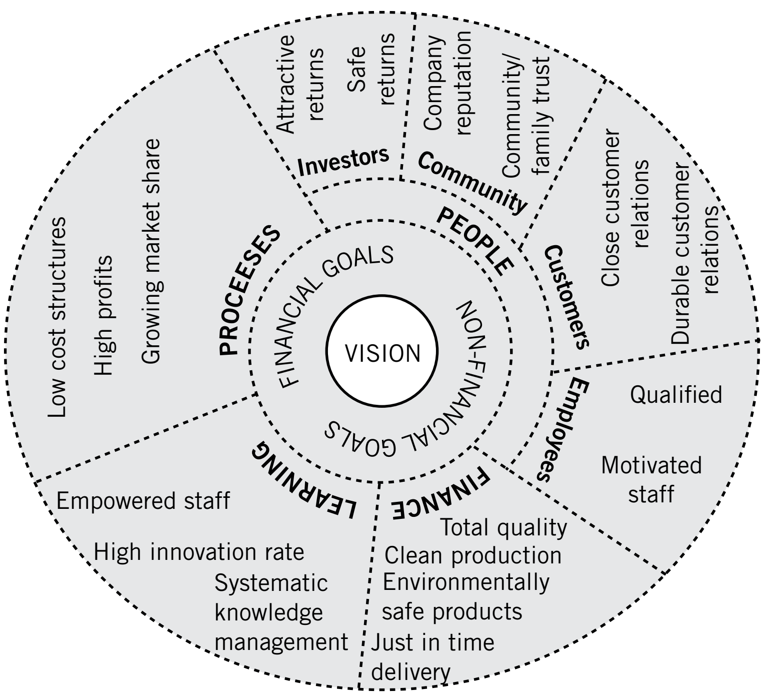

Figure 5: The business objective navigator

2. Set business objectives that fit your own business vision

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In the second step, you need to select objectives that firmly reflect the strategic thrust of your own business mission and vision. Objectives are measurable statements giving general guidance and direction for the business or the business function as for the outcome to be realized. They are result oriented expressions describing a longer term situation linked to your business vision and mission. For example, if you have stated high product quality as a core value of your business, you will need to emphasize quality in all business processes. If you have stressed environmental sustainability in your vision, you might need to emphasize clean production. If you place particular attention on social equity, the qualification and motivation of your employees might become a key business objective.
You can refer back to figure 4 on the business objective navigator graph for an overview of the main groups of objectives that jointly drive a business towards systemic competitiveness. Take these building blocks of business strategy as a starting point to define objectives that fit your specific context and emphasize what makes your own business special.

When you formulate financial and non-financial objectives for your own business, ensure that these objectives are SMART:

- **Specific**: The objective should be formulated in a language that is clear and easily comprehended by the target audience
- **Measurable**: You need to able to assign one or several indicators to quantify and/ or qualify progress in achieving the objective
- **Attainable**: The objective should be feasible
- **Realistic:** The objectives should be realistic
- **Time bound**: The objectives should indicate the timeline for its attainment.

An example of a specific and measurable objective is 'to achieve return on equity at 20% or above and real earning growth averaging 5% or better annually'. Your target audience will easily comprehend the meaning of this financial objective, and you can easily quantify the objective by assigning it an indicator like "return on equity" or "shareholder dividend". It is more difficult to provide an example of an attainable objective since the notion of attainability tends to be context-specific. Taking the example above, the threshold of what characterizes an attractive return is industry-specific and depends on your business.

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The table below shows the objectives chosen by Mega Juice industries (MJI) from the objectives Navigator.

Table 1: Mega Juice Industries Business Objectives

MEGA JUICE INDUSTRIES BUSINESS OBJECTIVES	
Objective	Comments
Attractive return	Financial objective
High profits	Financial objective
Low cost structures	Financial objective
High customer satisfaction	Non-financial objective, stakeholder dimension
Close relationships with business customers	Non-financial objective, stakeholder dimension
Good community reputation	Non-financial objective, stakeholder dimension
High operational efficiency	Non-financial objective, process dimension
Emphasis on quality products	Non-financial objective, process dimension
Close relationships with suppliers	Non-financial objective, process dimension
Clean production	Non-financial objective, process dimension
Qualified workers	Non-financial objective, learning dimension
Motivated workers	Non-financial objective, learning dimension
High innovation capacity	Non-financial objective, learning dimension

EXERCISE

Refer to the draft vision statement of your business and brainstorm about the range of possible objectives to specify your financial and non-financial goals. Then shortlist and write down up to 15 objectives below that express **the essence** of your vision. Where applicable, use the comments column to explain these objectives.

Table 2: Draft Strategic objectives template

Objective	Comments
1.	
2.	
3.	
4.	
5.	
6.	
7.	
8.	
9.	
10.	
11.	
12.	

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1.3 Align your performance measures

What is a performance measure?

Performance measures (sometimes also called Key Performance Indicators (KPI) are used to **quantify** or **qualify** your business objectives. For example, if you have declared "quality" as a core value of your business and defined "emphasis on quality" as a business objective, then a performance measure like "product defect rate" can provide you with important information on your progress towards meeting your objective.

A performance measure summarizes certain attributes of business performance, usually in a numerical description. For example, one numerical measure to describe business performance could be "annual net profit".

In most cases, you will need more than one measure to comprehensively assess the performance of your own enterprise. For example, you might combine a financial metric like "annual profit" with non-financial metrics like "staff turnover" in reflection of your financial and non-financial business objectives.

To be able to evaluate business performance against set objectives, each performance measure must have been assigned a performance threshold. For example, to evaluate business performance against a non-financial variable such as "staff turnover rate", you must have assigned this indicator a performance threshold, such as a "staff turnover below X%". Refer below for more details on the range of measures used by business to measure their performance, and on how to choose measures and targets that reflect the context of your own enterprise.

Performance measures are at the heart of the strategy control system introduced in Chapter 4 of this manual. The system allows you to effectively control the implementation of your growth strategy.

Why is it important to align your performance measures?

It is important to align your business performance measures to ensure that you measure attributes of business performance which are **relevant** for the achievement of your financial and non-financial business goals. For example, if you review your business vision and refine your business objectives in pursuit of business growth, then you also must align your performance measures in reflection of your growth targets.

Experience confirms that "what gets measured gets done". This means that people, – and business stakeholders in general perform on what they are measured against. You need to align your business performance measures to show your business stakeholders which aspects of their performance you consider critical for business growth.

How to align your business performance measures

Follow these steps to align the performance measures of your own business:

1. Screen the range of performance measures frequently used by businesses
2. Select performance measures that fit your own business objectives
3. Set a performance threshold for each measure.

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1. Screen the range of measures frequently used by businesses

Businesses can use various types of indicators to measure their performance:

- measures summarized in words or measures summarized in numbers
- qualitative measures or quantitative measures
- lag measures or lead measures
- financial measures or non-financial measures.

The pros and cons of these various types of measures are further discussed below.

Measures summarized in words (qualitative) or measures summarized in numbers (quantitative)?

Measures summarized in words capture an attribute of business performance by qualifying it in a short statement. For example, the employee motivation level in a business might be ranked as "excellent". The main advantage of measures summarized in words is that verbal statements often better capture phenomena that escape easy quantification, like "business culture" or "satisfaction rate" – people more readily associate a sensation with a term than with a number. The main disadvantage with measures summarized in words is that different people tend to associate different meaning with a given term.

Quantitative performance measures can either be expressed as (1) an absolute number, (2) as a ratio between two related or unrelated absolute numbers or (3) as a composite index of several absolute numbers:

1. **Absolute numbers** are constructed from a single data source and concern a single attribute of business performance. An example of a performance measure expressed as an absolute number is "net profit in value of currency". The main advantage of absolute figures is that they are comparatively easier to understand than many ratios or indices (see below). The main weakness of this type of performance measures is that they do not allow you to analyze an attribute of business performance in relation to other variables. Therefore, the measure tends to provide only a very narrow view of business performance.
2. A **ratio** compares two related or unrelated attributes of business performance. An example of a ratio measure constructed from related attributes is the "share of export sales in total sales". An example of a ratio constructed from unrelated attributes is the "liquidity ratio" that is expressed by dividing current assets less inventories by current liabilities. The main strength of ratios is that they enable you to analyze attributes of business performance in context and draw more informed conclusions. The main weakness of some ratio is that they require detailed explanation to be fully understood by people, particularly where financial ratios are concerned.

3. An **index** weighs attributes of business performance in a composite measure. For example, an “employee satisfaction index” might be constructed by weighing different aspects of employee satisfaction in a single basket. The main advantage of an index is that it summarizes multiple attributes in a single measure and thus can provide a more holistic picture of the situation on the ground. The main disadvantage is that it is often difficult for stakeholders to comprehend the calculation formula and to associate a “real” value with the resulting number – a particular challenge if the index is supposed to capture qualitative attributes like “staff motivation”, “business culture” or “customer satisfaction”.

Quantitative performance measures are generally considered more reliable because they are based on number based facts. However the reliability of the quantitative measure depends on the quality and reliability of the data used to feed it. A quantitative type of indicator fails to capture the intangible aspects of business performance.

Qualitative performance indicators allow you to approximate the intangible performance attributes such as organisational culture, staff motivation, cleaner production systems and customer satisfaction among others. The main disadvantage of qualitative performance measures is the reliability of the data source. For example, the perceptions of your business stakeholders that feed into the assessment of organizational culture are subject to fluctuations and thus constitute a rather shaky base for a strategic planning exercise.

> The quality of any performance measure, qualitative or quantitative, is wholly dependent on the quality of the data used to construct the indicator. Therefore, other than the capacity to construct and interpret performance measures, you also need to know how to collect the necessary data. Please refer to module IV of this manual for more details.

Lead or lag measures?

A lag measure summarizes the outcome of activities initiated or carried out in the past. For example, “return on equity” is a key measure to summarize the financial performance of a business in the past. A lead measure, by comparison, summarizes the activities performed today in order to achieve a desirable outcome in the future. For example, a measure like the “annual expenditure on staff training” indicates whether a business invests in the career development of its employees and thus paves the way for business performance in the future.

The main advantage of a lag measure is the fact that the data used to construct the metric is readily available – it refers to events in the past that are typically documented in annual reports, financial statements and other sources of business information. The main disadvantage of a lag measure is that it merely offers you a glimpse of the past and does not allow you to predict future performance.

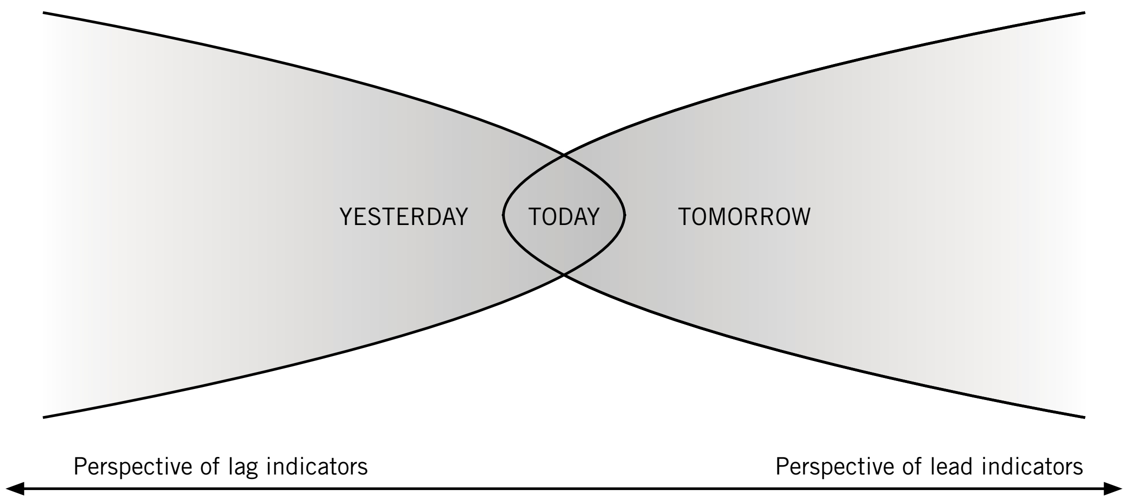

Figure 6: Lead and lag indicators illustrated

The main advantage of a lead measure is the fact that it summarizes what your business is doing to become "fit for the future". The main disadvantage is that the cause and effect relationship between today's" activities and future outcomes can be weak. For example, the business investment in staff training today might not pay off tomorrow because your employees might decide to change jobs.

Financial or non-financial measures?

Three sub-types of measures are distinguished in the following: Purely financial measures, purely non-financial measures and hybrid measures. Purely financial measures draw exclusively on financial data. An example of a purely financial measure is "return on equity". Purely non-financial measures are constructed exclusively from non-financial data. An example of a purely non-financial measure is "machine productivity". Hybrid measures, finally, are constructed from financial and non-financial variables to analyze the relationship between different attributes of business performance. An example of a hybrid measure is the "administration costs per employee".

The main advantage of purely financial measures is that they emphasize financial performance, an ultimate goal of any business. Furthermore, purely financial metrics are typically constructed from hard data published in the financial statements of a business. The main disadvantage of purely financial metrics is that most of them are lag indicators that merely report performance in the past. Also, the somewhat narrow focus on financial information can easily distract from the analysis of other critical aspects of the business system.

The main advantage of purely non-financial metrics is that they sharpen the view for the factor inputs (like labour and raw materials) needed to actually generate the value-added reflected in the financial statements. Furthermore, non-financial metrics are key to track phenomena that escape easy quantification but have strong impact on business performance, like employee motivation. Also, purely non-financial measures more easily lend themselves as lead indicators of present activities that are meant to boost future business performance. On the flipside of the coin, where purely non-financial measures are constructed based on qualitative data or turned into lead indicators, their precision can suffer from the unpredictability of future events and the unreliability of the data source.

The main advantage of hybrid measures is that they allow you to evaluate non-financial attributes of business performance in relation to their impact on overall financial performance. In turn, the main disadvantage of these hybrid measures is that most of them are lag indicators that only provide partial insight into past business performance. Exceptions apply, though, in cases where an investment made today is put in relation to an attribute of business performance thought key for the future. For example, a business might track the current investment level in staff training (per year per employee) to extrapolate its capacity for boosting performance in the future.

The table below provides an overview of performance measures often used by businesses to track progress in the implementation of their strategic objectives. The measures have been clustered according to four perspectives, namely "finance", "people, "processes", and "learning".

Refer to chapter 1.2 for more background information on these four perspectives of systemic competitiveness.

Each measure listed in the table is classified along the typology discussed earlier. The list is neither exhaustive nor complete but meant to serve you as a source of inspiration. It illustrates, among others, that the majority of performance measures tend to be quantitative, be constructed as ratios and have the character of lag indicators. The list also indicates that it might be context-specific whether a measure is classified as lead or lag indicator. For example, the annual expenditure on research and development (R&D) is essentially a lag indicator constructed from financial statements of the recent past, yet it summarizes attributes of business performance that are clearly future-oriented. A similar observation applies for measures like customer satisfaction.

Finally, the table indicates that some measures can be both expressed as absolute numbers or as ratios, like the "customers lost" by a business.

Table 3: Selected measures to track business performance

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Performance measures	**Classification**									
Performance measures marked with an asterisk are explained in module II "What is the growth potential of my business". Please refer to the chapter on "internal company analysis" for more details.	Lead	Lag	Qualitative	Quantitative	Pure financial	Pure non-financial	Hybrid	Absolute number	Ratio	Index
Financial performance										
Current liquidity ratio (or quick ratio/ acid test)*		+		+	+				+	
Activity ratios/ asset utilization ratios		+		+	+				+	
Profit before interest and tax		+		+	+			+		
Profit after tax		+		+	+			+		
Sales/ total assets		+		+	+				+	
Return on net operating assets		+		+	+				+	
Return on equity*		+		+	+				+	
Return on investment*		+		+	+				+	
Equity/ total assets		+		+	+				+	
Current liabilities / total assets		+		+	+				+	
Debt to equity ratio*		+		+	+				+	
Total assets/ equity		+		+		+			+	
Interest cover		+		+		+			+	
Sales to remuneration		+		+	+				+	
Dividend yield		+		+	+				+	
Price/ earnings ratio		+		+	+				+	
Earnings before interest, tax, depreciation and amortization		+		+	+			+		
Marketing cost to sales ratios (e.g. sales offices cost to total sales)		+		+			+		+	
Operations cost to cost of sales ratios (e.g. direct material costs to total costs)		+		+			+		+	
Total costs		+		+	+			+		
Market share		+		+	+				+	
Annual sales		+		+	+			+		
Net profit margin*		+		+	+				+	
People										
Customers										
Customer satisfaction	+	+	+			+			+	+
Customer service index	+	+	+	+		+				+
Customers lost		+		+		+		+	+	
No of Customers		+		+		+		+		

Performance measures	**Classification**									
Performance measures marked with an asterisk are explained in module II "What is the growth potential of my business". Please refer to the chapter on "internal company analysis" for more details.	Lead	Lag	Qualitative	Quantitative	Pure financial	Pure non-financial	Hybrid	Absolute number	Ratio	Index
Financial performance										
Brand image index		+	+			+				+
Average duration of customer relationship		+		+		+			+	
Average customer account size		+		+	+				+	
Average time from customer contact to customer response		+		+	+				+	
Customer retention rate (e.g. expressed as % of repeat customers)		+		+		+			+	
Service expense per customer per year	+	+		+			+	+		
Community										
Expense per year on community relations		+		+			+	+		
No of community projects supported by the company	+			+		+		+		
% of staff members involved in community activities	+			+		+			+	
Company image index		+				+				+
Employees										
Average Absenteeism		+		+		+			+	
No of women managers		+		+		+		+		
No of applicants for employment at the company		+		+		+		+		
Full-time staff who spent less than 50% of work hours at a corporate facility		+		+		+		+	+	
% of full-time employees		+		+		+			+	
No of full-time temporary employees		+		+		+		+		
Staff turnover		+		+		+			+	
Average employees years of service with company		+		+		+			+	
Average age of employees		+		+		+			+	
Employee / satisfaction index	+	+	+			+				+
Temporary employees/ permanent employees		+		+		+			+	
Share of employees with university degree	+	+		+		+			+	
Employees view (empowerment) index (No)	+	+	+			+				+
Investors	+	+	+			+			+	+
Investor service index	+	+	+			+			+	+
(Key) Investor satisfaction	+	+	+	+		+				+

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Performance measures	Classification									
Performance measures marked with an asterisk are explained in module II “What is the growth potential of my business”. Please refer to the chapter on “internal company analysis” for more details.	Lead	Lag	Qualitative	Quantitative	Pure financial	Pure non-financial	Hybrid	Absolute number	Ratio	Index
Processes										
Labour productivity (output per year per employee)		+		+	+			+		
Machine productivity (output per year per machine)		+		+		+			+	
Product defect rate		+		+		+			+	
Processing time		+		+		+		+		
On-time delivery		+		+		+			+	
Average lead time, from order to delivery		+		+		+			+	
Average lead time, product development		+		+		+		+		
Average lead time, suppliers		+		+		+			+	
Lead time, production		+		+		+			+	
Emission from production into the environment		+	+	+		+			+	
Production wastage (various)		+		+		+		+	+	
Green products as % of total range		+		+		+			+	
Average time for decision making		+		+		+			+	
Contracts filed without error		+		+		+			+	
Learning										
Information Technology (IT) capacity/ per employee	+	+		+					+	
Change in IT inventory	+			+		+			+	
IT expense/ administrative expense		+		+	+				+	
R&D expense/ total expense	+			+	+				+	
IT development expense/ total expense	+			+	+				+	
Investment in training/ customer	+			+					+	
Time in training (days/ year) entrepreneur & employees	+			+			+			
Investment in research	+			+	+			+		
Investment in new product support and training	+			+	+			+		
Investment in development of new markets	+			+	+			+		
Suggested improvements/ employee & entrepreneur	+			+		+		+		
Competence development expense/ employee	+			+			+		+	
Share of employees below age X	+	+		+		+			+	

2. Select measures that fit your own business objectives

After analyzing the range of measures used by businesses to track performance, you need to select performance measures that fit the emerging strategy framework of your own business.

To select the right performance measures for your own business, you are recommended to first review the generic selection criteria for performance measures below and then shortlist a set of measures based on the specific context of your own business.

The following are some **generic** selection criteria for strong performance measures:

Strategic: A strong performance measure tells you about outcomes rather than outputs. It addresses the significance of what has been undertaken. For example, a performance measure tracking return on equity is more strategic than a measure tracking number of products sold. In the first case, the measure provides clear insight whether the annual product sales (output) actually resulted in satisfactory financial performance (outcome) and thus contributed to the financial goals of the business.

Focused: The performance measure gets to the core of what matters for your business, rather than tracking some general business processes. This is sometimes referred to as the rule of empirical relevance. For example, if you have defined "punctuality" as a core value of your business, then a performance measure that gets to the core of your business would need to be able to track on-time delivery.

Attributable: What you measure is attributable to strategic initiatives that the business has implemented, rather than to something else that is happening. For example, an increase in annual sales might, or might not be attributed to a strategic initiative launched by your business while an above-industry average duration of the customer relationship will almost always be directly attributable to your services or products.

Neutral: As far as possible, the measure should not send value-laden messages. Every measure conveys messages to people who may not fully understand the limitations of the data and the data collection. For example, and as indicated earlier, a measure constructed on a verbal statement can mean different things to different people.

Transparent: Performance measures should mean what they appear to mean, without a lot of interpretation. For example, the "number of monthly hits" for your company website is a good example of an indicator that does not always mean what people suppose. To turn into a transparent indicator for the impact of your internet presentation, it would be more appropriate to measure the number of customers contacting you via the website for a product inquiry.

Feasible and economic: The effort and resources you have to expend to collect and process the data for the measure must be proportionate to its value. At best, the data collection effort is minimal. Also, if you delegate the data collection task to your employees, they must be able to comprehend the purpose of the exercise and the data collection requirements.

Repeatable: It must be possible to repeat the data gathering and analysis at a later time, and the meaning must remain the same. Otherwise, it is impossible to track performance over time and evaluate progress towards the achievement of your business objectives.

Reliable: The measure must produce consistent results. If you were to collect two sets of data and nothing was to be changed between the data collection exercises, then the value of the measure should be equivalent.

Valid: The measure must produce accurate results. In other words, the measure should accurately reflect what has actually happened.

The choice of performance measures for your own business will depend on the following context-specific technical and logistical aspects:

- the business objectives that you have specified to make your business vision actionable
- the resources and capacity at your disposal and the ambition level of your measurement effort

Within the framework set by these two parameters, the following tips are useful to draw a shortlist of **context-specific** performance measures.

Limit the number of measures: As a rule of thumb, each objective in your emerging business strategy map should be assigned at least one but not more than three performance measures. This means that a business with between 10 and 20 objectives (refer to chapter I.2. for more details) has to track between 10-30 performance measures – a considerable effort in time and resources.

> To greatly reduce the effort of tracking your performance measures, you can set up a computer based strategy control system. Refer to module IV for more information how to set up and run your own IT-based strategy controlling system.

Consider the aspect of confidentiality. Before selecting any measures, reflect about the expectations of the audience of your business strategy. Are you mapping these measures for your eyes only, or do you want to share it with your shareholders, the business stakeholders, or the wider public? This aspect is critical because some measure of business performance can touch sensitive issues that you might not want to share with a wider circle of people.

Combine lead and lag measures. As indicated earlier, lag indicators measure outcomes of past initiatives to track performance at present while lead indicators measure outputs of ongoing/ recently completed initiatives meant at boosting performance in the future.

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Jointly, lead and lag measures provide you with the "rear mirror" and the "front lights" needed to steer your business on the road to business growth. Therefore, you should aim at using both lead and lag indicators in your strategy control system. You might emphasize lag measures to track financial performance of your business and on lead measures to assess whether your business is placing sufficient emphasis on learning and innovation, and to continuously improve internal processes.

Consider the cause and effect relationships between measures. In line what has been written earlier on the interrelatedness of business objectives, seek to select interrelated performance measures. For example, a measure like "hours in training per staff member per year" is a lead indicator that tracks an enabler of (future) business performance. To assess the impact of this investment in staff training, the measure could be combined with another lead indicator tracking "number of new products to market per year". Also, a lead indicator measuring "number of hours spent on customer relations" might be combined with a lag indicator measuring "customer satisfaction" or "average duration of customer relationships". It is also possible to approximate cause and effect relationships between two lag indicators, by combining a measure of operational efficiency like "administration expenses/ total expenses" with a measure of business profitability like "profit after tax".

Combine quantitative and qualitative indicators. You are recommended to seek a mix of quantitative and qualitative measures in your strategy control system in order to take full advantage of the respective strengths and balance the respective weaknesses of these two types of indicators. The exact mix of measures depends on your own business but, as a rule of thumb, the majority of these measures should be quantitative because the data is more easily collected, more reliable and more accurate. Regarding the qualitative measures, you are recommended to use them particularly to track attributes of business performance linked to customers and employees.

Emphasize ratios. Among the various types of measures expressed in numbers, ratios tend to be relatively more powerful than absolute numbers because they enable you to analyze attributes of business performance in context. Ratios are also often preferred over indices because they are easier to construct and to comprehend (transparency). Keep in mind, though, that in some cases it makes very good sense to use an absolute number because the figure is quickly grasped and can convey a powerful message. Also, it can make sense to operationalize an index as a performance measure if the attribute of business performance is highly complex and neither a single figure nor a ratio would capture the various aspects of the matter.

Draw on financial *and* non-financial data. Finally, you are recommended to draw on both financial and non-financial data to track business performance. You can construct purely financial metrics to track business finances and purely non-financial metrics to track other attributes of business performance related to people and processes, but beyond that you should pay special attention to hybrid measures constructed from both financial and non-financial data that allow you to assess the cause and effect relationships between your investment in people and processes and the bottom line of your business.

For example a measure like "remuneration per employee" enables you to assess the impact of fair pay on staff motivation.

IN-DEPTH CASE STUDY

Table 4 shows Mega Juice Industry selected performance indicators

Table 4: Mega Juice Industries Selected performance indicators

Objective	**Measures**	**Target**				
		2012	2013	2014	2015	2016
Attractive returns	Annual return on assets in % (annual profit after tax in currency x 100 divided by value of fixed assets in currency)	15	15	20	25	25
High profits	Net Profit Margin	4	4	5	6	7
Low cost structures	Ratio of overheads to total costs (administrative expenses x 100 divided by total business expenses)	0.02	0.05	0.08	0.08	0.08
High customer satisfaction	Customer satisfaction rate in% (no of satisfied customer x 100 divided by total no of customers per year)	85	90	90	90	90
Close relationships with buyers	Average time spent with each business customer (no of days per year per business customer)	5	5	6	7	7
Good community reputation	No of community projects supported by company	1	2	2	2	3
High operational efficiency.	Machine productivity (no of litres per machine per year)	60,000	60,000	60,000	60,000	60,000
	Lead time, production (time in days from receiving a product order to product delivery)	2	2	2	2	2

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Emphasis on quality	Product rejection rate (no of deliveries rejected by customers x 100 divided by total no of deliveries made per year)	5	5	5	3	2
Close relationships with suppliers	Supplier turnover (no of suppliers lost x 100 divided by total number of suppliers per year)	25	20	15	10	10
Cleaner production	Recycling rate, machine oil (litres of machine oil recycled x 100 over total litres of machine oil used in production each year)	0	25	50	75	100
	Wastage rate, raw materials (kilograms of orange wasted x 100 divided by total kilograms of oranges processed in production per year)	10	10	10	8	7
Qualified workers	No of days in training per machine operators per year	5	5	7	10	10
	Course pass rate (no of machine operators successfully graduating from training x 100 divided by total no of operators in training per year)	75	85	85	85	85
Motivated workers	Worker satisfaction rate (no of workers satisfied with salary package x 100 divided by total no of workers per year)	60	75	75	80	85
High innovation capacity	No of new products to market each year	1	1	2	2	2

EXERCISE

Refer back to the draft list of strategic objectives for your own business. Now run through the list of performance measures earlier in this chapter and shortlist measures that pass both the generic selection criteria and the context-specific selection criteria. Please feel free to complement the list of measures as you see it fit, but ensure that each measure passes the test of the generic selection criteria. Please write down the results in the table below. At this stage, ignore the right column with the heading "Target".

Table 5: Draft performance measures template

Objective	Measures	Target				
		20__	20__	20__	20__	20__
No 1						
No 2						
No 3						
No 4						
No 5						
No 6						
No 7						
No 8						
No 9						
No 10						
No 11						
No 12						

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3. Set a performance threshold measure

Once you have short listed a set of performance measures, the last step is to define a performance threshold for each metric. The threshold serves as a target to assess the achievement of a business objective with regard to a given attribute. For example, if you have defined "operational efficiency" as a business objective, and set "machine productivity" as a measure, then machine productivity with the factor "x" could be fixed as a benchmark.

To be able to set thresholds for your measures or business performance, you need to first have a closer look at the different approaches to calculate a performance target, and then choose the approach that suits your own business best.

The following approaches are frequently used by businesses to fix thresholds for their performance measures:
- forecasting
- benchmarking

Forecasting

In forecasting, the analysis of past performance patterns becomes the basis for a projection of events in the future. Businesses can forecast future performance based on the analysis of both financial and non-financial data. For example, if you have collected reliable data about the "annual return on investment" and the "annual growth in customer base" of your business over recent years, then you can use the information to extrapolate your performance with regard to these two attributes.

The key strength of using forecasting to set performance targets is that the projections are based on empirical evidence. Therefore the predictions are often comparatively reliable and the targets more realistic. The main disadvantage of using forecasting to identify performance targets is that the approach implicitly assumes that "business will continue as usual", or at least that the system environment will remain stable – which might not be the case if you embark on an ambitious growth drive. Also, some attributes of business performance such as the duration of "customer relationships" can quickly change under influence of external factors – hence the reliability of the projection can be questionable, particularly in volatile markets.

To balance this weakness of forecasting, you can opt to develop various business scenarios for each measure, and to forecast a "better-case" and a "worse-case" scenario. These two scenarios would then set the target corridor for each measure and enable you to choose a target in line with your ambition level.

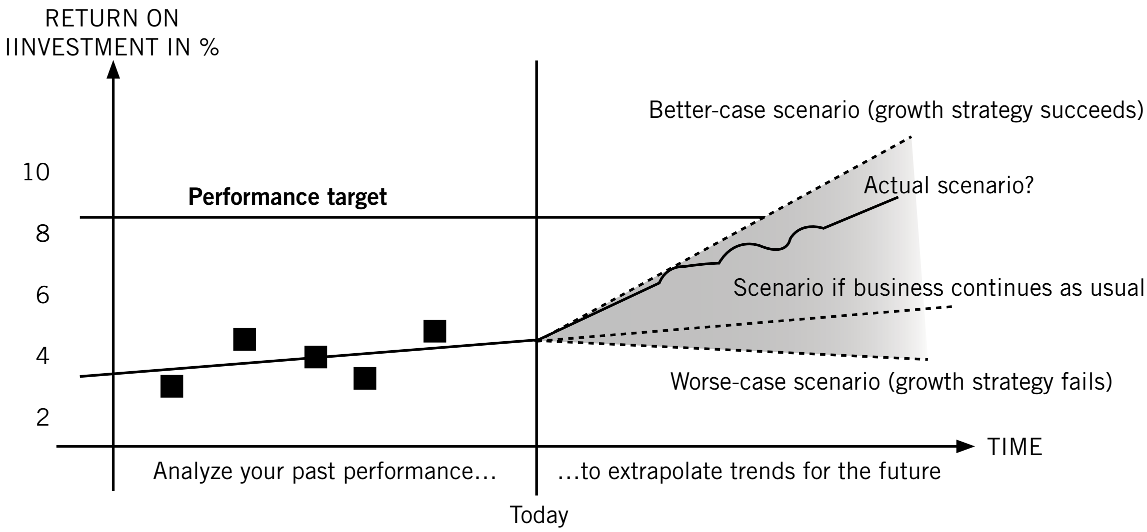

Figure 7: How to set performance targets based on forecasting

Benchmarking

In benchmarking, an organization that has defined an opportunity or ambition for better performance identifies another organization (external benchmarking) or a unit within its own organization (internal benchmarking) that has usually achieved better results and conducts a systematic study of the other organizations/ units achievements, practices and processes. Because of its focus on exemplary performance, benchmarks are sometimes referred to as "best practices".

The main strength of using benchmarks as targets for your own performance measures is that it offers plenty of room for strategic stretch. In internal benchmarking you aim at nothing short of realigning people and processes in your business according to internal best practice while in external benchmarking you aim at meeting and beating either an industry standard or - at the highest ambition level - the industry leader. The main disadvantage of using benchmarks as performance target is that they might be unrealistic to achieve. As a result, not only the target itself but the entire measure can end up being irrelevant. Furthermore, it can be very difficult to source the relevant information, particularly with regard to sensitive attributes of business performance related to people and internal processes. Finally, keep in mind that the competition is not resting on their laurels – benchmarks keep shifting and you might find yourself eternally one step behind the industry leader if you merely follow their example.

In practice, to set targets for your own business performance, you are recommended to use a combination of forecasting and benchmarking. Follow these steps to set targets for your own business performance:

- **Review your past business performance.** First, you need to refer back to the financial statements, annual reports and other internal reports to assess the performance of your business with view to the measures that you have short listed earlier. If this information is not documented, refer to the responsible department chiefs to collect the information. If the information is not precise but based on educated guess only, use these figures to come up with a rough trend analysis.

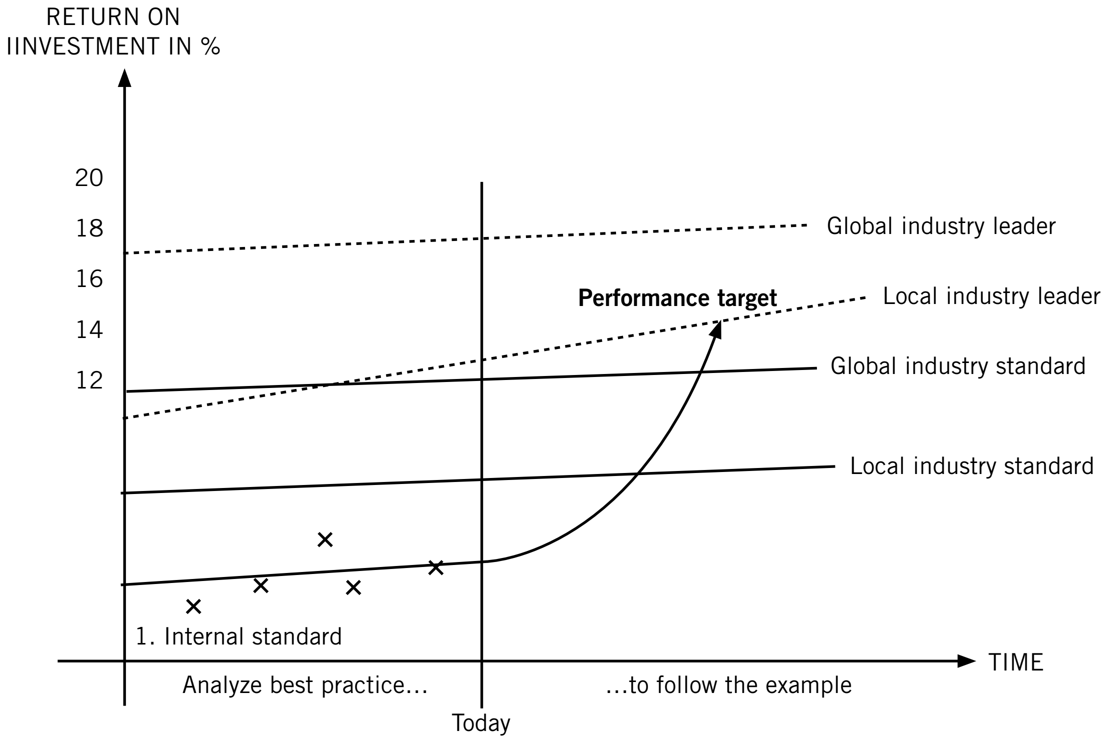

Figure 8: How to set performance targets with the help of external benchmarking

- **Extrapolate your future business performance.** Based on the results of the trend analysis, extrapolate future business performance along three scenarios, namely along a better-case scenario, a "business continues as usual scenario" and a "less-desirable case" scenario. Ensure that the better case and the worse case scenarios are constructed on realistic assumptions, taking the business as usual scenario as a starting point and then adjusting the projections.
- **Benchmark your own business performance.** In the next step, you need to compare your own past business performance with the corresponding local industry benchmark. If you find that you cannot source data on local industry benchmarks along the metrics of your measures, alternatively refer to the benchmarks of your direct competition. If you cannot access information about your competition either, refer to your internal benchmark, e.g. the best-ever result achieved with regard to each performance measure. The difference between your own business performance and the best practice in the local industry shows you the "performance gap" that you will need to eventually close in order to meet or beat the local competition.
- **Set yourself targets that are realistic yet ambitious.** Based on the analysis of the performance gap, draw performance targets that fall within the upper limits set by the "better case scenario" and the lower limits set by the "business as usual scenario". If the performance gap cannot be closed within this target corridor in the foreseeable future, you can either review the assumptions in the "better case" scenario, or extend the timeline to catch up with the competition, or both. When you review these variables, remember to be ambitious but remain realistic – do not be carried away by overoptimistic targets and always keep an eye on the worse-case scenario as a warning example of what could happen. If beating the industry benchmark means strategic overstretch, focus on beating your in-house standards year on year, or review

the strategic objectives underpinning your business strategy. It might be that you have decided to emphasize attributes of business performance where others have an unassailable competitive advantage.

IN-DEPTH CASE STUDY

MJI decided to use a combination of financial and non-financial measures in reflection of their financial and non-financial business objectives. To measure financial objectives they chose three measures expressed as ratios, namely 'annual return on assets in %', 'net profit margin (%)' and the 'ratio of administrative costs to total cost'. MJI also prefers to use a combination of lead and lag indicators to track both investments made today in expectation of performance delivered tomorrow, and performance delivered today as a result of wise investments made in the past. Table 6 presents the Mega Juice Industry tentative five year performance targets.

Table 6: MJI Performance measures

Objective	Measures	Target				
		2012	2013	2014	2015	2016
Attractive returns	Annual return on assets in % (annual profit after tax x 100 divided by value of fixed assets)	15	15	20	25	25
High profits	Net Profit Margin	4	4	5	6	7
Low cost structures	Ratio of overheads to total costs (administrative expenses x 100 divided by total business expenses)	0.02	0.05	0.08	0.08	0.08
High customer satisfaction	Customer satisfaction rate in% (no of satisfied customer x 100 divided by total no of customers per year)	85	90	90	90	90
Close relationships with buyers	Average time spent with each business customer (no of days per year per business customer)	5	5	6	7	7
Good community reputation	No of community projects supported by company	1	2	2	2	3
High operational efficiency.	Machine productivity (no of litres per machine per year)	60,000	60,000	60,000	60,000	60,000
	Lead time, production (time in days from receiving a product order to product delivery)	2	2	2	2	2
Emphasis on quality	Product rejection rate (no of deliveries rejected by customers x 100 divided by total no of deliveries made per year)	5	5	5	3	2
Close relationships with suppliers	Supplier turnover (no of suppliers lost x 100 divided by total number of suppliers per year)	25	20	15	10	10

Cleaner production	Recycling rate, machine oil (litres of machine oil recycled x 100 over total litres of machine oil used in production each year)	0	25	50	75	100
	Wastage rate, raw materials (kilograms of orange wasted x 100 divided by total kilograms of oranges processed in production per year)	10	10	10	8	7
Qualified workers	No of days in training per machine operators per year	5	5	7	10	10
	Course pass rate (no of machine operators successfully graduating from training x 100 divided by total no of operators in training per year)	75	85	85	85	85
Motivated workers	Worker satisfaction rate (no of workers satisfied with salary package x 100 divided by total no of workers per year)	60	75	75	80	85
High innovation capacity	No of new products to market each year	1	1	2	2	2

EXERCISE

Refer back to the draft list of strategic objectives and corresponding draft measures that you have drawn up earlier. Please follow the steps described on the previous page to fill in the right column of the table by setting a draft target for each draft measure, for five successive years starting from the year that your growth strategy will be launched. In the case of interrelated measures, make sure that the respective targets complement, not contradict one another.

CHAPTER 2: WHAT IS THE GROWTH POTENTIAL OF MY BUSINESS?

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This chapter will assist you to articulate the growth potential of your business. It covers the assessment of key success factors (KSF) for your industry which enables you to document the extent your business core competencies match these features. In this regard the chapter covers analysis of your customers, competition and the market environment, to identify their needs and strengths. The chapter will thus assist you to identify the competitive advantage of your business (the capacity of a business to perform better than its direct competitors in a given industry). Knowing your competitive advantage will help you choose a growth strategy that builds on your business strengths and takes advantage of market opportunities.

2.1 Assess the key success factors of your industry

Key success factors (KSF) in your industry are the strategy related approaches, competitive capabilities and business outcomes that your firm must be competent at doing, or must concentrate on achieving in order to be competitive and financially successful. KSF drive the industry you are in.

Why is it important to know your key industry success factors?

If you know the key success factor of your industry, you can assess to what extent the core competencies of your business match these features and whether and where you hold a competitive advantage that could be mined for business growth.

The table below lists examples for key success factors. The list is not exhaustive but meant to stimulate your thinking about the key success factors in your own industry:

Table 7: Examples of Key Success Factors

Technology related KSF	Manufacturing related KSF
• Production process innovation capability • Expertise in a given technology • Scientific research expertise • Product innovation capability	• Low-cost production efficiency • Quality of manufacture • High utilization of fixed assets • Low-cost plant locations • Access to adequate supplies of skilled labour • High labour productivity • Low-cost product design and engineering • Flexibility to manufacture a range of models and sizes

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Marketing related KSF	Distribution related KSF
• A well-trained, effective sales force • Available dependable service and technical assistance • Accurate filing of buyer orders • Breadth of product line and product selection • Merchandising skills • Attractive styling/ packaging • Customer guarantees and warranties	• A strong network of wholesale distributors/ dealers • Gaining ample space on retailer shelves • Having company-owned retail outlets • Low distribution costs • Fast delivery
Skills related KSF • Superior talent • Quality control knowhow • Design expertise • Expertise in a particular technology • Ability to come up with clever, catchy ads • Ability to get newly developed products out of the R&D and into the market very quickly	**Organizational capability** • Superior information systems • Ability to respond quickly to shifting market conditions • More experience and managerial knowhow
Other types of KSF • Favourable image/ reputation with buyers • Overall low cost • Convenient locations • Pleasant courteous employees • Access to financial capital • Patent protection • Meeting a social need or requirementEnvironmental sustainability	

How to assess your key industry success factors

Industry key success factors are analysed at three levels: Your market environment, your competitors and your customers as illustrated in the figure below:

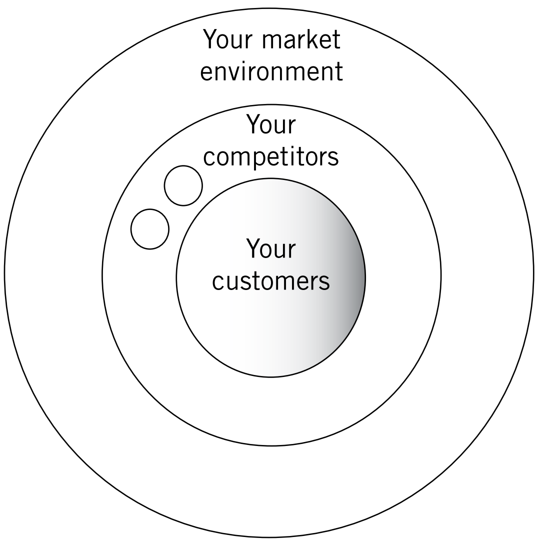

Figure 9: The three levels of industry analysis illustrated

Keep in mind that industries are product specific, e.g. their boundaries are determined by the spectrum of existing and potential customers with potential demand for a given product. For example, the industry for commercial catering equipment is demarcated by the spectrum of clients with a need for this type of equipment.

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This means that businesses will need to carry out an industry analysis for each distinct offering in their product portfolio. For example, business manufacturing commercial catering equipment and home kitchen utensils should carry out a separate analysis for each product.

In turn, in cases where products are very similar in nature and cater to the same market, a single industry analysis might suffice. For example, a bakery that produces bread rolls and bread loafs might be able to carry out a single industry analysis for this product group.

EXERCISE

How many distinct products does your business currently offer? Please list these distinct products or product groups below.

My business currently offers the following distinct products or product groups

Follow these steps to assess the key success factors in your industry:
1. analyze your customers
2. analyze your competition
3. analyze the market environment

1. Analyze your customers

The first step is to analyze the needs and wants of your customers. A customer is an individual or an organization with demand for your products and either:
- buys already from your business (existing customer), or
- buys from a direct competitor or has not yet bought anything at all (prospective customers).

Your customer analysis should cover both existing and prospective customers to give you a comprehensive overview of the market.

The customer analysis comprises three sub-steps:

- segment your customers
- analyze the core product benefit sought by each customer segment
- determine the customer-centred KSF of your industry.

Segment your customers

There are many ways of dividing the customer of your business. You can segment your customers by age, sex, income, usage rate, price sensitivity and a wide range of other segmentation variables. The figure 9 illustrates the range of segmentation variables frequently used by businesses.

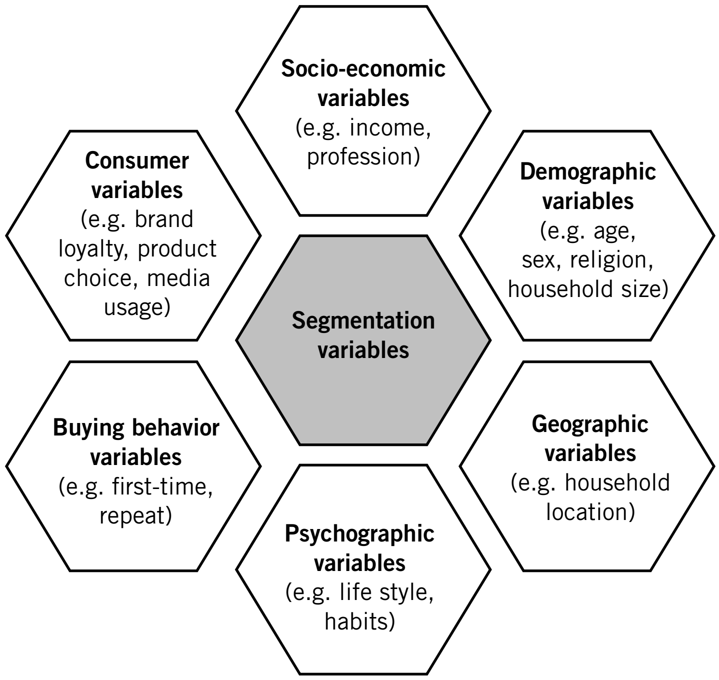

Figure 10: Customer segmentation variables

Segmentation variables should be chosen based on the following criteria:

- It should distinguish segments with distinctly different (heterogeneous) buying behaviour: For example, if your company produces beauty products for women, you might segment your customers according to location, age and income, or a combination of these variables. Location matters as customer in rural areas typically demand different products and respond to different types of promotion than women in urban areas. Age matters, because the type of beauty products demanded by women change with increasing age. Income matters, because rural customers often have less disposable income than urban customers to spend on beauty products.
- It should distinguish homogeneous segments: The customer group distinguished by way of the segmentation variables should expose largely similar patterns, e.g. have similar or identical buying behaviour. For example, "household location" is a geographic variable that often allows businesses to identify buyers with similar buying behaviour.
- It should distinguish segments that are large enough to justify the effort of developing a distinctive marketing strategy for this group. If the costs to develop a customized offering for a particular niche are prohibitive, then the segmentation criteria chosen are too narrow.

- The market information required to use the variables must be accessible with reasonable effort, and it must be reliable. Punitive data collection costs undermine the financial objectives of the programming exercise and if the information is not reliable, the results of the segmentation effort can mislead your business growth effort later.

Identify the variables that best suite your existing and potential customers and also that offer sales growth opportunities for your business for example a business may segment their customers along three variables, and namely;

- usage rate (heavy buyers, frequent buyers or occasional buyers?)
- main product benefit sought (quality or low price?)
- price sensitivity (e.g. whether the buying decision is determined by "price" or "product"; customers with high price sensitivity mainly look for low prices.

For your business list your existing / future market segments, based on your chosen segmentation variable. It is important to determine why the different segments buy from you (why do they come to you?) If it because you offer high quality, or they want low price. Based on this, what is it that you must be able to provide, or continue to provide, in order to keep your current customers / get more?

You can visualize the results of your segmentation exercise by drawing a simple matrix along your main segmentation variables. For example, you can map your main customer groups along usage and benefit segmentation variables as illustrated in the customer segmentation matrix in table 8. Complete a separate table for each product/segment mix.

Remember that, the analysis applies to both existing and would-be customers:

Table 8: Customer Segmentation Matrix

		Heavy buyers	**Frequent buyers**	**Occasional buyers**
Main benefit sought: Quality	Low price sensitivity			Segment A
	High price sensitivity			
Main benefit sought: Price	Low price sensitivity		Segment B	
	High price sensitivity			

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IN-DEPTH CASE STUDY

Table 9 presents how Maga Juice Industries (MJI) has segmented their customer spectrum in the market for high quality orange juice and in the market for canned pineapple.

Table 9: Mega Juice Industries Customer Segmentation Matrix

		Heavy buyers	Frequent buyers	Occasional buyers
Main benefit sought: Quality	Low price sensitivity	Five star hotels		
	High price sensitivity		Guest houses?	
Main benefit sought: Price	Low price sensitivity	Wholesale companies		
	High price sensitivity		School canteens? Goceries stores	

EXERCISE

Identify the relevant variables and segment your customer to determine those that offer sales growth for your business.

Fill in the main customer segments identified in the process into the matrix in table 10. Briefly describe the main characteristics of each segment, who these customers are, how often they buy, how much they are willing or able to pay and what their key buying considerations are.

Analyze the core product benefit sought by each customer segment

After segmenting your customers into groups with distinct buying behaviour, the next step is to zoom in on the core need that each customer segment seeks to satisfy with your product.

For example, if you run a bar, do your patrons mainly come to quench their thirst or to seek entertainment, or a combination of both? The identification of the core needs of each customer segment is crucial since these needs ultimately drive the customers' buying decisions.

Table 10: Customer Segmentation Matrix Template

		Heavy buyers	Frequent buyers	Occasional buyers
Main benefit sought: Quality	Low price sensitivity			
	High price sensitivity			
Main benefit sought: Price	Low price sensitivity			
	High price sensitivity			

Keep in mind also that the core benefit of your product might be variable. For example, if you run an ice cream parlour, does a given customer segment buy ice cream in summer for the same reasons as in winter? Or if you run a boutique, do the clothing needs of your clients vary with seasons and fashions? The examples show that the core benefit sought by your customers might change (sometimes quickly) and that as a result the customer-focused key success factors of your industry might also shift. This observation is critical for the long-term planning horizon of your business growth strategy.

Core benefits of products may be gender specific. Women and men perceive product benefits in different ways. Women may look for practicality, ease of application and compatibility with family responsibilities. For instance for a women a decision to buy a washing machine is likely to be motivated by how the gadget will reduce time allocated to household chores and hence free time for other things. On the other hand men may buy gadgets such as cell phone handsets for prestige.

When you analyze the core customer need that your product addresses, you need to distinguish between perceived needs and actual needs. Taking the example of the bar above, your patrons might claim to come because they want to quench their thirst but their actual need is to be in company of other people. In this case, a key industry success factor would be to create an enabling environment for people to meet.

Customer Buying Behavior

Customers buying decision making process is influenced by a number of factors such as their hierarchy of needs and their desires, fears and instincts. The study of human behaviour has resulted in human motivation theories such as the Freud, Maslow and Herzberg theories which cover the subtle differences between perceived and actual needs of a customer segment. These theories are applied by marketers to explain customers' buying behaviour.

For example, if you run a car showroom, a customer might claim to buy a luxury car for need of safe and comfortable transport - yet, another sub-conscious motivation might be to obtain social status with the vehicle. Carefully assess the sub-conscious buying motivations of each of your customer segments to discover their "real" product benefit.

Freud theory says that buying motivations are partly driven by impulse rooted in desires, fears and instincts. As you study your customer behaviour it is important to consider the impulses that trigger their buying decisions.

In addition consider the buying policies and procedures of different customers you are dealing with. Buying policies and procedures refer to how organizations and individuals procure a good or a service. For example, a company might decide only to buy from ISO certified suppliers or to always buy from the lowest bidder.

It is also important to remember that men and women have different societal and cultural influences that affect their value judgements on different products, these factors should be taken into account when analysing buying decisions.

Determine the customer-centred KSF of your industry

Once you have identified the buying behaviour of your main customer segments, and found out the reasons why they buy your products, then you have all the information needed to determine the customer-centred KSF of your industry. Keep in mind that these customer-centred KSF are segment-specific and that you need to analyze them separately for each main customer group.

To determine the customer-centred KSF of your industry you need to think through the implications of your findings for your own business and your competitors. For example, if you run a mail courier service, and the main product benefit sought by a group of clients is "punctuality", the KSF could relate to capabilities of your company to guarantee "speed in delivery" and a "strong network of local dealers". Or, if your company provides cleaning services to a local hospital, and the core benefit sought by your clients is "hygiene", then the KSF in your industry could be "qualified and motivated workers" and "high quality disinfectants".

In the thinking process about KSFs, you might come up with a large number of success factors. You should aim at limiting this number to up to five factors per market segment in order to control complexity and focus your mind on the most critical factors that make or break the market exchange. Keep in mind that many success factors are inter-related, and focus on the key enabler at the bottom of the cause-effect pyramid.

For example, in the optical lenses industry, customers typically need high-precision products. Here, two key enablers at the bottom of the cause-effect pyramid would be access to "high precision production technology" and "qualified machine operators" – without these two inputs, high precision lenses cannot be produced.

It is quite likely that some industry success factors will be of critical importance for more than one customer segment – ultimately these segments seek the same product, if for various reasons. In fact, repeated incidence might indicate a key enabler because of its relevance across the spectrum. It is unlikely, though, that the key success factors are the same for all segments, because these segments were originally grouped for their distinctive buying behaviour.

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N-DEPTH CASE STUDY

MJI has determined the customer-centered KSF of the industry for orange juice and canned pineapple. See how they have worked out the detailed customer–centered KSF for existing and potential customers on figure 11.

	What, how often and why do they buy?	Key Success Factor
Segment 1: Up-market hotels	High quality fruit juice in five-litre containers, delivered to the doorstep. Clients order about 550 litres every two days,@ 17.5 per litre, totalling 100,000 litres a year and revenues of 1,75 million. Clients are willingly paying a premium and they are loyal because Mega Juice Industries (MJI) has built up close, personal relationships with the food and beverages managers. The segment has good growth potential (up to an additional 70,000 litres per year)	MJI needs to be able to produce high quality fruit juice and to deliver it at the doorstep of the client. Furthermore, MJI needs to be able to respond quickly if product demand peaks and to maintain close and personal relationships with the decision making unit in the hotel, here the food and beverages manager.
Segment 2: Wholesalers	One client, Lucky Star Distributors. Client buys orange juice in one-litre plastic bottles for onward distribution to small retail shops and supermarkets. Client places bulk orders once a week. Total annual orders amount to 70,000 litres @ 10.5 per litre. Order volumes are secure until 2010. No growth potential	MJI needs to be able to produce high quality fruit juice in large volume and at a low unit price.

Potential customers

	What, how often and why would they buy?	Key Success Factor
Segment 3:Tourist guesthouses	Guesthouses are very price-sensitive and would only order small quantities of fruit juice at a time, about 1 litre a day or 364 litres per year per guesthouse. Guesthouses would place orders at short notice, subject to seasonal demand and want the product delivered quickly to their doorstep. They are not willing to pay more than 8 per litre.	MJI would need to be able to produce high quality fruit juice at a very low price and also need to be able to distribute their product in low quantities, at a low price and with a short lead time.
Segment 4: Kiosks in School canteens	Clients would require high quality fruit juice packed in 0.25 litre ` and pay up to 3.5 per unit, provided the product has been branded. Demand fluctuates according to school semester; adjusted demand per kiosk is equivalent to 10 litres per day per kiosk, or 3,650 litres per kiosk per year. Total projected demand in the market (one kiosk per school on 86 registered institutions) is 313,900 litres. Potential clients very interested in buying the product, potential revenues of up to 4,4 million	MJI would need to master the capacity to brand its product as a healthy choice (to parents of students) and as a fashionable drink (to students). They would also need to be able to package their juice in small bottles. They would furthermore need to be able to distribute their product on a daily basis, and respond to the fact that demand fluctuates strongly.
Segment 5: Grocery stores (retailers)	Would be clients not very interested in making business with MJI. Clients prefer buying their products in bulk from wholesaler. Many clients are also risk averse to placing ‘unknown’ MJI products on their shelves. Clients are very price sensitive. Very difficult to forecast prospective demand per client in this segment; anecdotic evidence suggests that demand per client is rather low – fruit juice does not seem to be a fast moving stock.	MJI would have to enter the market for wholesaling food and beverages and to either build up, or take a stake in, a wholesaling company. MJI would also need to be able offer fruit juice at a low price.

Figure 11: Mega Juice Industries Customer Centred Key Success Factors for the market for orange juice

EXERCISE

Please refer back to the customer segmentation matrix completed earlier and use it to fill in the boxes with the customer segment descriptions in figure 12. In the process, expand the number of customer segments in the table according to your requirements. As a first step, **determine the KSF for your industry for each customer segment separately**.

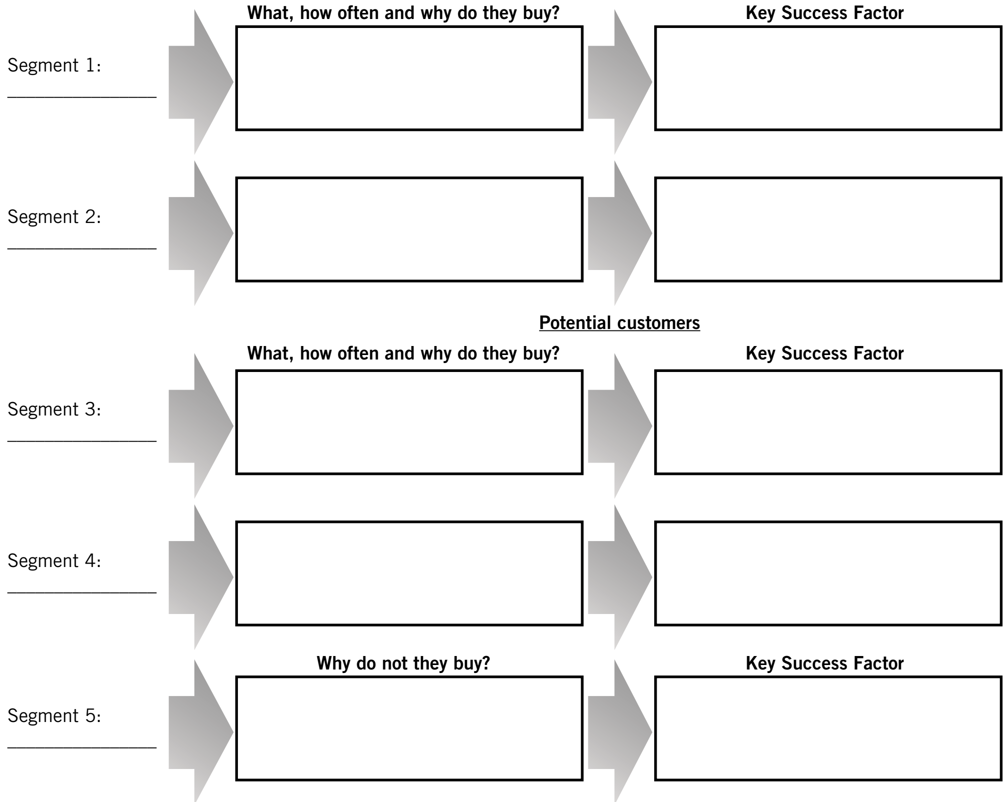
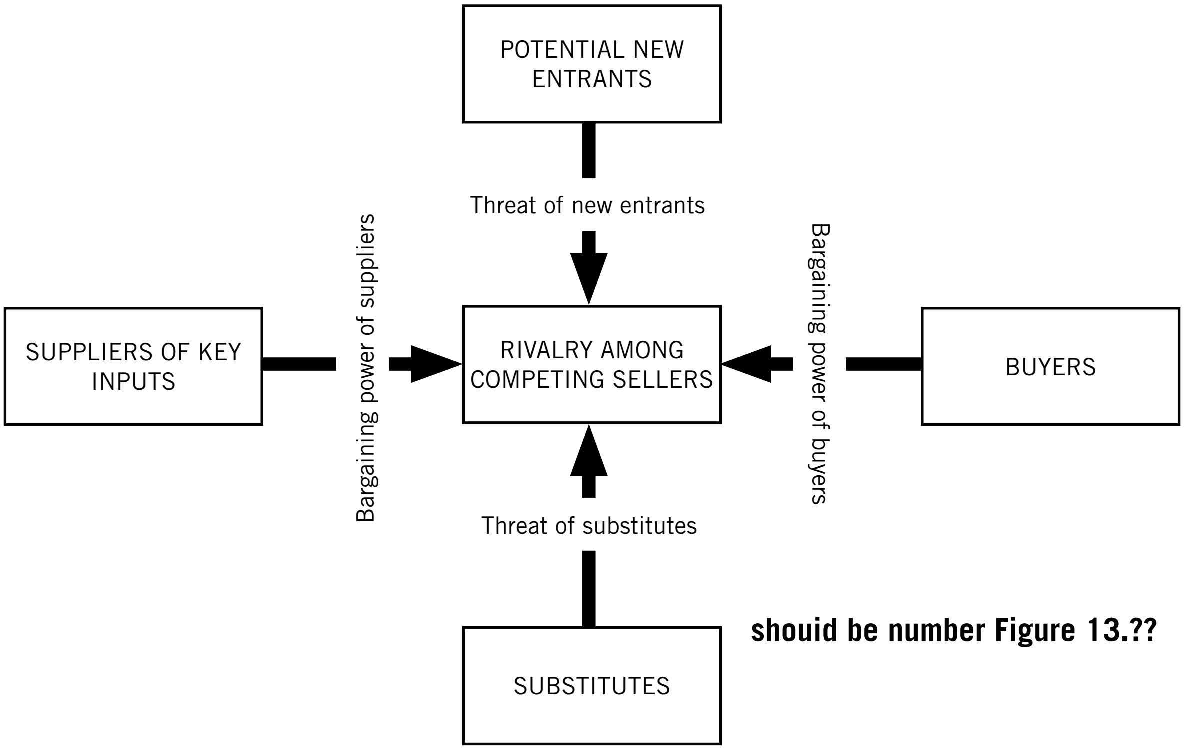


Figure 12: Customer Centred Key Success Factors Template

2. Analyze your competition

In the second step, you analyze the competition in your industry in order to identify the competition-specific key industry success factors. Analyzing key industry players assists you to identify the attractiveness and growth potential of the industry. For instance, if you are operating in an industry with many companies producing similar products, this will impact on the attractiveness of the industry and the way you position your business within this industry. Generally if an industry has a high level of competition it is unattractive. Competition specific key industry success factors are identified through analyzing new market entrants, bargaining power of supplies and buyers, the threat of market substitutes and level of rivalry with your main competitors. The competitive forces determining industry attractiveness is illustrated in figure 14.



shouid be number Figure 13.??

Figure 14: Competitive forces determining industry attractiveness

Follow these sub-steps to identify the competition-specific key industry success factors:
- analyze the threat of new market entrants
- analyze the bargaining power of your suppliers
- analyze the bargaining power of your buyers
- analyze the threat of market substitutes
- analyze the level of rivalry with your main competitors
- assess the strategic implications of your findings

Analyze the threat of new market entrants

New entrants to an industry bring new capacity and increase competition for market share. The seriousness of the threat typically depends on the height of the barriers to market entry. Put simply, higher barriers to market entry mean lower threat of market entrants. For instance, the market for car manufacturing has higher barriers because of the required capital, expertise and marketing arrangements. Women entrepreneurs often are involved in industries that require minimal investment in production technologies as well as low capital requirements because of related challenges to access to finance. This reality has limited the growth of women's enterprises since they are in industries with low entry barriers and hence less potential for growth and more competition.

Factors that determine the height of the barrier to new market entry include
- need for economies of scale
- required level of production differentiation
- required capital
- switching costs for potential customers

- access to raw material
- access to product distribution channels
- lobby protecting the interest of the current players in the market.

IN-DEPTH CASE STUDY

MJI discusses the implications of the findings of their competition analysis and deduces the competition-related KSF for their own industry in the local market as presented in figure 15:

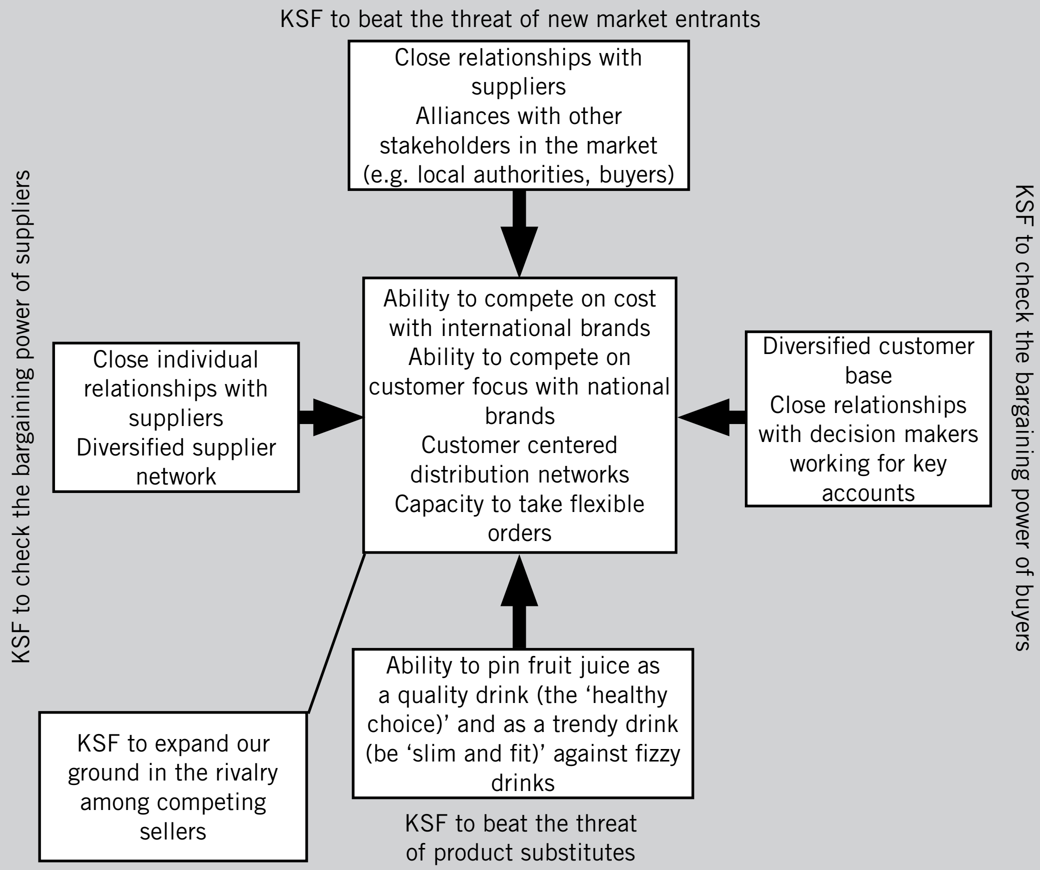
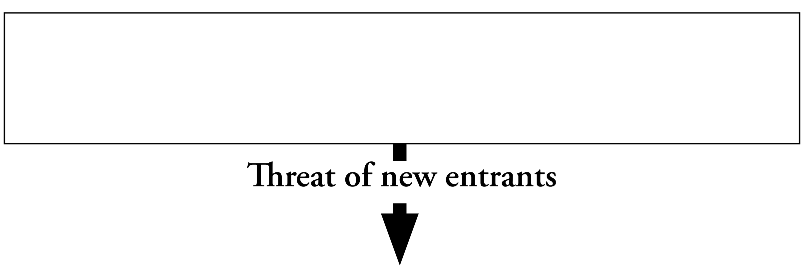


Figure 15: Mega Juice Industries competition-related KSF in the local market for orange juice

EXERCISE

Please describe the threat of new market entrants in your own industry along the criteria listed above.



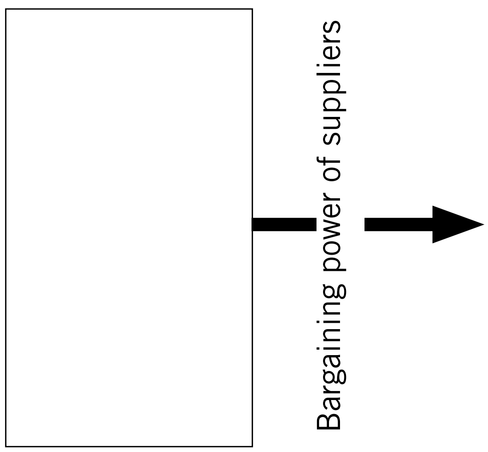
Analyze the bargaining power of suppliers

Suppliers can exert power by raising prices or lowering quality of supply, thereby enhancing their profitability at the cost of the buyer. Some of the main factors that determine the bargaining power of your suppliers are

- the number of suppliers
- the level of association/ coordination among these suppliers
- your switching costs
- the level of differentiation of the supplied product
- the capacity of suppliers to seek forward integration
- your importance as a buyer to these suppliers

EXERCISE

Please describe the bargaining power of suppliers in your own industry along the criteria listed above.



Analyze the bargaining power of buyers

Your customers can also exert competitive pressure on your business by forcing down prices, by demanding higher quality or by playing competitors against each other.

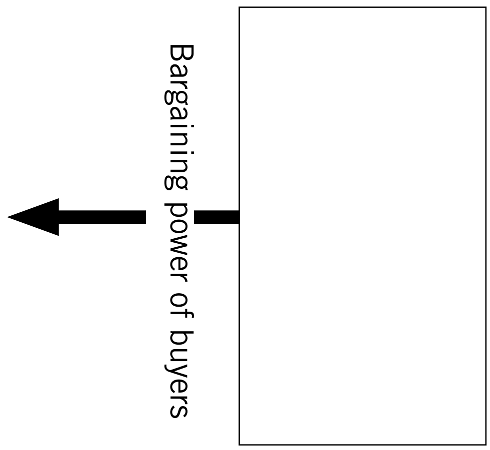
The bargaining power of customers is determined by factors like

- their number
- the question whether the products offered to them are standard or differentiated
- the percentage of costs of a product to total buying costs for the customer (the price sensitivity of buyers is likely to increase with increasing percentage of product costs in total buying costs)
- the importance of quality for these customers
- the money-saving potential for these customers

- their switching costs
- their economic situation
- the level of market information accessible to the buyer
- their capacity to seek backward integration (i.e. to replace you as a supplier by either taking over a direct competitor or alternatively by building up a new business that supplies the same or similar goods and services as your own business).

EXERCISE

Please describe the bargaining power of buyers in your own industry along the criteria listed above.



Analyze the threat of substitute products

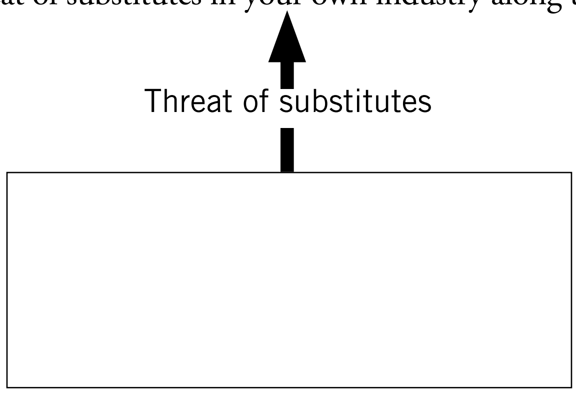
A substitute product is a product that has the capacity to replace your own products. For example, high-speed travel by train has the capacity to substitute air travel on short and medium distances. The existence of substitute products limits the price that can be charged by the industry.

Charging higher prices than the ceiling will lead to consumers buying substitute products. The main determinants of the competitive threat of a substitute product are the

- relative price performance of substitutes
- buyer propensity to substitute a product.

EXERCISE

Please describe the threat of substitutes in your own industry along the criteria listed above



Analyze the level of rivalry with your main competitors

Factors that determine the level of rivalry between your business and your main competitors are, among others, the

- size of the market
- number and size of the competitors
- heterogeneity of the competitor spectrum
- industry growth rate and profitability
- level of differentiation of the product on offer
- incremental industry (over) capacity
- level of capacity utilization
- diversity in competitive strategies
- type of competitive strategies
- high exit barriers for competitors

To determine the level of competitor rivalry with a higher level of precision, you can further expand on the competitive strategies of the major players in the market. For this purpose, and in addition to the analysis of the current competitive strategy of these major players, you need to assess these players from three angles:

- **capabilities:** What are the strengths and weaknesses of the competitor?
- **perceptions:** How does the business perceive itself and the competition?
- **targets for the future:** What are the performance targets set by the competitor?

To collect information about the (self-) perception, capabilities and performance targets of your competitors, you can refer to annual company reports, press clips from newspapers and magazines, the company website, radio and TV coverage of the company or interviews with company representatives.

The information from these sources allows you to construct a reaction profile of the competitor. Based on this profile you are in a better position to predict the strategic moves of your competitors and to prepare your strategic response to these moves. In reverse, you are also able to anticipate the likely reaction of your competitors to your own strategic moves and factor this reaction into your own strategic equation.

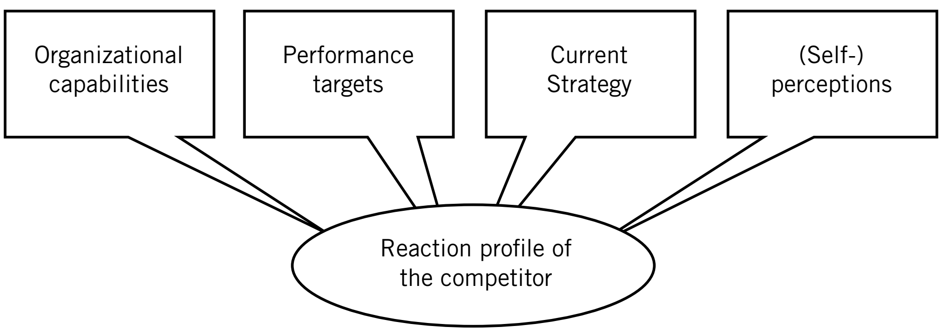


Figure 16: Elements of a competitor analysis

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Organization

IN-DEPTH CASE STUDY

Figure 16 presents a detailed description of how Mega Juice Industries (MJI) analyzed the level of rivalry with their main threat of substitute products.

Organizational capabilities
- Quality
- Team work
- Professional workforce
- Target-oriented (growth-oriented)
- Innovation

Performance targets
- 100% pure fruit juice
- Zero additives
- Freshness
- Quality of raw material
- Recycling packing materials

Current strategy
- To use raw materials grown locally to produce high-quality fruit juice for South African market

(Self-) Perceptions
- High quality fruit juice brand
- Industry leader in term of freshness
- Production cost is higher than local products

Reaction profile of the competitor:
Like MJI, Gold Fruit is a company that emphasizes on the high quality of its products, including the freshness of the juice and quality of the raw materials. Baso from MJI is impressed by the fact that Gold Fruit proudly markets the fact that it procures its raw materials domestically – thus turning an actual cost saving measure into a brand feature. Gold Fruit claims to be the industry leader in terms of freshness and also to be a growth-oriented company, two claims that might bring it on collision course with Isthelo if Mrs. Kana should embark on an aggressive growth drive in their local market. To avoid direct collision with Gold Fruit, MJI could emphasize on 'customer focus' in their growth drive and stress their unique distribution network as a distinctive feature.

Figure 16: Competitor analysis chart for MJI competitor Gold Fruit

EXERCISE

1. Please describe the level of competitor rivalry in your own industry along the criteria listed above.

Level of competitor rivalry

2. Next, carry out a competitor analysis for your main competitor in the market place. Looking at their organizational capabilities, performance targets, current strategy and (self-) perceptions, what are their likely next moves in the market, and how

would they react to your own efforts to expand your business operations? Based on your observations compose a brief reaction profile of your main competitor in figure 18 template. Then refer back to the results of your analysis of the current level of competitor rivalry and refine your observations.

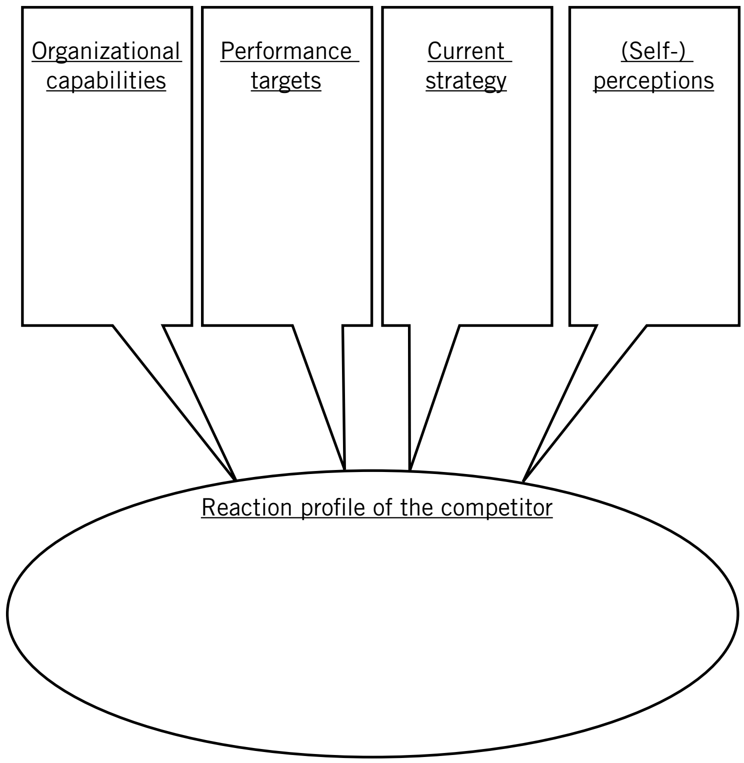


Figure 17: Competitor Analysis Chart Template

Assess the strategic implications of your findings

In the last step, you need to pull together the findings of your industry analysis and to assess their strategic implications from the point of view of your own business and from the point of view of your direct competitors. Which capabilities must your business master in order to meet the competitive challenges in your industry?

For example, if you run an airport limousine pickup service and compete with public transport for clients, the competitiveness of your business will be largely determined by your ability to reach out for a premium customer segment. A KSF, here, could be "strategic service distribution alliances with local five star hotels".

EXERCISE

Please refer back to the findings of your industry analysis and assess their strategic implications for business success. Which capabilities does your business need to hold in order to meet or beat the various competitive challenges? Write these capabilities down in the boxes of figure 18. **Repeat the exercise for each main market segment in your customer segmentation matrix**.

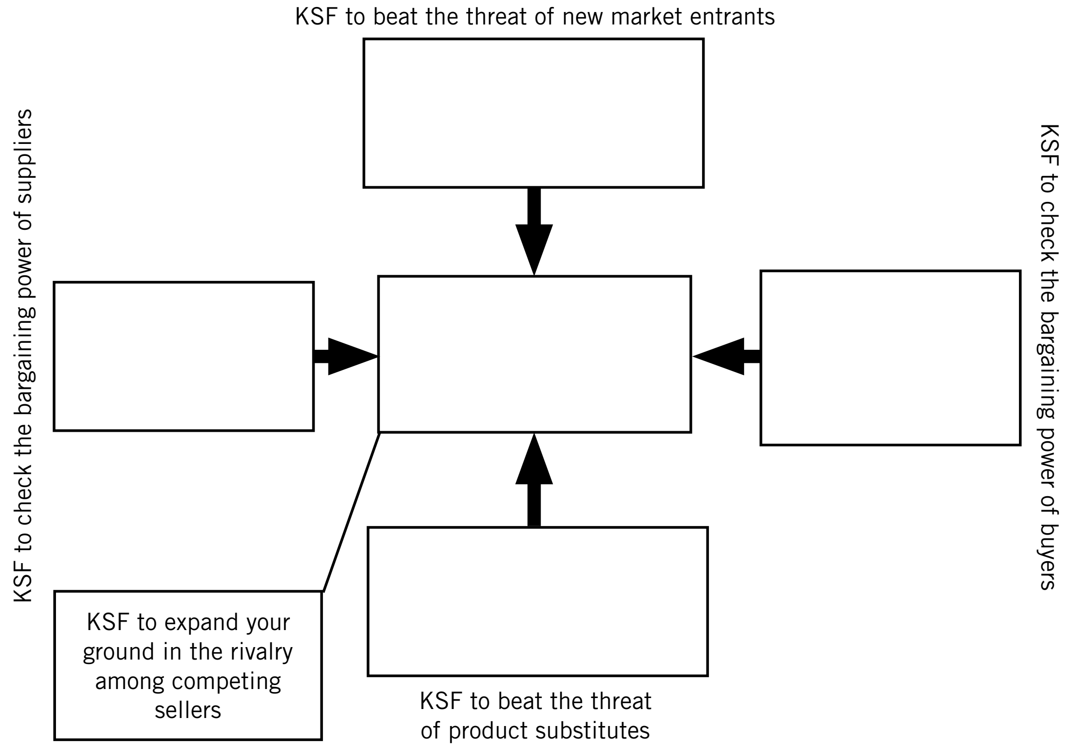


Figure 18: Industry Competition Related KSF Template

3. Analyze your market environment

The market environment your business is operating in determines the growth potential of your business and its success. Businesses operate in complex social, economic, technological and political environments. It is important for you to collect and analyze market environment information and assess how the changes in the market environment impacts on your business. The analysis helps you to position your business to be more competitive and grow.

STEEP[1] Analysis is a tool for analyzing the external macro-environment in order to highlight factors that will influence the way your business will develop. The tool isolates each individual component to establish the way each factor affects your business. Stakeholder analysis enables you to identify key stakeholders and their linkages to your business.

Follow these sub-steps to identify the market-environment related key success factors of your industry:

- Carry out a STEEP analysis.
- Carry out a stakeholder analysis.
- Assess the strategic implications of your findings.

1 STEEP stands for the following components: socio-cultural, technological, ecological, economic, and political/legal.

Carry out a STEEP analysis

International Labour Organization

STEEP analysis focuses on those factors that are outside your control yet impact on the way your industry and ultimately your business will develop. The tool isolates each individual component to establish the way each factor affects your business.

- Socio-cultural forces are forces impacting on your industry and business as a result of prevalent culture and value systems. For instance there is a great deal of gender segregation by sector and business location. Women generally dominate in food processing, services, hairdressing, dressmaking, and retail, while men dominate in metalwork, carpentry, vehicle repair, shoe making, construction and transport. Women entrepreneurs need to be aware of the socio-cultural norms that have an effect on their image in society and acceptability of their business venture. In some societies male employees have problems in accepting leadership of women entrepreneurs resulting in undermining the communication, coordination and leadership of the business. These culture and value systems are subject to constant change, and business people have to keep a careful eye on the long-term trends.

  To be able to grow their businesses women need to identify and overcome societal and cultural norms that inhibit communication, interaction, access to information, access to finance and confidence building. Growth oriented women entrepreneurs are raised under norms that have specific cultural and societal norms that have a bearing on who they are and how they perceive themselves. Building a successful business and competing with men is not acceptable in some societies. As a result successful women entrepreneurs are regarded as abnormal and outcast in some communities. Growth oriented women entrepreneurs need to beware of societal norms and cultural influences on women to be able to prepare themselves adequately as they grow their businesses.
- Technological forces are forces impacting on your industry and business as a result of technological development. For example, in South Africa, the arrival of the internet has revolutionized the way people work and communicate, created whole new industries in the service sector and marginalized other traditional trades. Entrepreneurs need to appreciate the technological development that affect their business and continuously increase knowledge and adoption of new technologies.
- Ecological forces are forces impacting on your industry and business from the surrounding ecosystem. For example, in the skiing industry cold weather is a main determinant of business activities. The patterns in the local, regional and global ecosystem are subject to constant change. In the African region, frequent spells of drought in recent years have driven up the cost of water and threaten to undermine the viability of irrigation farming. Climate change has resulted in the adoption of green businesses and interest in the business carbon footprint. In most countries there is specific legislation that governs the business environmental management requirements. It is important to analyze the cost and impact of complying with such legislation.
- Economic forces are forces impacting on your industry and business as a result of macro-economic developments at the national level, in the region and in the global economy. For example, revaluation of local currencies against the US Dollar drives up the cost of national exports and puts competitive pressure on export-oriented companies and may also lead to increased competition in the domestic market from imports.
- Political/ legal forces, are forces impacting on your industry and business as a result of

political developments and existing and new laws, or lack of enforcement of these laws. For example, due to a deficient legal structure, enforcement of commercial contracts continues to be a problem in many developing countries, and it remains very difficult for small enterprises to force clients to pay the bills for delivered goods and services. It is important for an entrepreneur to understand and interpret the legal framework governing business operations in the country.

It is important that your analysis focuses on both external threats and opportunities in the external environment. Consider what actions your business needs to take in order to either mitigate the impact of the threats or take advantage of the opportunities.

IN-DEPTH CASE STUDY

Refer to figure 19 to see how MJI Industries completed their STEEP analysis.

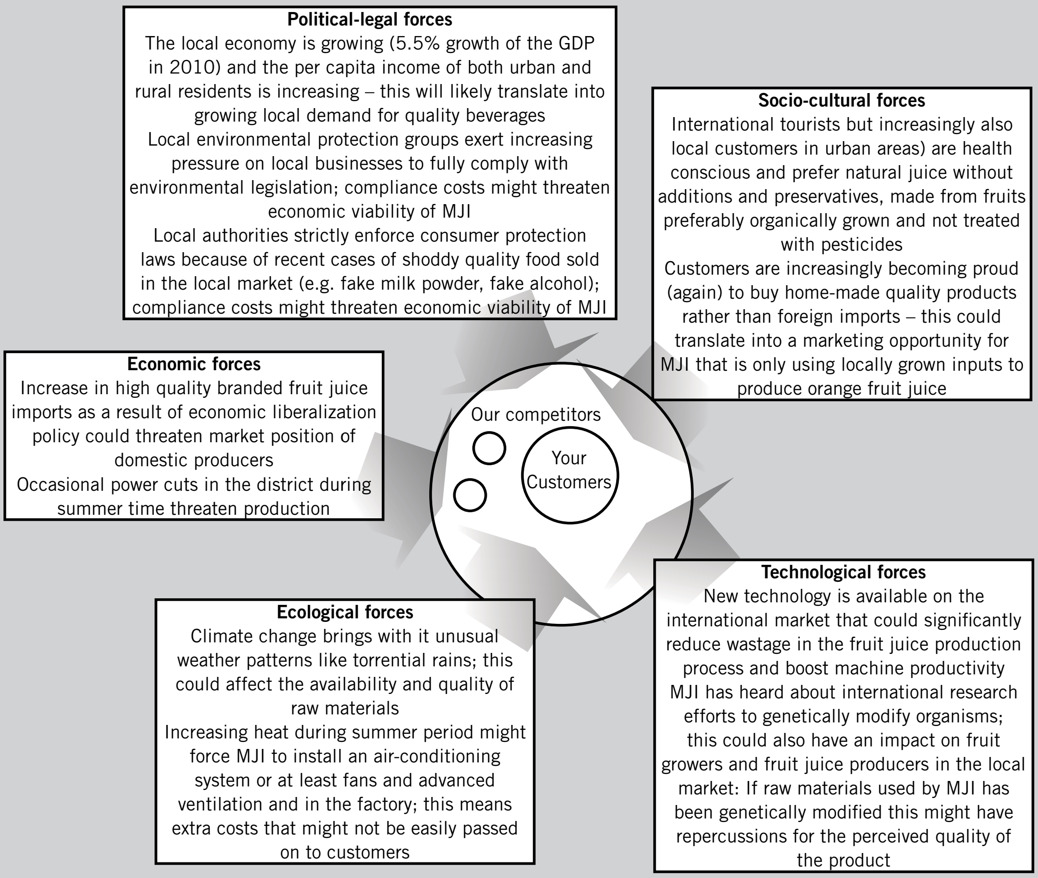


Figure 19: Results of the Mega Juice Industries STEEP analysis for the high quality orange juice market

EXERCISE

Carry out a STEEP analysis for your own industry. Fill the results in figure 20.

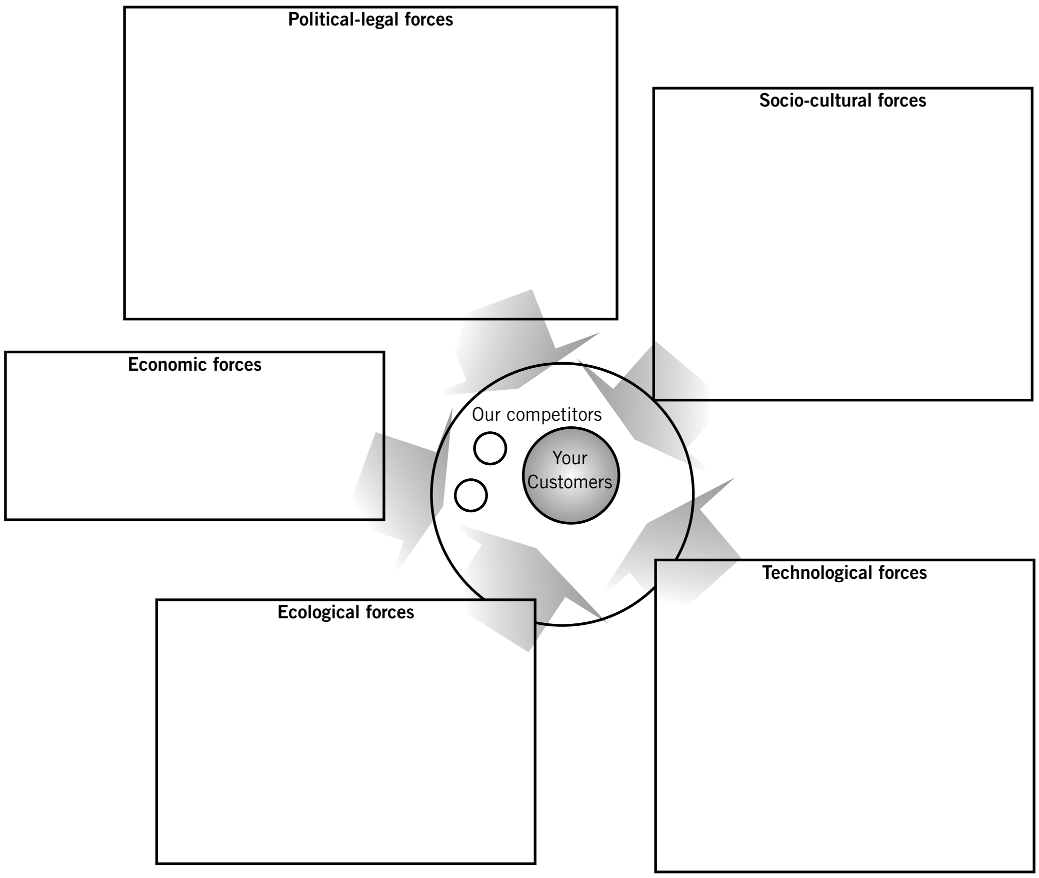


Figure 20: Results of STEEP analysis for own business template

Carry out a stakeholder analysis

In a stakeholder analysis, the first step is to identify the main stakeholders of your business. Refer to the checklist below to identify your main business stakeholders:

- Which groups formally or informally influence the formulation of strategies and policies in your business (For example the board of directors, trade unions, but also family members)?
- Are there groups that might react to the policies of your business and whose reaction impact on your business (For example customers, societal norms and culture)?
- Are there close linkages to other organizations that influence your business (like sector associations)?
- Which other groups take an interest in the way your business conducts business (for example tax authorities)?

The next step is to visualize the linkages between these stakeholders and your business by assigning each party a graphical symbol and drawing connectors between these symbols. Illustrate the relevance of these stakeholders to your own business by drawing symbols bearing highly relevant stakeholders in larger size and/ or by moving these symbols closer to the symbol of your own business. By choosing different types of connectors, or different filling colours for the symbols, you can furthermore illustrate the nature of the relationship between stakeholders and business (for example hostile or friendly to your business)

Finally, assess what expectations from your business each stakeholder group harbours, and in turn what benefits your business derives from each group. The analysis reveals what your business has to do in order to maintain mutually beneficial relationships with the major stakeholders, but also what kind of action these stakeholders might undertake if their expectations are not met. The analysis furthermore enables you to study the various coalitions that the stakeholder groups might set up among one another to press ahead with their expectations. It is important to review the gender dimensions of each stakeholder group. For instance your women customers may have different expectations from your men customers. On the other hand women employees may have different motivators for job satisfaction which would need to be met to avoid absenteeism and staff turnover. The template below is a useful tool to organize the results of your analysis in a single chart.

Stakeholder group	What they expect from your business?	How you benefit from these stakeholders?

IN-DEPTH CASE STUDY

Figure 22 presents Mega Juice Industries stakeholder map and table 11 defines its stakeholder expectations and benefits.

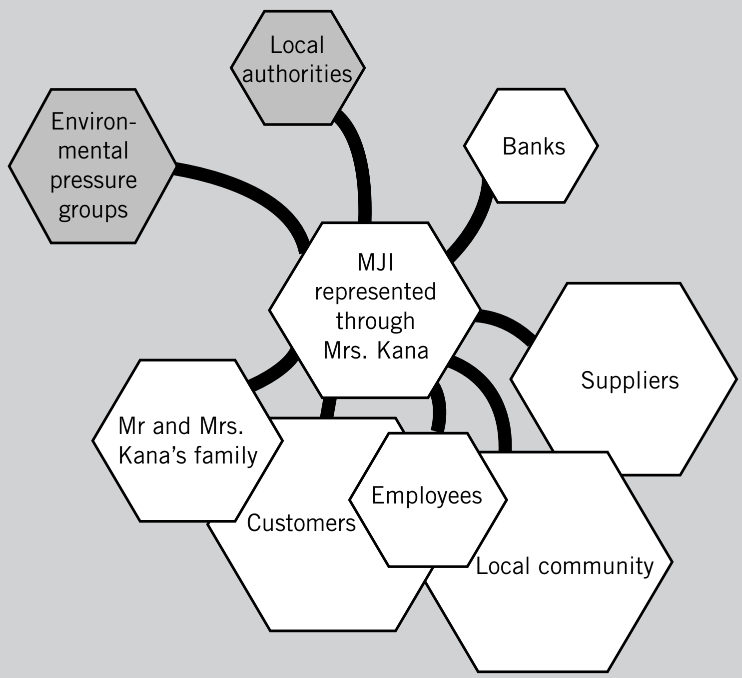


Figure 22: Mega Juice Industries Stakeholder Map

Table 11: Mega Juice Industries stakeholders: Expectation and Benefits

Stakeholder group	What they expect from MJI	How MJI benefits from these stakeholders
Family	Financial support Employment opportunities	Financial support Social protection and belonging
Customers	Quality products at attractive price	Revenue streams for MJI
Employees	Fair payment for their work Career development opportunities Recognition Job security	Without employees, the primary value creation activities in the business can not be performed
Local community	Employment opportunities for community members Tax income Corporate social and environmental responsibility	Revenue streams from community based customers buying your products Political support
Suppliers	Fair payment for quality raw materialsIncome security	Reliable supply with raw materials
Banks	Fair returns for their investment	Credit to co-finance growth
Local authorities	Compliance with laws Tax revenue Corporate social and environmental responsibility	Political support
Environmental pressure groups	Compliance with environmental laws	Political support

EXERCISE

Draw a stakeholder map for your own business in the box overleaf. Finally, analyze the expectations held by, and benefits derived from, these stakeholders and fill the results in the table below your map.

My stakeholder map

Stakeholder group	What they expect from your business	How you benefit from these stakeholders

Assess the strategic implications of your findings by referring back to the findings of your STEEP analysis and your stakeholder analysis and to reflect on the implications of the environmental forces impacting on your industry for business strategy: Which capabilities must your business command to anticipate and react to both market opportunities and business threats emanating from these market forces beyond your control?

For example, if you run a consultancy business and offer productivity improvement programmes for local medium and large-scale companies, the deregulation of the service industry can translate into competitive pressure from foreign consultants. To meet this competitive challenge, one market-environment specific KSF for your own business could be "access to knowledge on international best-practice in productivity improvement programmes".

IN-DEPTH CASE STUDY

The table 12 shows how MJI determined the market environment related KSF of their industry.

Table 12: Mega Juice Industries market environment related Key Success Factors

The key environment-related success factors for MJI in the market for orange juice are: **STEEP analysis** Diversified supplier relations to reduce risk of supply interruption Capability to brand fruit juice (as a healthy, home-grown product) Capability to access new generation fruit processing technology Capability to track developments in research on genetically modified organisms Capability to generate electricity on-site during summer period Access to clean production technology to meet/surpass environmental standards **Stakeholder analysis** Good community reputation Good relationships with the extended family A workplace policy for employees Good investor relations with the banks Capacity to maintain good public relations with local political/social pressure groups

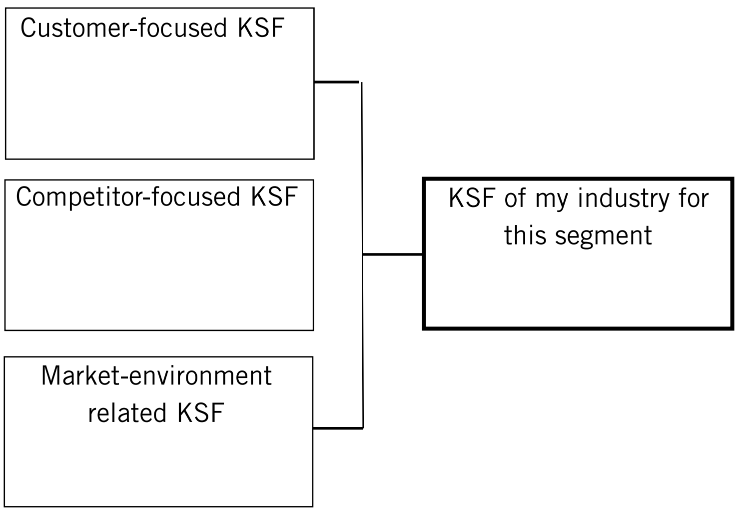
EXERCISE

1. Reflect on the strategic implications of the STEEP analysis and stakeholder analysis findings. What are the KSF to meet the competitive challenges of your market environment?

The key market-environment related success factors for my industry are:

2. Refer back to the results of your analysis of the (1) customer-focused, (2) competition-centered and (3) market environment-related industry success factors. List the success factors for each main customer segment in your market separately in the three boxes on the left side of the chart below. Then consolidate the list by clustering largely similar success factors as one single factor and by striking off double-entries.

Market segment: ___________________________



2.2 Assess the core competencies of your business

A core competency of a business is a capability, an asset or a skill especially well developed within the company. Core competencies are in-house capabilities, assets or skills that are usually unmatched by the competition. Core competencies are often industry specific, e.g. a competency in one market might not automatically translate into the same competency in other markets. In a business the combined skills of individuals and teams make up the organisation-wide capabilities. Human resources therefore make up the core of core competencies.

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The main sources of core competencies of a business are illustrated below.

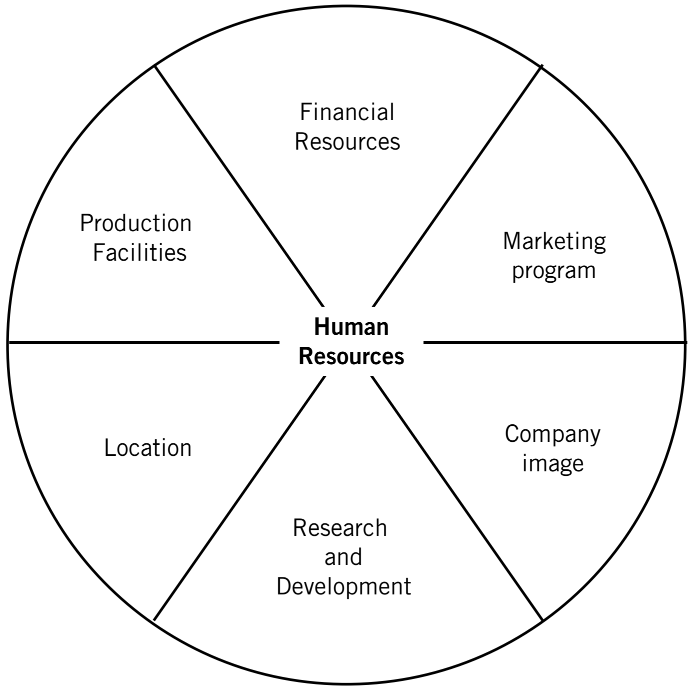

Figure 24: Sources of core competencies of a business

- "**Financial resources**" refer to the capability of the business to raise capital, either internally or externally, as a result of good financial performance.
- "**Human resources**" refer to the capability of the business to mobilize the skills required to perform the various business functions and to manage these functions.
- "**Company image**" refers to the perception of the business held by competitors, customers and other stakeholders
- "**Research and development**" refers to the capability of the business to develop new offerings and to innovate existing offerings.
- "**Location**" refers to the physical location of the business, preferably within convenient reach for employees, suppliers, buyers and other stakeholders.
- "**Production facilities**" refer to production processes and equipment that enable the business to produce quality products at low cost.
- "**Marketing program**" refers to the capability of the business to continuously scan the market for opportunities and threats, to provide the R&D department with the information necessary to design new offers and further develop existing offers, to price products, set up distribution systems and attract customers to buy the offer.

Why is it important to know the core competencies of your business?

It is important to identify the core competencies of your business because they are the internal enablers of business growth. Provided these competencies match the industry success factors, they translate into a competitive advantage that can be exploited to grow your business.

Refer to section 2.1. for more information how to assess the key success factors of your industry.

International Labour Organization

How to identify the core competencies of your business

Follow these steps to identify the core competencies of your business:
1. Carry out a financial performance analysis
2. Carry out a strengths and weaknesses analysis
3. Analyze the strategic implications of your findings.

1. Carry out a financial performance analysis

Accurate financial records are important for you to appreciate the performance of your business. Each item in the financial statements is difficult to understand and evaluate without putting it into its context by comparing it to other pieces of information and observing the trend. Financial ratios tell you how well or badly your business is doing and highlight specific areas that need attention. Your Income Statement and Balance Sheet are the basis of constructing the ratios. Ratios show trends and patterns when compared to the same ratios for previous years, and ratio of your competitors. It is important to note that ratios are as accurate as the numbers from which they are calcultated as they depend on the reliability and consistency of financial information.

The following ratios reveal the financial performance of your business: return on assets, net profit margin, return on equity, dept to asset ratio, and the current ratio.

Return on assets

The return on total assets (or ROA) shows the operating efficiency of the whole business. The return on total assets ratio measures how much profits before interest and taxes the total assets in the company generate. ROA is calculated as follows:

$$\text{ROA in \%} = \frac{\text{Operating profit before interest and tax}}{\text{Total assets}} \times 100$$

As a basic rule, the ROA should be higher than the cost of capital in the local financial market. If the ROA of your business is below that threshold then you should focus on improving operational efficiency, and not emphasize business growth.

Net profit margin

The net profit margin measures the profitability of your business. The net profit margin tells how many percent of the company's sales result in profit. The net profit margin is calculated as follows:

$$\text{Net profit margin in \%} = \frac{\text{Net profit}}{\text{Gross sales}} \times 100$$

A net profit margin of above 10% is normal but it can differ a lot from industry to industry.

Return on equity

The return on equity (ROE) measures how much profits the equity provided by owners generate. The ROE is important for two reasons. First, it takes the company's financing structure into account, which is important in order to get a picture of the company's overall performance. Second it looks at the business from an investor's perspective which means that it can be compared with the return from investing in other investment alternatives. ROE is calculated as follows:

$$\text{ROA in \%} = \frac{\text{Profit after taxes}}{\text{Average total equity}} \times 100$$

Since you can always choose to deposit your money in a bank account with a guaranteed interest rate, your company's ROE should always be above the risk-free interest rate. However, since there is a risk associated with investing in a small scale enterprise you should get a much higher return on equity than the interest rate at the bank. A satisfactory level of ROE is dependent on the risk of the business. The riskier business, the higher the ROE should be.

Debt to asset ratio

The debt to (total) asset ratio is an indicator reflecting the relative weight of debt on the shoulders of your business. The debt to asset ratio is calculated as follows:

$$\text{Debt to asset ratio} = \frac{\text{Total debt}}{\text{Total assets}}$$

A debt to asset ratio larger than 0.5 (meaning that total value of debt equals more than half of the total value of assets of your business) indicates that your business is already heavily indebted and has limited potential to raise further funds from the financial markets. The business actually faces the latent threat of liquidation from its investors if it should fail to promptly serve its debt. In turn, low debt to total assets ratios normally indicates potential to increase the debt of the company to finance parts of the investment.

Current ratio

Finally, in order to analyze the liquidity risk in the company, the current ratio can be used. The current ratio tells you how much current assets the company has to cover current liabilities. The current ratio is calculated as follows:

$$\text{Current ratio} = \frac{\text{Current assets}}{\text{Current liabilities}}$$

The minimum threshold for the current ratio is 1 – otherwise the business is technically bankrupt. A current ratio of around 1.5 is considered healthy and does not impose a risk of running low on liquidity. However a liquidity ratio above 2 is a sign of inefficient use of assets.

The table 13 has been drawn up to give an idea of the average financial ratios of companies in different industries. The ratios have been calculated from 1996-98 financial statements coming from companies in the European Union, the USA, and Japan. The companies were mature, large-scale listed companies with track record of consistent profitability in their sector. The ratios can thus not be directly compared with African companies, but they give an indication of differences between industries.

Table 13: Benchmarks for key financial rations in selected industrialised economies

	Brewing	**Construction**	**Hotels**	**Pharma-ceuticals**	**Food production**	**Food retail**
Net profit margin 1)	n/a	n/a	n/a	16.5	8.5	n/a
ROA 2)	7.4	5.5	3.2	11.7	9.1	6.0
ROE 2)	11.5	13.1	9.9	19.7	26.5	13
Debt to assets 2)	24	25	36	23	30	21
Current ratio 1)	n/a	n/a	n/ a	1.6	1.13	n/a

Sources: 1) Waish, Ciaran 2003. Key management ratios. Prentice Hall. 2) Vause, Bob 2001. Guide to analyzing companies. The Economist Books.

Financial Ratios will assist you to understand better:

- If there is short-term risk that the company cannot pay its workers and suppliers – The **Current Ratios**
- If there is long-term risk that the company is too reliant on borrowed Funds – The **Gearing**; and whether the interest on debt is supportable by the level of profits – the Interest coverage
- If the company is profitable in relation to the shareholders' investment and the level of sales and are these profits converting quickly into liquid cash resources needed to finance the growth plan? The **profitability ratios**
- If management is using efficiently the assets at its disposal, or are sloppy management practices allowing too much potential investment money to be tied-up in non-productive areas? **Inventory Turns**; Days Sales Outstanding and **Total Asset Turns**.

IN-DEPTH CASE STUDY

MJI carried out a financial health check for the business and documented the following results. From the Balance Sheet and the Profit and Loss Statement of MJI, it shows the company was profitable in 2010

Its **net profit margin** has been comparatively low (4%) but this is a typical feature of the food-processing industry, at least where part of the revenue is generated from the production of goods considered commodities in the local market.

The **Return on Assets** of Mega Juice Industries was 16.9% in 2010 and the Return on Equity was 19.5%. These are good ratios since a risk free investment in a savings account would have only generated an interest of not more than 2% after tax. However, since the company is quite small and has few clients the risk is fairly high and thus needs a high ROE to compensate the investors for the extra risk. Mega Juice Industries should therefore continue to strive for increased return on equity.

The **debt to total assets** ratio was 0.32 in 2010, a sign that the business was primarily financed from owners' equity and has some leverage to borrow capital from the financial markets.

The **current ratio** stood at 2 in 2010. The current ratio tells MJI whether it faces a liquidity risk. The ratio of 2 indicates that MJI has no cash flow problems – in fact, the comparatively high ratio indicates that MJI's current assets could be managed more efficiently.

EXERCISE

Analyze the financial performance and the strengths and weaknesses of your own business. Is the financial position of your business healthy, e.g. does it support growth, and does your company command any core competencies?

Financial performance of my business

Performance Measure	Ratio
Return on assets	
Return on equity	
Current ratio	
Net profit margin	
Debt to asset ratio	
Current ratio	

International Labour Organization

2. Carry out a strengths and weaknesses analysis

A strength and weakness analysis is an important tool that links the external analyses (STEEP and Porter's five forces Model) with the internal capabilities of your business. It assists in identifying what the company is doing right or wrong and what it can do well and what it can't, and laying that against the external environment. These pave the way for strategy creation. This analysis will assist the business to take advantage of opportunities identified in the external environmental analysis to position the business strategically in the market.

The strengths and weaknesses of your business are indicators of the existence or absence of assets and skills that might translate into core competencies. The table on the next page provides you with a checklist of selected areas in which a company can have strength and weaknesses. Strength is something that an enterprise/company is good at doing or a characteristic that gives it an important capability that others may not have. Strength can be a skill, important expertise, a valuable organisational resource, patents, connections.

In the checklist, each factor needs to be weighed on a scale from "less than average" up to "above average", where average marks the average performance of competing businesses in your industry. "Above average" indicates the existence of a core competency. For example if your business has acquired the latest production technology you will rate this aspect as an above average.

Keep in mind that this list is not comprehensive. The factors will vary from industry to industry, and you will probably have to customize the checklist so it fully suits the context of your own business. Your industry success factors can guide you on the factors to consider in your assessment.

IN-DEPTH CASE STUDY

TMega Juice Industries completed a strengths and weakness checklist, after adding some factors of critical importance to their specific industry. The results of their assessment are shown in table 14.

Table 14: Mega Juice Industries Strengths and weaknesses

Score Key

+	means	Above average
0	means	Average
-	means	Below Average

Area	Score	Area	Score
Financial resources (access to capital)	**Marketing program**		
From operations	+	Product characteristics/ differentiation	+
Ability to use debt and equity financing	+	Brand name recognition	-
Investors relations	-	Breadth of the product line	-
Production facilities		Customer orientation	+
Cost structure	+	Segmentation/focus	o
Flexible production operations	o	Distribution system	+
Equipment	-	Retailer relationship	-
Access to raw materials	+	Advertising/promotion skills	-
Production capacity	-	Sales force	+
Clean production	o		
Human resources	Customer service/ product support	+	
Quality of top management	+	Market information system	-
Quality of line managers	+	**Company image**	
Culture	-	Product quality reputation	+
Strategic approach to management	-	Company reputation	+
Entrepreneurial thrust	+	**Location**	
Systematic planning and operations	-	Convenient for suppliers (where applicable)	+
Technically skilled staff	-	Strategically close to customers	+
Workforce attitude and motivation	o	**R&D**	

		Product/production process innovation capability	o
Other			
Community relations	+		
Relations with local Government	o		

EXERCISE

Analyze the strengths and weaknesses of your own business. Select and adapt the checklist below and analyse your own strengths and weaknesses.

Table 15: Strengths and weaknesses analysis template

Area	**Score**	**Area**	**Score**
Financial resources (access to capital)	*Marketing program*		
From operations		Product characteristics/ differentiation	
Ability to use debt and equity financing		Brand name recognition	
Investors relations		Breadth of the product line	
Production facilities		Customer orientation	
Cost structure		Segmentation/ focus	
Flexible production operations		Distribution system	
Equipment		Retailer relationship	
Access to raw materials		Advertising/ promotion skills	
Production capacity		Sales force	
Clean production			
Human resources	Customer service/ product support		
Quality of top management		Market information system	
Quality of line managers		**Company image**	

Culture		Product quality reputation	
Strategic approach to management		Company reputation	
Entrepreneurial thrust		**Location**	
Systematic planning and operations		Convenient for suppliers (where applicable)	
Technically skilled staff		Strategically close to customers	
Workforce attitude and motivation		**R&D**	
		Product/ production process innovation capability	
Other			

3. Analyze the strategic implications of your findings

Review the findings of your financial performance analysis and your strengths and weaknesses analysis in order to extract the core competencies of your own business. As indicated above, any business strength – and also strong financial performance - can be an indication of a core competency. For example, if you run a beauty salon and your strengths and weaknesses analysis reveals that your senior stylists have highly specialized hair dressing skills, this knowhow might translate into a core competency of your business.

Keep in mind, though, that business strength does not necessarily translate into a core competency. Your business capabilities, assets or skills (even your capacity to raise cash) only translate into core competencies if they are unmatched by the competition and built up and retained in-house. For example, if you run a consultancy company and you have temporarily subcontracted an internationally recognized expert in business management training, this sector expertise does not translate automatically into a core competency of your business because this person might be subcontracted and marketed tomorrow by one of your competitors.

Apply the guidelines below in interpreting the results of your analysis

Result	Interpretation
Match between KSF and Core competencies	Strategic competitive advantage- Build on it!!
Aspects not matching between KSF and core competencies	Strategic competitive disadvantage, develop strategic initiatives to deal with issues
Core competencies not in KSF	Identify other possible product lines that can benefit from these

IN-DEPTH CASE STUDY

After analyzing their strengths and weakness checklist shows that Mega Juice Industries (MJI) has the following core competencies:

1. The Company produces quality juices at comparatively low cost. It can draw on local supply of raw materials and maintains close customer relations with key accounts in the hotel segment.
2. Company has good and experienced managers in production, sales management and an entrepreneurial flair
3. MJI also has excellent relations with the neighbouring communities, an essential asset for companies producing in the local market.
4. Finally, MJI is able to internally raise capital from operations to finance growth.

MJI also note weaknesses in the company

1. MJI is aware that their orange juice, while respected for its quality, does not enjoy any brand recognition in the local market
2. MJI is also over-dependent on few clients and that notwithstanding their faith in their own innovation capacity; in practice they have done little to actually develop new offerings in the recent past.
3. There is recognition that production technology is increasingly outdated and that their workforce, while doing their job properly, shows currently little enthusiasm for going the extra mile to successfully grow the business.

EXERCISE

Refer back to the results of your financial performance analysis and your strengths and weaknesses analysis. Do the strengths of your business translate into a core competency? List any core competencies below.

Core competencies of my business:

Weaknesses of my business

2.3 Identify the competitive advantage of your business

A competitive advantage is the capacity of a business to perform better than its direct competitors in a given industry. Competitive advantages result from core business competencies that match the key success factors for a particular industry.

Why is it important to know the competitive advantage of your business?

Knowing your competitive advantage enables you to choose a growth strategy that builds on your business strengths and takes advantage of market opportunities which is key to the success of business growth strategy.

How to identify the competitive advantage of your business

Follow these steps to identify the competitive advantage of your business

1. Compare the key industry success factors with your core business competencies to identify your industry-specific competitive advantage for each industry covered by your business and for each product.
2. Carry out a cross-comparison of your findings to identify the industries where you hold the relatively strongest competitive advantage.
3. Refine your business vision and business objectives based on the outcomes of your market analysis.

1. Identify your industry specific competitive advantage

In the first step you need to run a match between the key success factors of your industry and the core competencies of your business separately for each industry covered by your market analysis in your portfolio. A match between an industry key success factor and a core business competency is an indication of a product-specific competitive advantage.

For information about how to assess the KSF of your industry and the core competencies of your business, refer back to chapters 2 of this manual.

IN-DEPTH CASE STUDY

The figure 25 illustrates how MJI ran a match between the key industry success factors and the core competencies of your business.

Customer analysis

Competition analysis

Environment analysis

KSF of our industry

- Intimate supplier relationships
- Diversified supplier relations
- Ability to compete on cost with international brands
- Ability to compete on focus with local brands, namely flexibility in accepting orders even on short notice and by delivering our goods to the doorsteps of our clients
- Ability to brand the product
- Diversified customer base
- Intimate relations with key accounts
- Good public relations with local authorities and civil society groups
- Access to latest generation fruit processing technology
- Access to cleaner production technology
- De-centralized power generation capacity (e.g. an on-site generator)
- Access to market information on local and international best practice in fruit juice production
- A workplace policy for employees
- Good investor relations
- Good community reputation

Our core competencies

Area	Score	Area	Score
Financial resources (access to capital)		Marketing program	
From operations	+		
Ability to use debt and equity financing	+		
Investor relations (with the local bank)			
Production facilities		Customer orientation	+
Cost structure	+	Segmentation/focus	o
Flexible production operations	o	Distribution system	+
Equipment	-	Retailer relationship	-
Access to raw materials	+	Advertising/promotion skills	-
Production capacity	-	Sales force (Ms Wang)	+
Human resources		Customer service/ product support	+
Quality of top management	+	Market information system	-
Quality of line managers	+	Company image	
Culture	-	Product quality reputation	+
Strategic approach to management	-	Company reputation	+
Entrepreneurial thrust	+	Location	
Systematic planning and operations	-	Convenient for suppliers (where applicable)	+
Technically skilled staff	-	Strategically close to customers	+
Workforce attitude and motivation	o	R&D	
		Product/production process innovation capability	o
Other			
Community relations	+		
Relations with local Government	o		

Financial performance (2010)

- NPM: 4%
- ROE: 19.5%
- Debt to asset ratio: 0.32
- RoA: 16.9%
- Current ratio: 2

Do they match?

Our competitive advantage:
Intimate supplier relations
Intimate buyer relations (in the hotel segment)
Ability to compete on cost through local production base
Ability to compete on focus through customer-focused distribution networks
A quality product
Capacity to internally finance procurement of technology
Good community relations
Good company reputation

Competitive threats:
Lack of access to technology and information on local and international best practice
No brand identity for main product
Over-dependence on few buyers
No systematic approach to public relations
Current production capacity (old equipment, lack of motivation among workers)
Lack of close relations with local Government authorities

Figure 25: The competitive advantage of MJI in the market

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EXERCISE

Run a match between the KSF of your industry and the core competencies of your business for each product identified in your customer segmentation matrix earlier. A match indicates a product-specific competitive advantage of your business.

Environment analysis → Key industry success factors

Competition analysis → Key industry success factors

Customer analysis → Key industry success factors

Key industry success factors → Do they match?

Business core competencies → Do they match?

Do they match? → My competitive advantage:

Business core competencies

Area	Score	Area	Score
Financial resources (access to capital)		Marketing program	
From operations		Product c differenti	
Ability to use debt and equity financing		Brand na	
Investors relations		Breadth o line	
Production facilities		Customer orientation	
Cost structure		Segmentation/ focus	
Flexible production operations		Distribution system	
Equipment		Retailer relationship	
Access to raw materials		Advertising/ promotion skills	
Production capacity		Sales force	
Human resources		Customer service/ product support	
Quality of top management		Market information system	
Quality of line managers		Company image	
Culture		Product quality reputation	
Strategic approach tmanagement		Company reputation	
Entrepreneurial thrust		Location	
Systematic planning aoperations		Convenient for suppliers (where applicable)	
Technically skilled staff		Strategically close to customers	
Workforce attitude and motivation		R&D	
		Product/ production process innovation capability	
Other			

Financial performance
- Net profit margin
- Return on assets
- Return on equity
- Debt to equity
- Current ratio

Do they match?

My competitive advantage:

Any competitive disadvantage?

2. Carry out a cross-comparison of your findings

Once you have matched the core competencies of your business to the industry key success factors it is important to compare the competitive advantage held by your business in a given industry for each product your business offers. This will assist your business to identify the industry specific products where your business holds the relatively strongest competitive advantage. The industry attractiveness and business ability to compete matrix below provides you with a simple tool to compare the competitive advantage held by your business in a given industry for each product in your portfolio and the attractiveness of the industry.

Variables that might be used to evaluate competitive advantage and industry attractiveness include the following:

Business Ability to Compete		**Industry Attractiveness**	
Size	Distribution	Size	Profitability
Growth	Technology	Growth	Technological
Relative share	Marketing skills	Competitive intensity	sophistication
Customer loyalty	Patents	Price levels	Government regulations
Margins			

How to construct the Matrix

1. Plot each industry product in your business portfolio according to its growth potential or market attractiveness on the horizontal axis of the matrix. Industry market attractiveness might be either classified as "high", "medium" or "low", based on the results of your earlier market analysis, and the classification should be based on the results of your customer and industry analysis. For example, if your analysis reveals that the market is saturated and that sales are low, you should classify the market attractiveness as "low" and if you have found out that the industry is mature and offers no further growth potential, then you should classify its attractiveness as low.
2. On the vertical axis of the matrix, you plot each product according to the product/ industry specific competitiveness of your business. For example, if your market analysis has revealed that you hold a strong competitive advantage in a given industry for a given product, you should classify your products-specific business competitiveness in this industry as "high".

Interpreting the results in the matrix

The Matrix is defined by symbols that guide decision making for each of the nine squares of the matrix see key on figure 26. As visualized by the symbols in each of the nine squares of the matrix, an industry/products offering comparatively the best growth potential for your business would be located in the north-western corner of the matrix. A product offering your business low or no growth potential would be located in the south-eastern corner of the matrix, and a product with medium growth potential would be located in the north-eastern, south-western, or the central square of the matrix.

Following the logic of the matrix, you would want to focus your growth effort on industry / products in the north-western corner of the matrix and harvest or possibly divest from products in the south-eastern corner of the matrix, to be able to redeploy and focus your resources. Your business strategies with regard to medium-growth potential products would need to be determined from case to case.

IN-DEPTH CASE STUDY

Mega Juice Industries (MJI) carried out the comparison of their relative competitive advantage across industries and products and concluded that the business should focus its business expansion effort on its orange juice product with special attention to penetrating the existing hotel segment and entering the new segment of school canteens as the promising intervention points for growing the business.

The market for canned pineapple looks much less attractive with flat sales limited demand and price sensitive clients. MJI decides to divest from this market and redeploy the resources freed in the process to push for sales growth in the market for orange juice.

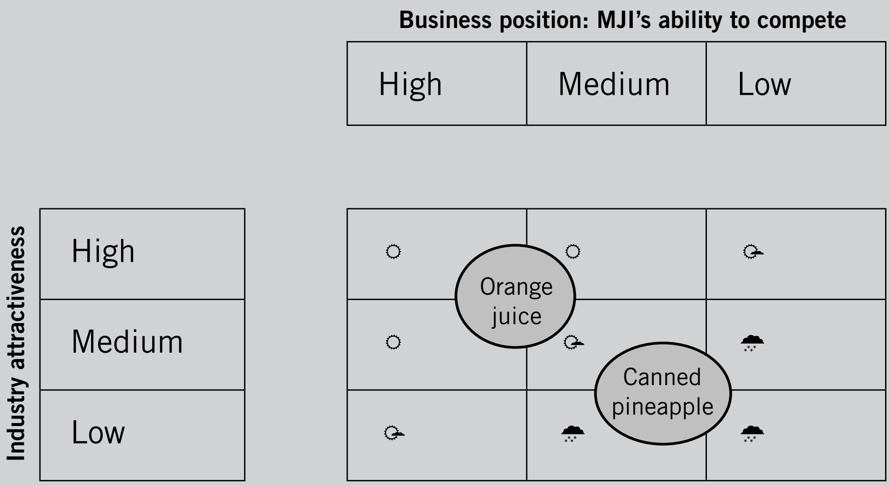

Figure 26: MJI industry Market segment attractiveness/business competitiveness position matrix

For information about how to grow your business and about what you need to do in order to gear your business for growth please refer to chapter 3 of this manual.

EXERCISE

Complete the industry attractiveness/business competitiveness matrix for your own business to identify the industries where you hold the relatively strongest competitive advantage. Then focus on this high-potential industry and further specify the segments with the relatively best growth potential.

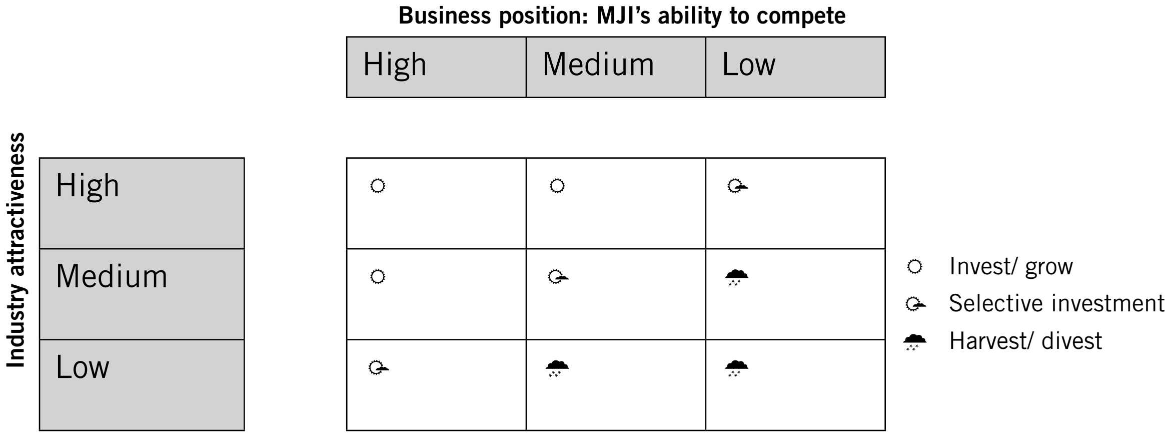

Figure 27: Industry market segment attractiveness/business competitiveness position matrix

3. Refine your business goals based on your market analysis

Finally, once you have identified the competitive advantage of your business, you need to study the implications of your findings for your draft business vision and objective to realign this strategy framework in the light of the findings of your market analysis.

Your business vision and your business objectives need to firmly build on the competitive advantage of your business, because this advantage will later be turned into the spearhead of your growth strategy. A business vision that ignores the competitive advantage of your business can misdirect the growth effort of your business.

Figure 28 illustrates how the results of your market analysis reshape your visions and business goals in the process of drawing up your business growth strategy. Please refer to Chapter 3 and 4 of this manual for more information on similar learning loops at later stages of the strategy development and implementation process.

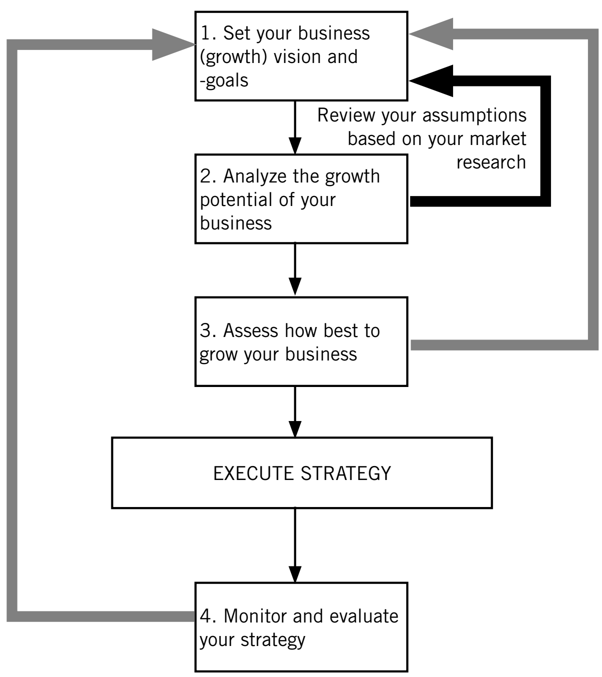

Figure 28: Strategy development as a process of learning loops

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IN-DEPTH CASE STUDY

Throughout the manual we will refer to a case study of a growth oriented entrepreneur who has developed a business growth strategy. In the case study Mega Juice Industries formulated their vision statement as:

This is how MJI team refined their vision statement and business objectives based on the results of their market analysis.

THE CONSOLIDATED DRAFT VISION OF MJ INDUSTRIES IS TO...

…become an internationally competitive company that meets the demand of consumers in South Africa for high quality fruit juice and other processed fruit products while ensuring attractive returns for our shareholders. We acknowledge our social responsibility to the welfare of our employees and our environmental responsibility to the communities with whom we are involved."

Table 16: Refined business objectives and performance thresholds for MJI

Objective	Measures	Target				
		2012	2013	2014	2015	2016
Attractive returns	Return on assets in % (annual profit after tax x 100 divided by value of fixed assets)	15	15	20	25	25
High profits	Net Profit Margin	4	4	5	6	7
Low cost structures	Ratio of overheads to total costs (administrative expenses x 100 divided by total business expenses)	0.02	0.02	0.02	0.02	0.02
High customer satisfaction	Customer satisfaction rate in% (no of satisfied customer x 100 divided by total no of customers per year)	85	90	90	90	90
Close relationships with buyers	Average time spent with each business customer (no of days per year per business customer	5	5	6	7	7
Good community reputation	No of community projects supported by company	1	2	2	2	3
High operational efficiency	Machine productivity (no of litres per machine per year)	60,000	60,000	60,000	60,000	60,000

	Lead time, production (time in days from receiving a product order to product delivery)	2	2	2	2	2
Emphasis on quality	Product rejection rate (no of deliveries rejected by customers x 100 divided by total no of deliveries made per year)	5	5	5	3	2
Close supplier relationships	Supplier turnover (no of suppliers lost x 100 divided by total number of suppliers per year)	15	15	15	10	10
Systematic market information management	No of new document entries in the market information database per year	100	150	200	250	300
Cleaner production	Recycling rate, machine oil (litres of machine oil recycled x 100 over total litres of machine oil used in production each year)	0	25	50	75	100
	Wastage rate, raw materials (kilograms of orange wasted x 100 divided by total kilograms of oranges processed in production per year)	10	9	9	8	7
Qualified workers	No of days in training per machine operators per year	10	15	15	15	15
	Course pass rate (no of machine operators successfully graduating from training x 100 divided by total no of operators in training per year)	75	85	85	85	85
Motivated workers	Worker satisfaction rate (no of workers satisfied with salary package x 100 divided by total no of workers per year)	60	75	75	80	85
High innovation capacity	No of new products to market each year	1	1	2	2	2

International
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Organization

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EXERCISE

Review your draft business vision and goals in the light of the findings of your market analysis. Write down the consolidated draft vision and the consolidated business goals and performance targets below.

MY CONSOLIDATED DRAFT COMPANY VISION IS TO...

____

____

____

____

____

Table 17: Consolidated draft business goals

Objective	**Measures**	**Target**				
		20__	20__	20__	20__	20__
No 1						
No 2						
No 3						
No 4						
No 5						
No 6						

No 7						
No 8						
No 9						
No 10						
No 11						
No 12						
No 13						
No 14						
No 15						

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Organization

CHAPTER 3:
HOW CAN I GROW MY BUSINESS?

International Labour Organization

This chapter will assist you to analyze a spectrum of growth strategies that you can consider in the process of choosing a growth strategy for your own business. Business growth can be defined as the improvement of the financial performance of a company by way of expanding its sales. A business growth strategy specifies the road you intend to take and how you intend to drive along to expand your sales within the broader framework of your business vision and your business objectives.

3.1 Analyze the spectrum of distinct growth strategies

A business growth strategy gives your growth effort direction. It is not always the shortest or easiest route that leads to business success. A business growth strategy clarifies the means you will apply to reach your target. Businesses have a broad range of growth options and it is important for you to be clear about these options and to be able to choose the option that suits your own business best.

As a result of a growth strategy, you will be able to grow your business later in a structured and well-planned manner, resulting in higher resource allocation efficiency and increased success chances. There are advantages with planning the growth of your business. Some key advantages of planned growth over unplanned growth of a business are listed in the table overleaf:

Table 18: Planned growth vs. unplanned growth

Planned Growth	Unplanned Growth
New markets are selected based on solid market information, not gut feeling	Grab new customers as they come along
New employees are hired in anticipation of expanding operations	Last minute hiring decisions – staff is added in response to crisis
New lines of business are not started unless they meet with stated plans and goals	New lines of business are taken on without establishing whether they can be absorbed
Activities are implemented, and targets are met, in accordance with deadlines	Management by exception – activities are implemented in a "firefighter" approach and results are often erratic
Owner/ manager focuses on leadership and entrepreneurial tasks; day-to-day management tasks are delegated	Owner/ managers suffer from acute stress and unsustainable workload

Managed growth	Unmanaged growth
Business has expanding sales and profits.	Business has expanding sales but elusive profits
Business has enough cash at the end of each month	Business perpetually runs out of cash, pays late
Customer orders always delivered on time	Customer orders frequently delivered late and incomplete
Inventory levels are appropriate for sales levels	Poor inventory management

How to analyze the spectrum of business growth strategies

Follow these steps to seek a clear understanding of the spectrum of business growth strategies:

1. Study the principal growth directions a business might take (where to go).
2. Study the main sources of thrust that drive business growth (how to grow).
3. Study how direction and thrust can be combined to become distinct growth strategies.

1. Principal growth directions for businesses

Businesses have essentially four strategic directions to choose from if they want to expand their sales. They can aim at

- **Market penetration:** Market penetration means that you sell more of the same products in their existing markets, either by way of increasing market share or product usage.
- **Market development:** Market development means that you sell more of the same products to new markets locally or abroad. When you aim for new markets, you can either focus on untapped segments in your existing markets, or on new markets.
- **Product development:** Product development means that you sell new products to existing markets. Product development entails developing new products or refining/upgrading existing products
- **Product diversification:** Product diversification means that you sell new products to new markets, typically by setting up a new business or taking a stake in an existing business.

The matrix below illustrates these four basic growth directions businesses can take, leaning back on a model originally developed by Ansoff.

Table 19: Principal business growth directions

	EXISTING PRODUCTS	NEW PRODUCTS
ESISTING MARKETS	Market penetration	Product development
NEW MARKETS	Market development	Product diversification

Source: Ansoff Matrix

As the matrix indicates, the borderline between the four strategic growth directions is often blurred. For example, it is often difficult to say from which point onwards the differentiation of an existing product for market penetration requires a more systematic (new) product development effort. The pros and cons of these growth options are illustrated in table 22.

Table 20: Pros and cons of business growth options

PROS	CONS
Market penetration	
The advantage of market penetration is that you likely already have a clear understanding of your target market and you already hold the expertise needed to provide the goods and services of your choice. As a result, the risk of the unknown is smaller and your required upfront investment in market research and, where applicable, product development is limited.	On the flip side of the coin, market penetration might yield lower growth rates than other growth options, for exactly the same reasons described to the left. The growth barriers in your existing markets are probably high because your direct competitors will command comparative product expertise and market information. Also, customers will likely have already made a product choice; as a result, there will be fewer first-time buyers. Furthermore, it will be especially difficult for you to win over customers that buy from your competitors and are satisfied with their offer.

Market development	
The advantage of market development is that you can • unlock new market segments while, at the same time, sticking to a known product – you rather stretch coverage of your tested brand than taking on the risk of new product development • escape a growth deadlock in mature markets • spread business risk over different market segments • better satisfy the needs of clients that themselves operate in more than one market. • exploit economies of scale for highly specialized products that might not find sufficient demand in one market (i.e. medical equipment)	The main risk with market development is that you usually lack personal experience in operating in these new markets and do not know your prospective customers yet. As a result, you might fail to judge the threats and opportunities in these markets properly, and that you mistake the capacity of your own company to enter these markets. Therefore, the risk of developing new markets is higher than the risk of penetrating existing markets.
Product development	
The advantage of product development is that your company might exploit the first/ early market entrant advantage, i.e. reap higher margins for new products with few or no competing substitutes. Also, product development means taking a active approach to competition and opting for innovation, not mere imitation. In extreme cases, your company becomes the pace setter in the industry. Product development also provides you with an escape from mature markets/ markets in decline or, alternatively, can be a strategy to revitalize a brand by upgrading/ innovating product features.	Early innovator dilemma: Statistically two out of three efforts to develop a new product fail, because companies misjudge consumer needs and wants or products do not meet standards and expectations. Costs: Your company has to invest in market research and R&D. Time factor: It can take years to develop new products and to eventually recoup your investment.
Product diversification	

The advantage of product diversification is that it enables you to tap new business opportunities outside the current boundaries of your business activities. Also, product diversification helps your business to spread business risk over a broader range of markets. Product diversification can result in synergies. For example, a guesthouse operator might offer daily tours to tourist attractions, exploiting his competitive advantage of direct access to tourists "at source". Pending the type of diversification strategy you choose, diversification can also be a way of exerting better control over suppliers and distributors in the value added chain, and to ensure continued access to raw materials and customers. Diversification might also result in reduction in competition within your industry, e.g. in cases where a company diversifies by acquiring a competitor.	The flip side of the coin is that product diversification carries many risks. Your business is taking the double risk of entering new markets with new products and may lose its competitive advantage as a result. Also, product diversification often fails because of technical or process-related reasons not directly related to customers or products. For example, related diversification by acquisition often fails because organizational cultures are incompatible, or logistical challenges prove to be too demanding. Therefore, product diversification is considered a high risk by comparison with other business growth options discussed earlier.

1. Main sources of strategic thrust driving business growth

To drive growth, a business strategy might emphasize on

- **Differentiation:** Business growth strategies emphasizing on differentiation aim at expanding sales by distinguishing one's offer more clearly from competing substitutes. For example, you might decide to brand your product, e.g. to give it some special features that make it unique in the eyes of your customers.
- **Focus:** Business growth strategies emphasizing on focus aim at expanding sales by (re-) positioning one's offer in a particular market segment thought of as highly attractive. For example, you might aim at entering a high potential export market with your existing product.
- **Cost:** Business growth strategies emphasizing cost, finally, aim at expanding sales by undercutting prices of competitors. A strategic emphasis on cost requires you to hold a cost advantage.

In practice, many businesses will aim at combining an emphasis on differentiation, focus and cost. For example, a business might brand its product - essentially a differentiation strategy - and focus its promotional effort on a new segment of up-market clients. Also, most growth strategies comprise at least tactical elements of a cost strategy, e.g. by launching a new product for a limited period at a low price to attract first time buyers. The overlap is illustrated below.

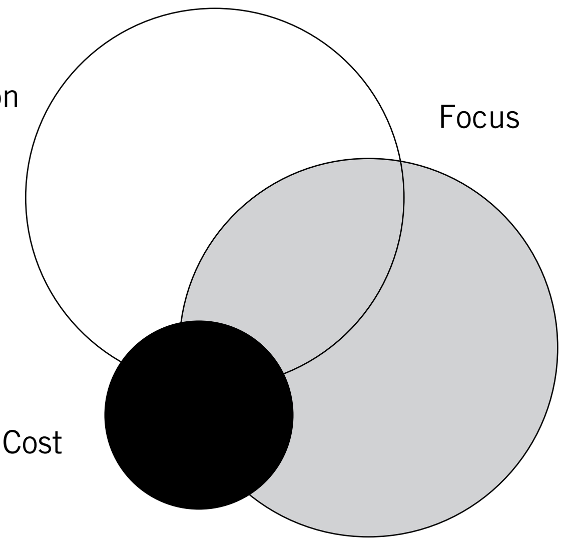

Figure 29: Strategic emphasis of business growth strategies

The main pros and cons of emphasizing differentiation within a business growth strategy, focus, and cost are described in the table overleaf. Table 23 illustrates that any of these strategies bears both potential benefits and risks.

Table 21: Pros and cons of emphasizing cost, differentiation, or focus with your growth strategy

PROS	CONS
Cost	
Growth strategies exploiting the cost advantage of your business to undercut prices of competitors are typically applied in mature markets where products have turned into commodities and are judged mainly by price Yet, most growth strategies somewhat emphasize cost, if for selling tactics only. For example, your company might decide to give quantity discounts to boost sales of existing products. Price is always a factor in making a buying decision.	To compete on cost, your business needs to actually hold a cost advantage – otherwise this strategy severely affects your cash flow and can quickly drive you into financial ruin. *Building up a cost* advantage can be costly. For example, if you decide to set up a productivity improvement programs or install new equipment, you incur upfront investment costs in training and hardware.
Differentiation	
Product differentiation helps you to escape price sensitive and/ or mature markets and to position your offer with customer segments that judge products along their features and quality.	Growth strategies laying emphasis on differentiation are costly and can be risky. You have to invest, among others, in market research on how to differentiate the product, staff training, and hardware. You also have to spend on packaging and promoting the differentiated offer.

Focus	
Emphasis on focus enables you to position your offering with higher target precision. Your growth effort becomes more efficient and effective because you can tailor-make your products to the needs and wants of specific customers and customize your distribution channels and promotional campaign. It is also easier for you to set a price for your product based on the thorough analysis of the distinct buying behaviour of the segment.	An emphasis on focus bears the cost of additional market research. You need to obtain a very detailed picture of the needs and wants of the customer segment of your choice. A strategic emphasis on focus also bears the risk of foregoing other business opportunities. If the focus is too narrow, you might not be able to create the critical mass of customers needed to create acceptable returns. In addition, you might miss other segments with latent demand for your product that you might have reached in a broader growth effort.

3. How direction and thrust combine to become distinct growth strategies

As illustrated above, the "source code" of a business growth strategy is quite complex. In theory, you can choose from (a combination of) various growth directions and you can emphasize either on cost, differentiation or focus, or a combination of these thrusts to drive your growth effort.

Table 24 illustrates how direction and thrust might combine to become a growth strategy. Each box in the matrix describes one principal combination and provides a real-life example for your reference.

The matrix explicitly acknowledges that many businesses combine an element of cost, differentiation, and focus in their strategies. It also acknowledges that the line between market penetration, market development, product development and product diversification can be sometimes blurred.

It also clearly emerges from the matrix, though, that whatever the strategy mix, there always needs to be an emphasis on one principal source of thrust and one principal direction. Otherwise, your business runs risk of losing direction and of too thinly spreading its resources in the strategy implementation process. In the worst case, strategic initiatives implemented in support of your growth goal might contradict one another and derail the entire growth effort.

Table 22: How direction and thrust can combine to become a distinct growth strategy

	Market penetration	Market development	Product development	Product diversification
Cost *Examples of complementary combinations*	The strategic emphasis is on cost to penetrate markets. An example is a large-scale bakery that exploits economies of scale to produce low-cost bread loaves. *The growth strategy might be complemented. By targeting factory canteens as clients only (focus) and by acquiring a local retail chain to gain shelf space for the bakery products (diversification).*	The strategic emphasis is on exploiting a cost advantage to enter new markets. An example is a local software company exploiting its (labor) cost advantage to enter an overseas market. *The growth strategy might be refined by developing a new internet browser especially for senior citizens (new product development-cum-focus).*	The strategic emphasis is on exploiting a cost advantage to develop new products. An example is a restaurant developing a new dish based on seaweed – a cheap raw material in abundant local supply. *The growth strategy might be complemented by differentiating the product as a protein rich and cholesterol-free dish and positioning it with health-conscious customers.*	The strategic emphasis is on diversification to exploit a cost advantage. An example is a coir product manufacturer buying into a coconut plantation. Diversification enables the business to cut material costs and to lower its own prices. *This growth strategy might be combined with a product development effort, aiming at developing new products like eco-friendly and allergy-free coir carpets.*
Differentiation *Examples of complementary combinations*	The strategic emphasis is on market penetration by means of product differentiation. For example, a hair-dresser might aim at expanding sales by offering standard hair treatment but with special perms. *The growth strategy might be complemented by promoting the offer exclusively to business women (focus).*	.The strategic emphasis is on market development by means of product differentiation. For example, a tailor located next to a five start hotel might modify the cut of his suits to attract foreign tourists. *The growth strategy might be complemented by specializing on extra-large clients (focus) or by adding a small leather workshop producing belts and other leather accessories (diversification)*	The strategic emphasis is on the development of new and differentiated products. An example is an internet cafe that sets up a wireless internet connection point. *The growth strategy might be complemented by targeting students from computer academies (focus) and by exploiting the cost advantage of the new technology - as WI-FI is cheaper to maintain than fixed networks.*	The strategic emphasis is on product diversification with emphasis on differentiation. For example, a travel agent might buy a yacht and market customized cruize packages. *The growth strategy might be complemented by marketing the packages through local yachting clubs (focus) and by offering a sail-yourself option (cost).*

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Table 22: How direction and thrust can combine to become a distinct growth strategy (continue)

	Market penetration	**Market development**	**Product development**	**Product diversification**
Focus	The strategic emphasis is on focus to penetrate markets. For example, a private hospital might increase its sales by targeting its services to senior citizens.	The strategic emphasis is on market development with an emphasis on focus. For example, a local dentist might offer special dental packages to foreign tourists.	The strategic emphasis is on product development with emphasis on focus. For example, a local fertilizer manufacturer might develop a new formula for a powerful flower fertilizer produced with local phosphate.	The strategic emphasis is on product diversification with emphasis on focus. For example, a consultancy company providing ISO 14000 certification to local tanneries might diversify into the import of clean tanning technology.
Examples of complementary combinations	*The growth strategy might be complemented by offering mobile medical treatment (differentiation) and selling medical equipment for home-use (diversification).*	*The growth strategy might be complemented by offering dental services in a package with a one week holiday in China (differentiation).*	*The growth strategy might be complemented by exploiting the cost advantage of producing fertilizer with phosphate from local quarries.*	*The growth strategy might be complemented by offering 24/ 7 customer support for the tanning equipment (differentiation).*

IN-DEPTH CASE STUDY

The table 23 illustrates how the MJI team has filled in their growth strategy matrix.

Table 23: Mega Juice Industries Growth Strategy Matrix

MJI'S GROWTH STRATEGY MATRIX				
	Market penetration	**Market development**	**Product development**	**Product diversification**
Cost	The strategic emphasis is on cost to penetrate markets. MJI might boost output to reduce the production costs per litre of orange juice, and pass the savings on in the form of lower prices to the wholesale customer.	The strategic emphasis is on exploiting a cost advantage to enter new markets. MJI might attract new clients in the guesthouse segment by exploiting its cost advantage as a local producer and by offering its quality fruit juice at initially lower prices or by granting quantity discounts	The strategic emphasis is on exploiting a cost advantage to develop new products. MJI might develop a new product formula that reduces the actual fruit content in the juice while retaining the taste of freshness.	The strategic emphasis is on diversification to exploit a cost advantage. MJI might buy into a neighboring citrus plantation and produce its own oranges to cut material costs and to compete on price
Differentiation	The strategic emphasis is on market penetration by means of product differentiation. MJI could build up a brand identity for its orange juice and market it as a premium product to other five star hotels in the hotel segment	The strategic emphasis is on new market development by means of product differentiation. MJI could build up a brand identity for its orange juice and market it as premium product to wholesalers.	The strategic emphasis is on the development of new and differentiated products. MJI might set up a cosmetic product line made of orange extracts and market the product via the spas of the five star hotels.	The strategic emphasis is on product diversification with thrust on differentiation .MJI might offer day-tours for foreign tourists to spend an afternoon on a local citrus plantation for a authentic experience of rural life
Focus	The strategic emphasis is on focus to penetrate markets. MJI might increase its sales in the hotel segment by hiring out mobile orange juice bars complete with processing equipment and barkeeper for hotel functions where hotel guests can order freshly squeezed juice-to-go.	The strategic emphasis is on market development with an emphasis on focus .MJI could build up a brand identity for its orange juice, pack it in 0.25 tetra-packs customized for students and market the product via school kiosks to students.	The strategic emphasis is on product development with thrust on focus. MJI might develop a chocolate toffee with orange jam filling and market the product via the school kiosks to school children.	The strategic emphasis is on product diversification with thrust on focus. MJI might enter the retail market for farming inputs and use its supplier relationships to sell fertilizer to local orange growers.

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EXERCISE

What about your own business? Use the matrix below to brainstorm about the range of growth strategies open to your business. Take the competitive advantage of your business as a starting point and try to come up with a combination of each box in the matrix. At this stage, feel encouraged to also come up with daring combinations as long as you feel that they hold potential and that you might be able to take this option up.

Table 24: Growth Strategy Matrix Template

Market penetration	Market development	Product development	Product diversification
Cost			
Differentiation			
Focus			

CHAPTER 4:
THE PRINCIPAL FUNCTIONAL-LEVEL STRATEGIC INITIATIVES IN SUPPORT OF BUSINEES GROWTH

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This chapter will explore the strategic initiatives that your business would need to pursue in order to support the growth of your business. Key functional level strategies need to be developed in the marketing, operations, human resources as well as financing. Strategic initiatives are clusters of activities performed in pursuit of a set business objective. Strategic initiatives translate the strategy framework set by your business vision and your business objectives into action "on the shop floor", and they drive the effort to achieve the key performance indicators assigned to these objectives. The number and scope of these strategic objectives largely determines the complexity and costs of the growth effort.

4.1 The marketing initiatives in support of business growth

A strategic marketing initiative is an initiative launched by the marketing department in support of a business level strategy and to achieve a given business objective. An example of a marketing initiative in support of a distinct growth strategy is new product development. This initiative could link to an objective like "high innovation rate" that in turn could be a milestone in a growth strategy emphasizing a boost of sales by introducing new products to existing markets. To quantify and measure product innovation rate, a performance measure like "number of new products to market per year" could be chosen.

To develop new products, several interdependent activities will need to be carried out. For example, the business might organize a workshop to brainstorm about new product ideas, develop a sketch or concept of the new product idea, produce a sample of the new product and test-market the new product. The choice of activities will be determined by their relevance for the achievement of the performance indicators, their cost and their feasibility.

The link between business objectives, strategic initiatives and individual activities is illustrated figure 30.

> For more information on how to develop new products refers below under "New Product Development."

Why is it important to study the principal strategic marketing initiatives in support of business growth?

It is important to carefully screen the initiatives that can be launched by your marketing people in support of business growth because the marketing function is a key pillar to support your growth strategy. Growing your business is about boosting your sales.

Therefore, the marketing function occupies a key role in your growth drive.

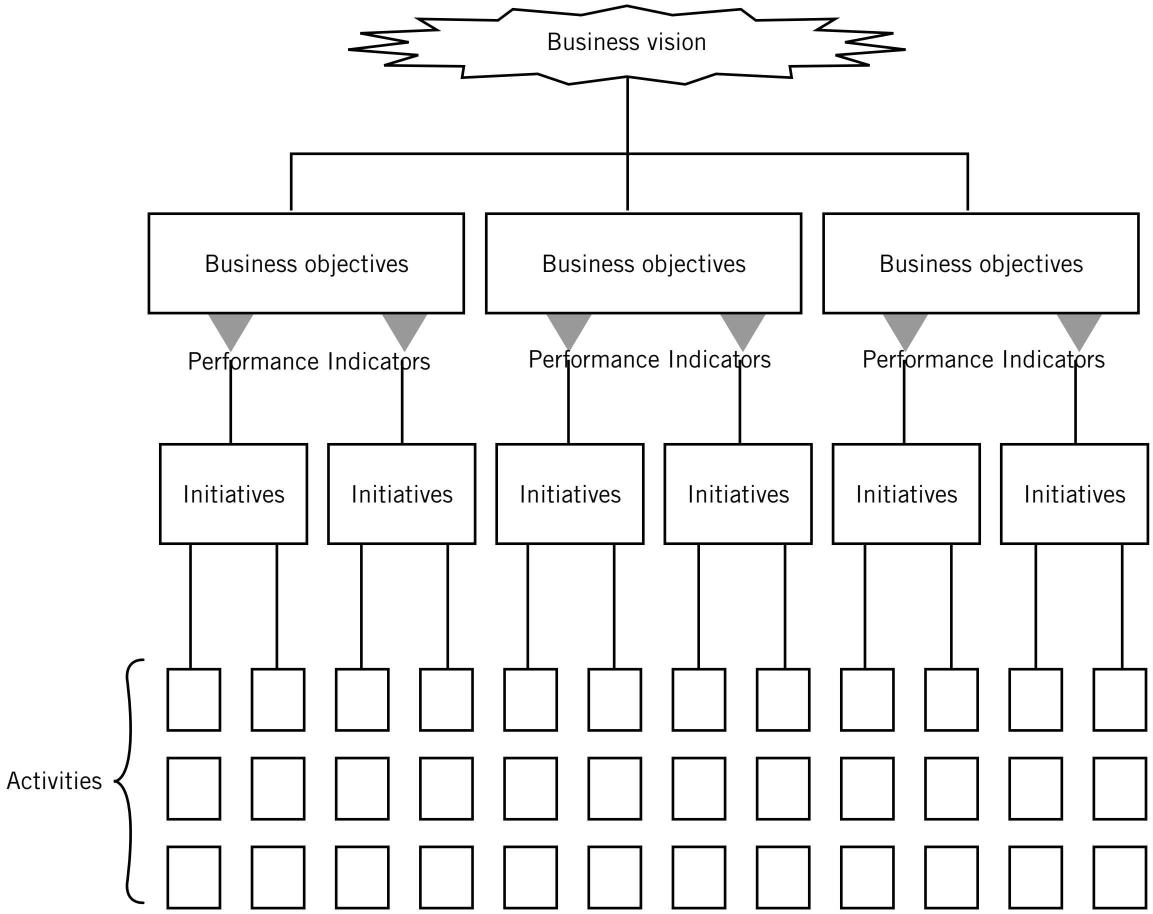

Figure 30: From vision to strategic initiatives

By assessing the pros and cons of various marketing initiatives in support of business growth you are also in a better position to choose marketing initiatives that directly contribute to the achievement of your own business objectives and yet keep the associated costs and risks under control. Furthermore, you will be able to quantify the costs of the growth strategy and to draft a timetable for its implementation for all initiatives to be performed by the marketing department.

How to study the principal strategic marketing initiatives in support of business growth

This section will review a number of marketing initiatives often launched by businesses to grow their sales. The review is not meant to exhaustively cover the range of marketing initiatives in support of business growth but serves to illustrate the implications of main growth strategies for your marketing function.

The following strategic initiatives are often launched by the marketing department in support of business growth:

1. branding
2. export marketing

3. new product development
4. related acquisition

"Branding" was chosen because this strategic initiative is relevant for most growth strategies that emphasize product differentiation or focus to boost sales in existing markets. "Export marketing" was chosen since this initiative illustrates how to reach new markets for existing products while "new product development" was chosen to illustrate how to expand sales in existing markets with new goods and services. Finally, "related acquisition" was chosen because this initiative illustrates how to enter new markets with new products.

Please note that any of these marketing initiatives also has implications for other business functions. For example, if you plan to develop new products, you will have to set up a research and development division and might have to install new production capacity – two activities falling under the responsibility of the operations department and the HRM department.

For more information on the implications of marketing initiatives launched in support of business growth on other business functions refer to chapters 3 and 4 of this manual.

1. Branding

Branding is about giving your products special characteristics to distinguish them from your competitors' offers resulting in increased sales and profits. Branding ensures that customers immediately recognize the distinctive products of your company in the market place. For example the Sony brand is associated with a certain level of quality and product performance.

Branding is a customer centered growth strategy because to succeed it requires you to first study carefully the profiles of your various market segments, and tailor your offer to the different needs and wants of these segments.

In the evolution of marketing, branding means a departure from mass marketing of generic products towards target marketing of target-specific products. Target marketing can focus on segments comprising thousands of customers, niches with hundreds of customers and even reach out for single customers.

Branding helps you to
- differentiate your products from the competition, and thus make them unique and immediately recognizable to the customers
- charge a price premium: To many customers, the uniqueness of a product is an important factor and they are ready to pay extra for it.

- build up and retain customer loyalty: If the branding effort goes hand in hand with strong concern for product quality, you will be able to retain your customers once you have attracted them to buy. Many customers stay for life with their preferred brands.

The figure 31 illustrates how to brand a product:

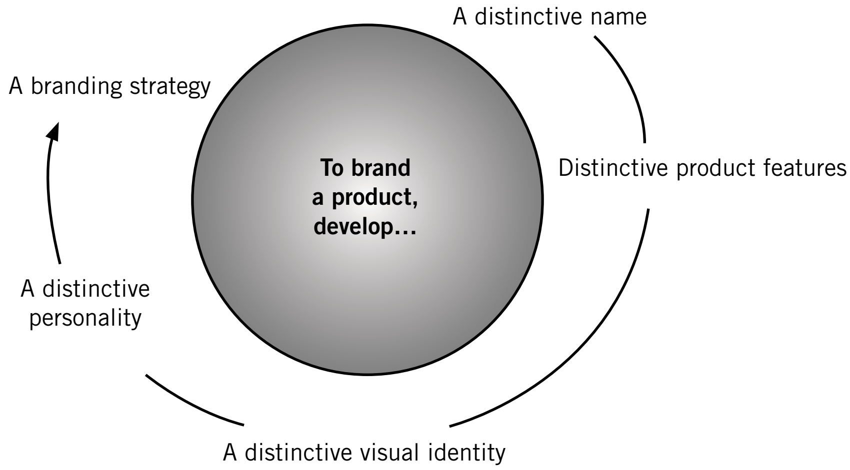

Figure 31: How to brand a product

How to brand a product

Step 1: Develop a distinctive name

The name of your product is very important. The product name determines the first impression a potential customers gets when hearing about your offer. A good name sticks to the memory of your clients. Consider the interpretation of a name by both men and women.

To develop a distinctive name, you should look for a name that
- has positive associations with the benefits and features of the product (e.g. include the words "sun", "bright" or "white" in case of detergents)
- has no associations with features that would project a poor or negative product image
- is easy to pronounce and remember
- is in a tone and language that is appreciated in the target market
- does not infringe on any other companies' brand names (particularly in cases where their name is copyright-protected).

Sometimes, it might be useful to engage a specialist firm to develop a brand name for your product. This investment can pay off quickly. In view of the possible downside costs of getting a name wrong, and the difficulties of changing it later. The risk of getting the name wrong is particularly high in export markets.

Step 2: Develop distinctive product features
Distinctive product features can be based on distinctive specifications of the physical product (including distinctive packaging) and/ or distinctive servicing processes. For example, a distinctive specification of a physical product could be a hybrid car engine running on both petrol and electricity. An example of a distinctive servicing process could be hotel pick-up service for airline passengers. What exactly makes a product distinctive will largely depend on the thrust of your growth strategy. If you emphasize differentiation, then you should put extra-emphasis on product quality, i.e. that specifications, durability, design, and packaging satisfy or exceed customer expectations. In turn, if you emphasize cost, you will need to balance quality expectations and quality costs. For example, the distinctive product feature of budget airlines is the low cost of the ticket – the quality of the service experience is a secondary buying criteria for their clients.
Step 3: Develop a distinctive visual identity
The design of a product creates a visual identity that is supposed to set off positive associations in the mind of the target customers. Here, colour and shape play a crucial role: • The subconscious mind of people associate colours with particular sensations. For example, bright reds and yellow are often associated with speed (i.e. fast food and one-hour film processing) and white is associated with purity • Distinctive shapes appeal to distinctive people. For examples, round shapes might be perceived sensual while straight and puristic shapes are usually perceived as “classic”. To achieve maximum effect, corporate visual identity should be applied consistently, i.e. not only to the product but throughout in the design and colour schemes of the retail outlets, promotional materials, uniforms and others. Logos are an important element of visual identity. The aim of a logo is to encapsulate the values of a brand and to provide an immediate reminder of the brand each time that it is seen by customers.
Step 4: Develop a distinctive personality
Brands carry not only functional attributes (see above) but also emotional attributes that appeal to the target market. Emotional attributes expressed in the design of a product are supposed to shape the psychological disposition of a customers towards the products, e.g. that they think of it as “fun”, “prestigious”, or “classic”. A brand with a distinctive personality mirrors the lifestyle of a target market, i.e. the “fun generation”, “generation X”, the “bold and beautiful”. Sometimes, brands even create lifestyles by setting new trends and fashions. Brands with distinctive personality often aim at reaffirming the self-confidence of the buyer and underline social status and prestige.

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Step 5: Develop a branding strategy

Brands can consist of more than one product. A brand name can be applied to a single product, or to a group of products, or to the entire product family.
You have a choice of three basic branding strategies:

- Development of a single strong brand: To create a single strong brand, you apply the brand name to all products supplied by your company. The main advantage of this approach is economies of scale in promotion. The main disadvantage is that it can create confusion among different target markets. For example, if your brand name is mainly associated with discount retail, you might find it difficult to market a top quality product coming at a price premium under the same label.
- Development of differentiated brands: To overcome the problems of brand confusion, you can aim at developing different brand names for each product supplied by your company. The main disadvantage is that it a costly and complex task to develop and manage a whole set of brands concurrently.
- Development of a brand family: Alternatively, you can create a brand family, i.e. groups of products of your company that are marketed under the same brand name. The advantage is that you greatly reduce the problem of brand confusion, yet keep costs and complexity level of the marketing effort under control. However, for this strategy to work, your portfolio must allow for grouping. To make a brand family work, the products in the group must be sufficiently similar to allow for the development of a consistent brand personality with a recognizable visual identity.

2. Export marketing

Export marketing means expanding the market for existing products to new markets outside your country, within the global environment. It is a market development strategy typically requiring a mix of focus strategy and differentiation strategy. Export marketing can help you to escape a growth deadlock in your existing local markets and to unlock new customer segments in less price-sensitive markets. Its main risk is that you will often lack the personal experience in operating in these new markets and do not know your prospective clients well.

Knowledge of local culture, gender differences, religion and language issues is important for the success of an export marketing strategy. For instance, there are some dressing styles for women that are not acceptable for certain communities. To develop an export market, businesses need to carry out research on the potential market and the local socio economic environment. Analytical tools and methods introduced in Chapter 2 can be used to collect and analyse information.

Challenges with collecting and analysing information from export markets include the following:

- Lack familiarity with characteristics of the potential markets, and as a result find it more difficult to source market information and to analyze their potential.
- Limited personal interaction with the prospective markets limiting updated information and impression of the social and cultural values of your customers, and the socio-economic context they are acting within.

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- Limited knowledge of competition and their competencies affecting ability of the business to assess whether your company is strong enough to face off competition from local suppliers more familiar with their domestic environment.

To adapt your offer you can choose one of the options described in table 25:

able 25: How to adapt your offer to a foreign market

Less expensice | Less customised

How to adapt your offer to a foreign market
Maintain a uniform product and promotion This strategy relies on a single marketing strategy for different markets. You keep the same product name, specification and functional and emotional attributes for all target markets, and follow the same promotional strategy. The key advantage of the approach is that your company can realize economies of scale in the production process and save on costs for promotion. Also, the product remains recognizable throughout different markets, an additional plus if your customers are physically mobile across markets and if you have created a brand identity. The key disadvantage of this strategy is that you run risk of mass marketing a "generic" product that does not satisfy the specific preferences of individual market segments. As a result, customers might either not feel attracted to try out and buy your product, or they might turn away to a substitute offer later.
Retain a uniform service formulation, but adapt promotion This strategy retains an essentially uniform product throughout different target markets, but aligns the promotional strategies to the local context. The key advantage of this strategy is that your company is able to realize economies of scale while at the same tailoring the product/ market mix more to the wants of the customers. The key disadvantage is that you still run risk of mass marketing a generic product that does not satisfy the specific preferences of individual market segments. In that case, a tailor-made promotional strategy might attract customers to try and buy the product, but it will most likely fail to retain them.
Adapt the product offer only This strategy might be applied to satisfy product standards and legislation in your new market, while retaining the brand identity. The key advantage is that it enables you to comply with market regulations while saving on costs for designing customized promotional campaigns for each market. The key disadvantage is that it might result in brand confusion or brand alienation since mobile and/ or "marketing-aware" customers might disapprove of varying product standards.
Adapt both product and promotion This strategy is applied to customize your products and promotion function to each target market. The key advantage of this strategy is that you will be in a position to make a truly tailor-made offer that meets the specific preferences of a customer group. The key disadvantage is that this strategy requires substantial upfront investment in product research and development, and necessitates designing and financing separate promotional campaigns in each market. Furthermore, the need to supply different products for each of your target markets creates challenges for the production process.

More expensice | Less customised

One radical alternative to the strategies listed above is to develop a new product altogether. New product development is described later in this chapter.

To enter the export market, you can choose from the options in table 26.

Table 26: Typology of distribution networks in export markets

Typology of product distribution networks in export markets
1 Directly sell to your new customers
If you decide you want to directly sell to your new customers, you have to set up or expand a product/ service distribution system which reaches from your company straight into to your target markets. To directly sell to your customers, you can employ salespersons that visit these customers, establish sales outlets and attract these customers to come and buy from your company, or set up an interactive website to enable customers making e-commerce transactions. The key advantage of selling directly to customers is that you maintain close interaction with your target market and thus are likely better informed about, and can react more quickly to, its needs and wants. Remember, though, that close customer interaction also means that you have to react quickly to changing needs and cannot hide behind any market intermediaries (and let them take the blame if your products are not satisfying the end customer). Poor product quality and weak customer service immediately backfire on companies selling directly to customers. The main disadvantage of selling directly to your customers is that you incur substantial costs to build up and maintain any of the distribution channels listed above (with the exception of sales from the factory gate). Furthermore, manufacturing and retailing of your products are two essentially different functions that require a different set of skills. Accordingly, it poses a double challenge for you to manage the operations of these two systems concurrently. This observation holds particularly true if you plan to develop export markets where you do not know the local environment well.
2 Sell your products through a market intermediary
If you decide you want to sell your product through a market intermediary, you have to consolidate or establish business linkages with middlemen in the product supply chain. To sell your products through a market intermediary, you have to establish/ consolidate market linkages with retailers and/ or wholesalers. Retailers buy products from you to sell them on to the final consumer, while wholesalers, buy products from you to sell them to retailers for onward distribution to the final consumer. The main difference from the perspective of your company is that wholesalers are likely going to buy your products in bulk (and bargain for quantity discounts) while retailers seek lower volumes. The key advantage of selling your products through a market intermediary (“middleman”) is cost savings. You save on building up and operating an extensive distribution system reaching out deep into the target market. This argument is particularly important when you intend developing export markets. Here, you can save substantial upfront investment if your rely on an intermediary to export your services. The intermediary carries the financial risk of product marketing and distribution in markets rather unknown to your company.

The key disadvantage is that you run risk of losing direct contact with your customers and rather aim at satisfying the requests of your market intermediaries, not the needs and wants of the end user of your products. As a result, your marketing strategy tends to be intermediary-driven, not customer-centred and it might emphasize more on low cost, and less on high quality. This risk can be particularly high if you deal with price-fighting wholesalers who aggressively bargain for quantity discounts. As a side effect, and where wholesalers are concerned, you might get over-dependent on a single business client.

Furthermore, if you decide to entrust the distribution of your products to a market intermediary, you will have to share the profit margin with that intermediary. Particularly where export markets are concerned, the intermediary will likely pocket the lion share of that profit margin, because, unlike you, they know the target market in detail, and can better assess the potential for marketing your products.

3 Invest in a subsidiary

As an alternative to selling your products through an independent intermediary, you can invest in a subsidiary, i.e. you either:

- acquire stakes in another company to utilize its distribution network, or
- set up a new company altogether to take care of production marketing and distribution.

The key advantage of investing in a subsidiary is that you retain better control over the distribution function and reap the profit margin of the intermediary. If you plan to develop export markets, a subsidiary in the target market can also help you a long way to collect and analyze the market information needed to position your products and sell them at a profit while satisfying the needs of your new customers. Furthermore, you might be able to exploit cost differentials for inputs like labor and raw materials supplied to your company in different market places. For example, you can source raw materials through your subsidiary in the target market, import and process these raw materials, then export the processed good to the target market and retain the value added.

The key disadvantage is that from a management point of view, the complexity of your business operations increases significantly. You either have to manage two businesses simultaneously in the future, or establish a third intermediate management level of factory or branch managers who work under your supervision and oversee the line managers.

Furthermore, the upfront investment to acquire a subsidiary can be substantial, particularly if you intend to develop a sunrise market that is heavily competed for by other market entrants and suppliers.

Finally, the overheads of operating the subsidiary can quickly put a severe burden on your cash flow. This concern should be carefully kept in mind if you plan developing markets with future growth potential, i.e. where it will take years, rather than months to at least reach the break-even point.

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Typology of product distribution networks in export markets continued

4 Seek a license/ franchise agreement

Another option to develop new markets is to enter into franchising or licensing agreements with selected intermediaries. Here, your company grants the right to market (sometimes also to manufacture) your products to other companies, usually tied to certain conditions and for a limited amount of time. This approach is often used by companies that have branded their products. Here, the brand becomes the unique selling proposition that attracts customers in new markets to buy from the franchisees or license holders.

The key advantage of a franchising/ licensing arrangement is that your company saves on the investment in setting up its own distribution network and might actually retain substantial income from franchising fees, while end-consumers enjoy increasingly wide access to your products through easily recognizable distribution points.

The key disadvantage is that it takes considerable effort and investment to develop a brand and to retain a uniform service formulation in different markets (cf. also above for the various tactical choices of adapting your product offer). Finally, the success or failure of your strategy largely depends on the reliability of the franchisees. Where the franchising party fails to deliver or delivers sub-standard quality, it can actually damage your brand severely, with negative ripple effects beyond the target market.

5 Set up a joint venture

A further option to develop new markets is to set up a joint venture with another company. In such a scenario, you jointly register a new legal entity tasked with manufacturing and/ or marketing your existing product.

Unlike the cases of a business subsidiary or a franchising/ licensing agreement where the main bargaining power in the business relationship rests on your side, in a joint venture the bargaining power of both sides is more balanced.

The key advantage of a joint venture is that you share risk with a business partner and can sometimes can exploit economies of scale and synergy effects. Particularly where you plan to develop export markets and enter into a joint venture with a foreign business, both sides can strongly benefit from the partnership.

Your company gains a physical representation in the export markets and access to vital market information, while your business partner gains access to an attractive product for onward sales on the domestic market – and vice versa. Both sides can exploit the full advantage of cost differentials of the respective target markets, and even share the production function beyond country borders.

The key disadvantage of a joint venture is that the parties to it will probably face the challenge of consoling different work ethics and corporate cultures. Also, the investment into a joint venture requires a long-term commitment and ties up substantial capital; joint ventures are not easily established, take time to work successfully, and are very painful to unwind.

If the joint venture fails, usually the foreign parties bear the lion-share of the costs, i.e. have to totally write of all fixed assets of the joint venture company.

6 Build strategic alliances

Yet another way of developing new markets for existing products is to build strategic alliances with other businesses. Strategic alliances are flexible arrangements relying on cooperation rather than joint ownership of a subsidiary. You enter strategic alliance to add to your competency by combining your resources with those of one or several partners.

The key advantage of a strategic alliance is that it allows you to sell on products through the existing network of your business partners – and vice versa. As a result, both sides save on costs. A good example of a strategic alliance at work is the airline industry where operators share their route networks through "code-sharing".

The key disadvantage of a strategic alliance is that it might result in brand confusion. Customers fail to distinguish your products from the products of your business partners.

3. New product development

Businesses need a flow of new products to keep their portfolios steady, their customers and sales force interested and sales growing. Developing these products is called new product development (NPD).

New product development acknowledges the fact that products go through so-called life cycles and might need to be replaced with new products at one point. The four stages of a typical product life cycle are illustrated in the graph below. As the graph shows, the main variable to determine growth and decline in the life cycle is market share.

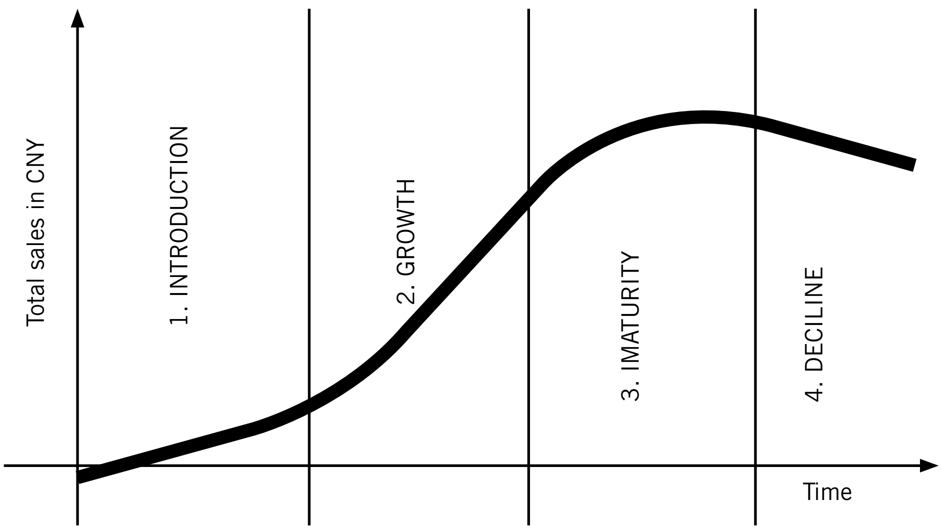

Figure 32: The four stages of the product life cycle illustrated

The lifespan of a product differs from market to market but eventually the market share of all products will decline. For example, in the fashion industry product life cycles tend to be very short. Here, fast changes in technology, customer taste, preference, and competitor's product ranges put pressure on you to adapt and modify your products from time to time, or to replace them with new products. In turn, in the music industry, product cycles can be very long – the music of some pop bands has remained popular for decades. However, even their songs are eventually forgotten or become "oldies".

To successfully develop new products, you have to decide first on the desired/required level of product newness. You have various options of product newness to choose from and all carry opportunities and risk for the planned development process.

Table 27: Levels of product newness

Higher
Level of productnewness
Lower

Levels of product newness
Entirely new to the world, i.e. new to both your business and the market. This option carries the highest risk of failure since the acceptance level of the new product is largely unknown to your company. At the same time, the potential return on investment is highest because you become the first market entrant and face no price-fighting competition.
Entirely new to your company, but not new to the world. Here, your business uses the "me too" approach and copies the successful new product of a competitor. As a latecomer to the market, you are likely facing high entry barriers. On the other hand, you do not have to bear the high product development cost of your competitors, and therefore can offer lower prices. This option can be successful when cheaper and low quality products are offered to the bottom end of the market.
An improvement of a product that is familiar to your business and to the market. Here, the product offered is not new to the market but it represents a new, upgraded product generation. Introducing a new product generation to the market is less risky than introducing a completely new product. Yet, you will have to convince customers why they should upgrade their existing products. Also, competition from other suppliers promoting their own products as mature and tested is likely to be high.
A modification of a product that is familiar to your business and to the market. Here, the core product concept is familiar but the product is given a new twist to make it more exciting. Therefore the marketing task is a little easier than the previous option and effectively means repositioning the product. The consumers can compare the new product with the old, and decide on the value of the innovation. The disadvantage of this option is that you will find it more difficult to differentiate your offer from your competitors.

Higher
Risk of failure
Lower

Once you have decided the desired/required level of product newness, you can embark on the actual new product development process. The steps of the NPD process are illustrated and explained in table 28.

Table 28: The steps of the new product development process

Idea generation	Idea screening-	Concept testing	Business analysis
Development of the physical product	Test marketing	Commercialization	Monitoring and evaluation

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Table 29: Steps in New Product Development

Steps of the NPD process
1 Idea generation
To generate ideas for new products, it is recommended that your brainstorm about the unmet needs of your customers. The customer analysis carried out in part II of this training course provides you with a wealth of information on these unmet customer needs. To initiate the brainstorming exercise, ask yourself how your business could meet these customer demands. At this stage, let your imagination roam free, and write down all ideas that come to your mind. In the brainstorming process, and to inspire your search for new products to meet these customer demands, you can also refer back to the findings of your competitor analysis (What are the product development plans of other companies?) and your market environment analysis (Extrapolating current trends, what will my customers need tomorrow and what new technologies will be available to meet these demands?).
2 Idea screening
In the second stage, all preliminary new product ideas are scanned in order to eliminate those that are inappropriate or unlikely to be successful. The objective of this screening exercise is to assess whether the ideas are within the broad strategic plans of the business. To screen your ideas, prepare a brief description of each product, e.g. specify the product benefit, how the product would complement your existing products, and what the likely market for the product would look like. Then, compare your product ideas along these parameters and rank them as “promising ideas”, “marginal ideas” or “bad ideas”. Bad ideas should be dropped at his point so that the new product development effort gets more focused.

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3 Concept testing
In the third step, promising ideas are visualized and described on paper/ computer as a sketch concept and presented to a focus group of potential customers for testing. The overall objective of the test is to assess the attractiveness of each idea to potential customers. The potential customers should be encouraged to gauge the strengths and weaknesses of each product idea presented to them on a scale from “definitely would buy” to “definitely would not buy”. Product ideas labelled as “definitely not buy” should be filtered out at this stage.
4 Business analysis
Product ideas that have survived to this stage are developed into concrete business proposals with production plans, marketing plans and financial projections. For example, you will need to estimate sales, costs, and profit projections for the new product to decide whether these projections satisfy your financial objectives. It is very important to prepare these business proposals thoroughly because beyond this stage your business will have to invest in the physical production of the new good or service, and it will have to write off this investment if the product development process is aborted. Management should be fully committed to any idea that goes beyond this stage.
5 Physical product development
At this stage, and assuming management has approved a business proposal for a new product, the actual development of the physical product is carried out. Your business will probably have to invest in research and development, equipment and staff training, or alternatively buy external product development capacity or the finished new product (e.g. under license). Furthermore, your business will have to develop pricing strategies, distribution systems and promotional tools to market the new product.
6 Test marketing
Once you have produced a beta-version of the new product, you are recommended to carry out test marketing. In test marketing, the beta-version of the product is offered on a limited time period, in a defined geographical area under conditions as realistic as possible. It is seen as a trial run for the major launch, in which all elements of the marketing effort are assessed. This gives a last chance for fine-tuning. By test marketing your new product, you will be able to find out whether the customers are actually buying the products and whether they will repeat purchase it or not. Test marketing may also show how the competitors will respond to the new product and will give you another opportunity to find out whether your product is technically mature. To avoid misunderstandings and irritations, make sure that all customers reached during the test trials are clear that they are dealing with a test product, and consider giving out product samples either for free or at discounted rates. It is essential to carefully sequence your test marketing exercise. Prolonged test marketing will give competitors a longer lead-time to respond to the national launch. A too short test market period might leave out important effects. Therefore it is essential to get the test market period just right, giving enough time for the consumers to tryout the product, to provide feedback and to develop regular purchasing patterns.

If you feel that the risk of testing the new product in your market is too big, there are alternative methods of market testing the new products: • Simulated test marketing. The product is distributed to a number of selected stores. The business will note how many consumers buy the new brand and how many buy competing brands. Free samples are distributed and consumers who do not buy the new brand, and they will be questioned about their buying habits and brand preference etc. • Controlled test marketing. Sales results are measured electronically through the checkouts of participating stores. This allows testing the impact of in-store factors and limited advertising on buying behavior. Selected consumers are interviewed to gain their impressions on the brand.
7 Full commercialization
???????our test marketing effort has been successful, and your product recipe and marketing strategies have been refined and finalized, you can go ahead and roll out the new product to the market. At this stage, you replicate your tested strategies on a large scale. The market introduction phase of a new product is a critical time in the product life cycle, because product awareness is low and product defects can quickly destroy emerging customer trust.
8 Monitoring and Evaluation
Before the new physical development of the new product gets underway, you need to establish performance indicators to measure success or failure of the NPD effort. Examples for such performance indicators could be the volume or value of targeted sales, the market share relative to competitors, or product take-up. Once the product has been launched into the market, you track its performance with the help of these indicators (monitoring). You should, furthermore, carry out performance evaluation in periodic intervals, e.g. every twelve months, to review the satisfaction of your customers with the new product in-depth. The customer feedback might then be used for the development of a second product generation, and to refine future product development efforts. The customer feedback, finally, might also become the basis for a decision to withdraw the product from the market.

Keep in mind that new products tend to fail at a very high rate. Many new products do fail even with a well-planned NPD framework. It is estimated that product line extensions fail at a rate of 33% and 80% of new industrial products fail at launch. A few reasons for new product failures:

- Poor marketing research and NPD process research.
- Technical problems in the new product design or in its production.
- Production capacity inadequate to meet the demand.
- Lack of raw material.
- Poor quality and performance.
- Insufficient differentiation from existing products. Products that did not offer any significant advantage over the competing products already in the market, e.g. in terms of lower price, better quality and design.
- Higher costs than anticipated, resulting in higher prices, resulting in lower sales volume.
- Poor timing of product introduction in relation to competitors, e.g. launching too late or too soon.

- Inadequate market analysis: misjudgement of what the market wants and overestimation of the market size; target markets could not absorb volumes needed for break-even.
- Lack of effective marketing effort.
- Not enough advertising and sales promotion.
- Poor trade distribution and no access to the market.

4. Related acquisition

Another growth strategy is to diversify operations by buying a stake in other businesses in the value chain. This is called related acquisition. Two types of related acquisition are distinguished, vertical integration and horizontal integration. Related acquisition is one strategy to build up a cost advantage and to compete on low prices for market share.

Vertical integration means that your business is acquiring a stake in a business within the value chain of its products. This can be done by either acquiring a stake in its supplier network (upstream integration) or acquiring aa stake in a buyer network (downstream integration) By way of vertical integration, you can exert better control over your material inputs (upstream integration) and/or your distribution network (downstream integration), increase your part in the value addition of a product and cut out (the margins of) the middlemen

Horizontal integration means that your business is acquiring a competing company in the market.

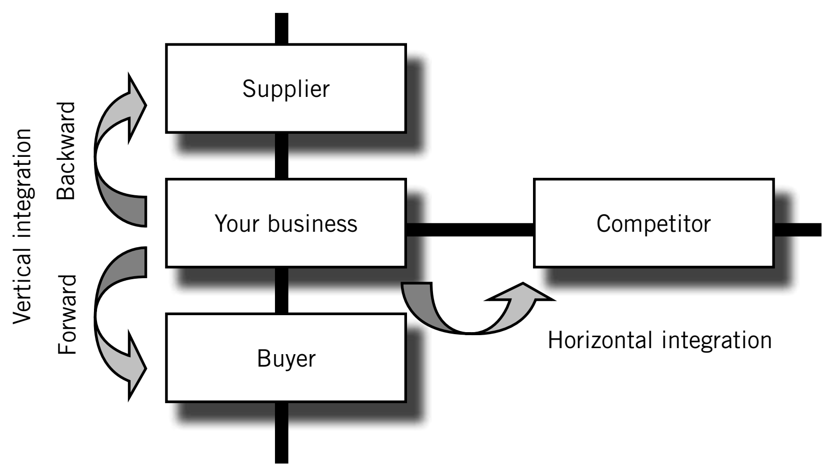

Figure 34: Types of business integration

In is important to note that product diversification by means of both vertical and horizontal integration is considered a high-risk growth strategy. Statistically, about 50% of acquisitions and mergers are not successful (refer below for reasons why many acquisitions fail). Failure in acquisition can result in loss of credibility and reputation, and it will almost always affect the financial health of your own company.

If you want to diversify your business by way of related acquisition, you need to first refer back to the results of your industry analysis and your competitor analysis. Review this market information to identify takeover candidates that enable your own company to improve its own overall competitiveness and to boost its overall sales.

> Refer to chapter 2 of this manual for more information on how to carry out an industry analysis and a competitor analysis.

When you scan the market for acquisition candidates, you should generally focus on the following criteria:

Financial performance of the takeover candidate	Potential for economies of scale	Potential for synergies
Compatibility of corporate culture	A match in core competencies	

Figure 35: Criteria for selecting takeover candidates for related acquisition

Criteria for selecting takeover candidates

1 Financial performance of the takeover candidate

The past and present finanical performance of the takeover candidate is a crucial criterion for an acquisition. You have to carefully analyze the financial health of the prospective candidate before making an acquisition decision. To that purpose, you can run a health check using the tools explained earlier, in chapter II of this manual.

The financial performance of a prospective takeover candidate can determine the prospects of an acquisition in two ways. If the financial performance of the takeover candidate is poor, it is probably easier and cheaper to acquire the company, but more costly to successfully manage it later. If the financial performance is good, it is most likely easier to run the company successfully, but more costly to acquire it.

As a rule of thumb, you should be cautious with acquisitions of heavily debt-laden companies. It requires specific expertise and time to turn around sick companies, and an unprofitable unit can quickly drain the cash flow of the parent company.

Potentially attractive takeover candidates, in turn, are healthy companies that are sold for private reasons, e.g. because there is nobody in the family to succeed the owner-manager, or because owners need money fast and decide to unload shares on the market.

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Other potentially attractive takeover candidates are companies with a severe cash flow problem but valuable fixed assets, strong "intellectual" capital (For example, in-house R&D programs, highly skilled staff), strategic distribution or supplier relations, and an established customer base. Here, buying into the company and paying off its short-term debt can be cheaper than investing in the establishment of separate units or the recruitment and training of new staff.

2 Potential for economies of scale

Scale of operation can be identified as one of the important factors affecting the cost of goods sold by an organization. As a result of acquiring another company you might be able to increase the scale of operations of your business, and as a result to bring down the unit costs of your products. For example, economies of scale might enable you to negotiate more favorable bulk purchase agreements with suppliers, to share product parts, or to access the R&D carried out by the takeover candidate.

To realize economies of scale, either the operations or the products of the takeover candidate have to be complementary to your own products and processes, either because you operate within the same value chain, or because your products use complementary distribution systems or reach the same customers.

3 Potential for synergies

Synergy refers to a phenomenon where the combined effort of two entities is producing a greater impact than the sum total of the impact generated by the two entities individually. For example, a banking institute might create synergies by acquiring an insurance company to market insurance policies alongside finance products through its country-wide branch network.

The potential for synergies is often bigger than the first look reveals. For example, it has become common in many countries to sell financial products in a local supermarket – an unthinkable combination some years back. Also, many local coffee shops attract customers by offering internet access, a seemingly unusual combination of services that successfully exploits the fact that many customers have demand for snacks and foods while surfing long hours on the internet.

4 Compatibility of corporate culture

Corporate culture refers to the formal and informal communication systems, management attitudes, values and work relationships binding people together in businesses. In some businesses people are informal and mainly output oriented while in other businesses people are more formal and strong emphasis is laid on correct administrational procedure.

For example, many of the "third wave" companies in the IT sector of the new economy pride themselves of extremely informal work relationships while in the banking sector, staff is expected to follow strict rules, down to a formal dress code.

Society plays a discrete part in forming the corporate culture of a business, by determining the mindset and expectations of employees, but there are many cases of businesses with a corporate culture that does not mirror the values of the majority – in fact, some businesses thrive on a corporate culture that is renegade and explicitly non-mainstream.

It is difficult to determine the exact nature of the corporate culture of a prospective takeover candidate and to analyze whether it is compatible with your own enterprise. Think of the corporate culture of your own business: Can you easily describe it, and would your employees agree? Corporate culture is the "soft underbelly" of a business and cannot be grasped just by reading the company rules and regulations.

Yet, it is extremely important to understand the corporate culture of the business before you make an acquisition decision because studies undertaken on worldwide acquisitions/ mergers have identified differing management attitudes/ cultures as the main reason for low performing mergers.

To grasp the corporate culture of another business, you have to spend time inside that company. You have to discuss with the management and the employees and observe the work processes. You have to study the rules and regulations and formal communication systems of the company, and how they are (not) enforced in practice. You also have to listen in to the informal communication networks of the company. People might not use the official complaint box to voice their dissatisfaction. What do they really think?

You should critically review the results of your research, and not brush aside signs for an incompatibility of corporate cultures just because the takeover prospects are otherwise excellent. Remember, great potential for economies of scale and synergies can only be realized if the employees in both companies are open for change and willing to cooperate – the very fabric of corporate culture.

5 A match in core competencies

Finally, a potential takeover candidate should possess core competencies that match, but do not duplicate, the core competencies of your own business. A core competency of a business is a capability, an asset or a skill especially well developed within the company. Core competencies of companies are in-house capabilities, assets or skills that are not mastered at the same levels by competing substitutes in the industry.

Before acquiring a company, you have to first analyze its core competencies. Second, you have to compare whether the core competencies of the takeover candidate and your own business are compatible and re-inforce each other, or whether they merely duplicate one another or are simply irrelevant for your own industry.

You should only go ahead with the acquisition if the competencies are compatible and complementary. For example, if a takeover candidate has a core competency in product development and your own company has the competency of a strong distribution network for said product, acquisition could increase the overall competitiveness of your business.

To acquire the takeover candidate, you have principally two options: You can either go for an outright purchase or buy controlling shares.

In an outright purchase, you submit a buying offer directly to the owner-managers or shareholders of the takeover candidate. Keeping in mind the ultimate goals of a business, your bid must beat the opportunity costs of capital in the financial market. For you, investing in this company must be more profitable than any alternative investment opportunity of less risk open to you. From the point of view of the takeover candidate, your offer must be more attractive to them than any financial alternative open to them.

If you buy controlling shares, you take active control over another enterprise by buying more than 50% of all shares issued by the owners. Alternatively, you can seek passive control over the business by acquiring at least 15% of all shares (of quoted companies only) and thus obtaining the right to block management decisions, if necessary by court order.

Buying controlling shares can either take the form of a hostile takeover or a friendly takeover. In a hostile takeover, you buy controlling share against the will of the board of the prospective candidate, while in a friendly takeover you buy controlling shares with its consent.

For most small-scale and medium-scale enterprises, buying controlling shares refers to other enterprises of similar or smaller size – larger scale or mega-scale share transactions on the stock exchange are typically the reserve of corporate or multinational investors. Shares of almost all small-scale ventures are transferred through private transactions without going through the stock exchange. Therefore, private negotiations play an important role for you when you want to acquire controlling shares in another business. In a hostile takeover, it is important that these negotiations are bilateral and kept confidential up to the point of purchase. In a friendly takeover, the negotiation process will be more inclusive and consensual. Whether you plan a hostile or a friendly takeover, it is always recommended that you first obtain professional advice from a lawyer or from other business people with experience on the subject in order to safeguard your investment.

IN-DEPTH CASE STUDY

The action plan on table 30 shows some of the marketing initiatives chosen by the MJI team to make their draft growth strategies actionable, and how they have specified these marketing initiatives with timelines and budget figures.

Table 30: Mega Juice Industries marketing initiatives

Growth strategy 1: Market penetration by means of cost	Corresponding marketing initiatives	Related to the following objective/indicator	Activities	By when	By whom	Budget
	Set up a market information system	**Systematic market information management** **No of new document entries in the market information database of MJI per year**	Create a market research task force	2012	Baso	–
			Procure one additional computer and upgrade internet access to broadband	2012	Baso	10,000
			Procure a market information management software	2012	Baso	5,000
			Recruit a local university graduate to collect market information and to set up and manage the database >HRM	refer to HRM plan		
			Take membership in the local business association	2013	Baso	500 p.a.
			Subscribe to specialty magazines for fruit processing companies/link up with e-market information providers	2013	Baso	1,000 p.a.
			Visit national food processing technology fairs	Each year	Baso	2,000 p.a.
	Set up a key accounts management system	**Close relationships with buyers** **High customer satisfaction** Customer satisfaction rate in % Average time spent with each business customer	Create a profile for each key account in the marketing database and continuously update these profiles	2013	Marketing assistant	–
			Assign each key account to a staff member	2012	Baso	–
			Maintain liaison with the key accounts	2012	Baso Marketing assistant	10,000 p.a.
			Evaluate key account feedback in periodic intervals	Every six months	Baso	1,000 p.a.
	Systematize community relationships	**Good community reputation** No of community projects supported by company	Carry out a community needs appraisal to identify priority needs/projects	2011	Marketing assistant	5,000
			Implement community projects	2011	Marketing assistant	20,000 p.a.
			Monitor, evaluate and document outcomes and impact	2011 onwards	Marketing assistant	1,000 p.a.
			Set up a public relations focal point in the business to maintain liaison with the community and to communicate the results of the projects	2011 onwards	Baso	5,000 p.a.

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EXERCISE

Refer back to the growth matrix introduced in chapter III of this manual and pick three growth strategies that build on the competitive advantage of your business and inspire your most. Then, use the template below to outline the marketing initiatives and related activities that you would launch in support of each shortlisted growth strategy. Also specify to which objective and which key performance indicator of your business these initiatives would relate, who would be in charge, by when you would intend to complete a given activity. Finally, provide a rough estimation of budget required to complete the activity. Feel free to expand the number of initiatives, clusters and activities for each strategy option as you deem necessary.

Table 31: Growth strategy options template

	Corresponding marketing initiatives	Related to the following objective/ indicator	Activities	By when	By whom	Budget
Growth strategy 1:	:					
	:					
	:					

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Growth strategy 2:	Corresponding marketing initiatives	Related to the following objective/ indicator	Activities	By when	By whom	Budget
	:					
	:					
	:					

Growth strategy 3:	Corresponding marketing initiatives	Related to the following objective/ indicator	Activities	By when	By whom	Budget
	:					
	:					
	:					

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4.2 The Strategic Operations initiatives in support of business growth

A strategic operations initiative is an initiative launched by the operations department in support of a business-level growth strategy.

Refer to section 4.1 for more information on the term “strategic initiative”.

For instance, a company with a growth strategy of differentiating an existing product to further penetrate existing markets might have an objective of improving product quality and a performance measure related to level of product defect rate. An operations initiative to support this growth strategy could be to introduce a 5s initiative which is a company movement that involves all employees in improving workplace organisation and cleanliness that is fundamental to quality improvement and process standardization. 5S stands for “sort”, “straighten”, ,”sweep”, “standardize”, and “self-discipline”.

Why is it important to study the principal strategic operations initiatives in support of business growth?

The operations function is one of the key pillars that support business growth strategies. It is therefore important to carefully screen the initiatives that might be launched by the operations department in support of business growth. While growing your business might be about boosting your sales, your business must also be able to increase the production of existing goods and services, or to launch the production of new goods and services, in line with the set growth targets.

How to study the principal strategic operations initiatives in support of business growth

Three principal strategic initiatives that might be launched by the operations department in support of business growth are described in the following:
1. gearing your products and production processes towards quality
2. fully utilizing existing production capacity
3. adding new production capacity.

These strategic initiatives were selected because they exemplify how to realign your business operations in support of distinct growth strategies. Gearing your products and production processes to the required quality is a strategic initiative highly relevant for any growth strategy – even in cases where the main emphasis is cost. Also, in any business growth scenario, the operations department will need to increase production output, first by fully utilizing existing capacity, but eventually by adding new capacity.

1. Gear your products and processes towards quality

The primary objective of operations is the production of goods and services that satisfy customer requirements. This can be achieved by focusing on quality. A practical definition of quality divides the subject in two parts:

1. *Quality of product* relates to how well the designed product meets the requirements of the customers.
2. *Quality of process* means how well the process of producing the goods or service manages to meet the design specifications.

Today quality has become a strategic concern because the number of competitors in each industry has increased due to globalization. Quality today has to do with global competitiveness. If a company wants to grow, quality is a key component in being competitive. Certified quality management systems are also an important basis for obtaining supplier contracts with numerous large-scale firms.

When you focus on quality you are able to produce the right products and services the first time around. As such, you will have better products and fewer defects.

Better products, in terms of meeting customer requirements, will please your customers and improve your reputation, leading to more sales and higher market shares.

Fewer defects, on the other hand, will mean higher productivity and lower costs since less production time is spent on reworking and reprocessing of defective items. Less material and labour effort are wasted on the rejected items. Finally, fewer defects reduce the risk of facing product rejections, legal measures, etc.

The following strategic initiatives to achieve quality in your business are discussed below:
- how to develop a quality culture in your business
- how to emphasize quality inputs
- how to emphasize quality processes.

Develop a quality culture in your business

To develop a quality culture and a quality work environment, you need to first define what the term "culture" actually means for your own business. A definition of culture could be that it is the shared beliefs, values, attitudes, institutions, and behaviour patterns that characterize the members of a community or organization. So, what is good for the company and for customers comes together, and becomes the driving force behind what you and everyone else do.

Development of a quality culture means having people constantly think about how to improve production as well as the quality of products and services while they work. While there are many ways to achieve this, developing a quality culture must first be rooted in management commitment. Many quality circles formed among workers did not work because supervisors did not take workers recommendations seriously or questioned their motives.

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Appropriate policies must also be put in place, such as a reduction in bureaucratic procedures and appropriate incentive systems. Training on quality provides employees with the skills to detect, solve, and prevent problems. Skills in facilitating teamwork can be provided, such as training on quality circles or on 5S (refer below for more details). Mechanisms for empowering employees are provided through quality teams or quality circles that involve workers in the improvement efforts of the company.

Value 1. We are all in this together: company, suppliers and customers

- Everybody should define the company as more than the buildings, assets, and employees. The company also includes customers and suppliers as part of the definition. It captures the point that the company's welfare is directly tied to that of its suppliers, employees, and customers.
- Encourage the development of teams and teamwork when collaboration is appropriate to execute work. In this kind of organization, people examine the tasks that need to be done.
- Managers do not just react to problems. Instead, they actively search for ways to improve all the time to reduce the possibility of problems occuring in the first place.
- Loyalty reduces the costs involved in recruiting, hiring, and training replacements. Employees recognize that it is hard to find an employer who really understands that we are all in this together, and what that means. When you care about them, they will care about you and the company.

Value 2: No subordinates or superiors allowed

- When a company culture eliminates the mentality behind superior-subordinate relationships, people more freely express what is on their minds. Of course, as with Value 1, this can only happen when you and everyone really believe that cooperation is what is most important. People have to experience this sense of cooperation. And that comes when everyone feels like a colleague and not just a cog in a machine controlled by someone else. It becomes a conscious driving force of behavior.

Value 3. Open, honest communication is vital

- Empathy has to do with actively seeing the world from the perspective of others, i.e. other members of the company, customers, suppliers, the community. It is having a sense and appreciation of their problems, their abilities, and their behaviors. It incorporates a reluctance to judge too quickly the behavior of others based on your own perspective to the exclusion of theirs.
- Listening: If you can suspend judgment and turn down the filter, you create a situation where others do the same, as they naturally imitate your behavior. This is an important way that you, as a manager, can encourage open and honest communication. The way you turn down the filter is by putting yourself in the other person's place. Then appreciate that the only way to find out what is on the mind of a colleague or a customer is to listen to him or her.

Value 4. Everyone has access to all the information they need

- Limited information means that decisions will be more speculative and thus more likely to introduce additional uncertainty into the company and its processes. Just think about when you or one of your employees made a poor decision. It probably happened because you did not have enough information. As a cultural value, everyone understands that full access to information is just the way things are at your company. Remember: You can never eliminate uncertainty in your business. However, you do not have to foster it by limiting access to information.

Value 5. Focus on processes

- Since organizations are systems that have processes for turning inputs into outputs, focus on processes is an important value. Industrial culture is however heavily oriented toward recognizing individual achievement and individual mistakes. Since about 80 to 95 percent of all production problems are due to variation in processes, it just does not make a lot of sense to blame individuals for all problems. Support this value by setting up teams and providing training and the tools needed to continuously improve these processes to everyone's benefit.

Value 6. There are no successes or failures, just learning experiences

- Failure and success are always value judgments we render after the fact. We can never predict with certainty whether what we do will end up as a success or a failure. It keeps company employees and managers from taking themselves too seriously. In other words, it keeps people open, humble, and focused on what they should care about -- figuring out how to do better and better by their customers. Further, it emphasizes a fundamental reality of our lives: We are always learning something. So it might as well be something that is for the mutual good of ourselves and our customers.

Figure 36: Values that can drive the development of a quality culture and a quality work environment in your own business

Quality products and services are produced in quality environments. The production environment includes the physical structure such as building, facilities, shop floor and layout. People are part of the environment that comprises the working conditions under which the products and services are made. You may be purchasing the right quality of raw materials and may have the right machines, but if the working environment is dirty, dangerous, and disorganized, then it will be difficult to produce quality products and services.

When the commitment and policies are well established, when employees are provided with the skills and means to participate in the company's improvement, and when the appropriate working environment is in place, then the culture of quality will begin to take root in the organization where everyone works towards the good for the company, improving its performance and simultaneously enhancing their own safety.

Emphasize quality inputs

To produce quality products, the quality of purchased raw materials and components should be according to requirements. You can avoid production defects by specifying your quality requirements to your suppliers and subcontractors.

Customers' feedback is also a good source of ideas for improvement. Make an effort to gather customers' feedback through interview and customer survey.

Emphasize quality processes

To create quality processes, you should first emphasize setting quality standards for each step of the production process. This is called standard-based quality management such as the ISO 9000 which is a series of standards agreed upon by the International Organization for Standardization (ISO) and adopted in 1987and recognised in more than 100 countries.

Standards are rules specifying how repetitive tasks at each step of the production process are to be performed to produce consistent quality. These standards will typically be documented in a process management manual, and all employees will need to be trained how to follow the methods and techniques relevant for their span of control in the operations process.

In addition to a standard-based quality management system, you can furthermore aim at striving at "continuous improvement". Continuous improvement is a management philosophy that approaches the challenge of product and process improvement as a never-ending process of achieving small wins. Continuous improvement seeks continuous improvement of machinery, materials, labour and production methods through the application of suggestions and ideas of team members.

Employee involvement and team efforts are the key ingredients to continuous improvement. You can involve your employees in continuous improvement through small group activities such as Quality Control Circles (QCC) and Employee Suggestion Systems (ESS) or use the 5S methodology.

A Quality Control Circle is a small group of workers from the same workshop established by a superior with the purpose of developing and implementing activities that would help improve quality and productivity of the company.

An Employee Suggestion System encourages employees to think and contribute their ideas in improving various aspects of the business.

Finally, 5S refers to "sort", "straighten", "sweep", "standardize", and "self-discipline", it involves all employees in improving workplace organization and cleanliness that is fundamental to quality improvement and process standardization. Employees' involvement in these activities can bring out their hidden talent and creativity and gives them a strong sense of belonging, thus enhancing their motivation to contribute more to your business.

2. Fully utilize your existing production capacity

Fully utilizing existing production capacity means bringing your level of effective capacity utilization as close as possible to the maximum operation capacity of your production system under normal conditions.

Fully utilizing the existing production capacity can help grow the business because it enables you to meet additional capacity requirements without investing in new production facilities and waiting until additional production facilities are installed. It will also enable you to make full use of your investment in existing facilities, thus increasing your return on capital investment. Fully utilizing existing production capacity can also address short-term production requirements and gives you enough time to prepare for long-term capacity requirements.
Follow these steps to fully utilize the existing production capacity:

- Determine your effective production capacity.
- Calculate your effective capacity utilization.
- Analyze the best frequence and volume of capacity increase.
- Identify productivity bottlenecks and implement productivity improvement measures.

Determine your effective production capacity

Your effective production capacity is the maximum output that can be expected from your production system under normal circumstances. Normal circumstances, here, assume operations at full capacity but taking into account holidays, machine maintenance and breakdowns and other factors typically negatively affecting productivity.

What are the 5S?
- SORT - Decide which things you need in order to accomplish your work.
- STRAIGHTEN - Decide which things you do not need to do your job and remove them. You do not need lots of files, hoards of paper, pens, etc. Just keep what you need to accomplish your job. You should be able to access everything you need to work within 30 seconds.
- SWEEP - Look at your workplace, perform maintenance of machinery. The general guidelines for sweep, suggest that this should be carried out on a weekly basis, with emphasis based on reviewing performance.
- STANDARDIZE - Apply standardized working procedures in your work place. Ensure there are standard instructions for machine operators and office staff. This is to ensure that people can do other people's work if it is needed.
- SELF DISCIPLINE - Ensure the logic of a clear and simple workplace remains and that employees understand the need for an uncluttered workplace.

How can the 5S help your company improve quality?
- Reduced accidents as a result of a cleaner and tidier environment.
- Improved employee morale as work will not be viewed as a "horrible place".
- Better inventory management on the shop floor as operators will know exactly where the tools to complete jobs are. The 5S would also mean work in progress is visible on the shop floor, which will lead to improved output, reduced lead times and better customer satisfaction.
- Visitors to your business will see a more organized environment, which can be turned into increased potential orders, and growth.

Some tips in implementing the 5S
- Set up a 5S team which explains the need for implementing the 5S in the workplace. Ensure that all supervisors and managers fully understand the logic. If the logic of the 5S is not clearly understood by the supervisors and managers responsible for implementing the 5S, then the end message received by employees could be just "a weekly/ monthly clean up". It will then be viewed as being a waste of time.
- Form 5S work groups for different sections of your business.
- Over a period of a few months get all the employees trained up in the 5S logic. This could be through the supervisors and managers.
- In an office environment you would look for a standard desk policy for all staff; differentiation between personal and business files; clean understandable notice boards; clean pantry areas; clean computers/ telephones/ fax machines; signs for fire exits/ first aid.
- In a shop floor environment you would look for clearly safe working environments; all dangerous substances under lock & key; all tools safely stored; clean notice boards; clean eating areas; machines utilizing correct safety guards; all work in progress safely transported.
- The best way to look at individual working areas is to get different employees looking at different peoples' work spaces.
- Make sure the 5S is implemented in the most suitable way to your business and ensure the process is reviewed and maintained. It will be a lengthy process at first but should become more and more reduced as all areas for improvements will become fewer.

Figure 37: 5S for higher quality in your business processes

You can determine the effective capacity of your production system by way of a simple time study. This involves:

- Calculate the cycle time per product/product batch under ideal conditions, e.g. assuming full machine load and uninterrupted and undisturbed work. For example, if it would take a bottler under ideal conditions 1 minute to produce one bottle with fizzy drink, the company would be able to produce 525,600 bottles in the course of a year.
- Add a time charge to the equation that factors in the typical production delays caused by factors beyond your control, for example, worker holidays and machine maintenance time. To derive at the time charge, add all hours in production lost in the course of a year due to these factors and divide the total by the cycle time per product. Factoring in a time charge of 30 seconds per product unit for normal production delays caused by factors like holidays and machine maintenance, the cycle time for one bottle increases to 1.5 minutes, and the effective production capacity is 350,400 bottles.

Once you know the adjusted cycle time per product then you can easily extrapolate the number of goods or services you can produce over a given time period.

The formula to calculate the effective annual production capacity of your business is illustrated below

$$\text{Effective annual production capacity} = \frac{\text{525,600 minutes or 365 days}}{\text{Cycle time in minutes/days per product under normal conditions}}$$

Calculate your effective capacity utilization

In the second step, you calculate the effective capacity utilization of your business. Effective capacity utilization is the ratio of actual output of your production system to effective capacity. It shows how close the level of production is to effective capacity.

The capacity utilization rate is expressed as a percentage and requires that the numerator and denominator be measured in the same kind of units and time periods. For example, if you run a company that bottles soft drinks in 0.5 litre bottles, you can calculate your effective capacity utilization by dividing your effective annual bottling production capacity over your actual bottle output. Assuming the effective production capacity of the company stands at 350,400 bottles, and assuming an actual output of 300,000 bottles, then the effective capacity utilization of the company stands at approximately 86%.

$$\text{Effective capacity utilization in \%} = \frac{\text{Actual output}}{\text{Effective production capacity}} \times 100$$

What is considered a high or a low effective capacity utilization ratio varies from industry to industry, and sometimes even from process to process, or machine to machine. The higher the capacity utilization ratio, the better – however, in many industries capacity utilization rates of between 50-75% are considered normal, sometimes unavoidable due to the structure of demand (which is also typically reflected in the pricing strategy as well). For example, in the tourism hotel industry, a seasonally adjusted capacity utilization of 50% is not considered problematic, as long as the hotel can achieve full capacity utilization during the high season and then earn extra from seasonal surcharges.

A low capacity utilization rate can have several reasons:

- Provided supply outstrips demand in your industry, it might mean that your production system has structural or seasonal overcapacity.
- Provided demand outstrips supply in your industry, it is a likely sign for low worker productivity, bottlenecks in your production system, and possibly a quality problem.

In the second case, and assuming growth potential for your business, you should aim at better utilizing your production capacity, starting by gearing your business towards quality products and processes, and next by setting up a productivity improvement program.

If your business has reached near full capacity utilization and still see further prospects for growth, you might consider adding new capacity to your existing production system, or setting up a new production line and or buying in additional external capacity.

Refer below for more information on how to add new capacity to your business operations.

Analyze the best frequency and volume of capacity increase

The best frequency and volume of capacity addition is relevant for any growth-oriented production management strategy, but it relates particularly to the addition of new production capacity, since this strategy carries higher risk and requires you to take more far-reaching investment decisions. In the third step, you analyze the best frequency and volume of capacity increase. The best frequency and volume of capacity additions relates to the question "how often" and "how much" you should increase your production capacity.

You have three strategic options of how and when to add new capacity to your production system in response to changing demand:

- Capacity cushion strategy through excess capacity. This strategy aims at ensuring that all demand is met at all times. It is common in some types of service organizations such as electricity distributors, fire departments, or internet service providers. The characteristics of these services are such that if the customers would not get the service at all times, they will change provider or stop using the service. This strategy is useful in the beginning of a product life cycle when a company seeks to exploit a first mover advantage. It is also useful if you want to compete on flexibility, speed, and superior service. This capacity strategy is the most risky one since you add capacity in anticipation of a higher demand.

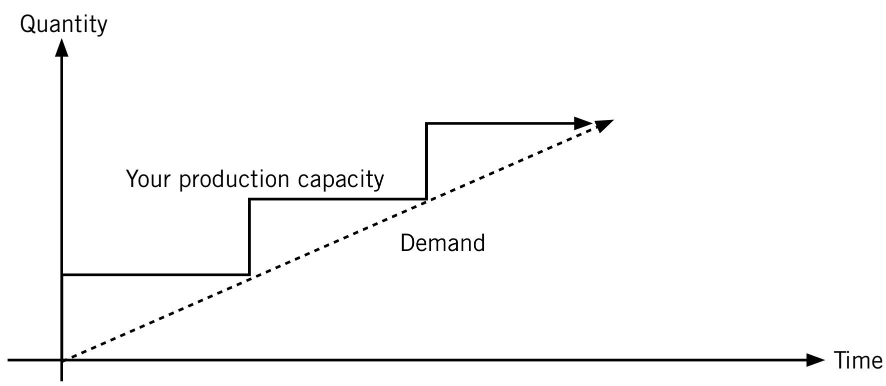

Figure 38: Capacity cushion strategy through excess capacity illustrated

- Demand cushion strategy through capacity shortage. This strategy can be used if you want to compete on price, not aim at being first to market, or work with aggressive marketing campaigns. With this strategy you will always work under full capacity utilization, and the company will be able to fully distribute its fixed costs. The danger with this strategy is that at a certain point of shortage, the backlog becomes too large, customers become dissatisfied, and you might lose customers to competitors.

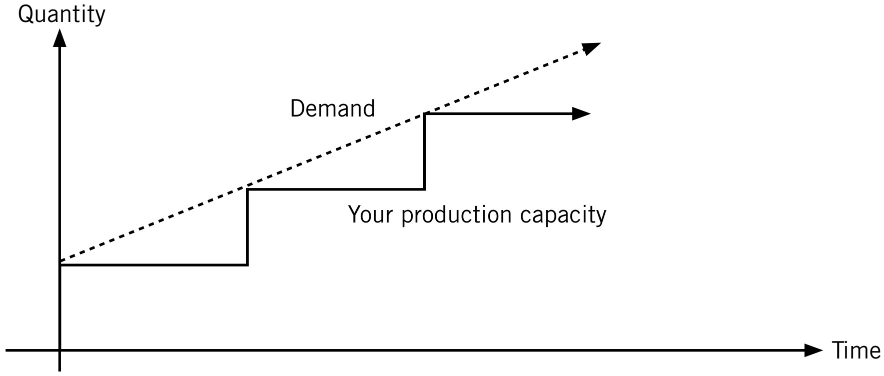

Figure 39: Demand cushion strategy through capacity shortage

- Balanced capacity strategy. The balanced capacity strategy aims at matching the capacity to near term demand. Depending on the business climate this type of strategy will result in cases of sometimes excess capacity or excess demand. This strategy is best applied in cyclical businesses where demand volatility is high or in mature industries. This strategy involves a bigger part of capacity flexibility. As a consequence these types of companies might prefer to lease rather than to own, rely on temporary employees rather than to hire permanent staff and in downturn develop complementary business to get use of their capacity.

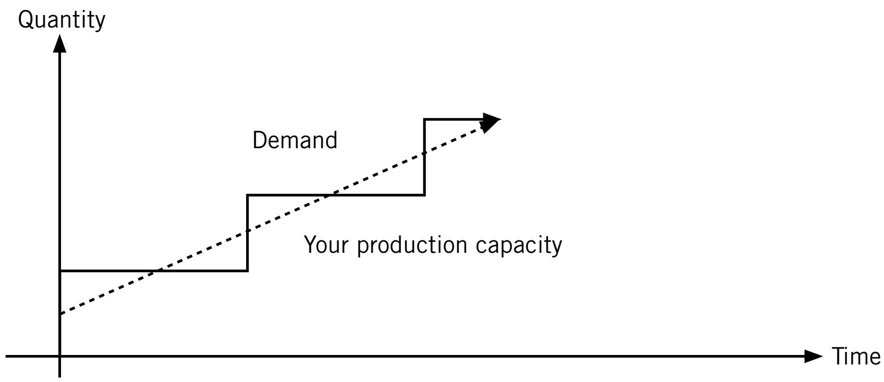

Figure 40: Balanced capacity strategy illustrated

Identify productivity bottlenecks and implement productivity improvement measures

In the fourth step, you increase your capacity utilization step by step by way of implementing productivity improvement measures. To identify intervention points for productivity improvement measures, you need to track down the "bottlenecks" in your production system.

A bottleneck in your production system is a point in the production process where workflow is sub-optimal or not following the so-called critical path. Bottlenecks can be caused by internal or external factors.

Signs for production bottlenecks are

- long queues of work-in-progress
- long delivery times
- unbalanced work flow
- any work-related accident - you should look at any production step that has caused an injury to a worker before
- idle equipment or people
- poor or inconsistent quality or high error rates

Internal factors causing production bottlenecks might be poor or inappropriate working methods, procedures or conditions that might be rectified as part of productivity improvement program.

Production bottlenecks might also be caused by external factors beyond the immediate control of the production managers, among them government regulations, union agreements, and supply capabilities.

For example, government laws or union agreements might prohibit work, during the weekends or on public holidays. Regular supply with production inputs like raw materials and power also affect production capacity utilization.

On the next page, there are examples for productivity bottlenecks often experienced by businesses along the value creation process, and suggestions for how to remove these bottlenecks.

The examples all refer to internal factors causing production bottlenecks because it is easier for a business to address them quickly. Addressing external causes of production bottlenecks requires a long-term strategy, and usually support from a business lobby. Addressing external causes of production bottlenecks is not further discussed in this manual.

3. Add new production capacity

Adding new production capacity means increasing your ability to produce existing and new products and services. This could be done both internally through investments in new production facilities, or externally through, for example, subcontracting.

Adding new production capacity can help to grow your business because it gives you the possibility to acquire the latest production technology that can give you a competitive edge over your competitors in terms of cost and/ or other product features. Additional production capacity, if used wisely, can also help you to improve your response rate and ability to accept bigger orders from your customers.

Increased production volumes will also enable you to benefit from economies of scale because as your production volume increases, the average cost per unit of output drops.

Symptom: delays in management decision making
Possible root cause: productivity bottlenecks at the management level
Examples for productivity improvement measures:
- development of a strategic plan for the business
- management staff training
- review of decision making processes and procedures
- delegation of non-core management tasks

Symptom: high employee turnover
Possible root cause: productivity bottlenecks in human resources management
Examples for productivity improvement measures:
- preparation of staff development plans
- staff training
- establishment of an employee feedback system
- improvement of work environment
- improvement of workplace safety
- increase in pay

Symptom: low innovation rate (e.g. low number of patents pending)
Possible root cause: productivity bottlenecks in R&D
Examples for productivity improvement measures:
- increase investment in R&D
- retrain existing/ recruit new R&D staff

Infrastructure (structure and leadership)

Human resources

Research and development

Materials management

Symptom: poor average lead time from order to delivery of supplies
Possible root cause: productivity bottlenecks in materials management
Examples for productivity improvement measures:
- review buying procedures
- change suppliers
- warehouse organization

Manufacturing **Marketing, sales, and service**

Possible root cause: workflow management

Examples for productivity improvement measures:
- Perform activities in parallel: Most of the steps in an operations process are performed in sequence. A serial approach results in the throughput time for the entire process being the sum of the individual steps plus transport and waiting time between steps. Using a parallel approach can reduce throughput time by as much as 80 percent.
- Change the sequence of activities: Documents and products are often transported back and forth between machines, departments, buildings, etc. If the sequence of some of these activities is altered, it may be possible to perform much of the processing at the first place.
- Reduce interruptions in the workflow: Many processes are performed with relatively large time intervals between each activity. For example purchase orders may be issued only every other day. Individuals preparing reports that result in purchase orders should be aware of deadlines to avoid missing them, because improved timing in these processes can save many days in throughput time.
- Improve plant layout and process flow: Is the current design scalable? Can it be redesigned? Is there any probability of obsolescence or inefficiencies of process and process technologies? Can you reduce the time for material handling in between processes? Can you reduce material losses and travelling time by improving layout and process flow?
- Simplify product design: Is the product/ service design and manufacturing compatible? Can capacity be improved by product/ service design modifications?
- Redesign/ change machines: Can the machines be redesigned to improve throughput? Are there other machines on the market that are better designed to handle the work tasks?

Symptom: low strike rate (sales closed/ sales contacts)
Possible root cause: productivity bottlenecks in marketing management
Examples for productivity improvement measures:
- training of sales persons
- development of new promotional materials
- establishment

Figure 41: Examples for productivity bottlenecks in the value creation process of a business, and how to remove them

This is partially due to operating and capital cost decline since a piece of equipment with twice the capacity of another piece does not cost twice as much to purchase or operate. Overhead costs such as marketing and research and development can also be distributed over a greater number of products.

Finally, your company will also benefit from the experience. The experience curve concept shows that as you produce more products you will gain experience in the best production methods, reduce your production cost and enhance your competitive advantage.

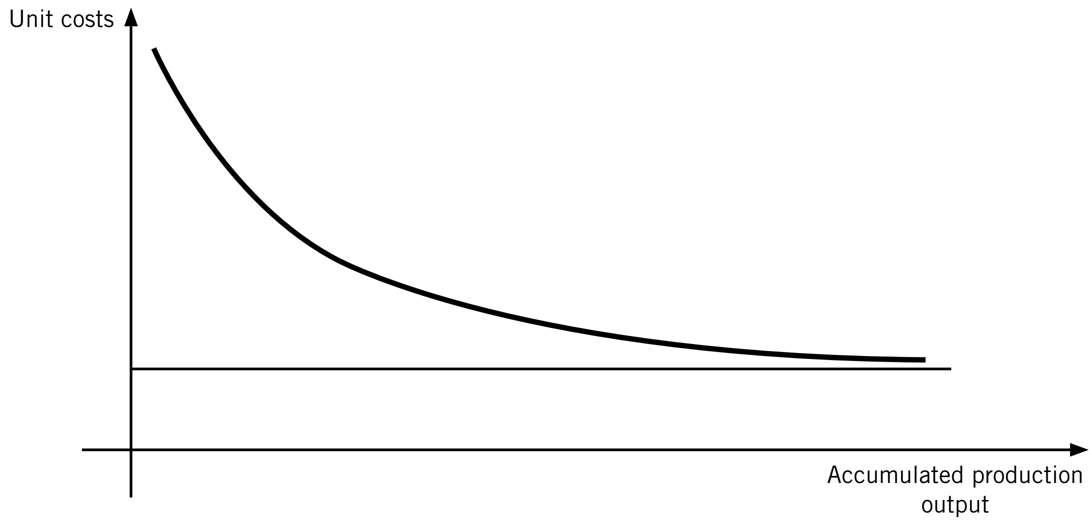

Figure 42: The experience curve illustrated

In principle you have two options if you want to add new capacity to your business. You can either
- build up additional in-house capacity, or
- buy external capacity

Build additional in-house capacity

To build additional in-house capacity, you can either add new capacity to an existing production line or alternatively add new capacity by installing a new production line.

To make an informed choice, you need to first identify whether your existing production line can still support additional capacity. For example, if you run a supermarket, adding more cash tills to boost handling capacity might upset the existing workflow, cause bottlenecks in routing customers and result in work overload for supervisors. In this case, other than procuring new equipment and recruiting new staff, you might also need to retrain the existing staff, reorganize workflows and invest in land and buildings for additional work space.

If you find out that your existing production line can still support additional capacity, you then need to quantify the total upgrading costs in terms of machines, training of personnel and investment in infrastructure. The total investment then needs to be appraised by calculating its payback period and net present value.

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> Refer to chapter 5 of this manual for more information on how to calculate the payback period and the net present value of your planned investment.

If, in turn, you decide that you should add a new production line, you need to clarify the following issues:

- Are there production synergies with the existing production line? For example slack capacity in one production line might be shared by both production lines, or unit costs might be reduced by procuring production material inputs in bulk from suppliers.
- Can the production complexity be effectively reduced as a result of the new production line? For example, you might focus on few products in each production line to reduce setup time and to achieve longer production runs.
- Is there any new technology that can be introduced in the new production line to boost output and bring down cost? If so, what would be the implications for maintenance (costs of ownership) if production lines run with different equipment?

Next, you need to determine the cost of setting up the production line, e.g. the costs of machines, fine-tuning of production facilities, machines and services processes. In the process, you also need to pay attention to the impact of the new production line on the existing support functions of your business. For example, if an airport plans to add a new runway to boost its operations capacity, the management would have to find out whether the existing airport customer and freight handling facilities can handle the increased air traffic and whether the access roads to the airport are designed for the increased car traffic. Any of these factors can drive up the costs of the expansion drive and might in fact exceed the costs of the core investment in the runway.

Finally, you need to again appraise your planned investment.

> Refer to chapter 5 of this manual for more information on how to calculate the payback period and the net present value of your planned investment.

Buy in external capacity

Alternatively to adding new in-house production capacity, you might opt for buying in external capacity. Buying in external capacity is an effective strategy in addressing immediate requirements. For example, if you run a consultancy company and you have won a tender for a project that requires expertise not held by any of your professional staff, you may decide to partially subcontract the order.

If you intend to buy in production capacity it is important to select suppliers or subcontractors with good reputation and proven achievements, or subcontractors and suppliers who are not yet fully developed but who are worthy of being developed because of their strong cooperative attitudes and attractive price quotations.

When buying in external capacity, the following factors should be given consideration to maximize production economy:

- Level of quality required. You should have clear quality standards for the subcontractors and suppliers to prevent quality errors.
- Level of synchronization required between processes. This will enable you to set the production lead-time and delivery schedules.
- Product cost. This will enable you to correctly determine the price of products or services to be outsourced. In addition to the product or service cost, you should consider transportation and material handling costs.
- Costs for inventory of raw materials, work-in-progress and finished products at the subcontractors and suppliers end.
- Capital cost of loans extended to preferred subcontractors and suppliers.
- Administrative expenses incurred in planning, administration and control.
- Expenses incurred for education and training of subcontractors and suppliers.

IN-DEPTH CASE STUDY

The table 32 illustrates operations initiatives selected by Mega Juice Industries (MJI) to make their draft growth strategies actionable.

Table 32: Mega Juice Industries draft growth strategies for operations initiatives

Growth strategy 1: Market penetration by means of cost	**Corresponding marketing initiatives**	**Related to the following objective/indicator**	**Activities**	**By when**	**By whom**	**Budget**
	Close down production line for canned pineapples	High profits Attractive returns Net Profit Margin Return on Assets	Decommission equipmen	2012	Baso	2,000
			Re-train workers to carry out fruit juice production	refer to HRM plan		
	Fully utilize existing production capacity for fruit juice	Emphasis on quality High operational efficiency Machine productivity Product reject rate	Participate in a Work Improvement in Small Enterprises seminar (WISE) to identify no-cost, low-cost productivity improvement measures	2012	Baso	1,000
			Train staff in workplace improvement	refer to HRM plan		
			Upgrade workstations and reorganize workflows	2012	Baso/ consultant?	1,000
			Develop a monitoring system to track output	2012	Baso/ consultant?	1,000
	Add new capacity to the existing production line	High profits	Forecast capacity needs	2013	Baso	–
			Carry out market research on equipment	2013	Marketing assistant	1,000
			Buy and install the equipment	2013	Baso	100,000
			Retrain current staff or recruit new workers	refer to HRM plan		

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Table 32: Mega Juice Industries draft growth strategies for operations initiatives (continue)

Growth strategy 2 Market penetration with thrust on focus	Corresponding marketing initiatives	Related to the following objective/ indicator	Activities	By when	By whom	Budget
	Close down production line for canned pineapples	High profits Attractive returns Net Profit Margin Return on Assets	De-install and sell equipment	2012	Baso	2,000
			Re-train workers to carry out fruit juice production	refer to HRM plan		
	Set up an additional mobile production line	Emphasis on quality Attractive returns High profits Product reject rate Return on Assets	Forecast capacity needs	2012	Baso	–
			Carry out market research on the mobile unit	2013	Marketing assistant?	50,000
			Buy the mobile unit	2013	Baso	1,000
			Retrain current staff or recruit new workers to operate the mobile unit	refer to HRM plan		
			Develop a quality manual for the use of the mobile unit	2013	Baso	2,000
			Test-run the new equipment prior to market introduction	2013	Baso	2,000

EXERCISE

Refer back to the three growth strategies that you have shortlisted earlier in chapter III.1 of the manual and use the template below to outline the operations initiatives and related activities that you would launch in support of each strategy. Also specify to which objective and which key performance indicator of your business these initiatives would relate, who would be in charge, by when you would intend to complete a given activity. Finally, provide a rough estimation of budget required to complete the activity. Feel free to **expand the number of initiatives, clusters and activities for each strategy option as you deem necessary**.

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Growth strategy 1:	Corresponding marketing initiatives	Related to the following objective/ indicator	Activities	By when	By whom	Budget
	:					
	:					
	:					

Growth strategy 2:	Corresponding marketing initiatives	Related to the following objective/ indicator	Activities	By when	By whom	Budget
	:					
	:					
	:					

	Corresponding marketing initiatives	Related to the following objective/ indicator	Activities	By when	By whom	Budget
Growth strategy 3:	:					
	:					
	:					

4.3 The human resources management initiatives in support of business growth

A strategic Human Resource Management (HRM) initiative is an initiative launched by the HRM department in support of a business-level growth strategy.

Refer to chapter 4. for more information on the term "strategic initiative".

An example of a strategic HRM initiative in support of a distinct growth strategy could be to develop the sales staff. This initiative could link to an objective like "highly qualified staff" that in turn could be a milestone in a growth strategy emphasizing the boost of sales by entering an export market with your existing products. To quantify and measure staff qualification, a performance measure like "% of sales staff with a foreign language diploma" could be chosen.

To develop the skills of the sales staff, several interdependent activities will need to be carried out. For example, the business might introduce a performance measurement system which is linked to staff remuneration and staff personal development plans. With the help of these development plans, identify sales staff members willing to learn a new language and to work abroad, then contract a language teacher to organize classes for the sales staff and eventually send sales staff abroad to practice the foreign language.

The choice of activities will be determined by the question to what extent each activity contributes to increased business performance measured along the performance indicator assigned to the business objective. Other selection criteria are cost and feasibility of the planned activity.

> Refer below for more information on how to develop your staff.

Why is it important to study the principal HRM initiatives in support of business growth?

It is important to carefully study the principal initiatives that can be launched by the HRM department in support of business growth because the HRM function is the third key pillar to support your growth strategy. If growing your business is about increasing production and successfully marketing your products, then somebody must perform these value creation tasks. The people who coordinate and perform the value creation activities in your business are the human resources of the enterprise - their skills, knowledge, experience and commitment are vital for business success.

How to study the principal strategic HRM initiatives in support of business growth

The principal strategic HRM initiatives in support of business growth are described below:

1. creating dynamic organizational structures
2. developing your staff
3. delegating non-core management tasks
4. creating effective work relationships

The four strategic initiatives were selected for closer description because **all** of them are vital for business growth – independent of the direction and emphasis of your growth strategy. What differs from growth strategy to growth strategy is the scope of these initiatives. For example, a new market development strategy will likely put more strain on your organizational structures than a market penetration strategy and hence requires a more substantial investment in restructuring your organization. Refer below for more details.

1. Create dynamic organizational structures

An organizational structure describes the division of labour in the organization, i.e. who performs which tasks. Organizational structures reflect both the vertical and the horizontal differentiation of the division of labour. Vertical differentiation refers to the hierarchy and authority in the organization across organizational levels, and the reporting relationships between employees. Horizontal differentiation refers to the division of labour at different organizational levels, by grouping tasks into functions/ positions and these positions into departments.

Dynamic organizational structures are organizational structures that allow for flexible integration of the division of labour, as and when need arises, i.e. in times of rapid business growth. A dynamic organizational structure is an important asset to facilitate growth. It helps your company to quickly adapt to changing conditions in times of growth and to integrate new staff and process technologies in a more flexible manner.

Follow these steps to set up more dynamic organizational structures:
- study the principal organizational structures used by businesses
- assess the pros and cons of these structures
- restructure the organization of your own business in line with your growth
- strategy

Principal organizational structures used by businesses

As illustrated in the graph below, businesses will typically have either a functional structure, a divisional structure or a combination of a functional and a divisional structure (hybrid structure).

Table 33: Typology of organizational structures

Typology of organizational structures	
Functional structure	
The functional structure is the most common way for SME to organize activities. This design groups people on the basis of similar skills or their use of the same resources. A functional structure includes those functions that are directly related to the achievement of the primary purposes of the organization, such as "finance", "personnel", "marketing and sales", "operations" and so on. Functions may be grouped in departments where combining of specialized tasks by skilled and knowledgeable employees is efficient.	
Divisional structures	
The Divisional Structure is a design that groups functions together into divisions based on the needs in the market. The market and therefore the structure may require a focus on products (illustrated above), customers, or geographic areas. Such divisions are relatively autonomous from each other and they are more dynamic than functional structures.	
Hybrid structures	
Hybrid structures, finally, combine functional and divisional organizational structures.	

Pros and Cons of different types of organizational structures

Each type of organizational structure has its advantages and disadvantages for businesses. The pros and cons of each type organizational structure are summarized in the table 34.

Table 34: Pros and cons of different types of organisational structures

Type	Pros	Cons
Functional structure	*Tested*. Most SME operate based on functional structure. *Efficient and cheap*. The clear distinction between functions allows for clear allocation of responsibilities. Focus of staff development is on building up functional expertise. *Centralized*. For the managers and supervisors this setup allows for a relatively easy control of their employees as they are grouped along common skills.	*Lack of synergies*. Due to functional split, departments tend to focus on their own activities and ignore the interrelatedness of functions in the value chain of the business. *Centralized*. There is a risk of all major decisions to be taken at the top of the hierarchy. Lower levels are passive and reactive, not active. *Rigid*. The structure does not easily support quickly shifting resources in time of business growth. Also, with increasing number and volume of tasks, co-ordination between the departments becomes ever more complex.
Divisional structure	*Customer driven*. Divisional structures with customer/ focus are client-centered not process centered. *Decentralized*. Divisional structures with geographic focus allow for localized and decentralized operations. *Autonomous*. Divisional structures with product focus have greater autonomy of operations. Primary business functions are clustered, thus facilitating smooth flow of processes in the value chain. *Synergies*. Businesses can bundle support functions like administration at the at the top of the organization and serve different customer, product and geographic structures at divisional level.	*Threat of resource duplication*. Structuring an organization by product, market or geographic divisions may result in resource duplication (for example, repeating production and sales in different divisions). *Loss of immediate control*. Organizations with divisional structures require delegation of management control from the top level to middle managers. *Costs*. Businesses with divisional structures need multi-skilled staff with more than one functional expertise, at least from the lower management level upwards.
Hybrid structure	*Balance*. Hybrid structures balance rigidity against flexibility, and efficiency against client focus.	Costs and complexity (see above).

How to realign the structures of your business to support growth

To realign the organizational setup of your business in support of growth, you need to first understand the implications of a given growth strategy for its structures. Principally, all business structures come under pressure during times of growth. Some of this pressure is "generic" and an inevitable side effect of business growth while some additional pressure is directly linked to particular growth strategies.

Growth always puts some pressure on the organizational structures of your business, independent of the chosen growth path. For example, as your business grows communication and administration will inevitably become more anonymous and you might find it increasingly difficult to directly interact with all employees. You will therefore need to reorganize the communication processes and administration procedures. This might require setting up internal communication networks like an intranet and standardizing and codifying administrative routines from filing procedures to routing slips for business correspondence.

Also, you will find it increasingly difficult to personally devote sufficient time to strategic initiatives because the complexity of your management work increases with the complexity of your business operations. (This is particularly true of growth oriented women entrepreneurs who also have additional roles in their families and communities that they are expected to fulfill.) You will need to identify key performers among your existing staff, or recruit high performing new staff, develop these employees into mid-level or line managers and delegate non-core management tasks to them

> Refer below for more information on how to delegate non-core management tasks in your business.

In addition to this generic pressure in times of growth, your organizational structures might feel the additional strain of supporting a particular growth strategy.

For example, if you intend to
- develop export markets for existing products, you might have a strong case for setting up divisional organizational structures along geographic markets
- boost your sales by focusing your growth efforts in existing markets on a particular segment of your existing customers, you will most likely need to reorganize your business by divisional structures along customer segments
- diversify your business operations, you might be challenged to integrate a separate organization with usually different structures into the existing organizational structures of your own enterprise. This integration effort might be further complicated by the fact that at least the employees working for the takeover candidate are often skeptical about the process.
- develop new and highly differentiated products, you might need to create an entirely new (R&D) function and link it firmly to both the marketing and the operations department
- divest from an existing market as part of any of the growth strategies above, you might need to close down operations of an entire unit, and redeploy its resources

In practice, as your business grows, its structure will likely move towards a hybrid setup, combining a functional structure with a divisional structure. Again, the hybrid setup needs to reflect both the direction and the emphasis of your growth strategy in order to facilitate growth. For example, if you intend to boost sales with the development of a new product targeting a niche of your current client spectrum, you will probably need to combine a divisional structure along customer segments with a functional structure that includes a separate R&D department.

If your business grows by way of diversification, you might furthermore decide to run two (hybrid) organizational structures as separate entities under the roof of a holding company. For example, if you opt for unrelated acquisition of another business to spread business risk over different markets, it might advisable to run both entities as separate organizations. The limited potential for synergies and economies of scale might not justify the risk of merging organizations with largely different background.

Whether you choose a divisional structure, a functional structure or a hybrid structure for your business, it is critical to communicate the purpose of the organizational development exercise and the details of the new organizational structure to all employees before you start the realignment. This means that each employee should know exactly where they are allocated, what is expected from them, and who their supervisors and managers will be. The buy-in of your employees in the organizational development effort is essential.

When you embark on the actual realignment exercise, seek to implement change in many small steps rather than in a single radical overhaul while clearly communicating the final target of the exercise. Radical organizational restructuring can cause substantial friction costs, like a steep decline in labor productivity while staff moves from one function to another. Also radical organizational change can uproot the business stakeholders and therefore often meets their fierce resistance. In turn, evolutionary change gives all stakeholders breathing space to get acquainted with new structures and even to grow to the occasion and to drive the change process.

Be aware that the organizational development effort is not a once-off exercise but rather a continuous process. During times of fast business growth, you will likely need to repeatedly fine-tune your organizational structures, redeploy resources and reallocate responsibilities.

2. Develop your staff

Staff development refers to the process of enabling your employees to develop their work-related skills, in line with the challenges of a quickly growing business, and to fulfil both your expectations as an employer and their personal career goals. Staff development also means giving employees the authority to participate in the decision-making process and to be responsible for their jobs.

Staff development enables your employees to acquire the skills needed to perform their jobs in a changing work environment. Staff development also enables your employees to become more productive, efficient and less resistant to change because they have more job satisfaction. In turn, your company may benefit from their talents and commitment as necessary to become successful.

Staff development, if properly done, also results in staff empowerment. Rather than devising a training program for your employees in a traditional top-down approach, modern staff development relies on the employees to design their personal development plan together with you. As a result, your employees will feel more involved an in charge of their personal development, to the benefit of your company.

Implement the following activities to develop your existing staff:
- assess the skills requirements of your business
- analyze whether the existing skills of your staff match these requirements
- develop and implement personal staff development plans

In cases where your existing staff cannot meet all skills requirements of your growing business, implement the following activities:
- recruit new staff
- subcontract external resource persons

Assess the skills requirements of your business

In the first step, you have to assess what skills are needed to carry out the various tasks in your growing enterprise. If your existing staff does not possess the skills to discharge the expected tasks, you have to either develop their skills further or recruit new staff members with matching qualification.

Your staff skills requirements depend on the planned direction and emphasis of your growth strategy. The direction and emphasis of your growth strategy, in turn, is reflected in the realigned organizational chart of your business where each box stands for a position that will have to be filled by one or several staff with certain skills.

To specify your staff skill requirements, you need to prepare a job description for each position in the organizational chart of your business. Job descriptions define employees' tasks and responsibilities, and also delineate authority. They should contain information on several aspects of a job along with the skills, knowledge and abilities required to perform the tasks.

You will find a sample job description for an accounting clerk in table 35.

Analyze whether the existing skills of your staff match these skill requirements

In the second step, you have to analyze whether the skills of your existing staff match the skill requirements of your growing business.

To find out whether your existing staff matches your staff needs, you have to compare the current job descriptions of your business employees with the new job descriptions for your growing enterprise. Any discrepancy indicates a skills gap.

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Table 35: Sample job description

Job Title: ACCOUNTING CLERK *Department/ Function: Finance/ Accounting* *Reports to: Accountant* *Reporting to job holder: -* *Main objectives:* • perform basic accounting activities. *Principal responsibilities and main tasks:* • maintenance of the general ledger • preparation of various accounting statements and financial reports *Job requirements:* • knowledge of commonly used accounting concepts, practices, and procedures • relies on instructions and pre-established guidelines to perform the functions of the job • high school diploma or equivalent • minimum 1 year of experience in the field or in a related area

If your business did not issue job descriptions in the past, list the skills required by each staff members to perform their current duties, and compare the list with the required skills specified in the new job descriptions.

The comparison does not apply to positions that are to be newly created or abolished in the realigned organizational structure. In family owned/run businesses this process can be very useful to assess the capacity of employed family to be able to contribute to growth plans and if there are skills gaps either retrain or recruit to fill those gaps.

Develop and implement staff development plans

Once you have identified the gap between the existing skills of your staff and the required skills in the realigned organization, you need to identify appropriate action for closing the gap. In a nutshell, you can train existing staff, recruit and train new staff or subcontract external resource persons to perform a given task. In practice, you will likely opt for a combination of these activities.

To train your existing staff, it is recommended that you first assist each staff member to prepare a personal development plan; this should include family members who are employees.. A personal development plan enables your staff members to understand what is expected from them in the new organizational structure, and what they can do to satisfy your expectations and secure and further their own career in the business. On your part, the plan enables you to monitor the staff development progress and to undertake timely action if a staff member is failing to close the skills gap.

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Table 36 presents a sample staff development plan for a textile worker.

Table 36: Sample of a personal staff development plan

Name:
Ms. Smithe

Position:
Machine operator

Objective of the development effort:
To enable Ms. Smithe to independently and effectively operate the sewing machines in the newly installed production line for high quality shirts.

Performance indicators and – benchmarks:
- machine breakdown time below x hours per month
- product defect rate below x units per shift
- labour productivity above x shirts per shift

My training needs and wants	**My action plan to address these needs and wants**	
	What I will do	By when
Introduction to the workflow process in the new production line	Attend group briefing and study the instruction materials	
Training in machine operation	Attend group training and study for machine operator certification	
Training in basic machine maintenance	Attend group training and study for certificate in machine maintenance	
Individual follow-up counselling in machine maintenance	Be seconded for one day to the technician in charge of fixing machine defects	
Training in occupational health and safety	Attend group training and study for certificate of attendance	

When you sit down with your staff member to complete the form, it is important that you first explain the larger picture of the planned growth effort, for example what exactly you plan to do and how it will affect your staff. Transparency is imperative to unlock the goodwill of your staff and to avoid a defensive attitude towards the planned growth effort.

Next, ask your staff members to make a self-assessment of their current skills, and to identify the skills gap by themselves – do not just confront them with the results of your own analysis.

Finally, discuss with your employees individually how to develop their skills further. Your business may offer a number of activities aimed at developing staff skills. The choice of the staff development strategy should be informed by the skill to be developed, time available as well as the learning style of the targeted staff members. Some of the forms of staff development include the following:

- **Training**: Training can be carried out by in-house staff or by external resource persons, on-the-job or away from the workplace. Training can take any form, from group training to individual training, and from in-plant training to an ex-house training course, short and modular or long-term and stretching over entire semesters. The choice of delivery method and the training curriculum will largely depend on the needs and wants of your employees, on the requirements of your business, and on your willingness and ability to invest in the human resource development effort.
- **On the Job training**: This is where a more experienced employee provides work guidance to another employee and imparts practical skills about a specific job
- **Apprenticeships/internships/secondments**: These methods involve individuals getting practical experience in a job, including on-the-job and/ or off-the-job training. The individuals earn while they learn, and immediately apply the learning theory at the workplace.
- **Exchange visits**: A method to expose employees as observers to a variety of jobs and decision-making situations.
- **Distance learning**: This method refers to off-the-job learning developed to enable individuals to study from learning materials prepared elsewhere, in their own time and at home. The most common method of distance learning is the correspondence course, in which students send their materials by post and which are returned later, marked by the teacher. Other methods of distance learning could involve computer-based training techniques, video, television, radio, etc.

Recruit new staff

To recruit new staff for a particular position, you can use the written position description as the basis for advertising the vacancy.

There are several methods of attracting potentially suitable candidates. The most common is through advertising, i.e. in the local newspapers or on the internet. Agencies or recruitment consultants can also be hired. The advertisement should contain information on the organization, the job, the qualifications and experience required the location and the action to be taken (such as sending the resume by mail or contacting the organization by phone). Interested candidates should be invited to submit their applications in writing with a cover letter and resume attached. You can ask each applicant to provide copies of references so that you can verify their paper qualifications.

Next, you should shortlist the potentially most suitable candidates and invite them for a selection interview to get a better impression of their respective personalities.

Where applicable, this personal interview might be complemented by a practical test or assessment centre, to verify the actual skills of the applicant.

The following criteria should determine your final selection:
- the match between the skills of the applicant and the skills specified in the original position description
- the personality of the applicant, and more in particular the applicant's ability to integrate into the organizational culture of your business and to interact with other employees.
- Subcontract external resource persons
- Subcontracting external resource persons is another option for your business to bring together the skills required to perform the various tasks in the realigned organizational structure of your business.

The main advantages of subcontracting external resource persons are lower payroll costs and higher flexibility: Your business can acquire highly specialized external expertise on demand and does not need to invest in building up and maintaining this expertise in-house.

The main disadvantages of subcontracting are that your business runs risk of losing its core competence in performing value creation activities. Also, your business might become over-dependent on external human resources and end up paying more for external persons than for full-time staff. Furthermore, the temporary nature of subcontracting tends to severely curtail the loyalty of the external person to your business. Finally, for your full-time employees, the latent threat of sourcing can result in low workplace morale

If you intend to outsource business activities, you should ensure that:
- you only outsource non-core value creation activities
- the outsourcing contract clearly spells out the terms of reference of the assignment
- the organization has control mechanisms in place to ensure there is no loss of important information because a resource person leaves the company

3. Delegate non-core management tasks

Delegation is the process of passing non-core tasks, responsibilities and decision-making authority to lower-level positions in the organization. Delegation is of critical importance during the growth process of your business. By delegating tasks to your subordinates, you will improve your effectiveness by setting priorities and will be able to focus on performing your essential tasks.

The inability of owner-managers to delegate tasks is one of the main causes for business failure. It is often difficult for owner-managers to delegate tasks to subordinates. The reason is that these business people started their "own" business whereby they were, right from the beginning, in charge of all activities and acted as the sole base of all knowledge. As the business grows they still want to be aware of everything that is going on within the organization and centralize the decision making power on their hands because they believe that employees do not bring in the full business-oriented experience required, neither at a managerial nor at a working level. As a result, the businesses may suffer a loss of guidance, control, co-ordinated efforts, opportunities in the market, and decreased employee morale. In addition, the owner-manager in this situation faces enormous work pressures and a lack of control on business operations and progress. The work load can also result in psychological pressure and a health risk.

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As the owner-manager of a growing business, it is important to overcome the fear of delegation and transfer some of the decision-making power and responsibilities to capable subordinates. Delegation of tasks will give you the time required to concentrate on essential business functions and important decision-making. This is particularly important in dynamic organizations where change is a continuous process. Delegation of power also assists in improving employee morale. This is caused by the increase of authority and responsibilities that are motivational factors for most employees, and in particular for high achievers.

Implement the following activities to successfully delegate tasks:
- assess your current duties and responsibilities
- delegate the functional management tasks

Assess your current duties and responsibilities

1. As the owner or manager of a small business, you typically execute tasks related to three separate but linked roles. You are:
   - an entrepreneur
   - a manager
   - a leader

Your **entrepreneurial role** comprises the core task of identifying and assessing market opportunities and, consequently, to invest in these opportunities before competitors become aware of them. This role is essential as it is related to the creation of a competitive edge and the success of the business.

Your **managerial role** relates to two sets of tasks, namely functional management and strategic management.
- Functional management is related to the day-to-day management of value adding activities in your business. Examples for functional management tasks are financial administration, production management, materials management, quality control, marketing and human resource management. Functional management tasks are typically standardized along written procedures, performed routinely and require a set of specialized and clearly prescribed functional skills. Your employees can perform these tasks provided they have acquired the required skills and accumulated some work experience.
- Strategic management, in turn, focuses on the coordination of functional business

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tasks in the value chain of a business. Strategic management requires a systemic understanding of the value chain of the business, the core competencies of the latter, and the key success factors of the industry and the environment it is operating within. Strategic management skills can be learned but require a lot of effort and the capacity to think abstract and in conceptual frameworks. Many people find it difficult to think in these abstract levels and prefer a more tangible functional task.

Your **leadership role**, finally, is related to the responsibility to drive the entire organization towards the achievement of goals, and to motivate and inspire your employees. Leadership means elaborating a vision, providing direction, providing affirmation and articulation of values, and motivating followers. Good leadership requires charisma, enthusiasm, honesty and strictness, integrity, commitment, and respect shown to subordinates.

The checklist on table 37 lines up tasks typically related to these three roles of an owner-manager of a small business. It allows you to run a quick scan of your current duties and responsibilities and to find whether you emphasize your role as entrepreneur, manager, or leader.

Table 37: Tasks typically performed by owner-mangers of SMEs

No	Do you...	Tick
1	...constantly scan the market for business opportunities?	√
2	...closely follow up on trends in the macro-environment of your business?	√
3	...personally recruit staff, carry out selection interviews?	√
4	...personally discipline staff?	√
5	...maintain networking linkages to local chambers and business associations?	√
6	...maintain two-way communication with your employees, that is instruct and listen?	√
7	...visit fairs and exhibitions, scan periodicals and newspapers for market information?	√
8	...personally carry out quality control on the factory floor?	√
9	...set business objectives?	√
10	...check all official communication coming into your business (e.g. letters, faxes)?	√
11	...reward high performers among your staff?	√
12	...maintain cordial relations with the neighbouring communities and the local religious and political leaders?	
13	...personally supervise production?	√
14	...personally oversee buying of raw materials?	√
15	...personally maintain daily records?	√

16	...define the vision and mission of your business?	√
17	...prepare strategic plans and set growth targets?	√
18	...get physically involved in the production of goods or services?	√
19	...handle the important customer contacts yourself?	√
20	...maintain sole control over the cash box?	√
21	...have a close rapport with the investment department of the local bank?	√
22	...sign off any official communication going out of your business?	√
23	...personally handle customer complaints?	√
24	...pay the bills and issue receipts?	√
25	...prepare the annual financial statements?	√
26	...prepare the annual business report?	√
27	...present the annual business report?	√
28	...reserve the sole right to take any type of investment decisions, even minor ones (e.g. to purchase a set of tools for production)?	√
29	...know the key performers among your staff by name?	√
30	...share your thoughts, ideas and concerns with these key performers?	√
31	...know how to read the financial statements of your business and use them as a basis for investment decisions?	√

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Many SMEs who complete the checklist above will find that they are heavily involved in management tasks and have limited time to perform their other roles. For example, owner-managers of small-scale enterprises typically centralize control over all functions of the business. It is not uncommon that they insist on monitoring any communication flow going in and out of the company.

Also, many small to medium scale entrepreneurs are directly involved in a wide array of functional tasks from administration to finance, production and often in sales. Because of their heavy day-to-day management workload, many of these SMEs find it hard to carry out strategic management tasks or to perform their leadership and entrepreneurial roles. They find no time to systematically analyze their industry and to prepare strategic plans.

To free capacity for performing entrepreneurship and leadership tasks, and to emphasize strategic management, growth-oriented owner-managers of small- medium scale enterprises need to delegate functional management tasks.

The key functional management tasks that you can delegate are shaded in grey in the checklist above. As far as question 28 about investment decisions is concerned, functional management refers to the right to take minor investment decision to maintain/ improve operational efficiency in a business function with a measure of financial autonomy.

Delegate the non-core management tasks

To successfully delegate these functional management tasks, you need to select adequate subordinates in your business. It is important to ensure that these subordinates are able and willing to carry out these tasks and responsibilities and are given the corresponding decision making authority. The subordinates should have the skills, capabilities, knowledge, motivation, and time required to perform the tasks.

You can refer back to the staff development sections in the previous section to assess whether the staff has the required skills or whether additional training is required. The job descriptions for the staff should match the persons executing the respective tasks. However, if none of the employees including family members would be capable of taking over these additional tasks, even after training, you will have to consider recruiting a new staff member.

Subsequently, it must be ensured that the staff teams have all the human resources, equipment, money, and information necessary to carry out these tasks.

These team members need to be effectively empowered to perform their new tasks, and, for this reason, it is important that you develop a new job description for their new positions with the inclusion of the new tasks, responsibilities, authorities, and span of control.

The time for the completion of the tasks should be planned jointly with the empowered staff teams on the basis of the overall planning along the path of the chosen growth strategy. Additionally, you should demonstrate availability to be contacted in case of problems and issues to be discussed as perceived by the employees. In contrast, minor managerial issues should be handled at the level where they belong and by those empowered.

It is very important that you continuously express confidence in your employees and ensure that you will support the outcome of their actions. You will need to exercise some patience and allow your employees to gradually build up the required technical expertise, work experience, and confidence to perform their new duties.

4. Create effective work relationships

The term work relationship refers to both formal and informal relationships between the management and the employees of a company. Effective work relationships are relationships between employers and employees that are based on a framework of transparent, fair, and even-handedly applied rules.

The development and maintenance of effective work relationships benefits both the organization and its employees. Effective work relationships build and maintain employee motivation and commitment, and help management to solve conflicts in the workplace in a fair and consistent manner.

Effective work relationships are crucial particularly for growth-oriented enterprises.

Expanding businesses go through turbulent times of change – and many employees do perceive change as a threat. Effective work relationships are the bedrock for your growth drive – providing employees with the trust needed to embrace change.

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Develop and implement a human resources management policy that directs the following activities to establish more effective work relationships:

- adoption of basic conditions of employment
- Improve occupational health and safety
- codify staff disciplinary procedures
- develop a gender equity policy.

Adopt basic conditions of employment

To adopt basic conditions of employment, you have to first familiarise yourself with the legal framework relating to employment. The mandatory basic conditions that you have to offer to your employees are a written employment contract, equal employment opportunities, and the freedom of association.

Law obliges the provision of a written employment contract to each of your employees. The employment contract establishes a relationship that binds both employees and employer. A labour contract usually includes:

- duration of the contract
- job description
- labour protection and working conditions
- salary and wage of the position
- rules on discipline
- rules on termination
- obligations and rules on breach of contract
- other clauses other than compulsory clauses in the labour contract

You should seek the services of a lawyer to draw a standard contract form in line with the labour law and other applicable legislation. This way, you can avoid legal complications in case of a labour dispute.

Equal employment opportunity refers to the rights of workers to be equally employed, to choose jobs, to obtain equal pay for work of equal value, to take leave, to be provided with safe and health protecting appliances, to receive vocational training, to be provided with social security and benefits, to seek arbitration in labour disputes, and to enjoy other rights stipulated by laws and stipulations. This equality includes taking into account the reproductive role of women through maternity protection.

You and your management team must also recognize and respect labour rights represented by the trade union. Workers have the right to establish and participate in a trade union. A trade union represents and protects the legal rights of workers, and organizes activities independently by law. Workers, in accordance with the law, are to be involved in management of the enterprise in democratic way, or to negotiate with employers in terms of legal rights protection of workers, through convening of workers plenary meetings, worker representatives meetings or other format. Therefore, you should keep constructive dialogue with the trade union and consider their needs and requirements in dealing with the working relationship with all employees.

In addition to the mandatory employee benefits, you are also encouraged to consider providing optional benefits to your employees. These enhancing services, while not required by law, can greatly improve the work motivation of your employees and result in higher labour productivity. Higher labour productivity translates into reduced costs and ultimately in higher income for your business – thus balancing off the expenditure of providing these optional benefits.

Optional employee benefits comprise, among others,

- pension schemes at business level
- medical aid insurance schemes
- transport for employees to and from the company
- incentive payments for high performers
- training, exposure visits, and other personal skills development opportunities (refer to the chapter develop your staff for further details).

Improve occupational health and safety

It is very important that your organization provides a healthy and safe workplace to your employees. Health refers to a general state of physical, mental, and emotional well-being. Safety refers to protecting the physical well-being of people.

Occupational health and safety programs aim at maintaining the overall well-being of employees by way of preventing work-related injuries and accidents.

To work out enterprise policies on safety and occupational health, you should first study the Labour Laws, Occupational Safety and Health Laws, and other related regulations in your country as well as the Environmental Protection Laws.

These laws could address issues such as:

- Workers compensation: Specifying who shall pay how much under what condition to compensate workers for injuries occurred during work.
- Protection of female workers and workers under the age of 18.
- Occupational health and safety: The Occupational Health and Safety Laws provide general stipulations related to safety and occupational health in the workplace. Please review whether there is any clause in the law relevant to your industry.
- Environment: The Environmental Protection Laws mainly deal with disposal of hazardous articles.
- Discrimination in employment and occupation: making negative distinctions in the workplace based on race and/or colour; sex discrimination; religious discrimination;

discrimination based on political opinion; national extraction; social origin age; HIV/AIDS status: disability: sexual orientation: workers with family responsibilities: trade union membership or activities are often outlawed in labour laws.

For more information on these laws, you are recommended to contact the local Labour Relations Office, the Environmental Protection Authority, your Employer's Organisation and your sectoral business associations.

Within the legal framework provided by these laws, you are encouraged to write down a health and safety policy for your business. Your occupational health and safety policy should cover at least the following areas:

- the assessment and successive elimination of occupational hazards in your production processes, e.g. the substitution of toxic chemicals with environmentally friendly substances
- the restriction of access to hazardous areas
- the use of warning systems, such as signs, instructions, and labels
- the clear demarcation of traffic ways and exits
- the procurement of first aid boxes and the training of selected staff in first aid
- the procurement and installation of fire extinguishers, and the training of your staff in a basic fire emergency drill
- the provision of personal protective clothing to all employees exposed to the risk of occupational hazards

Workplaces that are classified as potentially highly hazardous are, among others:

- manufacturing or storing explosives
- driving a motor vehicle and being an outside helper
- mining
- logging and saw milling
- using power driven woodworking machines
- exposure to radioactive substances and to ionizing radiation
- operating power driven, metal-forming, punching, and shearing machines
- slaughtering or meat packing or rendering
- using power driven bakery machines
- operating power driven paper products machines
- manufacturing brick, tile, and related products
- using power driven circular saws, and guillotine shears
- wrecking, demolition and ship-breaking operations
- roofing operations
- excavation operations

The list above shows that mining, construction and manufacturing are among the most accident-prone industries. Keep in mind, though, that occupation health and safety is not limited to these high-risk workplaces.

Occupational health and safety starts with slippery-safe staircases, ergonomic computer chairs, a first aid box in the office, a fire extinguisher on the wall, and the demarcation of emergency exits. As such, basic occupational health and safety procedures apply to any type of business, from a video rental store to a shipyard.

When you have formulated your occupational health and safety policy, you should write down the rules in a manual and distribute it to all employees. The main principles or golden rules of your occupational health and safety policy should be displayed on posters at clearly visible places in your company.

To implement your occupational health and safety policy, you need to train your staff. A continuous program of education and training on safe working habits and methods of avoiding accidents is highly recommended for this purpose.

You might also want to train one of your staff as an occupational safety and health inspector, to oversee the implementation of, and the respect for, your occupational health and safety policy.

Gender policy

It is important for your business to institutionalize gender concerns at different levels, decision making level, employee level, customer level and the community at large. Increasingly the business case for gender diversity in enterprises has become impossible to ignore for business who wish to grow sustainably. To be able to do this, businesses need to identify their strategic gender needs for growth and document the business response through a gender policy. The policy needs to address issues of:

- Staffing: This relates to proportion of women your business will target for employment at managerial and other technical levels.
- **Career Development**: Allowing women access to career development opportunities and take up non-traditional employment positions in the business.
- **Improving team work**: Educating and informing all workers on the importance of gender mainstreaming and company policies

HIV/AIDS and Growth Oriented Businesses

Most businesses today are faced by the multiple threats caused by HIV and AIDS on their businesses. The impact manifests itself in two main ways; factors that cause declining productivity arising from increased absenteeism due to illness or attending funerals, loss of skills due to death and increased staff turnover. There are also factors that lead to increased costs because of increased funeral covers, payment of retirement benefits to sick employees, contribution towards medical insurance and funeral expenses to employees or members of their families. These two factors combined impact negatively on the profitability of the business and therefore its ability to reinvest for expansion. In the end, the business will be unable to grow.

In order to guide the implementation of policies and programmes in the world of work, the International Labour Organization (ILO) has developed the Code of Conduct on

HIV and AIDS in the World of Work. The code has ten (10) principles that should guide small and medium enterprises, including GOWEs in developing and implementing HIV and AIDS workplace programmes. The ten principles are summarized below;

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1. Recognition of HIV/AIDS as a workplace issue

HIV/AIDS is a workplace issue, and should be treated like any other serious illness / condition in the workplace. This is necessary not only because it affects the workforce, but also because the workplace, being part of the local community, has a role to play in the wider struggle to limit the spread and effects of the epidemic.

2. Non-discrimination

In the spirit of decent work and respect for the human rights and dignity of persons infected or affected by HIV/AIDS, there should be no discrimination against workers on the basis of real or perceived HIV status. Discrimination and stigmatization of people living with HIV/AIDS inhibits efforts aimed at promoting HIV/AIDS prevention.

3. Gender equality

The gender dimensions of HIV/AIDS should be recognized. Women are more likely to become infected and are more often adversely affected by the HIV/AIDS epidemic than men due to biological, socio-cultural and economic reasons. The greater the gender discrimination in societies and the lower the position of women, the more negatively they are affected by HIV. Therefore, more equal gender relations and the empowerment of women are vital to successfully prevent the spread of HIV infection and enable women to cope with HIV/AIDS.

4. Healthy work environment

The work environment should be healthy and safe, so far as is practicable, for all concerned parties, in order to prevent transmission of HIV, in accordance with the provisions of the Occupational Safety and Health Convention, 1981 (No. 155). A healthy work environment facilitates optimal physical and mental health in relation to work and adaptation of work to the capabilities of workers in light of their state of physical and mental health.

5. Social dialogue

The successful implementation of an HIV/AIDS policy and programme requires cooperation and trust between employers, workers and their representatives and government, where appropriate, with the active involvement of workers infected and affected by HIV/AIDS.

6. Screening for purposes of exclusion from employment or work processes

HIV/AIDS screening should not be required of job applicants or persons in employment.

7. Confidentiality

There is no justification for asking job applicants or workers to disclose HIV-related personal information. Nor should co-workers be obliged to reveal such personal

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information about fellow workers. Access to personal data relating to a worker's HIV status should be bound by the rules of confidentiality consistent with the ILO's code of practice on the protection of workers' personal data, 1997.

8. Continuation of employment relationship
HIV infection is not a cause for termination of employment. As with many other conditions, persons with HIV-related illnesses should be able to work for as long as medically fit in available, appropriate work.

9. Prevention
HIV infection is preventable. Prevention of all means of transmission can be achieved through a variety of strategies which are appropriately targeted to national conditions and which are culturally sensitive. Prevention can be furthered through changes in behaviour, knowledge, treatment and the creation of a non-discriminatory environment. The social partners are in a unique position to promote prevention efforts particularly in relation to changing attitudes and behaviours through the provision of information and education, and in addressing socio-economic factors.

10. Care and support
Solidarity, care and support should guide the response to HIV/AIDS in the world of work. All workers, including workers with HIV, are entitled to affordable health services. There should be no discrimination against them and their dependants in access to and receipt of benefits from statutory social security programmes and occupational schemes.

Codify staff disciplinary procedures

Staff discipline refers to the adherence of employees (of any rank!) to set organizational rules. Staff disciplinary procedures codify the just cause and due process for disciplinary action.

A just cause constitutes the reason for disciplinary action while due process establishes the fairness of the means used to determine employee wrongdoing and/ or disciplinary measures. Due process also entails the opportunity for individuals to explain and defend their action.

Frequently quoted reasons or just causes for disciplinary action against employees or employers are:

• Discrimination	• negligent evaluation
• sexual harassment	• wrongful discipline (e.g. substance abuse or theft)
• wrongful termination	• deprivation of career opportunity
• breach of employment contract	• infliction of emotional distress
• failure to employ or promote	• improper management of employee benefits
• constructive discharge, in cases where an employer deliberately makes conditions intolerable in an attempt to get an employee to quit.	

To ensure due process, businesses should codify

- the just causes for disciplinary action in your standard employment contract, or alternatively incorporate the list in the written disciplinary policy of your company
- the procedure for disciplinary action initiated by either the employer or the employee, e.g. the steps to be followed by the employer in case of wrongful discipline of an employee, but also the steps to be followed by the employee to register work-related grievances
- what is considered legitimate evidence of guilt (physical evidence and/ or eyewitness accounts?)
- reasonable penalties for each just cause of disciplinary action, in case of minor offences preferably on an gliding scale, from a mere warning for first time offenders up to contract termination for repeat offenders

It is imperative that the investigation of breach of discipline is fair, transparent, and even-handedly applicable to all employees, from the management staff to the security guard.

Whether or not your employees will judge the disciplinary action to be justified and fair will also depend on how your company has handled precedents, on whether a complainant was retaliated against after a given case, on whether the decisions were made based on facts, and finally on whether the actions and processes were viewed as "fair" by outside parties.

A just cause must not automatically result in disciplinary action. More and more companies look to alternative means of ensuring that due process occurs in cases involving employee rights.

Alternative dispute resolution methods such as arbitration, peer review panels and an ombudsman can administer justice regarding breaches of discipline without resorting to disciplinary action or lawsuits.

Arbitration means that a third party is called in to decide the case between two employees, or an employee and the employer, after a hearing of all sides. Peer review panels are internal employee committees acting as an appeal institution.

A peer review panel composed of employees hears appeals from disciplined employees and makes recommendations or decisions. Panel members are typically specially trained group of volunteers and sign confidentiality agreements, after which the company empowers them to hear appeals. An ombudsman, finally, is a person outside the normal chain of command who acts as a problem solver for both management and employees.
Both employer and employee have to agree beforehand whether or not to accept alternative dispute resolution methods – preferably making these mechanisms part of a separate clause in the employment contract.

You should consult with a lawyer before introducing any of these methods into your standard contracts, and you need to carefully brief your employees on the clause. The

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upfront consent is important because the resort to alternative dispute resolution methods might mean that an employee is barred from taking his or her case to a labor court later.

International Labour Standards

Because of its broad mandate to promote social justice, the ILO has always been concerned with equal opportunities. This concern has entailed measures such as the adoption of several international labour standards to redress inequalities at work. Some of these instruments, which enshrine the principle of non-discrimination, cover all workers while others address narrower categories of workers.

The following two Conventions are the core conveyers of the fundamental principle of non-discrimination:

- ILO Convention No. 111 on Discrimination (Employment and Occupation) (and Recommendation No. 111), which aims at eliminating discrimination in employment, regardless of the grounds on which it is based or the forms it takes;
- ILO Convention No. 100 on Equal Remuneration (and Recommendation No. 90), which enshrines the principle of equal pay for work of equal value by men and women.

Other Conventions which are important for the elimination of discrimination in employment and occupation include:

- ILO Convention No. 156 on Workers with Family Responsibilities (and Recommendation 165), which addresses equality of opportunity for workers with family responsibilities and, amongst such workers, equal treatment for men and women;
- ILO Convention No. 183 on Maternity Protection (and Recommendation 191), which deals with protection of women workers during and after pregnancy, entitlements they should receive, and protection of their employment.

The above instruments provide guidelines and standards that member states freely decide to follow in order to make sure that equal opportunities are afforded to workers and that no discrimination takes place at work.

The ILO Declaration on Fundamental Principles and Rights at Work is another instrument adopted by the International Labour Conference which is important in the field of non-discrimination. This Declaration aims to reconcile the desire to stimulate national efforts towards social progress with economic progress and the need to respect the diversity of circumstances, possibilities and preferences of individual countries. It identifies four fundamental principles and rights, among them non-discrimination. It seeks to promote their universal recognition and application, and entrusts the ILO with a duty to assist ILO member states in implementing these principles.

An array of other tools developed by the ILO, such as its Decent Work Agenda, gender mainstreaming and gender audits, complement its action for equality through technical cooperation activities.

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Using the above documents and other international tools and instruments for the promotion of women's rights and non-discrimination (such as the Convention on the Elimination of All Forms of Discrimination Against Women (CEDAW) and other regional models) this programme seeks to give sound, appropriate information to people who work on equal opportunities, non-discrimination and the improvement of the status of women at national level. Sessions covering freedom of association, collective bargaining and migration will provide participants with tools for action at national level.

Local labour standards and instruments developed in the context of the above need to be taken into account as in the end they lead to more productive and more motivated workforce.

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The table 38 shows some of the HRM initiatives selected by the MJI team to make their draft growth strategies actionable.

Table 38: Mega Juice Industries growth strategy human resources management initiatives

Growth strategy 1: Market penetration by means of cost	**Corresponding marketing initiatives**	**Related to the following objective/indicator**	**Activities**	**By when**	**By whom**	**Budget**
	Close down production line for canned pineapples	High profits Attractive returns Net Profit Margin Return on Assets	Decommission equipmen	2012	Baso	2,000
			Re-train workers to carry out fruit juice production	refer to HRM plan		
	Fully utilize existing production capacity for fruit juice	Emphasis on quality High operational efficiency Machine productivity Product reject rate	Participate in a Work Improvement in Small Enterprises seminar (WISE) to identify no-cost, low-cost productivity improvement measures	2012	Baso	1,000
			Train staff in workplace improvement	refer to HRM plan		
			Upgrade workstations and reorganize workflows	2012	Baso/ consultant?	1,000
			Develop a monitoring system to track output	2012	Baso/ consultant?	1,000
	Add new capacity to the existing production line	High profits	Forecast capacity needs	2013	Baso	–
			Carry out market research on equipment	2013	Marketing assistant	1,000
			Buy and install the equipment	2013	Baso	100,000
			Retrain current staff or recruit new workers	refer to HRM plan		

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Table 38: Mega Juice Industries growth strategy human resources management initiatives

Growth strategy 2 Market penetration with thrust on focus	Corresponding marketing initiatives	Related to the following objective/ indicator	Activities	By when	By whom	Budget
	Close down production line for canned pineapples	High profits Attractive returns Net Profit Margin Return on Assets	De-install and sell equipment	2012	Baso	2,000
			Re-train workers to carry out fruit juice production	refer to HRM plan		
	Set up an additional mobile production line	Emphasis on quality Attractive returns High profits Product reject rate Return on Assets	Forecast capacity needs	2012	Baso	–
			Carry out market research on the mobile unit	2013	Marketing assistant?	50,000
			Buy the mobile unit	2013	Baso	1,000
			Retrain current staff or recruit new workers to operate the mobile unit	refer to HRM plan		
			Develop a quality manual for the use of the mobile unit	2013	Baso	2,000
			Test-run the new equipment prior to market introduction	2013	Baso	2,000

EXERCISE

Refer back to the three draft growth strategies that you picked earlier in chapter 3 of this manual, and use the template below to outline the HRM initiatives and related activities that you would launch in support of each shortlisted growth strategy. Also specify to which objective and which key performance indicator of your business these initiatives would relate, who would be in charge, by when you would intend to complete a given activity. Finally, provide a rough estimation of budget required to complete the activity. Feel free to **expand the number of initiatives, clusters and activities for each strategy option as you deem necessary**.

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Growth strategy 1:	Corresponding marketing initiatives	Related to the following objective/ indicator	Activities	By when	By whom	Budget
	:					
	:					
	:					

Growth strategy 2:	Corresponding marketing initiatives	Related to the following objective/ indicator	Activities	By when	By whom	Budget
	:					
	:					
	:					

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	Corresponding marketing initiatives	Related to the following objective/ indicator	Activities	By when	By whom	Budget
Growth strategy 3:	:					
	:					
	:					

CHAPTER 5: SELECTING THE RIGHT GROWTH SRATEGY FOR YOUR BUSINESS

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This chapter will assist you to select a growth strategy that is inline with your vision and builds on the competitive advantage of your business. The right growth strategy for your business will have the following features:

- Congruence with your business vision and your financial and non-financial business objectives.
- Builds on the competitive advantage of your business – it turns your competitive advantage into the spearhead of your growth effort.
- Allows you to pursue your business goals while exposing your business to moderate risks
- Allows your business to build up provisions for, and respond flexibly to, unforeseen events along the strategy implementation path.

5.1 Why is it important to select the right growth strategy?

It is important to get the selection of a growth strategy right to ensure that your various strategic initiatives actually contribute to the achievement of your business objectives and ultimately your business vision.

It is also important to get the selection of your growth strategy right to ensure efficient resource allocation in the strategy implementation process. If your strategy is incongruent with your business objectives, your strategic initiatives might steer off target, and you might need to re-plan activities and redeploy your resources during the strategy implementation process. As a direct result, the costs and time duration of the growth effort will increase.

Selecting the right growth strategy enables your business to control the inevitable risks related to its implementation. Strategy is about planned action to achieve set targets in an uncertain future, and it needs to take these uncertainties into account. Many good strategies have failed because of events beyond the control of the strategy designer. You cannot avoid these “inevitable surprises” but you can at least prepare your business for many eventualities.

5.2 How to select the right growth strategy

Follow these steps to select the right growth strategy for your own business:

1. consolidate the action plan for each growth strategy
2. carry out a technical appraisal of each strategy
3. carry out a financial appraisal of each strategy
4. compare the results of your appraisals and choose the strategy that suits your business best.

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1. Consolidate the action plans for each growth strategy

In the first step, you need to refer back to the action plans that you have drafted earlier for the marketing department, the operations department, and the HRM department.

Now you need to consolidate these action plans by pulling together the initiatives belonging to the same growth strategy. More in particular, you need to synchronize the activities to be launched in each business function in support of a given growth strategy.

At this stage, you might also complement these action plans with additional activities related to other business functions. For example, you might decide to add an activity related to procurement policies or materials management.

IN-DEPTH CASE STUDY

Review Mega Juice Industries (MJI) consolidated action plan for strategy 1 in table 39 on the next page.

EXERCISE

Follow the example of MJI to consolidate your action plans for each shortlisted growth strategy.

2. Carry out a technical appraisal of each strategy

In the second step, you carry out a technical appraisal of each shortlisted strategy.
You should appraise each strategy against two criteria:

- strategic fit
- risk exposure

Strategic fit

The term "strategic fit" refers to the match between your business vision and the thrust and direction of your growth strategy. At this advanced stage of strategy development, it can be assumed that all shortlisted growth strategies and corresponding strategic initiatives are at least broadly in line with your business vision, but the extent of congruence will likely differ. Some scenarios might fully match your vision, while other scenarios might "bend" the frame of mind.

To screen the strategic fit of your shortlisted growth strategies, refer back to the consolidated draft action plans for each shortlisted growth strategy developed earlier. Ask yourself to what extent each growth strategy meets your business vision and rank them according to your findings. Each growth strategy should be scored on a scale from 1-5 where one marks "poor strategic fit" and 5 marks "very strong fit".

Table 39: Consolidated Growth Strategy for MJI

Growth strategy 1: Market penetration by means of cost	Corresponding marketing initiatives	Related to the following objective/indicator	Activities	By when	By whom	Budget
	Set up a market information system	**Systematic market information management** No of new document entries in the market information database of MJI per year	Create a market research task force	2012	Baso	–
			Procure one additional computer and upgrade internet access to broadband	2012	Baso	10,000
			Procure a market information management software	2012	Baso	5,000
			Recruit a local university graduate to collect market information and to set up and manage the database >HRM	refer to HRM plan		
			Take membership in the local business association	2012	Baso	500 p.a.
			Subscribe to specialty magazines for fruit processing companies/link up with e-market information providers	2012	Baso	1,000 p.a.
			Visit national food processing technology fairs	Each year	Baso	2,000 p.a.
	Set up a key accounts management system	**Close relationships with buyers** **High customer satisfaction** Customer satisfaction rate in % Average time spent with each business customer	Create a profile for each key account in the marketing database and continuously update these profiles	2012	Marketing assistant	–
			Assign each key account to a staff member	2012	Baso	–
			Maintain liaison with the key accounts	2011	Baso	10,000 p.a.
			Evaluate key account feedback in periodic intervals	annually	Baso	1,000 p.a.
	Systematize community relationships	**Good community reputation** No of community projects supported by company	Carry out a community needs appraisal to identify priority needs/projects	2012	Assistant	5,000
			Implement community projects	2012	Marketing assistant	20,000 p.a.
			Monitor, evaluate and document outcomes and impact	2012 onwards	Marketing assistant	1,000 p.a.
			Set up a public relations focal point in the business to maintain liaison with the community and to communicate the results of the projects	2012 onwards	Baso	5,000 p.a.

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For example, a construction business that has defined the construction of low-cost housing for families as its main value proposition (What is my business?) would likely need to have a thrust on "cost" and "focus" in its growth drive. Hence, growth strategies with clear emphasis on "cost" and "focus" would most likely score as having "very strong fit".

Another example is a computer training school that has successfully specialized on computer classes for school children, and wants to focus on this market segment in its future growth drive (Who are my customers?). For this school, a growth strategy with very strong fit would have a thrust on "focus" and might take the direction of "market penetration" or "new product development". Other strategies might also score a good fit, but the exact grade will probably depend on the extent to which they combine with an emphasis on "focus" and existing customers.

IN-DEPTH CASE STUDY

MJI have assessed the fit between their shortlisted growth strategies and their business vision. They refer back to the vision statement of their own business and reflects to what extent the short-listed growth strategies have strategic fit with the ultimate business goals. Then they score each strategy option on a scale from 'poor fit (1)' to 'very strong fit (5)'.

Strategic fit strategy 1				
1	2	3	4	5

Strategic fit strategy 2				
1	2	3	4	5

Strategic fit strategy 3				
1	2	3	4	5

EXERCISE

Refer back to the vision statement of your own business. Ask yourself to what extent the shortlisted growth strategies for your own business have strategic fit with your business goals. Then score each strategy option along its strategic fit using a scale of 1-5 where one marks "poor strategic fit" and 5 marks "very strong fit".

Strategic fit strategy 1				
1	2	3	4	5

Strategic fit strategy 2				
1	2	3	4	5

Strategic fit strategy 3				
1	2	3	4	5

Risk exposure

The term "risk exposure" refers to the amount of risk associated with the implementation of a shortlisted growth strategy. For example, if you opt for a diversification strategy with emphasis on cost and seek to take over one of your direct competitors, the success of this acquisition drive might be influenced by events beyond your control – an anti-cartel authority might block the deal or a third party might decide to start a bidding war for the takeover candidate. The likelihood and the impact of these events together determine the degree of risk exposure.

The risk exposure matrix below illustrates the likelihood and impact of a given event on your growth strategy. Likelihood or probability is plotted on the vertical axis of the matrix, and an event might be classified as having either a "low", "medium" or "high" probability to occur. Impact is classified on the horizontal axis, and impact might be classified as "low", "medium" or "high". Events that have medium or high probability and medium or high impact are critical events that could derail your growth strategy.

Table 40: Risk exposure matrix for a growth strategy

Impact / Probability	Low Low impact on business activities/ finances	Medium Moderate impact on business activities/ finances (could be difficult to control)	High Significant impact on business activities/ finances (very difficult to control)
Low An impact on business activities/ finances is not likely to occur			
Medium An impact on business activities/ finances is likely to occur (more than 25% chance of occurrence)		**DANGER ZONE**	
High An impact on business activities/ finances is likely to occur very soon (more than 50% chance of occurrence)			

To complete the risk exposure matrix, you need to first brainstorm about possible events that might negatively impact on the implementation process and expected outcome of your growth effort.

First, write down all risks that come to your mind on a piece of paper. During the process, you can seek inspiration from the results of your market analysis carried out in Chapter II of this manual, but you should also think of risks that are related to your private life and your family, and that might negatively affect your business.

When you map your "worst-case scenario" of things to come, do not make the mistake being over-optimistic. People tend to filter out worst-case scenarios when they plan for

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the future, and in particular business people tend to ignore the associated risk if a growth strategy is financially promising or has personal appeal to them. For example, most car drivers choose not to picture the worst-case scenario of a frontal collision with another vehicle. However, these accidents do sometimes occur. Are you prepared for it?

Match the risk you identify through the scenario mapping exercise to the shortlisted business growth strategies. Some of these events will have a generic negative impact, e.g. they might negatively affect your business in any growth scenario, while others might be case-specific. For example, if you operate a commercial chicken farm, a chicken disease might impact on your growth effort in any growth scenario, while a new customs tariff on chicken meat might impact mainly on your growth strategy if you plan to develop export markets.

Now, draw a separate risk exposure matrix for each strategy and plot the corresponding risks for each strategy in one of the nine boxes. For example, a T-shirt manufacturer might brainstorm about the likely event of new import tariffs on selected garments, and conclude that this event would pose a risk particularly for growth strategies aiming at export market development. In the risk exposure matrix for this type of growth strategy, the manufacturer would plot "new import tariffs" as an event with medium or high probability and substantial impact. The event would thus be located in the "danger zone" of the matrix and indicate that this growth strategy bears a comparatively higher risk.

Finally, based on the risk exposure matrix, rank each growth strategy on a risk exposure scale from 1-5, where "1" marks the highest risk exposure and "5" marks the lowest risk exposure. Scores "2" "3" and "4" marks the intermediate risk exposure on a gliding scale.

Keep in mind that a high-risk exposure does not mean that you should not choose this strategy – in fact, high-risk strategies often hold the promise of attractive returns. However, a high-risk strategy always means increased danger of failure, and that you will have to carefully think about risk mitigation initiatives. These initiatives are likely to drive up the costs of the growth effort, and these additional costs will need to be factored into the financial appraisal of the planned investment. See below for further details.

IN-DEPTH CASE STUDY

MJ Industries has assessed the risk associated with their short listed growth strategy 1 and prepare the risk exposure table 41 matrix.

Table 41: Mega Juice Industries growth strategy risk assessment matrix

Probability \ Impact	Low	Medium	High
Low			Death of entrpreneur Economic depression Raw material shortages because of global climate change Poloitical instability
Medium		Fuel/electricity shortages	Interruption of raw material supply because of sudden environmental disaster
High			Collapse of tourism

DANGER ZONE

Based on the risk analysis MJI concludes that the growth strategy increases risk exposure since its growth drive will largely depend on the uninterrupted supply of raw materials They then score the first growth strategy as 2.5 (between medium risk and elevated risk). The follow this process for the other two strategies.

Strategic fit strategy 1				
1	2	3	4	5

EXERCISE

Use the template below to brainstorm about events that might negatively affect your business in the future. Then draw a risk exposure matrix for each shortlisted growth strategy and plot the applicable events in each matrix. Based on the outcome of the analysis, score the risk exposure level of each growth strategy on a scale from 1-5. where "1" marks the highest risk exposure (=least attractive scenario) and "5" marks the lowest risk exposure (=most attractive scenario).

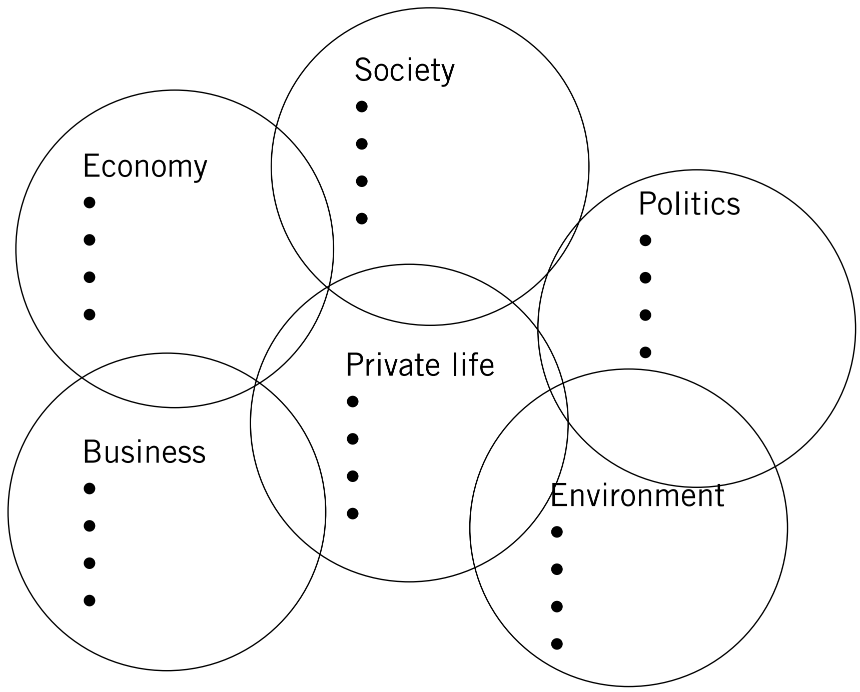

Figure 40: The following events might negatively impact on my business growth efforts

Table 42: Risk exposure matrix for growth strategies

Risk exposure matrix for growth strategies 1

Impact / Probability	Low	Medium	High
Low			
Medium			
High			

Risk exposure matrix for growth strategies 2

Impact / Probability	Low	Medium	High
Low			
Medium			
High			

Risk exposure matrix for growth strategies 3

Impact / Probability	Low	Medium	High
Low			
Medium			
High			

Final score of the risk associated with each growth strategy

Strategic fit strategy 1				
1	2	3	4	5

Strategic fit strategy 2				
1	2	3	4	5

Strategic fit strategy 3				
1	2	3	4	5

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3. Carry out a financial appraisal of each growth strategy

Investing in your business growth strategy implies a cost commitment before your business can start reaping the benefits which accrue over a period of several years. It is therefore necessary to be sure that the investment decision is profitable over the entire life of the investment project and meets the profitability goals. When you have sufficient funds to invest in a number of projects, you will need to select projects not only according to the availability of funds, but also according to their profitability. You may find it helpful to rank projects in order of profitability. This ranking will help you choose the best investment for your business.

Capital investments tie-up your precious capital, and may lead to cash shortages for the day-to-day business activities making it necessary to borrow additional finance. Borrowed funds must be re-paid with interest. In that regard you must consider the cost of capital and ensure that the rate of return you get from your investment is adequate to cover your costs.

A financial appraisal is an assessment whether your planned investment meets the performance benchmark set for your financial business objectives. It is like a "reality check", helping you to double check whether a seemingly attractive growth strategy is really as promising as you think, or whether you could invest your money to equal risk but higher return elsewhere.

A financial appraisal is also related to financial planning and analysis. The investment appraisal will show how the investment affects the company's financial health such as the cash flow. If the investment puts a heavy strain on the business' finances, even a very profitable investment should not be undertaken since it could put the whole business at risk.

At the operational level of a business, financial appraisal is also used to assess the relative attractiveness of a specific investment project over alternative options. For example, an operations supervisor might appraise whether the investment in machine A is more attractive than the investment in machine B. **Financial appraisal at the operational level is not further discussed in this manual**[2].

There are number of techniques to analyse the feasibility and attractiveness of investments you are considering. Further these techniques can be used to choose the best option from alternative investment opportunities. The two tools that will be considered in this manual are: the Pay-Back Period (PBP) and Net Present Value (NPV).

Follow these steps to appraise your planned investment in business growth:

- prepare an investment plan
- forecast your finances
- calculate the payback period of your investment
- calculate the net present value of your investment
- calculate key investment ratios.

2 Your business accountant will be able to help you do a financial appraisal of your business.

Prepare an investment plan

An investment plan quantifies the capital investment and working capital needs of your business required to implement the growth strategy. All cash going out of the business due to the investment must be taken into account and it must be clear when the money is going out.

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To assess your capital needs, you can refer back to the consolidated action plan that you developed earlier for each shortlisted growth strategy.

Table 44 demonstrates how MJI calculated the planned investment and cash needed in to implement their growth strategy. The format allows you to spread your investment over a period of up to five years. If you plan to spread your investment over more than five years, you can add more columns to the template.

Table 43: MJI Capital Requirements for growth strategy 1

Capital required	2012	2013	2014	2015	2016
1. Once-off investments					
Operations					
to upgrade workstations	5,000				
to buy new machines and equipment		100,000			
to develop an output tracking system	1,000				
Marketing					
to procure a market information software	5,000				
to procure a computer for the marketing department	10,000				
to implement community projects		5,000	26,000	26,000	26,000
to carry out market research on new machines		1,000			
Human resources					
to assess staff needs	2,000				
to draw development plans for existing staff	5,000				
to search for HRM consultants	1,000				
to develop existing staff (incl. owner managers)	50,000	30,000	30,000	30,000	30,000
to recruit and develop new staff	22,000	10,000	10,000	10,000	10,000
to carry out a staff satisfaction survey	1,000				

to draft and issue labour contracts		5,000			
to set up grievances procedures		2,000			
Other investments					
to decommission the canned pineapple production machines	2,000				
1. Total investment requirements per year	**104,000**	**153,000**	**66,000**	**66,000**	**66,000**
2. Working capital requirements					
Operations					
Increased maintenance costs	5,000	7,000	7,000	9,000	9,000
Increased costs of raw material inputs	48,900	172,320	308,082	1.004,994	1,224,026
Other factor inputs except labour	10,000	20,000	30,000	40,000	50,000
Marketing					
to maintain liaison with key accounts	10,000	10,000	10,000	10,000	10,000
to periodically evaluate key account feedback	1,000	1,000	1,000	1,000	1,000
to carry out a supplier survey		10,000			
for public relations work with suppliers and the community		12,000	12,000	12,000	12,000
Human resources					
to monitor development of existing and new staff	5,000	5,000	5,000	5,000	5,000
Additional salary costs for new staff	15,600	15,600	16,600	16,600	17,600
Additional salary costs for existing staff	60,000	60,000	70,000	70,000	80,000
Other costs					
Membership fees in business association	500	500	500	500	500
Subscription fees for magazines	1,000	1,000	1,000	1,000	1,000
Visits to technology fairs	2,000	2,000	2,000	2,000	2,000
Total working capital requirements per year	**159,000**	**316,420**	**463,182**	**1,172,094**	**1,412,126**
Total capital requirements by year	**263,000**	**469,420**	**529,182**	**1,238,094**	**1,478,126**
3. TOTAL CAPITAL REQUIREMENTS			**3,977,822**		

Are you wondering how to raise the capital required for financing your growth effort? On request, your EYB trainer can also organize an EYB Bankers forum for EYB trainees to meet local providers of financial services. Please refer to your EYB trainer for more details.

Table 44: Template for an Investment Plan

Growth Strategy ____					
Capital Required	20__	20__	20__	20__	20__
1. ONE-OFF INVESTMENTS					
1.1 Operations					
1.2 Marketing					
1.3 Human resources					
1.4 Other investments					
2. TOTAL INVESTMENT REQUIRED BY YEAR					
3. WORKING CAPITAL					
3.1 Operations					
3.2 Marketing					
3.3 Human resources					
Other					
4. TOTAL WORKING CAPITAL REQUIRED BY YEAR					
5. TOTAL CAPITAL REQUIRED BY YEAR					

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Forecast your finances

A profit and loss forecast and a balance sheet forecast are the financial instruments used to assess your likely financial situation in a given business growth scenario. Profit and loss account shows income generated by the business and operational expenditure incurred to generate such income. A balance sheet is a statement showing the business assets, liabilities and reserves. It reflects the business net worth.

Your business records and financial statements for the past years provide important information about your sales and costs and allow you to project these sales and costs in the future. Refer to your financial statements as a basis for forecasting your profits and losses and your assets and liabilities. Financial records and statements furnish important information about your sales and costs and allow you to project these sales and costs in the future. In addition to the financial records, refer to the results of your market analysis completed in Chapter 2 of this manual. The market information allows you to hypothesize about your likely sales and costs in various growth scenarios.

The financial forecasts show how the growth strategy affects your financial position over time. For example, you can follow how your business' liquidity will be affected by investments or increased credits coming from increasing sales. The forecasts also give you an idea about how well your financial objectives will be met. If your forecasts show that your objectives cannot be met you should evaluate whether your objectives are set to high or if the strategy is not optimal.

Based on the financial forecasts you can also calculate key financial ratios for your business. See below for more details.

IN-DEPTH CASE STUDY

MJI have prepared their financial forecast for strategy 1 as illustrated in table 45:

Table 45: MJI Profit and Loss Forecast growth strategy 1

Item	2012	2013	2014	2015	2016
1. Gross sales from main business	**4034450**	**5938275**	**7073925**	**8227950**	**9555000**
Less: Cost of goods sold					
Raw materials	2275152	2616504	3008984	346034	3979536
Other input costs	69900	199320	345082	1053994	1283026
2. Gross Profit from main business	**1689398**	**3122451**	**3719859**	**6827922**	**4292438**
Less: Expenses					
Sales and marketing expenses	58890	70980	83070	98460	196920
Administration expenses	83660	91720	100880	110040	120300
Financial expenses:					
Interest Paid	15000	0	0	0	0
Motor Vehicle Expenses	24000	24000	24000	24000	24000
Provision for Welfarism	63364	74648	87472	100296	111602
Professional Association fees	3500	3500	3500	3500	3500
Decommissioning Expenses	2000	0	0	0	0
Recruitment and development	81000	47000	40000	40000	40000
Provision for Depreciation:					
Fixed Assets	36000	36000	36000	36000	36000
Land rights	4500	4500	4500	4500	4500
Personal Computer	950	950	950	950	950
Production Equipment	9500	9500	9500	9500	9500
Net Profit Before Taxes	1,307,034.00	2,759,653.00	3,329,987.00	6,400,676.00	3,745,166.00
Income Tax	392110.2	827895.9	998996.1	1920202.8	1123549.8
Net Profit After Taxes	914,923.80	1,931,757.10	2,330,990.90	4,480,473.20	2,621,616.20
Less Reserves	137238.57	289763.565	349648.635	672070.98	393242.43
Net Profit After Reserves	777,685.23	1,641,993.54	1,981,342.27	3,808,402.22	2,228,373.77

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Assumptions

1. A growth rate of 25% for kiosk is assumed from 2012 to 2016.
2. The cost per one litre of juice is 3 units for the period 2012 to 2013. And 4 units from 2014 to 2016.
3. The selling price shall also rise by 30% both for wholesale distribution and Luxury Hotel lines.
4. Kilograms required per litre of juice shall be 2.2kg
5. Welfarism and Reserves will use 15% as required in the national policy.
6. Other labour overheads are apportioned as follows 75% Direct Labour, 10% Administration, 15% Sales and marketing.
7. The pineapple line is decommissioned at 2000 and has no salvage value.

Table 46: Balance Sheet Forecast strategy 1

	2012	**2013**	**2014**	**2015**	**2016**
	0.00	0.00	0.00	0.00	0.00
Assets	**2012**	**2013**	**2014**	**2015**	**2016**
Current assets					
Cash	791,291.30	2,848,646.40	5,318,059.30	9,949,778.50	12,733,946.70
Short-term Investment	0	0	0	0	0
Notes Receivable	0	0	0	0	0
Arrear Receivables	0	0	0	0	0
Stocks	0	0	0	0	0
Subtotal current assets	**791291.3**	**2848646.4**	**5318059.3**	**9949778.5**	**12733946.7**
Total Current Assets	**791291.3**	**2848646.4**	**5318059.3**	**9949778.5**	**12733946.7**
Fixed Assets					
Original value of fixed assets	800000	800000	800000	800000	800000
Accumulated depreciation	288000	324000	360000	396000	432000
Net value of fixed assets	**512000**	**476000**	**440000**	**404000**	**368000**
Liquidation of fixed assets:	0	0	0	0	0
Invisible assets					
Land use rights(Original Value)	90000	90000	90000	90000	90000
Accumulated depreciation	22500	27000	31500	36000	40500
Net Invisible Assets	**67500**	**63000**	**58500**	**54000**	**49500**
Other Equipments					
Personal Computer (Original Value)	10000	10000	10000	10000	10000

Accumulated Depreciation	950	1900	2850	3800	4750
Net Personal Computers	**9050**	**8100**	**7150**	**6200**	**5250**
Production Equipment	100000	100000	100000	100000	100000
Accumulated Depreciation	9500	19000	28500	38000	47500
Net Production Equipment	**90500**	**81000**	**71500**	**62000**	**52500**
Total Assets	**1470341.3**	**3476746.4**	**5895209.3**	**10475978.5**	**13209196.7**
Equity and Liabilities					
Current Liabilities:					
Provision for Welfarism	55417.5	130065.5	217537.5	317833.5	429435.5
Long term Loan					
Total Liabilities	55417.5	130065.5	217537.5	317833.5	429435.5
Equity:					
Capital Investment	500000	500000	500000	500000	500000
Surplus Reserves	137238.57	427002.14	776650.77	1448721.75	1841964.18
Retained Profit	777,685.23	2,419,678.77	4,401,021.03	8,209,423.25	10,437,797.02
Total equity	**1,414,923.80**	**3,346,680.90**	**5,677,671.80**	**10,158,145.00**	**12,779,761.20**
Total liabilities and equity	**1,470,341.30**	**3,476,746.40**	**5,895,209.30**	**10,475,978.50**	**13,209,196.70**

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EXERCISE

Use the template to draw up a profit and loss account forecast and a balance sheet forecast for the next five years and separate for each growth scenario.

Table 47: Template for a Profit and Loss Account Forecast

Profit and Loss Account Forecast					
Company:				Unit:	
Item	**20__**	**20__**	**20__**	**20__**	**20__**
1. Main business Income					
Operating income (Turnover)					
Less: Direct operating cost					
Gross profit margin					
2. Other income					
Other income (Analyse the categories)					
Total business income					
3. Business Expenditure					

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Business operating expenses					
Management expenses					
Financial expenses of which: Interest payments Exchange rate losses					
4. Net Operating profit					
Other non-business Operations					
Add: Income from investment Other income					
Less: Other expenses					
Add: Previous year's income adjustment					
4. Profit before tax					
Income tax					
Other tax					
5. Net profit after tax					

Table 48: Template for a Balance Sheet Forecast (1)

	20__	20__	20__	20__	20__
Assets					
Current Assets					
Cash					
Short-term investment					
Accounts receivable (A/R)					
Deferred and prepaid expenses					
Inventories					
Other current assets(see notes)					
Subtotal current assets:					
Long-term investment					
Long-term stock rights investments					
Long-term creditor rights investments					
Subtotal long-term investment:					
Fixed assets:					

Original value of fixed assets					
Subtotal fixed assets:					
Work-in-process					
Intangible assets:					
Land usage rights					
Other intangible assets					
Subtotal intangible assets:					
Other assets:					
Total Assets					

Template for a Balance Sheet Forecast (2)

Liabilities and Equity	**20__**	**20__**	**20__**	**20__**	**20__**
Current liabilities:					
Short-term loans					
Accounts payable (A/P)					
Accrued payroll					
Taxes payable					
Dividends payable					
Other payables					

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<u>Subtotal current liabilities:</u>					
Long-term liabilities:					
Long-term loans					
<u>Subtotal long-term liabilities:</u>					
Other liabilities:					
Total liabilities:					
Equity:					
Share capital					
Capital reserve					
Retained profit/Accumulated profit					
Total equity:					
Total liabilities and equity					

Calculate the payback period of your investment

The payback period of an investment tells you the number of years it takes to recover your initial investment based on expected cash flows from that investment. The formula for the payback period calculation is simple.

Firstly calculate your net cash flow by subtracting your total financial inflows from your total outflows. Then divide the initial investment by the net annual cash flow.

$$\text{Payback Period} = \frac{\text{Original investment}}{\text{Net Annual cash flow}}$$

For example if your required investment is 2,000,000 and your net annual cash flow is 500,000 then payback period will be 2,000,000 / 500,000 = 4 years.

If the cash flows are not evenly spread, the payback period calculation is somewhat more complicated. In this case, the annual cash inflow is accumulated until the original investment is recovered. The payback period in years equals the amount of time necessary to recover the initial investment.

It should be noted however that the payback period, whilst providing valuable information from a cash management perspective, does not give any indication about the real profitability of the investment. It ignores the value of any income flowing in once the original investment has been recovered. Businesses use payback mostly as a restrictive criteria in that they will chose not to take projects with payback beyond say three years as this ties up capital for a too long period, and the longer the time to recover the original investment, the greater the risk.

Calculate the net present value of your investment

The concept of net present value is based on the principle of "the time value of money". This means that cash today is worth more than the same amount tomorrow or next year. Since your business has a cost of raising capital, all investments should be evaluated against that cost. Assume that your business raises 100,000 for an investment today and gets back 100,000 in one year's time. Then the company has actually lost money. Why? Because during that time the business had to pay interest on loans it took for the investment and return to shareholder for their equity contribution. The "time value of money" is thus the company's cost of capital.

When you are going to assess whether your investment is profitable enough to cover your cost of capital you have to compare one large cash outflow today with cash inflows in the future. The net present value (NPV) model takes the cost of capital and its time aspect into account and helps you to compare the cash flow streams in the future with an investment today.

A 100,000 investment today must be at least 100,000 + the business cost of capital in one year's time to be profitable.

Follow these steps to calculate the net present value of your investment:
- assess the size and timing of cash flows
- calculate your company's weighted average cost of capital
- discount the future cash flows with the company's weighted average cost of capital
- decide to implement or not implement the investment

Assess the size and timing of cash flows

As mentioned above, the problem with investment appraisal is to compare cash flows that go in and out of the company at different times. The first step in making the cash flow streams comparable is to assess when they occur. Under the section "forecast your finances" you have already assessed the size and timing of your cash flows relating to an investment.

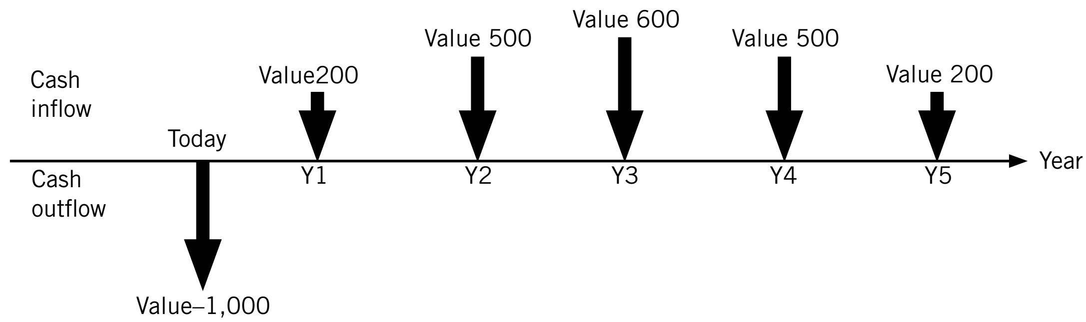

Figure 41: Size and timing of cash flows in an investment appraisal

A typical investment could look like figure 43 where, we can see how the size and timing of cash flow has been assessed. An initial investment valued at 1,000 is made, and it is followed by a series of smaller cash inflows. The total sum of the cash inflows without taking the time value of money into account is 2,000. It might look obvious that the investment is profitable, but in reality it is impossible to know without calculating today's value of the future cash inflows.

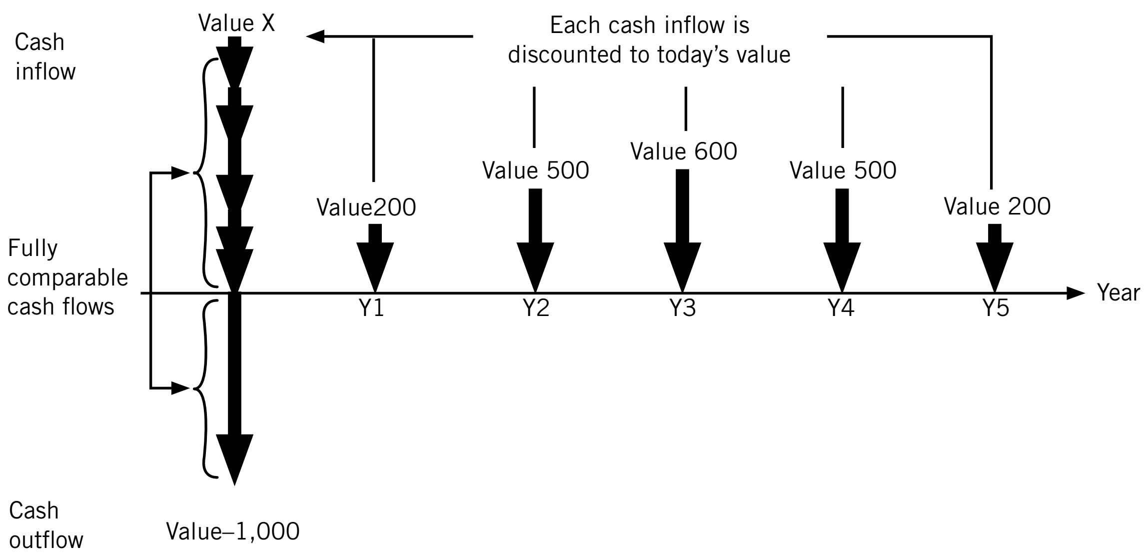

Figure 42: Discount future cash flows to today's value

The future cash flows are discounted using the cost of capital that your business faces. The next section takes you through the procedure of calculating the business cost of capital.

Decide whether to implement or not implement the investment

The final outcome of the net present value formula is a value that can be either positive or negative. If the final NPV is negative, this means that the total future net cash flows that will occur due to the investment are smaller in today's value than the initial investment. In other words, the investment will lead to losses.

If the final NPV is positive, this means the future net cash flows coming from the investment are bigger in today's value than the investment today. The investment will yield a positive return.

In case the NPV calculation shows a zero or a result close to zero, this indicates that the discounted net cash flows will be big enough to cover the initial investment, the interest rate on debt, and pay the required rate of return on the equity.

So even a zero NPV project can be worth implementing. However, you must be very careful with your revenue assumptions. Just a small deviance in future cash flow can make the project unprofitable. And common wisdom has it that investments tend to be more costly than planned, and revenues often come later than expected.

Negative NPV = Do not implement the investment.

Positive NPV = Implement the investment.

The difficult part in using this kind of tool is therefore to prepare good estimates of the cost of the investment and the potential revenues and operating costs relating to the specific investment project. Here, there is no alternative to making a very detailed and realistic study of these elements, based on all available information.

The risk is always to be too optimistic in order to justify the investment, as emotionally you will naturally want the result to show the project to be attractive. It is therefore advisable for each investment that you determine the performance really achieved, year by year, in order to build your experience in making these forecast evaluations.

IN-DEPTH CASE STUDY

MJI has calculated the payback period and for their planned investment for each growth scenario presented below:

MJI Payback period Strategy 1

Original Investment/Net Annual Cash Inflows $\frac{500\ 000}{2572378.64}$ 2months

EXERCISE

Use the templates below to calculate the payback period of your own planned investment for each shortlisted growth scenario.

Payback period for the planned investment

		Original investment
____________	=	____________ ____________
		Annual cash flow

Calculate key investment ratios

Chapter 2 of this training manual introduced selected financial ratios frequently used to assess the financial health of a business. The same ratios can be also applied to assess the likely profitability of business operations in the future and to indicate whether your business will be able to maintain a positive cash flow during expansion.

IN-DEPTH CASE STUDY

MJI has calculated key financial ratios for each growth scenario as presented in table 49.

Table 49: MJI Financial Ratios Strategy 1

KEY FINANCIAL RATIOS					
	2012	2013	2014	2015	2016
Liquidity					
Current Ratio	**14.28**	**21.90**	**24.45**	**31.31**	**29.65**
Net cash flow	919237,8	2057355,1	2469412,9	4631719,2	2784168,2
Profitability					
Gross Profit Margin	**0.42**	**0.53**	**0.53**	**0.83**	**0.45**
Return on equity	**1.83**	**3.86**	**4.66**	**8.96**	**5.24**
Return on assets	**0.62**	**0.56**	**0.40**	**0.43**	**0.20**

EXERCISE

Use table 50 to fill in key financial ratios for your own business for each growth scenario separately. Refer to Chapter 2 for more information on how to calculate these ratios.

Table 50: Financial ratios for growth strategies template

	Year 1	Year 2	Year 3	Year 4	Year 5
Liquidity					
Current ratio					
Net cash flow					
Profitability					
Net profit margin					
Return on equity					
Return on assets					
Capital structure					
Debt to asset ratio					
Need for external finance					
Long-term					
Short-term					

4. Compare the results of your appraisals and choose the strategy that suits your own business best

In the last step of the selection process, you compare the results of your financial and technical appraisal of each shortlisted growth strategy, and choose the option with the comparatively best results. The template overleaf provides a useful format for the cross-comparison of your strategy options:

The ideal growth strategy should have strong strategic fit, expose your business to limited risk, must have an NPV exceeding 0, should have a short payback period and ensure returns that meet the financial objectives of your shareholders. Also, the ideal growth strategy should not drain your cash flow, and you should be able to raise at least part of the planned investment from equity. If your business experiences cash flow problems and/or is saddled with heavy debt because of business growth, it becomes more vulnerable to external shocks and might fall victim to a takeover bid by a competitor. MJI growth strategy assessment grid is presented in table 51.

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Table 51: MJI Growth Strategy Assessment Grid

	Option 1					Option 2					Option 3				
Technical appraisal															
Strategic fit (1=poor fit – 5 = good fit)	1 2 3 4 5					1 2 3 4 5					1 2 3 4 5				
Risk associated with this option (1=high risk – 5= low risk)	1 2 3 4 5					1 2 3 4 5					1 2 3 4 5				
Financial appraisal															
Total required investment	**3,977,822**					**2,684,618**					**9,073,234**				
NPV															
Payback period	2 months					8 months					4 months				
Key financial ratios	Y1	Y2	Y3	Y4	Y5	Y1	Y2	Y3	Y4	Y5	Y1	Y2	Y3	Y4	Y5
Current Ratio	14.3	21.9	24.5	31.3	29.7	8.1	6.6	6.4	5.1	4.3	20.7	19.3	20.4	20.6	20.9
Net cash flow	920,000	2,057 m	2.5 mill	5 mill	2.8 mill	647,000	653,064	1, m	719,288	738, 682	1,701 405	1354 230	1,585 749	1467 832	1642 059
Gross Profit Margin	0.42	0.53	0.53	0.83	0.45	0.44	0.43	0.44	0.31	0.32	0.49	0.34	0.31	0.24	0.23
Return on equity	1.83	3.86	4.66	8.96	5.24	1.10	0.99	1.63	0.89	0.82	3.25	2.79	2.91	2.67	3.01
Return on assets	0.62	0.56	0.40	0.43	0.20	0.50	0.29	0.30	0.13	0.10	0.74	0.38	0.28	0.20	0.18

Table 52: Growth strategy assessment grid

	Option 1			Option 2			Option 3		
Technical appraisal									
Strategic fit (1=poor fit - 5 = good fit)	1 2 3 4 5			1 2 3 4 5			1 2 3 4 5		
Risk associated with this option (1=high risk – 5= low risk)	1 2 3 4 5			1 2 3 4 5			1 2 3 4 5		
Financial appraisal									
Total required investment									
NPV									
Payback period									
Key financial ratios	Year 1	Year 2	Year 3	Year 1	Year 2	Year 3	Year 1	Year 2	Year 3
Current ratio									
Net cash flow									
Net profit margin									
Return on equity									
Return on assets									
Debt to assets ratio									
Need for external finance									
Long-term									
Short-term									

If your comparative analysis reveals that none of the strategy options meets your financial and non-financial objectives, you need to go back to the growth strategy matrix and choose alternative scenarios for a detailed assessment.

If all options fall short of your financial objectives, you should either revert to your planned initiatives and review the cost implications of your activities, or revert back to the growth strategy matrix and brainstorm about alternative scenarios.

If all options meet your financial objectives and have good strategic fit but expose your business to high risk, you will need to carefully consider whether you are ready to take on this “gamble” on the future. If you feel that the risk exposure is too high, you have to think of additional strategic initiatives that would help to mitigate the risk, or alternatively revert back to the strategy growth matrix and brainstorm about alternative scenarios. If you decide on additional initiatives, remember to firmly link them to one of your business objectives, define indicators to measure outcomes, and to budget for the corresponding activities.

If all options meet your financial objectives and only expose your business to low or moderate risk, *but* have a **poor** strategic fit, you need to revert back to the strategy growth matrix and brainstorm about alternative scenarios. Do not confuse "means" and "ends" in the strategy development process – it is your strategy framework that determines the thrust and direction of the growth effort, not vice versa. Otherwise, you might quickly end up losing orientation in the strategy implementation process – a typical phenomenon of fast growing businesses with fluid goals and values.

Finally, if all options meet your financial objectives and only expose your business to low or moderate risk, *but* have only **moderate** strategic fit, you might have a case for either brainstorming about new growth scenarios, or for refining your business objectives and corresponding performance measures. This exercise acknowledges the circular link between business goals and business strategy. As illustrated in the graph below, while the business goals have determined the overall layout of your business strategy, the detailed game plan based on this layout can have repercussions on your business goals that need to be taken into account.

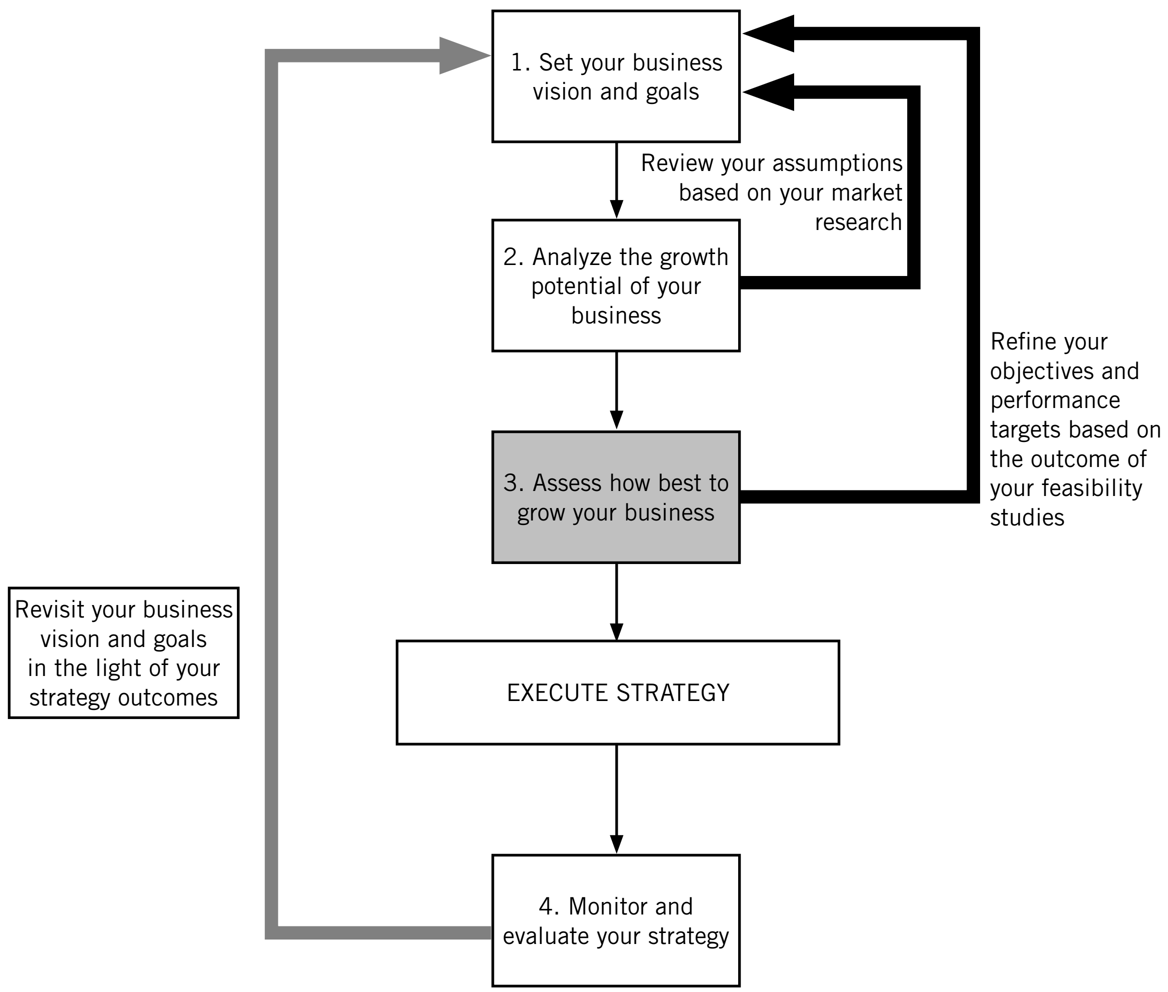

Figure 43: Recursive learning loops in the strategy development process

IN-DEPTH CASE STUDY

MJI selected and refined their business objectives to reflect their choice.

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Table 53: MJI refined list of business objectives and performance thresholds

Objective	Measures	Target				
		2012	2013	2014	2015	2016
Attractive returns	Return on assets in % (annual profit after tax x100 divided by value of fixed assets)	15	15	20	25	25
	Growth in production output in%	15	15	15	15	15
High profits	Net Profit Margin in%	4	4	5	6	7
Low cost structures	Ratio of overheads to total costs (administrative expenses x 100 divided by total business expenses)	0.02	0.05	0.08	0.08	0.08
High customer satisfaction	Customer satisfaction rate in% (no of satisfied customer x 100 divided by total no of customers p.a.)	85	90	90	90	90
Close relationships with buyers	Average time spent with each business customer (no of days per year per business customer)	5	5	6	7	7
Good community reputation	No of community projects supported by MJI	1	2	2	2	3
High operational efficiency	Speed of management decision making (average time in days for management to decide on proposals made by line managers	10	10	7	7	7
	Machine productivity (no of litres per machine p.a.)	60,000	65,000	70,000	77,000	85,000
	Lead time, production (time in days from receiving a product order to product delivery)	2	2	2	2	2
Emphasis on quality	Product reject rate (no of deliveries rejected by customers x 100 divided by total no of deliveries made p.a.)	5	5	5	3	2
Close relationships with suppliers	Supplier turnover (no of suppliers lost x 100 divided by total number of suppliers p.a.)	15	15	15	10	10
Systematic market information management	No of new document entries in the market information database of MJI	100	150	200	250	300

Cleaner production	Recycling rate, machine oil (litres of machine oil recycled x 100 over total litres of machine oil used in production p.a.)	0	25	50	75	100
	Wastage rate, raw materials (kilograms of orange wasted x 100 divided by total kilograms of oranges processed in production p.a.)	10	10	10	8	7
Qualified workers	No of days in training per machine operators	5	5	7	10	10
	Training course pass rate (no of machine operators successfully graduating from training x 100 divided by total no of operators in training p.a.)	75	85	85	85	85
Motivated workers	Worker satisfaction rate with salary packages (no of workers satisfied with salary package x 100 divided by total no of workers p.a.)	60	75	75	80	85
	Worker satisfaction rate with career development opportunities (no of workers satisfied with salary package x 100 divided by total no of workers p.a.)	60	75	75	80	85
High innovation capacity*	% of customers describing MJI as an innovative company	50	75	75	75	75

EXERCISE

Use the growth strategy evaluation grid to select a growth strategy for your own business. Then refer back to the list of your draft business objectives that you drafted earlier in this training course and refine these objectives in reflection of your choice.

Table 54: Final list of objectives for my business

Objective	Measures	Target				
		20__	20__	20__	20__	20__
No 1:						
No 2:						

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No 3:						
No 4:						
No 5:						
No 6:						
No 7:						
No 8:						
No 9:						
No 10:						
No 11:						
No 12:						
No 13:						
No 14:						
No 15:						

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CHAPTER 6: HOW CAN I MAKE MY GROWTH STRATEGY ACTIONABLE

This final chapter will introduce you to the tools that will assist you in the implementation of your growth strategy. The two main tools are a strategy map and a strategy control system. A strategy map is like a road map of your growth strategy, it shows the destination of your strategy voyage (your business vision) and the main milestones along the roadside (your business objectives). A strategy control system consists of various tools used to monitor progress in implementing the growth plan.

6.1 Draw a strategy map

Strategy maps acknowledge the complexity of business strategy – they allow you to depict the cause-effect linkages between the business objectives, and track multiple initiatives performed at the same time in pursuit of different business objectives. By assigning each milestone a coordinate in time and space (e.g. a deadline for completion and performance thresholds), you can turn this map into a compass of the strategy implementation process. The main building blocks of a strategy map are measures, cause effect relationships, your business objectives and your business vision as illustrated in figure 47:

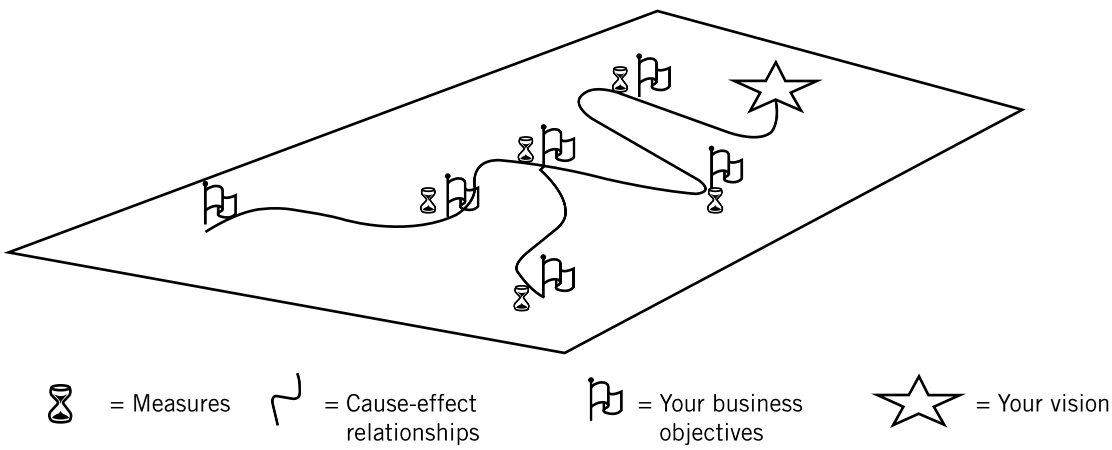

Figure 44: Main building blocks of a business strategy map

> Refer to section 6.2 of this manual for more information on how to turn the strategy map of your business into a strategy control system.

Why is it important to draw a strategy map?

A strategy map helps you to make your business vision "actionable" by visualizing and communicating your growth strategy to all business stakeholders. A strategy map is particularly helpful to illustrate how you will balance the financial and non-financial goals of your business on the road towards the achievement of your business vision.

Furthermore, a strategy map assists you to control progress in the implementation of your business strategy. With the help of the map, you can track the implementation status of your growth strategy, and whether you will meet the strategy milestones as planned. Based on the strategy map, you can then devise corrective action to put the strategy implementation process back on track.

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How to draw a strategy map

Follow these steps to draw a strategy map for your business:

1. Draw up the cause-effect relationships between your business objectives.
2. Adjust the measures and targets assigned to each business objective.
3. Review the strategic initiatives planned to achieve your business objectives.

1. Draw up the cause-effect relationships between your business objectives

In the first step, you need to visualize the cause and effect relationships between your financial and non-financial business objectives. You can literally draw up these relationships by assigning each business objective a graphical symbol and then linking these symbols with connectors.

Figure 48 illustrates an example of a simplified strategy map for a business. The business objectives have been grouped along the strategic perspectives introduced earlier in this manual, and namely are "learning", "finance", "people" and "processes".

The map clearly highlights the cause-effect linkages between the financial and non-financial objectives of the business. For example, the map illustrates that qualified and committed workers are one key factor contributing to intimate relationships with the local community - where many of these workers might come from and where the livelihood of entire families might depend on their salaries. Intimate relationships with the local community, in turn, are one factor paving the way for close customer relationships (at least where the local community is part of your market), and the income from your sales to the local community can become an important source of income for your business.

Refer to the business objective navigator in chapter 1 of this manual for details about the classification scheme for your business objectives.

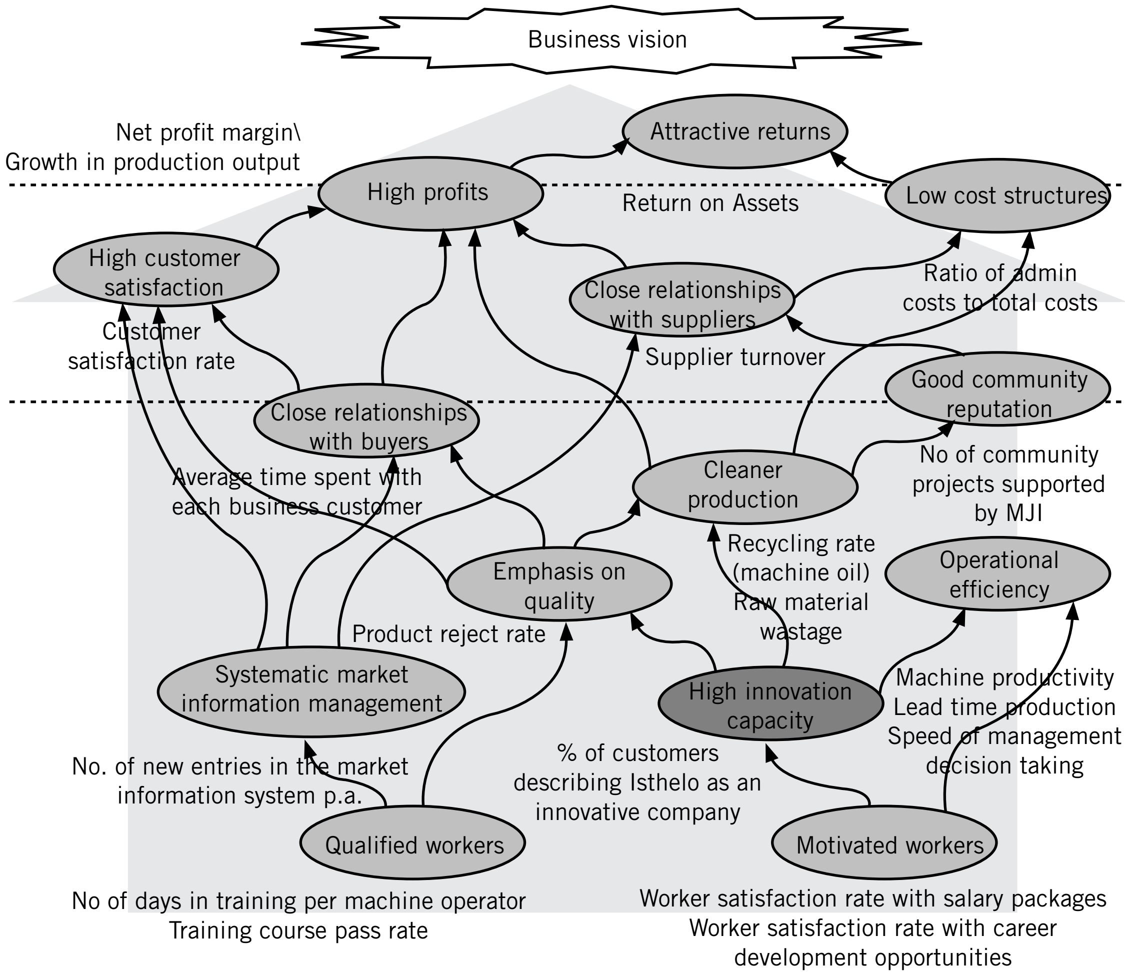

Figure 45: MJI strategy map

It is important to note that strategy maps are not intended to reproduce the complete matrix of your growth strategy. They only aim at highlighting the **key** cause-effect relationships in the strategy matrix in order to foster systemic thinking. Strategy maps have certain weaknesses just like any other tool that communicates and visualize strategy.

Firstly, the map only highlights selective cause and effect relationships between strategic objectives. One could argue that in a business "everything is connected with everything", and that the strategy map oversimplifies the situation on the ground. Secondly, the map can create the impression of linear cause-effect relationships between business objectives, where for example qualified and committed workers are an enabler for intimate relationships between the business and the local community. One could argue that these relationships are rather mutually enforcing ("dialectic") than linear because intimate community relationships can in turn also boost the commitment of workers. Thirdly, the map implies that financial performance is the top perspective of the business vision and the ultimate stepping-stone to the achievement of your business vision.

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Also, while the cause-effect linkages between many strategic objectives are nonlinear, it is also true that some building blocks of business success have to be put in place first to set the wheel of mutually enforcing relationships in motion. For example, well-trained and committed employees are a critically important enabler for product quality and a strong customer focus. Also, workers' qualification and commitment is needed **first** to set the circular relationship between quality products and worker pride (in producing these goods or services) in motion.

EXERCISE

Please draw a strategy map for your own growth strategy.

MY DRAFT BUSINESS STRATEGY MAP

2. Adjust your business performance measures and targets

In this second step, you need to review the draft measures and targets for your business objectives in the light of the emerging growth strategy. Firstly, you should review the draft measures and targets of your business objectives one by one and with regard to the targets set in your emerging strategic plan. For example, if you plan to increase your production output by 20% over the next 24 months, the performance measures and targets associated with your business objectives need to reflect this capacity increase.

Secondly, you should review the inter-relations between these draft measures and targets in the light of the cause-effect linkages depicted in the strategy map. For example, you might need to ensure that an increase in production output in the "processes" perspective is

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flanked by an increase in the number of sales persons in the "stakeholder" perspective. If you ignore the cause-effect relationships between these two performance measures, an increase in production output can undermine rather than support the performance of your business.

Thirdly, you should review the measures and targets once again in the light of your effort to balance lead and lag indicators in your performance measurement framework. For example, an "R&D investment target of X% of revenues" is a lead indicator for the innovation capacity of your business in the coming future while "growth in market share" is a lag indicator signalling the performance of your business in the recent past. The lead indicators are especially important to measure your investment today in business growth tomorrow.

Refer to chapter I for more information about how to set performance measures and targets for your business objectives.

IN-DEPTH CASE STUDY

MJI's refined business performance measures and targets illustrated in table 55:

Table 55: MJI Refined business performance measures and targets

Objective	Measures	Target				
		2012	2013	2014	2015	2016
Attractive returns	Return on assets in % (annual profit after tax x100 divided by value of fixed assets)	15	15	20	25	25
	Growth in production output in%	15	15	15	15	15
High profits	Net Profit Margin in%	4	4	5	6	7
Low cost structures	Ratio of overheads to total costs (administrative expenses x 100 divided by total business expenses)	0.02	0.05	0.08	0.08	0.08
High customer satisfaction	Customer satisfaction rate in% (no of satisfied customer x 100 divided by total no of customers p.a.)	85	90	90	90	90
Close relationships with buyers	Average time spent with each business customer (no of days per year per business customer)	5	5	6	7	7
Good community reputation	No of community projects supported by MJI	1	2	2	2	3

High operational efficiency	Speed of management decision making (average time in days for management to decide on proposals made by line managers	10	10	7	7	7
	Machine productivity (no of litres per machine p.a.)	60,000	65,000	70,000	77,000	85,000
	Lead time, production (time in days from receiving a product order to product delivery)	2	2	2	2	2
Emphasis on quality	Product reject rate (no of deliveries rejected by customers x 100 divided by total no of deliveries made p.a.)	5	5	5	3	2
Close relationships with suppliers	Supplier turnover (no of suppliers lost x 100 divided by total number of suppliers p.a.)	15	15	15	10	10
Systematic market information management	No of new document entries in the market information database of MJI	100	150	200	250	300
Cleaner production	Recycling rate, machine oil (litres of machine oil recycled x 100 over total litres of machine oil used in production p.a.)	0	25	50	75	100
	Wastage rate, raw materials (kilograms of orange wasted x 100 divided by total kilograms of oranges processed in production p.a.)	10	10	10	8	7
Qualified workers	No of days in training per machine operators	5	5	7	10	10
	Training course pass rate (no of machine operators successfully graduating from training x 100 divided by total no of operators in training p.a.)	75	85	85	85	85
Motivated workers	Worker satisfaction rate with salary packages (no of workers satisfied with salary package x 100 divided by total no of workers p.a.)	60	75	75	80	85
	Worker satisfaction rate with career development opportunities (no of workers satisfied with salary package x 100 divided by total no of workers p.a.)	60	75	75	80	85
High innovation capacity*	% of customers describing MJI as an innovative company	50	75	75	75	75

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EXERCISE

Refer back to your consolidated list of business performance measures and targets. Based on the cause and effect relationships between the business objectives in your strategy map, is there any need to fine-tune any of the targets, or to change a measure?

Review your initiatives

In the third and final step, you need to review the strategic initiatives of your growth strategy in the light of the refined business vision, business objectives, performance measures and performance targets. The purpose of the review is to align these initiatives with the final architecture of your business growth strategy.

In the realignment process, you have to pay particular attention to the cause-effect linkages between the business objectives, and the need to carefully sequence your strategic initiatives in response. For example, you might plan to simultaneously launch a staff training program in the "learning" perspective, a productivity improvement program in the "process" perspective, and a marketing campaign in the "stakeholder" perspective to pursue your growth objectives. You will need to carefully sequence these initiatives to make sure that you put the critical enablers of business success into place first, that you can maintain control over a multitude of activities at the same time, and that you can unlock scale benefits and synergies in the process.

EXERCISE

Please refer back to the list of initiatives planned in execution of the growth strategy for your own business, and review each initiative based on the finalized strategy map. In the process, pay particular attention to the sequence and timing of individual activities.

6.2 Set up a strategy control system

What is controlling?

In the context of this manual, controlling refers to the process of monitoring progress in implementing your growth strategy and of evaluating your final strategy outcomes against a set of performance indicators. Monitoring emphasizes collecting streaming information about ongoing activities while evaluation looks at the outcomes of these activities after a reasonable time lapse. Evaluations build on the analysis of monitoring data but will usually comprise an additional separate data collection effort to complement and qualify the existing management information.

A strategy control system typically comprises the following components:

- control tools to collect selected management information
- control processes that rule the data collection, data processing and data interpretation routines
- reporting formats to present the findings

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Why is controlling important?

Controlling is important because it provides you with the monitoring data needed to track actual performance in the strategy implementation process against set indicators and targets.

Controlling is also important because it offers all business stakeholders a means for objectively verifying their own performance in the strategy implementation process. The performance indicators provide detailed proof of the part-contribution of stakeholder groups to the implementation of the larger business growth effort. At the same time, they enable you to trace back under-performance to individual stakeholders and to undertake corrective action.

Controlling is also important because it furnishes you with the information needed to evaluate the outcomes of your strategy implementation effort, and to feed your findings into your next strategy-planning loop. More in particular, an evaluation enables you to conclude about the effectiveness and efficiency of your growth strategy. Efficiency, relates to the question whether you have "done things the right way" while effectiveness relates to the question whether a business is "doing the right things".

How to control your strategy implementation effort

Follow these steps to control your strategy implementation effort:
1. Choose the right strategy control system for your own business.
2. Monitor the strategy implementation progress.
3. Evaluate the strategy outcomes.

1. Choose the right strategy control system for your own business

Two monitoring and evaluation systems for your business growth strategy will be described in the following: A manual system working with colour codes (a traffic light style system) and an example of an IT-supported system based on a freeware software package.

The two systems are complementary, i.e. both of them build on strategy maps to visualize performance and in fact the user of a manual control system can any time upgrade to an IT supported system. Their main difference is the different level of operation complexity and application spectrum. In a nutshell, manual strategy control systems are easier to operate but also more limited in their application spectrum.

Table 56 provides a summary overview of the strengths and weakness of the two control systems.

Table 56: Strengths and weaknesses of different strategy control systems

	Strengths	Weaknesses
Manual control systems	Low-tech and as a result easy to use. The system operator can quickly comprehend its setup and operation routines. Cheap. No upfront investment other than training of the system operator and development of the control tools required. Cost-effective. Very low costs of ownership. Quickly established.	Limited capacity to manage complex data streams. Because the system has no computer support, all data collection and tabulation has to be carried out by hand by the system operator. Limitations in visualizing data effectively and in real-time. Unlike computer-based control systems, the system operator may have to redraw the strategy map each time to visualize the status quo. Also, gradual fine change goes largely unnoticed by the system.
IT-based control systems	Capacity to process complex data streams in real-time. The measurement instruments on the digital enterprise "dashboard" are immediately updated to reflect the new status for each performance indicator. Furthermore, if you place the "dashboard" on your company intranet or your company website, all stakeholders can continuously track the implementation progress. Capacity to visualize gradual change in the performance patterns of an organization. Unlike the traffic light system, the electronic gauges and dials allow the system operator to specify performance down to single digits.	Operations complexity. To install the system, computer hardware is required. To operate the system, the system operator needs to be trained. Also, the stakeholders might need training how to interpret the monitoring data on the "dashboard", since the gauges and dials are often not as self-explanatory as traffic lights. More vulnerable to malfunctions – if the hardware breaks down or the software gets infected with a virus, the system is literally "down".

Manual monitoring and evaluation with a traffic light system

In a traffic light system, the monitoring data is collected and processed manually. The performance status for each measure is visualized with colour codes organized like traffic lights on a printout of the strategy map.

The traffic lights translate the data into a trend signal that is intuitively understood by all stakeholders. The colour red signals clear underperformance while the colour green signals performance that meets the set targets.

The colour amber signals a transitory status where performance is close to the actual target. For example, if your business has set "long-term customer relationships" as a business objective, and measures performance along the indicator of "repeat usage" of your products, the traffic light next to the indicator shows whether repeat usage is in line with growth targets.

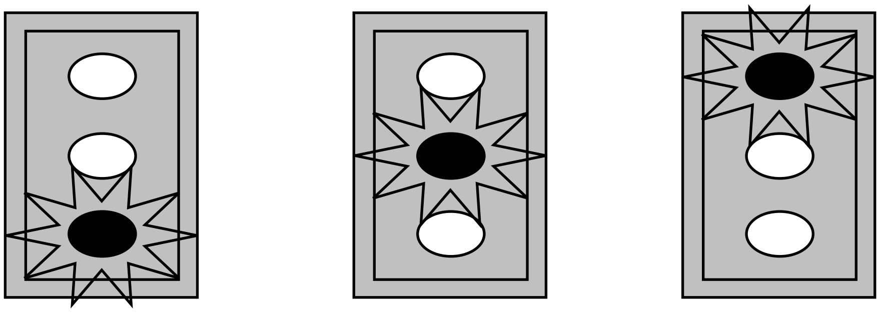


Figure 46: Colour coding with the traffic light system (1)

Refer to figure 50 for an example of a color coded strategy map for a consultancy company.

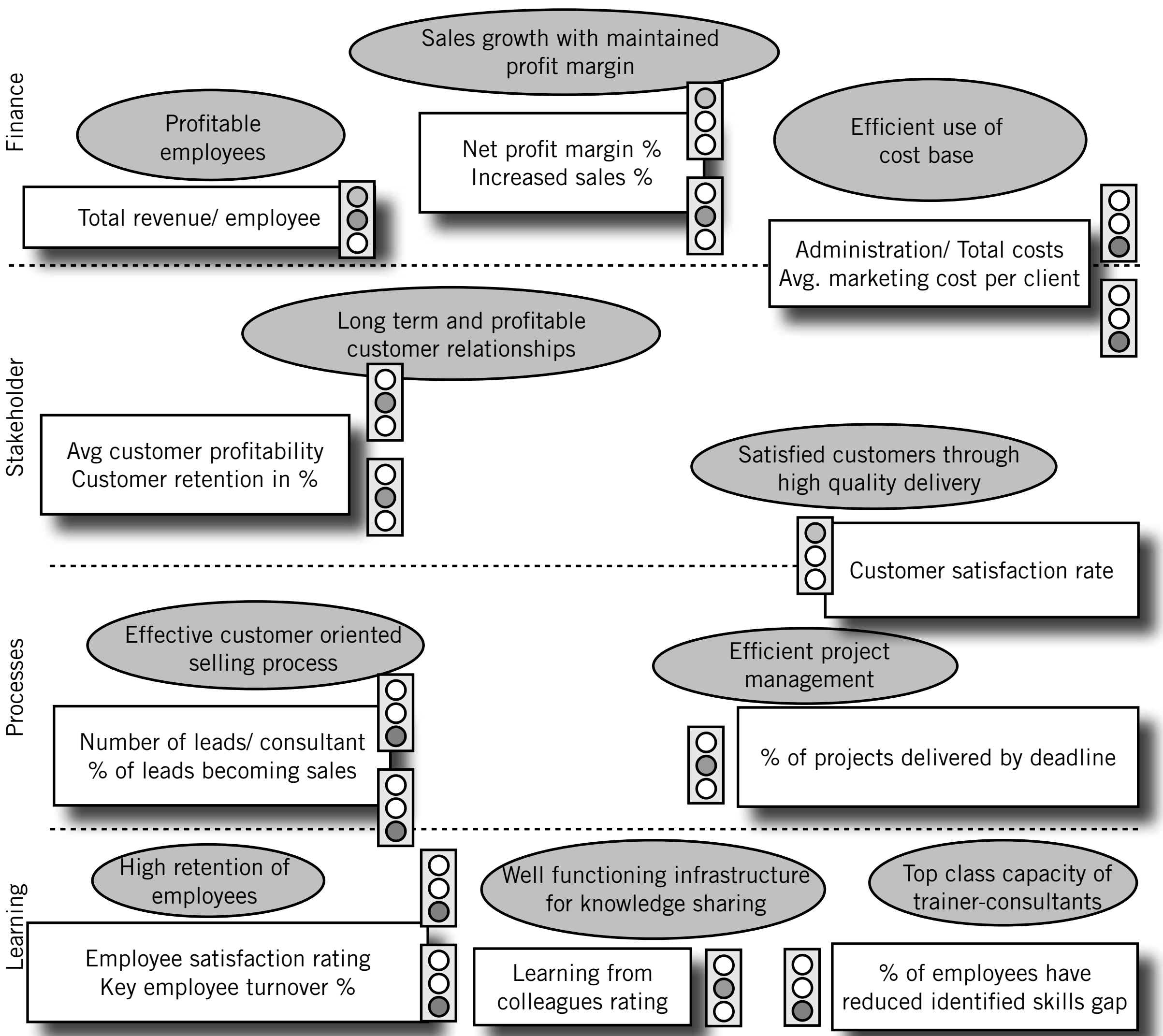
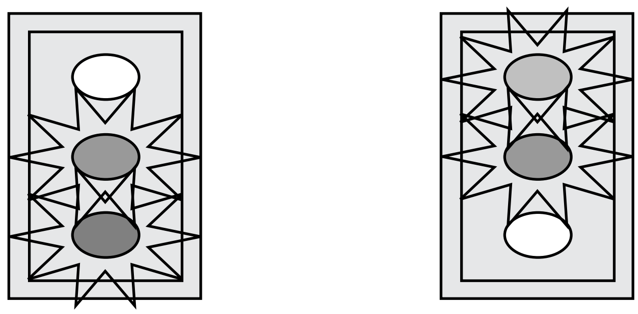


Figure 47: Example of a colour coded strategy map

As the figure 52 illustrates, a colour coding system based on the traffic light system is comparatively crude: Performance is either good, in a state of transition from good to bad, or bad to good, or bad.

To partly overcome this problem and to make the colour coding more sensitive for gradual shifts in performance, the traffic lights can be switched on green-yellow, or yellow-red, thus indicating a transition from one status to another.



Transition status: Trend pointing towards performance in line with set targets

Transition status: Trend pointing towards under-performance

Figure 48: Colour coding with the traffic light system (2)

To set the traffic light for a given performance measure, it is necessary to first define thresholds for "non-satisfactory", "satisfactory" and "fully satisfactory" performance for each performance measure of your business growth strategy.

For example, if you have set "long-term customer relationships" as a strategic objective in the marketing dimension and chosen the "percentage of customers at least satisfied with the quality of a given product" as the performance measure, the next step is to fix thresholds for "fully satisfactory", "satisfactory" and "less than satisfactory" performance on a scale from 0-100% customer satisfaction. In the process, the measures and thresholds of the scale need to firmly reflect the measures and targets set for your business growth strategy.

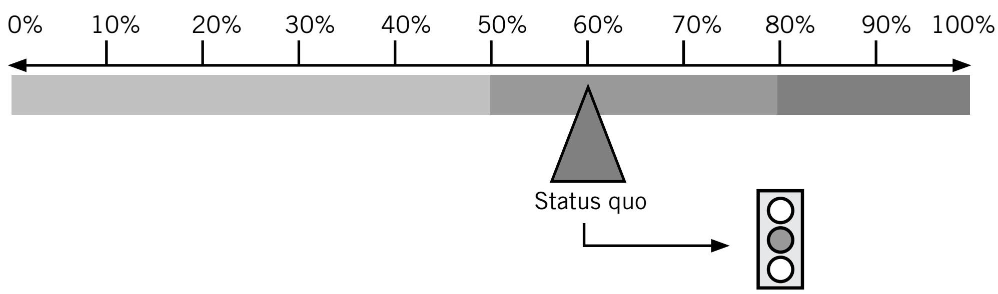


Figure 49: Example of colour coded performance thresholds (1)

Refer back to chapter 2 for a list of the performance measures and targets of your business growth strategy.

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If you want to make the colour coding more sensitive for gradual shift in performance and be able to switch the traffic lights on yellow-red and yellow-green, you must define a switching point on the scale. The graph below illustrates how to set a switching point.

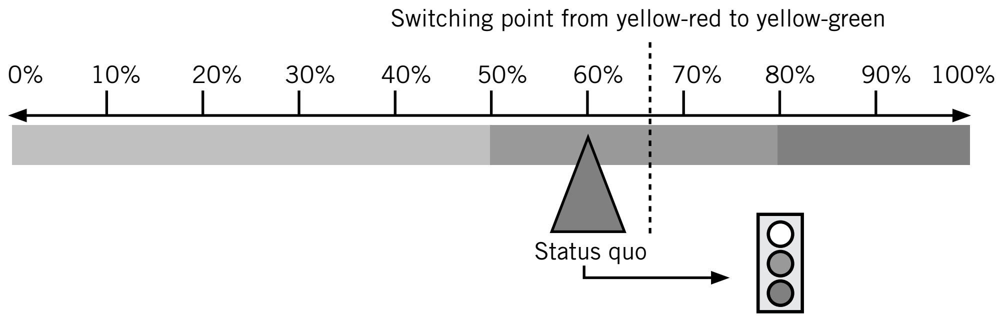

Figure 50: Example of colour coded performance thresholds (2)

Computer-supported monitoring and evaluation

Computer-supported controlling means that the system is IT-based and uses a software application to store, process and visualize monitoring and evaluation data. Stand-alone control system software will typically enable you to set up a so-called digital enterprise "dashboard" built on your strategy map. In the "dashboard", you assign each objective a digital gauge to measure performance. The gauges are electronically fed with information entered by the system operators through a data interface "behind the dashboard". At the most advanced level, the data interface behind the digital enterprise "dashboard" is "wired up" with the electronic management information system of the business. In this case, the "dashboard" turns into the electronic "cockpit" of the business and reflects the strategy implementation status in real-time, e.g. as an activity in pursuit of business growth is carried out.

The figure 56 illustrates an example of a digital enterprise "dashboard".

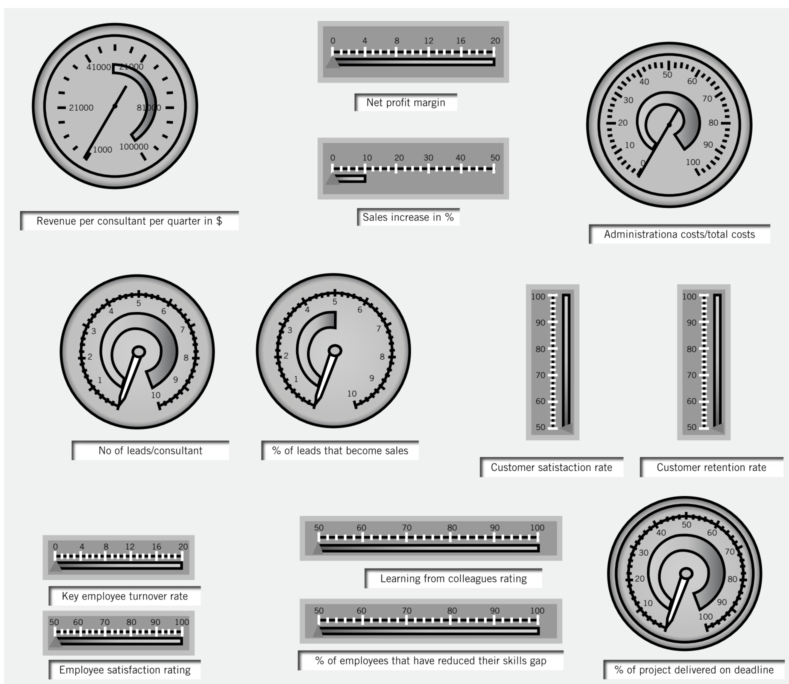

Figure 51: Digital organization "dashboard"

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2. Monitor the strategy implementation progress

In the second step, you use the strategy control system to monitor the strategy implementation process. To this end, you need to choose monitoring tools and methods and a data management mechanism that suits your business. Furthermore, you need to agree on the interpretation of the monitoring data.

Monitoring tools and methods

To collect the data needed to measure performance, you can introduce so-called performance measurement cards. In a nutshell, a performance measurement card specifies which data is collected, to which performance indicator it relates (and to which strategic objective this indicators relates), how often it is collected, and who is in charge of collecting it. The card also shows the current indicator status as compared to the ultimate performance threshold, the baseline figure and, where applicable, the annual milestones.

The performance measurement card can be used for both a manually operated traffic light strategy control system and a software-supported system because the monitoring information required to feed the indicators is the same in both cases. The main difference between the systems is how the information is collected, processed, managed, and visualized (see below, under data management, for more information).

Illustrated overleaf is a template of a performance measurement card, complete with an example of how data could be recorded for the indicator of “employee retention” in the “learning” perspective of a business. In this example, the HR Manager is responsible to provide the monitoring data to the managing director, and the main data source is the salary system of the company.

The monitoring data should be collected as a matter of routine since the underlying purpose of the monitoring effort is to furnish all stakeholders with timely information on the progress of implementation the strategic initiatives in pursuit of the business vision. To minimize the data collection effort for the stakeholders, the monitoring routines should be synchronized with the existing data collection routines in your business and the data should be easily accessible.

Ideally, all measures should be updated in real time to ensure that the implementation status reflected in the strategy map represents the actual status. For this reason, and as discussed in the first module of this training manual, a business should choose performance indicators that can be frequently and simultaneously measured.

Data management

It is also very important in monitoring to devise a mechanism for safely storing monitoring data. Storing the monitoring data serves two main purposes: to verify data in retrospective, and to allow for comparison of performance over time.

Table 57: Data reporting form

<table>
<tr><td colspan="5">Management profile</td></tr>
<tr><td colspan="5">Prospective ❑ Financial ❑ Stakeholder ❑ Process ■ Learning and gross</td></tr>
<tr><td colspan="3">Strategic objective:
L & G High retention of key employees</td><td colspan="2">Measure: Empoyee turn over</td></tr>
<tr><td colspan="3">Calculate for the measure:
Number of employees that left the last
12 months/total employees</td><td colspan="2">Status as of 01/07/2006:
17%</td></tr>
<tr><td colspan="2">Data source:
Salary system</td><td colspan="3">Update frequency:
❑ Monthly
❑ Quarterly
■ 2 Year
❑ Annual

Review frequency:
Monthly
❑ Quarterly
■ 2 Year
❑ Annual</td></tr>
<tr><td colspan="5">Action to implement and earliest available data:
REQUEST HT MANAGER TO SUPPLY THE EMPLOYEE TURNOVER FIGURES</td></tr>
<tr><td colspan="5">Responsibility</td></tr>
<tr><td colspan="2">Target setting:
Mamanging Director with
HR manager</td><td>Accountabiliyty for results (Objective owner):
Managing director</td><td>Tracking/ reporting responsibility:
Person
HR manager</td><td>Accountable for thedev't of the measure:
IBID</td></tr>
<tr><td>Ultimate target: 10%</td><td>Baseline in 2005: 22%</td><td colspan="3">Annual milestones: 2006 14% 2007 12% 2008 11% 2009 10%</td></tr>
</table>

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The ability to verify data in retrospective is an important aspect of system transparency, and builds trust regarding the accuracy of management information. The ability to measure performance over time, in turn, paves the way for the prediction of trends – a key aspect for reliable business forecasting.

A simple way of storing monitoring data in a manually operated system is to file the performance measurement templates. Furthermore, it is recommended to file the strategy map snapshots of the strategy implementation progress produced by the system operator. The performance measure templates can be used to produce data time series about a given indicator while the snapshots of the strategy maps allow for the comparison of performance along the colour codes of the traffic lights.

In a computer-supported monitoring system, the data is stored automatically by the system. The system allows you to compare monitoring data along timelines and to visualize your findings in charts and graphs.

Interpretation of the monitoring data

A key issue in effective monitoring is the ability of the management – and by extension of all business stakeholders – to interpret the monitoring data. The main challenge, here, is to read a performance measures in context with other measures, and in the light of your overarching growth strategy.

To begin with, your own ability, and the ability of other business stakeholders, to interpret the findings depicted on the strategy map will largely depend on the readability of the matrix depicted on the map. As discussed earlier in this manual, a strategy map with high readability will strike a fine balance between the intent to depict the true complexity of the game plan and the need to emphasize the main cause-effect relationships.

Also, a good strategy map will build on specific objectives, clear measures, and realistic targets, and rely on data inputs that can be verified with a measure of objectivity.

> Refer back to chapter 1 and 4 for more information on how to set specific objectives, specific measures, and realistic targets for your growth strategy, and how to draw up cause-effect relationships in a strategy map.

Assuming good readability, the next step is to train your mind in interpreting the data based on the analysis of cause-effect relationships between the objectives and their corresponding measures.

The colour coded strategy map of the consultancy company described earlier in this chapter provides a good example how to interpret the performance measures in context. The snapshot of the strategy map indicates that the company is at a comparatively early stage of the strategy implementation process.

The company seemingly has invested in the “learning”-related attributes of business performance and also made good progress in implementing strategic initiatives related to internal processes. From these two perspectives of the strategy map, traffic lights linked to the performance measures are either switched on green or yellow.

However, these initiatives - and the corresponding initiatives launched in the finance and stakeholder perspective of the strategy map - are yet to develop their full impact on stakeholders and sales. From these two perspectives, traffic lights are switched either on amber or red. The exception is the growth objective related to the efficient use of business resources. Here, the initiatives seem to have translated into a lower cost base that is in line with performance targets.

From the analysis of the strategy map snapshot, the management of the business might conclude that it needs to further emphasize strategy initiatives related to the “stakeholder” and the “finance” strategy perspectives during the strategy implementation process, and more in particular to focus on marketing to boost market outreach. Along the way, the management might need to ensure that earlier achievements made with regard to an effective customer-oriented selling process and efficient project management might be more actively exploited for the urgent improvement of customer relationships.

A secondary focus of activities of this business could be to further shape the in-house infrastructure for knowledge sharing, and namely improve mechanisms enabling learning on the job from colleagues. Furthermore, timely delivery of services might require more attention.

3. Evaluate the strategy outcomes

In the third step, you evaluate the outcomes of your business growth strategy. To this end, you select and then apply evaluation methods and tools that suit your own business. You also need to explain how to read the evaluation results, and how to feed these results back into the design of the next strategy planning loop.

Evaluation methods and tools

As indicated at the outset of part IV of this manual, evaluation is different from monitoring. Monitoring is a continuous exercise and aims at tracking progress against a set of performance measures while evaluations are carried out periodically and assess the outcomes of business strategy in retrospective.

Evaluation exercises build on the results of the monitoring effort, and take the monitoring data into account when assessing strategy outcomes. For example, any evaluation will start with an assessment of strategy outcomes measured along the indicators of achievement/ key performance indicators fixed at the outset of the strategy implementation process. In the process, evaluations will pay particular attention to the lag indicators in the strategy map.

Lag indicators, as stated, reflect the outcome of past initiatives to boost business competitiveness. They are often quantitative, and based on hard data (and are thus thought to be more reliable), and they frequently relate to financial performance – a key evaluation parameter particularly for shareholders.

Refer back to chapter 1 for more information on lag indicators.

Beyond the analysis of monitoring data, evaluations also tap into other information sources. Another complementary evaluation method is to qualify the strategy outcomes by way of seeking feedback directly from the core business stakeholders specified in the strategy map.

The purpose of these consultations is to verify whether the intended benefit of the various initiatives launched as part of the growth strategy have materialized for a given stakeholder group, be it customers, employees, the local community or shareholders. The purpose of these consultations is also to test whether the assumed cause-effect relationships between the strategic objectives in the strategy map hold, and whether they can explain success or failure of the growth effort.

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To seek stakeholder feedback, you can, among others,

- **conduct** telephone interviews, organize a mailing survey, or set up a focus group with customers
- **organize** individual meetings or group meetings with shareholders
- **set up** a feedback/ suggestion box for your employees
- **meet** with your employees/ representative bodies set up by your employees
- **systematically** screen the local media for coverage of your business
- meet with local community leaders and representatives of other stakeholder groups that influence the competitiveness of your business
- **consult with direct competitors under the roof of local sector associations or other** representative bodies of your industry

In cases where you seek interaction with larger groups by way of telephone interviews or mailing surveys, it is recommended that you structure the data collection effort with a standardized questionnaire. In the case of focus group discussions and group meetings, it is recommended to work along a list of open questions to guide the communication process.

The questions to ask during these feedback exercises will depend on the stakeholder group but the purpose is always the same: to test your assumptions about the benefits that have materialized for these stakeholders as a result of your strategy.

How to interpret and use the evaluation results

To unlock the full benefit of the evaluation as a learning opportunity for your business, you must train your mind how to qualify the evaluation findings. To begin with, you need to double check on the quality of the data sources for the evaluation. As with the ability to read monitoring data, the ability to read evaluation data largely depends on the precision of the strategy map and the reliability of the data sources.

For example, remember that the map can imply cause and effect relationships between your initiatives and stakeholder benefits that do not really exist. You may have had only hypothesized about these relationships when you drew the map.

> Refer back to chapter I for a critical reflection about performance measures, and to chapter 2 for the limits particularly of market research on customers.

To double check the evaluation results, you need to compare the stakeholder feedback with the findings from your assessment of the strategy outcome along the performance indicators. More in particular, you need to ask yourself whether there is a contradiction between the findings from the assessment of the performance indicators and the findings produced by the stakeholder consultations.

A contradiction in your findings could point towards a technical problem, for example, that an indicator was unsuitable to measure the attribute of business performance, that the data used to feed the indicator was unreliable or manipulated, that the evaluation methods and tools did not produce reliable results, or that the performance target was unrealistic in the first place.

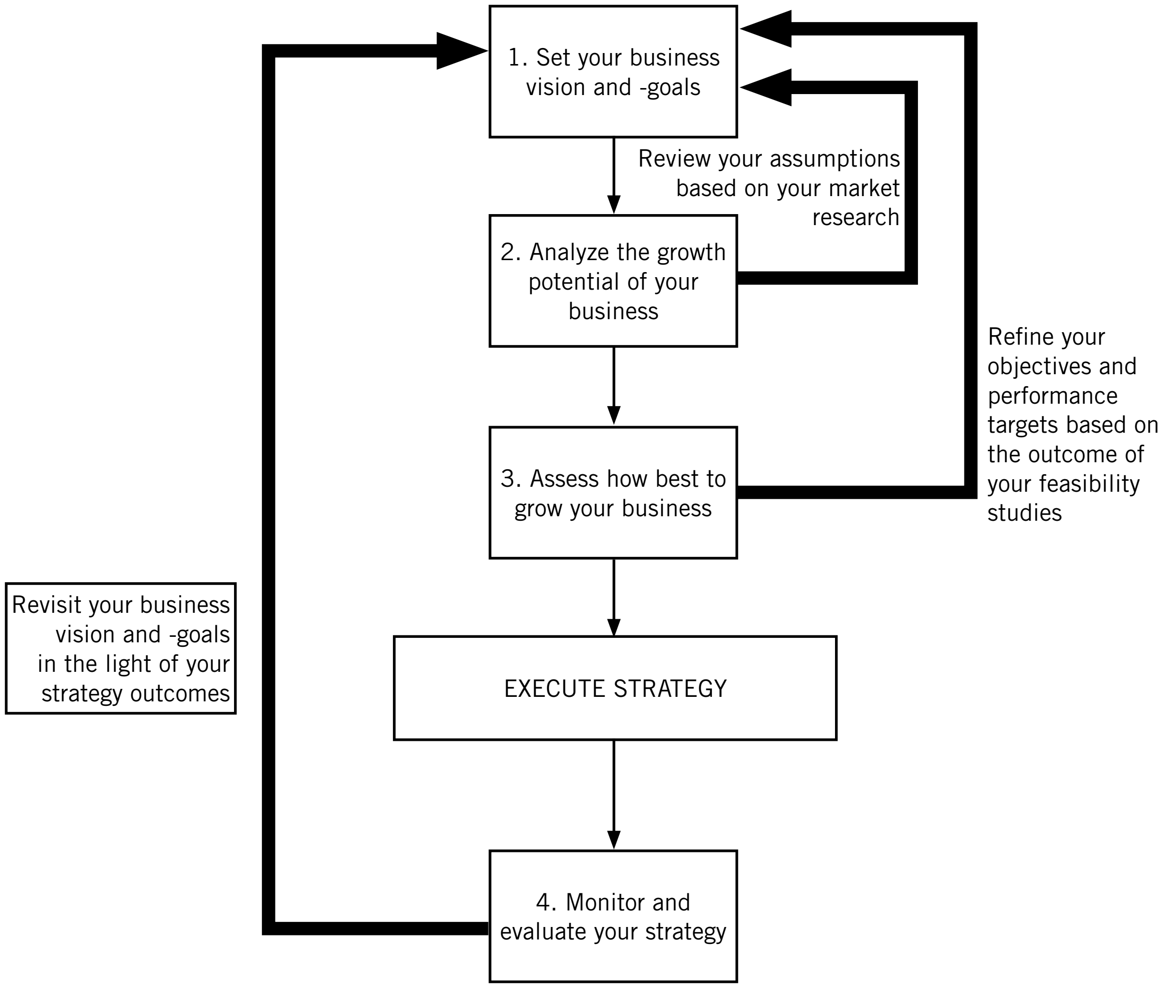

Figure 52: Learning loops towards systemic competitiveness of your business

A contradiction could, however, also point towards a weakness of your strategic initiatives and mean that your assumed cause-effect relationships between your business objectives do not hold. In the first case, you need to fine-tune the strategy control system of your business while in the second case, you need to review the intervention mix of your growth strategy.

Once you have verified the underlying assumptions of the strategy map, you next need to reflect on the implications of your strategy outcomes for the design of future strategies. To this end, ask yourself first whether you have "done things right" (efficiency) when you implemented your strategies, and whether you have "done the right things" (effectiveness) to achieve your objectives. The distinction between effectiveness and efficiency is important because it is possible that a business implements an initiative with success but without achieving the overarching objective.

For example, the strategy of a business to boost sales with new products might have failed even though its R&D division successfully completed a new product development

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initiative. In this example the management has to ask: Did somebody in the business fail to do things right or did the business fail to do the right things? In the first case, the root cause might be underperformance of a department while in the second case the root cause might be a misdirected business strategy.

Once you have identified on the root causes behind the success or failure of your business strategy, you need to consolidate these findings in a set of conclusions for how to further fine-tune business strategy in the future. As indicated in the graph overleaf, the outcomes of one strategy loop determine the analytical framework of the next strategy loop.

Your ability and willingness to incorporate your learning lessons about success and failures into the design of future growth strategies will effectively determine the capacity of your business to step-by-step strengthen its systemic competitiveness.