

# FORMULATING STRATEGY

## CHAPTER 8

### GENERIC STRATEGIES

When most people think about organizational strategy, they usually think about a **business-level strategy**, *which describes the combination of goals, plans, and actions that an organization in a specific industry uses to accomplish its mission*. For example, a trucking company like Reimer Express uses a business-level strategy to compete in the transportation industry. Business-level strategies are also used by managers of non-business organizations, such as a thrift store operated by the Salvation Army. While each organization will have its own distinct strategy, there are several “generic” strategies that managers may adopt and adapt for use in their organization.

#### The FBL approach to generic strategies

- A **cost leadership strategy** is evident when an organization has lower financial costs than rivals for similar products, so that it can capture more profit and/or a higher market share via lower prices.
- A **differentiation strategy** is evident when an organization offers products or services with unique features that cost less for it to provide than the extra price which customers are willing to pay for the features.

#### The TBL approach to generic strategies

- A **TBL cost leadership strategy** is evident when an organization has lower financial costs than its rivals thanks to reductions in its ecological and/or social negative externalities, thereby contributing to its financial well-being. In recent years Walmart has adopted a TBL cost leadership strategy, by reducing its use of fossil fuels (e.g., by using a more fuel-efficient fleet of trucks, by using LED lighting in its stores) and minimizing packaging.
- A **TBL differentiation strategy** is evident when an organization offers products or services with socio-ecological benefits that cost less for it to provide than the extra price which customers are willing to pay for them. For example, thanks to a being able to charge a higher markup for their produce, organic farmers are generally more profitable than conventional farmers. Whole Foods became a leading grocer by offering organic foods to consumers, and helped to grow the larger organic eco-system.

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**Strategy** refers to the combination of goals, plans, and actions that are designed to accomplish an organization’s mission.

**Strategic management** refers to the analysis and decisions that are necessary to formulate and implement strategy.

Formulating strategy can be described as unfolding in a four-step process: 1) establish mission and vision; 2) analyze internal resources to identify strengths and weaknesses; 3) analyze external forces to identify opportunities and threats; 4) choose and develop the strategy.

While this is a useful way to think about formulating strategy, the four steps are not as neatly laid out or linear in real life and, as will be described in the Chapter 9, in reality some of the most important strategy formulation happens concurrently with strategy implementation.

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## The SET approach to generic strategies

The SET approach uses two qualitatively different generic strategies: minimizer and transformer.

A **minimizer strategy** is evident when an organization minimizes negative socio-ecological externalities while ensuring that it remains financially viable. A minimizer strategy is evident at Seventh Generation, a founding B Corporation. Seventh Generation provides “cleaner and greener” products for household and personal care (e.g., ranging from laundry detergent and household cleaners to feminine care). Founder Jeffrey Hallender is passionate about reducing the negative socio-ecological externalities created by business. The desire to minimize externalities is evident in the firm’s product development standards, ingredients, and transportation choices. It reduces waste, GHG emissions, and has eliminated the use of toxic materials.

Glimpses of a minimizer strategy are often evident in the TBL cost leadership strategy. However, unlike the TBL cost leadership, the minimizer is not limited to reducing only those negative externalities that enhance on organization’s profits. Consider the explanation Bill Gates gives for why millions of children have died of diseases even when medication costs less than one dollar per person. He suggests that it is not in the financial interest of FBL and TBL companies to do anything to save the children: “The market did not reward saving the lives of these children, and governments did not subsidize it.” In other words, firms can make more money doing other things rather than helping these children. The increased flexibility that SET organizations enjoy precisely because they do not need to *maximize* profits gives them greater latitude to enhance value creation in areas of ecological and social well-being (e.g., helping the socially marginalized) that would not be considered profitable enough by FBL and TBL firms.

A **transformer strategy** is evident when an organization creates positive externalities, often by adding value to resources that were previously under-appreciated or wasted. A transformer strategy is apparent, for example, in an organization that recycles tires and uses them to make garden hoses, office supplies, floor mats, and road surfacing. A transformer strategy is also evident in volunteer agencies that encourage senior citizens to volunteer in after-school programs that help children with reading difficulties. Terracycle, Inc. was founded based on an ecological transformer strategy when founder Tom Szaky discovered he could profitably take waste from institutional kitchens (like the university where he was a student), feed it to worms, and sell the worms’ excrement in used soda bottles as fertilizer. Today Terracycle transforms (“upcycles”) a wide variety of consumer waste items into marketable products, working with school recycling programs and other large corporations who want their after-market packaging to be recycled into saleable products.

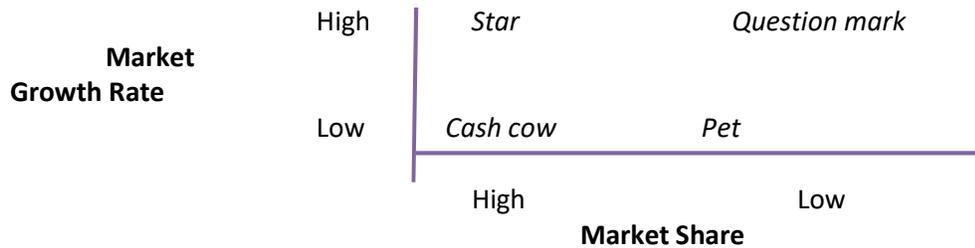
A **compounder strategy** is evident when an organization simultaneously follows both a minimizer and a transformer strategy, thus reducing negative externalities and enhancing positive externalities. In fact, many organizations that have primarily a minimizer or a transformer strategy will also have elements of the other. A compounder strategy is evident in an organization like Habitat for Humanity, which transforms waste via their ReStores, transforms lives by enabling people who otherwise would not be able to afford it to live in their own homes, and minimizes use of fossil fuels by building energy-efficient homes. Firms can work together in community to implement a compounder strategy; this allows them to create value together that they would not be able to create independently. Glimpses of this can be seen in the industrial ecological community in Kalundborg, Denmark, where different organizations transform each other’s “waste” into valuable inputs, significantly minimizing waste and converting it into valued resources.

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### Conventional portfolio matrix based on FBL management

Perhaps the best-known FBL tool for business portfolio planning was developed by the Boston Consulting Group and is called the **BCG matrix**, which classifies each strategic business unit according to (a) its market share, and (b) the rate at which its industry is growing (see Figure 8.3).

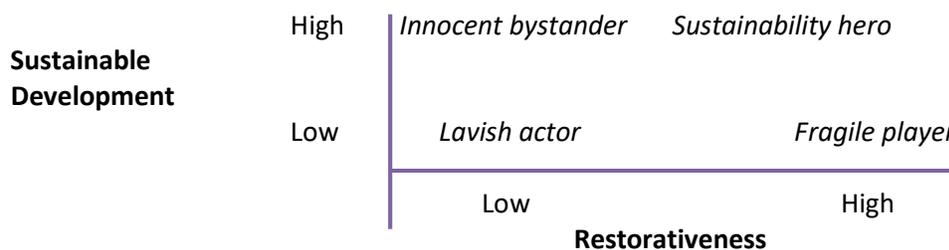
**Figure 8.3: BCG portfolio matrix for managing diversified organizations**



### An alternative portfolio matrix based on TBL and SET management

From a TBL or SET perspective, a significant weakness of the BCG portfolio matrix is its total disregard of issues related to socio-ecological well-being. This shortcoming can be addressed by developing a 2x2 framework that is relevant for TBL and SET managers (see Figure 8.4). The vertical dimension is *sustainable development*, which focuses on how effectively an industry reduces its socio-ecological negative externalities. Managers who are interested in reducing or minimizing negative *ecological* externalities will be less attracted to, say, the conventional automobile industry and more attracted to software that enables virtual travel (e.g., video conferencing). Managers who are interested in minimizing negative *social* externalities will be less attracted to the garment industry (because many workers are poorly paid) and more attracted to the software development industry (which has relatively good working conditions). For some industries there is considerable debate about sustainability, such as whether hydro or wind power is more sustainable in the long-term. At other times there is general agreement, such as coal being less sustainable than hydro or wind power.

**Figure 8.4: A TBL/SET approach to a corporate strategy portfolio matrix**



The horizontal dimension, *restorativeness*, refers to how effectively an industry creates positive socio-ecological externalities. A high level of restorativeness is evident in industries where organizations enhance the socio-ecological well-being of their stakeholders. For example, an industry would score high in ecological restorativeness if it takes carbon out of the atmosphere and uses it to enrich the soil (e.g., Conservation Agriculture). An industry would score high in social restorativeness if enhanced mental health (e.g., Big Brother/Sister organizations, national parks, and retreat centers).

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Dichotomizing these two dimensions—sustainable development and restorativeness—yields four types of organizations. A **sustainability hero** *reduces or minimizes negative externalities (high sustainable development) and enhances positive externalities (high restorativeness)*. An example of an *ecological* sustainability hero is an organization that provides curb-side composting services. Rather than throw organic waste into landfills, where it may contribute to methane gas release, it can be composted and returned to the soil, where it provides nutrients to grow healthy food. An example of a *social* sustainability hero is a seniors' center where retired people (who are looking for more meaningful things to do) can participate in physical activities and adult education, or in after-school programs that help young children with reading difficulties. Such industries should be encouraged and invested in, and lessons learned and practices developed in these industries be transferred to others.

TBL managers may wish to diversify by investing in an **innocent bystander**, *which has high sustainable development but low restorativeness*. For example, industries related to renewable energy or electric cars are designed to reduce GHG emission, but they do little to restore existing waste. However, restorativeness could be added if, for example, a source of electricity or an automobile engine were developed that was powered by carbon dioxide (mimicking photosynthesis). SET managers may enter this industry if they believe they can help to add restorative dimensions to it, and thereby help move it to becoming a sustainability hero.

A **fragile player** *creates both positive and negative externalities*. For example, the Children's Wish Foundation provides trips to Disneyland for children with life-threatening illnesses. This provides positive social externalities (joy and respite for the families), but also creates a negative ecological externality (the pollution that is generated by the air travel). Managers may try to create substitute products and services (possibly from other industries) that create similar positive externalities but reduce negative externalities. For example, rather than fly a family to Disneyland, families could be treated at a local resort or amusement park. Managers should enter this industry if they believe they can help to increase its level of sustainable development, and thus help move it to becoming a sustainability hero.

Finally, **lavish actors** *are low on both sustainability and restorativeness*. These industries represent great opportunities for positive change, either from within or by rendering them obsolete. For example, like other firms in its industry, the Statoil oil refinery in Kalundborg, Denmark at one time created negative ecological externalities while doing little to transform the waste of others. Now managers at the refinery have begun to utilize "waste" steam from the coal plant, and have improved their refinery's filtering process to emit less wasteful sulfur gas and instead provide sulfur inputs valued by neighboring companies. However, it might be even better if the oil refinery were made obsolete by using its profits to invest in advances in, say, solar energy.

Using an alternative matrix like this—in contrast to the conventional BCG portfolio matrix—provides a very different frame of reference with regard to choosing which industries to enter, how to move funds from an SBU in one quadrant to an SBU in another, and what sorts of products to invest in or bring to market. This matrix can also be used in non-business organizations. For example, imagine what would happen if governments used the matrix—with its explicit attention on sustainable development and restorativeness—to make decisions about the services they provide with respect to waste removal, caring for seniors, education, health care, and so on. That could unleash powerful entrepreneurial forces to increase the sustainability of how we live.

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