# *Strategic Management 4th edition Rothaermel Solutions Manual*

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# CHAPTER 2

# Strategic Leadership: Managing the Strategy Process

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# Teacher's Resource Manual: Implementation Guide

This improved **Teacher's Resource Manual (TRM)**, formerly the Instructor's Manual (IM), supports delivery of your chosen curriculum and pedagogy. This manual contains more than just guidance on how to cover concepts discussed in the fourth edition of *Strategic Management*; it also provides tips and best practices for how to utilize the full product suite (from the textbook to SmartBook® to Connect®). In addition, this manual includes a variety of supplemental teaching resources to enhance your ability to create an engaging learning experience for your students. Regardless of whether you teach in face-to-face traditional classrooms, blended (flipped) classrooms, online environments, or hybrid formats, you'll find everything you need in this improved resource.

The TRM follows the order of the textbook outline for each chapter and is divided into sections for each learning objective. Each section identifies the relevant PowerPoint slides from both the Lecture slides and the Supplemental Lecture slides (more on this below). This eases your preparation time for class as you can adjust slides as needed to ensure your students stay actively engaged throughout each session.

## What instructor resources are available?

Within each section of the TRM you will find an assortment of examples, exercises, Connect® Integration assignments, updates on the latest research, Strategy Smart Video discussions, and end-of-chapter discussion questions and exercises from which you can choose to enhance your students' learning and engagement. Where the activities are related to program-level learning objectives established by AACSB 2015 Standard 9, the learning objective has been identified for you.

Within the **Instructor Resources Tab,** located in the Connect® Library, the following **Instructor Resources** can be found:

- Teacher's Resource Manual
- PowerPoints (Accessible)
- Test Bank
- Create™ Case Support
- MiniCase Support
- Strategy Term Project
- Video Resources
- Capsim's Capstone Simulation

1) This **Teacher's Resource Manual** is posted by chapter.
2) Two sets of ADA-accessible **PowerPoints** are available with each chapter:
    a. *Lecture* slides cover chapter concepts and exhibits.
    b. *Supplemental Lecture* slides cover:
        i. ChapterCases
        ii. Strategy Highlights
        iii. Implications for Strategic Leaders
        iv. End-of-chapter myStrategy and Small Group Exercises
        v. Take-Away Concepts
        vi. Key Terms
        vii. Strategy Smart Video selections (not part of the book, but an additional resource found here)
3) **Test Bank** questions are posted by chapter. You will find a variety of question types within the test bank such as Matching, Ranking, Multiple Choice, Select-All-That-Apply, True/False, Short Answer, and Essays to test student mastery across Bloom's Taxonomy (i.e. Understand, Apply, and Analyze). Due to the evolving needs around generating high-quality print test experiences, McGraw-Hill Education provides a free copy of the industry-leading test generation software TestGen® to users (more details can be found within the Instructor Resources tab under "Test Bank"). Furthermore, due to its limitations to function with the latest browsers and operating systems,


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McGraw-Hill Education has discontinued EZ-Test Online. Some of the robust new features present in TestGen®, include:

- Cross-platform software compatibility with Windows and Mac
- Multiple LMS export formats, including Blackboard, Moodle, Desire2Learn, and Sakai
- Highly customizable formatting and editing option

4) **Create™ Case Support** (all cases are available in Create™ and selected ones in HBS)
   a. A *case matrix* that identifies the industry sector covered by each case, as well as the primary and secondary chapter alignments
   b. One-page *case abstract* for quick overview of each case
   c. *Case Teaching Notes* for instructor use only
   d. *Case Financials* in Excel files for the exhibit data in the most popular cases
   e. *Case Strategic Financial Analysis* template
   f. Instructions on *How to Download SEC Financial Data into Excel Spreadsheets*
5) **MiniCase Support** (all MiniCases are located in Part Four of the book)
   a. *MiniCase Matrix* that identifies chapter alignment
   b. *MiniCase Teaching Notes* comprising suggested answers to the MiniCase discussion questions. In some instance, they also provide specific additional article and video resources to accompany each MiniCase.
6) **Strategy Term Project**
   a. *Modules* for students on how to conduct a strategic management analysis of a company of their choosing; there is one module per chapter so that students can build upon their analysis and tie each section of their analysis to specific chapter concepts.
   b. *Running Case Teaching Notes* that cover the strategy term project found in Connect®. HP is used as the example firm to demonstrate how pieces of the term project align with each chapter.
7) **Video Resources**
   a. The *Video Grid and Guide* provides links to supplemental video resources to accompany both the MiniCases and full-length Create™ cases.
   b. The *Video Library* provides links to all the assignable videos in Connect®.
8) A link to ***Capsim's Capstone Simulation*** is provided; this simulation allows students to apply their knowledge of key strategy concepts.

## How can SmartBook® enhance my students' performance?

The LearnSmart®-powered **SmartBook®** is assignable through Connect®, McGraw-Hill's online assignment and assessment system. One of the first fully adaptive and individualized study tools designed for students, it creates for them a personalized learning experience, giving them the opportunity to practice and challenge their understanding of core strategy concepts. The reporting tools within SmartBook® show where students are struggling to understand specific concepts.

Typically, SmartBook® is assigned by module (chapter), and instructors can set which learning objectives to cover as well as the number of probes the student will see for each assignment. Instructors also set the number of points a SmartBook® module is worth in the course. Usually, applying a minimal number of points for completion of each module is enough to encourage students to read the chapter. Many instructors assign these modules to be completed *before* the class or online session.

SmartBook® provides several diagnostic tools for instructors to gauge which concepts their students struggle to understand. Below is the set of adaptive assignment reports available in SmartBook®:

- Progress Overview: View student progress broken down by module
- Student Details: View student progress details plus completion level breakdown for each module
- Module Details: View information on how your class performed on each section of their assigned modules
- Practice Quiz: This gives you a quick overview of the quizzes results for your students
- Missed Questions
- Metacognitive Skills


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By selecting "Module Details" the instructor finds the results for the students in the class overall. These details reveal where in the chapters students might be struggling. The module gives the chapter section, average time spent, average questions per student correct/total, and the percentage of correctness (number of assigned items). Information about the most challenging sections for students can help instructors refine the focus of the next classroom or online session.

For more detailed analysis, SmartBook® captures students' confidence in their competency using the "Metacognitive Skills" report. Below (a recreation of the Metacognitive Skills report), we find the second student is confident and mostly correct (91% in the correct & aware column) while the first student "doesn't know what she doesn't know" (39% in the far-right column).

| STUDENT | CORRECT and AWARE | CORRECT and UNAWARE | INCORRECT and AWARE | INCORRECT and UNAWARE |
|---|---|---|---|---|
| Student 1 | 61% | 0% | 0% | 39% |
| Student 2 | 91% | 0% | 3% | 5% |
| Student 3 | 81% | 0% | 0% | 19% |
| Student 4 | 83% | 0% | 0% | 17% |
| Student 5 | 76% | 0% | 3% | 21% |
| Student 6 | 66% | 0% | 9% | 25% |
| Student 7 | 77% | 0% | 3% | 12% |
| Student 8 | 91% | 0% | 2% | 7% |
| Student 9 | 93% | 0% | 2% | 5% |
| Student 10 | 70% | 0% | 6% | 25% |

## Application Exercises, Quizzes, and Test Bank

### What resources are available at the book level?

**Connect®** offers a wealth of content for both students and instructors. **Application Exercises** require students to apply key concepts to close the *knowing* and *doing* gap, while providing instant feedback for the student and progress tracking for the instructor. Before getting into chapter-level assignments, let's look at the book-level assignments available.

Four exercises are available for instructors to assign beyond the chapter materials. These are 1) MiniCase Case Analyses, 2) Case Strategic Financial Analyses (SFAs), 3) Financial Ratio Reviews, and 4) Case Exercises.

1) To encourage analytical thinking, each MiniCase from Part Four of the book is also an assignable application exercise (**MiniCase Case Analysis**). Each MiniCase is followed by four to five multiple-choice questions that assess students' understanding of the key issues presented in the MiniCase.
2) The **Case SFA** provides assignable key ratio comparisons for the Create™-only full-length cases available with the textbook. These require the student to analyze the case financial statements and calculate answers to several ratios in the spreadsheet. The Case SFAs engage students' financial analysis skills—skills many professors have identified as requiring more practice among their students.
3) **Financial Ratio Reviews** give students the opportunity to further hone their financial analysis skills; review exercises cover each type of financial ratio (activity, leverage, liquidity, market and profitability).
4) **Case Exercises**, which are new to this edition of *Strategic Management*, focus on the key symptoms and influences of a problem a firm might be facing, followed by a series of questions that help students understand how the firm eventually achieves a solution to that problem (or asks students to suggest a solution). Case Exercises for this edition accompany the most popular full-length cases: Amazon, Apple, BestBuy, Facebook, McDonald's, and Tesla.

### What resources are available for each chapter and how should I integrate them in my course?

Consider assigning one or two Application Exercises per chapter. They are built around chapter learning objectives, so the instructor can choose based on his/her focus for each specific chapter. Several types of application exercises are available in each chapter. The newest addition is the **Whiteboard Animation** series, comprising four- to five-minute videos on key concepts or concepts that tend to challenge students the most. Each animation is accompanied by three to four multiple-choice questions to check student attention and comprehension. Comprehensive **Case Analyses** and **Video Cases** each


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feature firms and industries different than those discussed in the textbook. Finally, **Click-and-Drag** exercises help students actively demonstrate their understanding of the associated learning objectives. Application Exercises can be assigned as preparatory exercises due ***before*** class (this is especially good for flipped classrooms), or ***after*** class as concept comprehension checks. Applications Exercises will generally be assigned as homework or practice as part of the overall class grade. A general rule of thumb would be to make application exercises worth 5 to 10 points each since these require time and thought.

To find the Applications in Connect®, go to "Add Assignment" and then select "Question Bank." Application Exercises are organized by chapter. Instructors have the option to select for one attempt only, but they may want to give students unlimited or multiple attempts on the first few assignments to give students a chance to learn and navigate the system. (As the course progresses, instructors may want to tighten up the time on task and reduce the number of attempts to complete each exercise).

Chapter **quizzes** and full chapter **test banks** are available for assignment, and like the Application Exercises, are organized by chapter. The value applied to each question should be relatively low because numerous questions are usually assigned for each chapter. As such, make these questions worth 1 or 2 points each. The feedback given to students is time-flexible. Selecting feedback to be displayed ***after*** the assignment due date helps to keep students from giving the correct answers to other students while the questions are still available. For this reason, it is suggested that no feedback to quizzes and test bank exams be made available until after the assignment is due.

### When should I assign these digital components?

To fully utilize the power of the digital components, instructors will often assign the SmartBook® reading and adaptive learning probes ***before*** class meets. Application Exercises can be completed either before or after class; if they are completed before class, they can sometimes serve as good springboards for class discussions. The chapter quiz makes a good check on comprehension of the material and may work best if assigned ***after*** each class period. The test bank serves as a good resource for building mid-term or final exams.

More detailed information on SmartBook® and Connect® is available through several resources at McGraw-Hill. A good starting point is your local Learning Technology Representative, who can be found here:
http://www.mheducation.com/highered/platforms/connect/features-educators.html

## Course Preparation

**Helpful Suggestions Regarding Assignment Policies:** Connect® gives instructors a wide array of flexibility in making assignments and creating grading policies. Instructors may choose to:

- assign as many assignments as appropriate given the level and time commitment expected for the class,
- determine point values for each question/application that works within the total course percentages,
- make available multiple attempts per assignment with options of accepting the *highest* score or *averaging* all the attempts together (several attempts are particularly good for homework assignments),
- deduct points for *late* assignment submissions (percentage deduction per hour/day/week/etc.) or create hard deadlines thus accepting *no* late submissions,
- show feedback on application/questions immediately upon submission **or** at the time the assignment is due for the whole class, create new assignments or questions from scratch, or edited versions from a variety of provided resources.

Throughout the TRM for each chapter, we will **integrate** materials from the Lecture PowerPoint slides, Supplemental Lecture slides, Connect® Application Exercises, end-of-chapter activities, and MiniCases. This integration of resources will allow for a cohesive presentation of the relevant resources at your disposal, helping you to convey these topics effectively and efficiently to your students.


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# CHAPTER 2

## Learning Objectives

LO 2-1 Explain the role of strategic leaders and what they do.

LO 2-2 Outline how you can become a strategic leader.

LO 2-3 Describe the roles of corporate, business, and functional managers in strategy formulation and implementation.

LO 2-4 Evaluate top-down strategic planning, scenario planning, and strategy as planned emergence.

LO 2-5 Assess the relationship between stakeholder strategy and sustainable competitive advantage.

LO 2-6 Conduct a stakeholder impact analysis.

In this chapter, we turn our attention to the role of strategic leaders in creating competitive advantage. We will cover how they guide the strategy process across different layers of large organizations. We will also spend some time on three different frameworks used to develop strategy. Expanding beyond a strictly financial perspective, we bring in a stakeholder strategy framework to look at the role of business more broadly in society.

A chapter opening case on Sheryl Sandberg COO at Facebook and two strategy highlights are included in the chapter for tangible applications of the theoretical frameworks discussed.

## ChapterCase 2 Sheryl Sandberg: Leaning in at Facebook

The opening ChapterCase discusses the important role of COO Sheryl Sandberg at Facebook. Ms. Sandberg was hired away from Google where she had been a vice president of global online sales and operations. In 2017 Facebook was the fourth most valuable company on earth and much of the business success can be attributed to Sandberg's contributions. When Sandberg was hired into Facebook, Myspace had more users. In addition to her accomplishments at Facebook, Sandberg is also a vocal advocate for expanding female leadership, particularly in technology firms.

### Instructor Supplement Slides 3-5

### Discussion Topics

Facebook has taken the whole issue of "fake news" and foreign backed election related news and events much more seriously now that they found evidence of Russian groups using the platform to set up over 60 protests on **both** sides of divisive issues leading up to the 2016 U.S. presidential election. (See "Russian-Backed Facebook Accounts Staged Events Around Divisive Issues," *The Wall Street Journal*, October 30, 2017.) Facebook, along with Google and Twitter all testified to the U.S. Congress in fall 2017 about Russian election related activity on their digital platforms. (See "Tech Giants Disclose Russian Activity on Eve of Congressional Appearance," *The Wall Street Journal*, October 30, 2017.) Conclusive actions are still under consideration by the firms and also the U.S. government in moving forward to prevent or mitigate foreign intrusion in future U.S. elections.


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# Consider This Discussion Questions

## Instructor Supplement Slide 6

1. **Describe Sheryl Sandberg's strategic leadership. Which qualities stand out to you, and why? Is she an effective strategy leader? Why, or why not?**

Based on the ChapterCase, it would seem Sandberg has brought considerable business skills into Facebook. Her contributions to their incredible success seem to be quite significant. She has a good working relationship with the CEO and founder. The chapter notes that she exhibits the Level-5 traits of enduring greatness through humble and powerful willpower and influence. She also has written a book about building resilience after very suddenly losing her beloved husband and her pathway back from that devastating loss. Profits from all her books go to a charitable foundation she set up to help others.

2. **What current challenges (as detailed in this ChapterCase) is Facebook facing? How should Sandberg deal with each of them? Please make specific recommendations.**

Some would argue Facebook has been a victim of its own success. Many of the issues it faces are due to the tremendous audience on the platform across the globe. Privacy and "click bait" news stories are issues across the internet and Facebook is a focal point for them due its singular size and contact time with users. The firm needs to be more transparent in the privacy default options which a large number of users just adapt. Sandberg could guide the firm towards more restrictive baseline settings and allow users to expand their privacy levels at their own discretion. On fake news, the firm needs to continue work on the algorithms to check the validity of news stories on the platform as the engagement with material grows. Students may also discuss the firm's appropriate use of data voluntarily provided by the billions of users on its variety of applications.

3. **What are the main issues Sandberg brings to the fore in her TED talk, titled "Why We Have Too Few Women Leaders"? You can view the 15-minute talk here: http://bit.ly/1czSD6n. How can your awareness of these issues help you to be a more effective strategic leader? How can these issues be addressed?**

The perhaps surprising data that the percent involvement of female leadership has plateaued across a variety of industries and countries in the last decade is one of the key issues Ms. Sandberg discusses. She also presents research showing that women are less assertive in professional environments than men. This is exemplified by a lower percentage of women asking for raises or seeking promotions than men. Awareness of these issues by both men and women can result in recognition that firms may need to do more to encourage a wider variety of candidates for promotions. Larger firms also need to continue to evaluate salaries of current employees to be sure there is not a gender bias present.

4. **Rumors persist that Sandberg might pursue a political career in the future (she was chief of staff to Larry Summers, former Treasury secretary under President Bill Clinton). Do you think Sandberg would make a good politician? Do you think the required qualities of strategic leadership are the same or similar in business and politics? Why or why not? Support your arguments.**

The chapter notes that Ms. Sandberg has already turned down several CEO opportunities so she does not seem to be motivated by power or prestige. In many ways this would make her a perfect candidate for public service such as holding political office. The leadership skills she developed and executed at Google and Facebook should be very useful running a major executive function such as a cabinet position (for example, Secretary of Commerce). The executive branch has many large organizations that could benefit from the flexibility and responsiveness someone with Ms. Sandberg's experience would bring in.

# Strategy Smart Video Example

## Instructor Supplement Slide 32


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This slide links to a 3-minute video of Sheryl Sandberg in 2017 describing how Facebook helps firms, especially small firms, grow and create more jobs.

# 2.1 Strategic Leadership

## LO 2-1 Explain the role of strategic leaders and what they do.

### LECTURE SLIDES 4–7

## EXAMPLES

You may want to open the topic of strategic leadership with a discussion about what a leader is. A video case that could be used to start that discussion is "What Is a Leader?" with Col. Gayle Colvin, U.S. Air Force, from Stanford Leadership in Focus.

Indra Nooyi, CEO of PepsiCo explains her passionate and personal reasons for driving the "Performance with a Purpose" strategy in this three-minute video interview available at: https://www.youtube.com/watch?v=BDTVdX-enr4. With respect to the Level-five pyramid of strategic leadership, she would be located at or very near the top of it. Nooyi has proven to have superior interpersonal, informational, and decisional skills. She has also proven to be capable not only of guiding a company the size of PepsiCo for over a decade, but of steering it toward a significantly different goal and convincing the organization to follow through by guiding with example and conviction.

✓ *AACSB 2015 Standard 9 Leading in organizational situations*

## LO 2-2 Outline how you can become a strategic leader.

### LECTURE SLIDES 8–12

You may want to give the students a deeper understanding of what the Level-5 leadership pyramid means for their own careers. You might describe it thus: Taken together, you become an effective and ethical leader by sequentially mastering each of the five steps in the strategic leadership pyramid. Your training in college allows you to become a highly capable individual who can make productive contributions. If you take a first job immediately after your undergraduate degree, you will likely begin your corporate career in a functional area that was your focus or major in college (e.g., accounting, operations management, marketing, finance). As you move down the learning curve through group work in college and on-the-job training, you develop the ability to work effectively with others to achieve team objectives. With these skills, you move to Level-2 leadership. As responsibilities come to you, you will be able to develop and demonstrate the ability to organize resources efficiently and effectively to achieve strategic objectives. At Level 3, you have become an effective manager—someone who produces results. Levels 4 and 5 require a stronger element of strategic leadership than the prior levels. When given the chance to work as a general manager (someone who has profit-and-loss responsibility for a unit or group), you will need Level-4 strategic leadership qualities. At Levels 4 and 5, you will have increasingly dramatic opportunities to put to use the AFI framework you've learned from this book: You will need to be able to present a compelling vision and mission to inspire others to achieve superior performance. Doing so requires an intimate understanding not only of the inner workings of your company (Chapters 1 and 2), but also of the external environment. The internal and external analysis concepts (Chapters 3 and 4) will help you lay the foundation to formulate strategies that can improve firm performance (Chapters 5 through 7). Having produced results at the business level, you might be tapped as the CEO of the company. At Level-5 strategic leadership, you need to reconcile a strong will and work ethic (which got you to the top) with the humility to lead a company by example. To do this effectively, you need a deep understanding of corporate-level strategy


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(Chapters 8 through 10) and organizational design (Chapter 11). You also will need to exhibit unfailing personal integrity (Chapter 12).


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## Strategy Smart Video Example

### Instructor Supplement Slide 30

This slide links to a 2 ½ -minute video of Jim Collins discussing what defines a Level-5 leader.

Strategic leadership refers to the behaviors and styles of executives that influence others to achieve organizational goals. The three roles of a leader are interpersonal, informational, and decisional. According to the upper-echelons theory, organizational outcomes including strategic choices and performance levels reflect the values of the top management team (the individuals at the upper echelons, or levels, of an organization). The theory states that executives interpret situations through the lens of their unique perspectives, shaped by personal circumstances, values, and experiences. The Level-5 leadership pyramid (Exhibit 2.2) is a conceptual framework that shows leadership progression through five distinct, sequential levels. Jim Collins in *Good to Great* found that all the companies he identified as great were led by Level-5 executives.

## End of Chapter **Ethical/Social Issues 2**

2. **This chapter discusses some of the key strategic leadership issues (such as privacy and fake news) facing Facebook leaders Sheryl Sandberg and Mark Zuckerberg. Consider other firms mentioned in the chapter such as Amazon, PepsiCo, Uber, VW, and Starbucks. What social and ethical issues do the leaders of these firms face today? Choose a firm or industry and explore the relevant controversial issues it faces. How should strategic leaders address the major issues you have identified?**

Instructors may want to guide the students to a particular industry based on current events. Uber's numerous ethical issues are discussed in the Chapter 12 case opener. VW had large scandals surrounding software work arounds that were designed to generate higher miles per gallon results than their vehicles actually produced. PepsiCo and Starbucks have to balance delivering cost effective products with sustainable suppliers and a greater awareness of healthy eating. Strategic leaders will address these type of issues rather than follow a tendency to ignore them until there is no other choice.

## Strategy Smart Video Example

### Instructor Supplement Slide 31

This slide links to a 15-minute TED talk by Sheryl Sandberg that discusses why we have too few women in leadership roles.

# LO 2-3 Describe the roles of corporate, business, and functional managers in strategy formulation and implementation.

### Lecture Slides 15–18


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connect INTEGRATION

## Interactive Labeling: Formulating Strategy Across Levels

This click-drag labeling activity starts with a brief case using IBM as an additional example of the different levels of strategy. This complements the book's discussion. The student must read the textbook and also the case provided here. Then, the student will drag the elements to the correct locations in both columns of this activity. Next the student will answer three related questions following the interactive activity.

- ✓ ***Difficulty**: Medium*
- ✓ ***Blooms**: Evaluate*
- ✓ ***AACSB**: Analytic*

## EXERCISE

This can be used as a small group exercise in class or as a quiz to assess decision making skills (ability to identify a problem). Assign five newspaper articles or mini-cases for students to read and ask them to identify for each one the firm's key problem and whether its solution will be a functional-, business-, or corporate-level strategy.

- ✓ *AACSB 2015 Standard 9 Framing problems*

Here are some possible examples that you might use:

| Source | Problem | Level |
|---|---|---|
| Porsche Mini Case | What is the appropriate level of product diversification from sports cars? | Corporate |
| Starbucks Strategy Highlight | Should we add a line of Frappuccino products? | Functional |
| Instagram | Can we gain revenue with advertising without losing our competitive advantage with users? | Business |
| Apple | How can Apple differentiate its next iPad more effectively from the Samsung Galaxy to increase customers' willingness to pay? | Business |
| Yahoo | Should we sell our stake in Alibaba? | Corporate |
| Twitter | How can we compete more effectively with Facebook for ad revenue? | Business |

# 2.2 The Strategic Management Process

## LO 2-4 Evaluate top-down strategic planning, scenario planning, and strategy as planned emergence.



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## LECTURE SLIDES 19-33

# EXAMPLES

Top-down strategic planning is typically performed by senior managers and strategy specialists on a 3- or 5-year cycle. The output is usually a detailed book (or PDF file these days) with analysis of current positions and plans for future growth. In scenario planning, critical elements are to create a diverse set of "what if" plans in the formulation stage and then to drive forward with a dominant strategic plan in the implementation phase. Planned emergence is the less formal process that tends to emerge from the "bottom-up" of the organization. The Mintzberg framework reflects the strategy that it may be driven from the top or the bottom of the organization. Exhibits 2.4 and 2.5, show how the AFI framework overlays on the top-down and scenario planning processes respectively. This provides an opportunity to walk through the strategy-making process.

To conduct successful scenario planning, managers need current information. The network-equipment giant Cisco Systems has invested huge sums in technology to generate just this kind of data. Cisco's senior executives can track daily customer order data from its sales teams around the globe with up-to-the-minute accuracy. Walmart's recently retired CEO Mike Duke indicates that he too is using real-time sales data tracking, enabling top executives to monitor daily sales of each of the over 8,500 Walmart stores worldwide in real time. With these real-time data systems, managers can identify emerging trends in each region and market segment long before they materialize in financial data. This in turn allows them to fine-tune their functional strategy with unprecedented accuracy and speed.

An unexpected event at the largest rail carrier in the world, Japan Railways, led to diversification from railroads into bottled water using an emergent strategy. Japan Railways was constructing a new bullet train through the mountains north of Tokyo, requiring many tunnels. In one of the mountains, persistent flooding caused huge problems. Engineers responded by drawing up complex plans to drain the water. Meanwhile, workers inside the tunnel were making good use of the water—they were drinking it. A maintenance worker suggested the water should not be pumped away but rather bottled and sold as premium drinking water because it tasted so fresh. Its source was snow pack, purified and filtered in the slow percolation process through the mountain's geological layers and enhanced on the way with healthy amounts of calcium, potassium, and magnesium. Eventually, Japan Railways set up vending machines on 1,000 railroad platforms in and around Tokyo, and home delivery of water, juices, and coffee followed. The employee's proposal had turned an expensive engineering problem into a multimillion-dollar business. Because Japan Railways was willing to define its business as broader than just being in railroads, it was able to capture the emergent strategy and diversify into drinking water. In contrast, given its product-oriented vision to be the safest, most progressive North American railroad, it is doubtful that CSR Railroad would have reacted in a similar fashion had it encountered the same serendipitous event.

A functional manager at IBM suggested entry into the emerging life sciences field. She saw a business opportunity for IBM, in which application of high-performance computing and information technology could solve thorny problems that accompanied data-intensive work such as decoding human genomes and furthering personalized medicine. IBM's general and corporate managers supported this strategic initiative, dubbed "information-based medicine." This new business opportunity generated more than $5 billion in revenue a few years later.

Patsy Sherman—Scotchgard—3M: In 1953 researchers at 3M were working with fluorocarbons to be sold as coolant liquid in air conditioning equipment. One of the researchers noticed, after accidentally spilling some coffee on her shoe, that the residue of fluorocarbons turned the coffee into small beads of liquids without staining. After observing this unique experiment Sherman contacted the chemist Sam Smith, and together they began developing a product that could actually repel oil, water, and other residues from fabric. In 1956 the Scotchgard protector was launched. What skills are needed to go from a coffee spill to an idea for a commercial product to meet a consumer need? You might discuss the role of absorptive capacity, deep understanding of customer needs, or intuitive thinking.

George de Mestral—Velcro: In 1948, when Mestral was returning from a nature hike with his dog, he noticed that both the dog and he were covered with burrs. Filled with an instant curiosity to determine what made this material so sticky on his


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clothes and the dog's hair, he immediately headed out to his microscope and observed the little burrs in order to try to understand why they were so incredibly adhesive. What he discovered from this serendipitous event is that the burrs contain millions of miniature hooks which allowed those seeds to attach so strongly to the fabrics of his clothes and his dog hair. He thought of a fastening system that contained both parts (one similar to the fabrics and the other to the burr). He set himself out to the task of identifying the appropriate combination of materials in order to build the ideal fastening machine he had envisioned. In spite of the high level of skepticism and laughter that his idea initially generated, he joined efforts with a weaver from the French textile industry and began a joint R&D effort for the product. Through trial and error, he found out that nylon provided the best grip over other fabrics like cotton. By 1955 Mestral filed a patent for his product named Velcro (velours which means velvet, and crochet which means hook). Why was the textile weaver critical to the innovation process? Discuss complementary resources.

# Discussion Topics

Scenario planning may become more widely used going forward if the economic, political, and technological forces keep changing rapidly. The global power shift from the west toward Asia would make a good discussion that ties sociopolitical uncertainties to scenario planning.

Working professional students may find the growth in the supply of shale gas to be an interesting area of analysis. Some major areas of uncertainty are (1) whether or not the United States will allow natural gas to be exported to increase demand and (2) the extent to which environmental concerns for fresh water aquifer contamination or earthquake inducement may limit supply. This discussion creates for different scenarios in a 2x2 matrix with different supply/demand balances. Teams could be assigned one of the four quadrants and asked to develop implications for multiple supporting industries (chemical manufacturing, energy-intensive manufacturing, gas transportation, etc.), as well as the gas production firms.

✓ *AACSB 2015 Standard 9 Integrating knowledge across fields*

## End of Chapter **Small Group Exercise 2**

### Instructor Supplement Slide 19

The chapter includes a discussion of black swan events that were improbable and unexpected yet had an extreme impact on the well-being of individuals, firms, and nations. Nassim Nicholas Taleb, author of *The Black Swan*, has argued that policy makers and decision makers need to focus on building more robust organizations or systems rather than on improving predictions of events. This notion is reflected in the response to the predicted increase in powerful storms and storm surges. Hurricanes Katrina (which devastated New Orleans and parts of the Gulf Coast), Sandy (which wreaked havoc on the New Jersey coast) Harvey (which caused massive flooding in Houston) and Maria (which overwhelmed Puerto Rico, leaving much of the island without clean water and electricity for several months) have stimulated discussions about how to not only build a more resilient infrastructure and buildings, but also develop more flexible and effective responses.

2. **Form small groups of three to four students. Search the internet on the following topic and debate your findings. For each group, search the internet for options and plans to (1) build more sustainable communities that would help areas cope with superstorms, or droughts, and (2) organize responses to black swan events more effectively. Brainstorm additional recommendations that you might make to policy makers.**

Major storms are a one key aspect of black swans; in the United States there have also been periods of drought causing problems in agriculture across the country and also massive wild fires, especially in the western United States. Students can reflect on how firms, governments and society can be more proactive in preparing for these sorts of natural events.


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# Case Analysis: Planned Emergent Strategy

This case and multiple-choice question activity builds student comprehension of the planned emergence form of strategy by examining a case about the development of Post-It Notes by 3M Corporation. The student must read the case provided, as well as the relevant textbook section, and answer the related questions in this exercise.

- ✓ ***Difficulty**: Medium*
- ✓ ***Blooms**: Evaluate*
- ✓ ***AACSB**: Analytic*

**Follow-Up Activity:** The instructor can expand on the concepts from this case analysis by having students discuss another example of this strategy formation process—this one concerning Starbucks in Strategy Highlight 2.2. There are similarities in corporate culture and personal persistence that are present in both applications of this concept. Class or small group discussions can also be created around the similarities and differences in the three approaches to strategy: strategic planning, scenario planning, and planned emergence. What would the development of Post-It Notes or Frappuccino have looked like using one of the other two approaches?

# Strategy Highlight 2.1

### Instructor Supplement Slide 8: Starbucks CEO: "It's not what we do"

## Discussion Topics

There are two key points we like to bring out about this Strategy Highlight. The first is what type of risks was the store manager taking to offer a drink on the menu after it had been turned down by the executive committee? In some organizations, this would be cause for termination. So not only was the store manager relentless in pursuit of the idea, she may have been putting her job on the line. Second is the idea that the organization must be willing to accept ideas that "emerge," and implement them even if they were not driven by senior leadership. Ask students what conclusions they might draw about how firm culture and processes for experimentation and decision-making authority may impact firm innovation.

## End of Chapter **Small Group Exercise 1**

### Instructor Supplement Slide 18

In many situations, promising ideas emerge from the lower levels of an organization, only to be discarded before they can be implemented. It was only extraordinary tenacity and disregard for the policy of selling only corporate-approved drinks that permitted the Frappuccino to "bloom" within Starbucks (see Strategy Highlight 2.1).

Some scholars have suggested that companies set aside up to 2 percent of their budgets for any manager with budget control to be able to invest in new ideas within the company. Thus, someone with a $100,000 annual budget to manage would be able to invest $2,000 in cash or staff time toward such a project. Multiple managers could go in together for somewhat larger funds or time amounts. Through such a process, the organization could generate a network of "angel investors." Small funds


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or staff time could be invested in a variety of projects. Approval mechanisms would be easier for these small "seed-stock" ideas, to give them a chance to develop before going for bigger funding at the top levels of the organization.

1. **What problems would need to be addressed to introduce this angel-network idea into a firm? Use a firm someone in your group has worked for or knows well to discuss possible issues of widely distributing small funding level approvals across the firm.**

This exercise builds on some of the ideas applied in the Starbucks Strategy Highlight, combined with thoughts from Gary Hamel's book *The Future of Management* (Harvard 2007). It also integrates some of the real options concepts, because these "seeds" of funding spread throughout the organization will enable limited funding of many different ideas and give each project some time to get traction without it being a "bet the business" decision.

Implementation ideas may take on many issues, depending on the student's prior work experience and knowledge. Most apparently, where does the department manager take the 2 percent from the budget to invest it in these small-scale experiments? What if some managers want to invest and others don't? What sorts of controls would the firm have on the types of projects the employees could explore? Then there's the loss of control by the senior managers or finance, who have been approving all projects previously. At what point do these small projects need to get larger approvals within the organization? The mid-level manager should bring the idea to the attention of the top executives, ideally with a proposal of what would need to be changed as well as what it would offer. A good executive has to look at all possibilities for improving the company even if it requires significant change. Raise the issue of the importance of brand value and global brand image as a core competence of Starbucks, as a key success factor in the industry, and as the most valuable asset on the balance sheet. Encourage your marketing majors to explore the risks associated with independent, bottom-up experimentation with elements of strategy that have high brand impact. How might relationships with franchisees been harmed by offering products in company-operated stores that were not available to partners?

# Class Exercise

Shell predicts that in 2025 most of our energy will continue to be generated from fossil fuels but 20 percent will come from alternative energy sources like wind, solar, and hydro power. Given Shell's past success in using scenario planning, one ought to pay attention to its predictions. Shell can claim a number of accurate predictions to its credit. In the 1960s, with the price of a barrel of crude oil around $10 (compared to a record high of close to $150 in the summer of 2008), managers at Shell began to formulate strategic plans for a future with a strong OPEC (the cartel of oil-exporting countries) and an accompanying drastic rise in oil prices. When the price of crude oil suddenly surged to over $80 a barrel in the late 1970s, Shell was well-positioned to take advantage of this new situation; other oil companies were scrambling to adjust. Shell activated one of its alternative strategic plans that detailed how to obtain crude oil from North Sea drilling, to which the firm had already secured the rights. In the early 1980s, Shell made strategic preparations to take advantage of another apparently far-fetched scenario when it speculated that communism might fail, bringing down the powerful Soviet Union and ending Soviet artificial restrictions on the supply of natural gas. More information is available on Shell's website on the process of scenario planning, their past scenarios, and their projections on renewable energy adoption. Shell's latest scenarios (Shell's New Lens on the Future) envision the world as it might be in 2100. You might ask small teams of students to brainstorm the implications that these two scenarios have for industries other than the energy industry. For example, the automotive and passenger airline industries are strongly impacted by both fuel supplies/pricing and air quality controls. Other new scenarios focus on envisioning the cities of the future, which might have broader appeal to your students and a global perspective from Los Angeles to Marrakesh, Chonqing, Manila, and Copenhagen.


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# 2.3 Stakeholders and Competitive Advantage

## LO 2-5 Assess the relationship between stakeholder strategy and sustainable competitive advantage.

### LECTURE SLIDES 34-36

## DISCUSSION TOPICS

Stakeholders are organizations, groups, and individuals who have a vested interest in the performance and survival of the firm. Stakeholder strategy is a framework that connects corporate governance, business ethics, and strategic leadership and thus helps managers think through these issues in a holistic fashion. Stakeholder theory is a theoretical framework that is concerned with how different stakeholders create and trade value. Instructors can discuss the importance of public companies and their influence on our daily life. Students need to understand the interdependent relationships between these organizations and the average citizen. Then, discuss the importance of the public companies' stakeholders and why companies need to take good care of them. The answer is, "It is an interdependent relationship." Only by taking care of the stakeholders can they create a win–win, with mutually beneficial results to both companies and to society. This section sets a foundation that allows instructors to talk later about social responsibilities.

Tap into the students' very real experience of the impacts of the recent financial crisis on society and its trust in business institutions. How has their trust in the financial system changed? What impacts might a loss of trust have on financial firms' ability to operate? (See "Life on Wall Street Grows Less Risky," *The Wall Street Journal,* September 9, 2013.)

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# Click and Drag: Internal and External Stakeholders

This click-drag sequencing activity starts with chronological ordering of some black swan events, as discussed in the textbook. Then, the students are asked to consider the benefits and contributions of several different types of stakeholders by answering two multiple-choice questions from the text material. The student must read the textbook and then drag the elements to the correct locations in both stages of this activity.

The instructor can expand on the concepts from this interactive by discussing recent activist stockholder activities at firms pulled from the headlines.

✓ ***Difficulty***: *Medium*
✓ ***Blooms***: *Apply*
✓ ***AACSB***: *Analytic*

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## LO 2-6 Conduct a stakeholder impact analysis.

### LECTURE SLIDES 37-39

### DISCUSSION TOPICS

Stakeholder impact analysis is a decision tool with which managers can recognize, assess, and address the needs of different stakeholders to allow the firm to perform optimally and act as a good corporate citizen. Stakeholder impact analysis is a five-step analysis. Who are our stakeholders? What are our stakeholders' interests? What opportunities and threats do our stakeholders present? What economic, legal, ethical, and philanthropic responsibilities do we have to our stakeholders? What should we do to effectively address the stakeholder concerns?

Possible examples to illustrate the five-step stakeholder impact analysis could be BP's relationships with its shareholders and U.S. government agencies. Another possibility is Nestle's relationships with its shareholders, its customers, and nutrition activists. If you choose the Nestle example, you may want to ask students to read the comments about Nestle in its social media pages. A way to make this discussion more interesting if you have journalism, public relations, public health, or communications majors in your course, would be to invent an "event" for Nestle or use the real event for BP. Then ask selected students to "report" on the incident from a few different perspectives and ask other students to present the company's position, as if they were the CEO.

✓ *AACSB 2015 Standard 9 Social responsibility, including sustainability, and ethical behavior and approaches to management and written and oral communication*

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## Click and Drag: Social Responsibilities: Stakeholders and Competitive Advantage

This interactive drag-and-drop exercise covers the textbook examples of firms using a variety of generic business-level strategies. The student will read the brief application case and move the firm name into the correct box provided. A related quiz with questions follows the interactive activity.

✓ ***Difficulty**: Medium*
✓ ***Blooms**: Apply*
✓ ***AACSB**: Analytics*

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# Strategy Highlight 2.2

### INSTRUCTOR SUPPLEMENT SLIDES 9 -11: BP "GROSSLY NEGLIGENT" IN GULF OF MEXICO DISASTER

The BP Horizon environmental disaster shows the consequences of failure to live up to the expectations of society for corporate social responsibility. One might argue that they were effective in responding to stakeholder concerns after the fact, by setting up processes for rapid payment of claims, supporting fishing communities, and running advertisements for tourism. Others will fault their performance after the fact, arguing that the CEO at the time was too standoffish and that the firm took too long to recognize and solve the technical issues and stop the leak. You might invite students to research BP/Amoco safety incidents. They will find that one of the reasons the U.S. government was unwilling to excuse this disaster as an unavoidable


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accident is that BP/Amoco had a track record that included several large-scale safety incidents with fatalities. Persistent accidents argue that safety leadership and safety culture were lacking, thus breaching the public trust. If time permits, you might also open a discussion as to whether energy, food, and pharmaceutical firms that serve basic human needs should be held to a higher standard than manufacturers of less critical products, such as fashion.

✓ *AACSB 2015 Standard 9 Social responsibility, including sustainability, and ethical behavior and approaches to management*

## END OF CHAPTER ETHICAL/SOCIAL ISSUES 1

1. **BP's experience in the Gulf of Mexico has made it the poster company for how *not* to manage stakeholder relationships effectively (see Strategy Highlight 2.2). What advice would you give to BP's managers to help them continue to rebuild stakeholder relationships in the Gulf region and beyond? How can BP repair its damaged reputation? Brainstorm ways that top management might leverage the experience gained by reactions in the Gulf and use that knowledge to motivate local managers and employees in other locales to build stakeholder relationships proactively so that BP avoids this type of negative publicity.**

The BP Horizon environmental disaster shows the consequences of failure to live up to the expectations of society for corporate social responsibility. One might argue that they were effective in responding to stakeholder concerns after the fact, by setting up processes for rapid payment of claims, supporting fishing communities, and running advertisements for tourism. Others will fault their performance after the fact, arguing that the CEO at the time was too standoffish and that the firm took too long to recognize and solve the technical issues and stop the leak. You might invite students to research BP/Amoco safety incidents. They will find that one of the reasons the U.S. government was unwilling to excuse this disaster as an unavoidable accident is that BP/Amoco had a track record that included several large-scale safety incidents with fatalities. Persistent accidents argue that safety leadership and safety culture were lacking, thus breaching the public trust. If time permits, you might also open a discussion as to whether energy, food, and pharmaceutical firms that serve basic human needs should be held to a higher standard than manufacturers of less critical products, such as fashion.

✓ *AACSB 2015 Standard 9 Social responsibility, including sustainability, and ethical behavior and approaches to management*

# 2.4 Implications for Strategic Leaders

### INSTRUCTOR SUPPLEMENT SLIDES 13-15

The chapter has provided several examples of strategic leadership actions taken at several major corporations. Such leadership when combined with an effective process of managing strategic issues can yield a sustained competitive advantage. Leaders need to consider the relative pace of change impacting the organization as well as stakeholders in designing a successful strategic management process.

## STRATEGY SMART VIDEO LECTURE

### INSTRUCTOR SUPPLEMENT SLIDE 29

This slide links to a 2-minute video of Jim Collins describing his 25 years of research in contrasts looking for what makes organizations great in all types of situations.

## RELATED MINICASES



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Instructors may want to consider assigning and discussing any of the following MiniCases that cover topics found in this chapter. All MiniCases have assignable McGraw-Hill Connect® case questions available.

MiniCase 1: Michael Phelps: The Role of Strategy in Olympics and Business
MiniCase 2: PepsiCo's Indra Nooyi: Performance with Purpose
MiniCase 3: Yahoo: From Internet Darling to Fire Sale
MiniCase 4: How the Strategy Process Killed Innovation at Microsoft

# END OF CHAPTER DISCUSSION QUESTIONS

1. **In what situations is top-down planning likely to be superior to bottom-up emergent strategy development?**

As the text notes, top-down strategic planning is usually best in relatively stable environments. Emergent strategy is preferred in more uncertain times. However, the Mintzberg framework identifies that combining the two approaches is likely to yield the best results. An organization in today's environment should strive to be flexible enough to adjust the proportion of top-down and bottom-up ideas based on the situation. Top-down planning and decision making may also be best in businesses in which reliability and consistency are key success factors (Do you want your nuclear power plant operators experimenting with emerging ideas? Should auditors experiment with new accounting principles?). Bottom-up planning and decision-making offers advantages in innovation-based businesses where (1) being closer to knowledge of customer needs and competitive trends may create information advantages at lower levels of the organization and (2) a diverse stock of non-redundant knowledge may yield more radical innovations.

2. **This chapter introduces three levels appropriate for strategic considerations (see Exhibit 2.3). In what situations would some of these levels be more important than others? For example, what issues might be considered by the corporate level? What do you see as the primary responsibilities of corporate-level executives? When might the business-level managers bear more responsibility for considering how to respond to an issue? In what situations might the functional-level managers have a primary responsibility for considering an issue? How should the organization ensure the proper attention to each level of strategy as needed?**

The "Where, How, Implementation" questions can be quite useful to help students think about a particular strategic decision and which level of strategy it represents. Balance of the strategic levels is difficult and can be an area where many companies falter. In larger organizations, the strategic responsibilities will reside in different individuals and teams. This helps assure that no level is completely neglected, but it doesn't address the appropriate mix of strategic levels. Some organizations have implemented a periodic review of strategies at all levels of the firm to try to assess the health of the overall company and its business models.

Students may be more familiar with functional and business-level strategies from their own work experiences. Functional areas can develop many great ideas on how to implement business and corporate strategies. Given a supportive organizational climate, these areas can also produce emergent strategies. Relative importance is often based on external factors. When Lou Gerstner came to IBM and started to refocus the firm on services rather than hardware, the corporate strategy and transition was preeminent. Many of the business-level strategies—for example, in hardware-focused SBUs—were likely abandoned. On the other hand, when Microsoft rolls out Bing and partners with Facebook, Google's business-level strategies will be most important in figuring out how to compete in this new online search environment.

3. **Identify an industry that is undergoing intense competition or is being featured in the business press. Discuss how scenario planning might be used by companies to prepare for future events. Can some industries benefit more than others from this type of process? Explain why.**

Industries that by their nature need to make "big bets" are often users of scenario planning. This would include the oil industries. It would also include other major extraction companies (Alcoa, for example) and capital-intensive industries such


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as semiconductors (Intel). These firms must make major investments around the globe to be successful in their industries. Scenario planning can help them with boundary conditions on their choices.

Students can relate to the growing sociocultural concerns about obesity and the impact that this may have on the beverage and quick service restaurant industries. You can invite student teams to write a rich, narrative description of life in a world where high caloric food is highly regulated. Then they should be asked to identify implications for either industry.

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# HP Running Case: Module 2

While offering each student the opportunity to explore and analyze the company of his/her choice can add interest to the exercise, there are many advantages for an instructor when the entire class works on the same firm. Connect® allows you to do this with a running case for a single firm that encompasses every chapter in the textbook and tracks the Strategy Term Project. Hewlett-Packard is provided as an example firm your students can use to see what information and analysis would be helpful to cover this portion of the term project.

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# Strategy Term Project: Managing the Process

## Term Project Module 2

In this section, you will study the business strategy of the firm you have previously selected for this project. Be sure to instruct the students to focus only on ONE business unit if they have selected a larger firm with several operations.

**Search for a vision, mission statement, and statement of values for your chosen firm. Note that not all organizations publish these statements specifically, so you may need to make inferences from the available information. Relevant information is often available at the firm's website (though it may take some searching) or is contained in its annual reports. You may also interview a manager of the firm or contact Investor Relations. You may also be able to compare the official statement with the business press coverage of the firm.**

First, the student will search for the firms' mission statement. Remember some firms use the term mission and vision interchangeably, so the student may need to adapt a vision statement as the mission if it is appropriate.

**Identify the major goals of the company.**

Major company goals are quite often available through the annual reports that each public firm must file with the SEC (free at http://www.sec.gov/edgar.shtml).

**Trace any changes in strategy that you can identify over time. Try to determine whether the strategic changes of your selected firm are a result of intended strategies, emergent strategies, or some combination of both.**

Longer-term goals are usually in the annual reports. We suggest going back a few years in the annual reports and comparing what the firm said three or five years ago to what they said most recently. Pulling a couple of older annual reports will also help in the formation of a timeline for major changes in the organization. Also, check the firm's website. Often, firms will include a history or "timeline" section from their home page under "About Us" or the "Investors" tab.


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# *my*Strategy

## INSTRUCTOR SUPPLEMENT SLIDE 17: WHO ARE YOUR STAKEHOLDERS?

Here, we encourage the student to take what he/she has learned about competitive advantage and apply it to his/her personal career. Encourage students to spend a few minutes looking at themselves to discover their own competitive advantages.

✓ *AACSB 2015 Standard 9 Reflective thinking (able to understand oneself in the context of society)*

1. **List your personal goals. Which stakeholders are supportive of these goals? Which are likely to try to block these goals?**

These questions are meant to be personal, but we offer a few thoughts on them. Values should play some part, but it is not likely to be the most important influence. If your only goal is to become head of a large company, market growth and expansion may become a high priority. However, success can be found in many places, and it is usually more important to find a company with good leadership (firm effects) than to worry solely about market growth (industry effects).

2. **Develop a plan to address key stakeholder concerns from each perspective. Can you find a pathway in the stakeholder analysis to build support for your key goals?**

Studies have shown that once workers get above a certain "pay the bills" space financially, intrinsic rewards often become more important than money. We have found a wide variance of answers when we have run this exercise in our classes.

3. **What would it take to implement your ideas/plans to move forward with these goals?**

Encourage students to consider work/family life balance and recognize the implications of long hours and extensive travel that usually accompany high-paying jobs.


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**Case Title:** Alphabet's Google

**Unique ID:** MHE-FTR-055-1259927628

REV: September 27, 2017

**Abstract**

The case is written from the perspectives of Larry Page, CEO of Alphabet and Sundar Pichai, CEO of Google. The case focuses on opportunities and challenges faced by Alphabet's largest business unit, Google. Competition in Google's advertising space has intensified, mostly by the way of Facebook. This poses a threat because Google still secures more than 90 percent of Alphabet's profits and revenues. The case also highlights challenges of managing a multi-business conglomerate pursuing an unrelated diversification strategy. As Alphabet continues to implement an M-form structure to administer unrelated diversified, the adjacent business units will have a significant impact on Google. Most notably, the Waymo subsidiary has the potential to enter a multibillion-dollar market. The uncertainty of this venture along with Google's core competencies present new opportunities and challenges to the firm. There is also the question if Alphabet can manage this new structure while securing future growth and profitability.

**Concepts:** Business Model**,** Competitive Strategy**,** Platform Strategy**,** Innovation and Technology Strategy**,** Corporate Strategy**,** Unrelated Diversification**,** Profit Pools, and Organizational Structure

**Context:**

- Ticker Symbol: GOOGL
- Protagonists: Larry Page, CEO Alphabet; and Sundar Pichai, CEO Google
- Country: USA (worldwide reach online)
- Sector: Diversified conglomerate, including online search and advertising
- Company Employee Count: 76,000
- Company Revenue: $100 billion (2017)
- Market Cap: $650 billion (Sept. 2017)
- Event Year: 2017

**Teaching Note**: Available

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# MiniCase 2 PepsiCo's Indra Nooyi: Performance with Purpose

## DISCUSSION QUESTIONS

1. **What grade would you give PepsiCo CEO Indra Nooyi for her job performance as a strategic leader? What are her strengths and weaknesses? Where would you place Nooyi on the Level-5 pyramid of strategic leadership (see Exhibit 2.2), and why? Support your answers.**

   *PepsiCo's CEO Grade: Students will have a variety of answers. Here is an example of an appropriate one.*

   *Nooyi gets an A- at this point. She clearly is well aware of PepsiCo's internal resources and capabilities and how the external environment threatens the firm. Her actions to restructure and diversify have cleared the firm's path and opened significant opportunities in the food industry, where PepsiCo has leveraged its capabilities and gained a competitive advantage. After initially disappointing results, PepsiCo has, over the past six years, consistently out performed Coca-Cola Company and this is reflected in the respective share prices. However, revenue growth over the past few years has been flat, as the market for carbonated soft drinks has come under pressure. (It should be noted here that PepsiCo has a greater weighting in snack food and so is less vulnerable than Coca-Cola to the weakening market for carbonated soft drinks.) Despite this, Nooyi's corporate social responsibility strategies, while initially criticized for not producing results, now seem to be paying off. PepsiCo has successfully anticipated changes in public attitudes and state regulation and has staked out favorable positions in its markets.*

   *Nooyi would be placed at Level 4 or 5 on the Level-5 pyramid of strategic leadership. She has certainly presented a distinctive and different vision and mission to guide PepsiCo to superior performance (i.e. outperforming Coca-Cola). That would at least make her a Level-4 leader. A Level-5 leader builds enduring greatness through willpower and humility. Nooyi has moved the company in an entirely different direction, leading through example and conviction. The only question here is whether PepsiCo's competitive advantage will endure. There may be some concerns about the lack of significant revenue growth over the past few years, but that would be the only reservation about classifying her as a Level-5 leader.*

2. **The first few years after Indra Nooyi took over as PepsiCo's CEO and implemented *Performance with Purpose*, the company underperformed archrival Coca-Cola Co. by a wide margin. What should a strategic leader do if his or her vision does not seem to lead to an immediate (financial) competitive advantage? What would be your top three recommendations? Support your arguments.**

   *Recommendations for leaders when their vision does not provide an immediate competitive advantage include:*
   - **Continue to Adapt.** *When* Fortune *asked CEOs, including Nooyi, to give advice, her response was that you should never stop learning. The most successful leaders were lifelong students. Plans are rarely perfect, so strategy should be modified based on feedback and learning.*
   - **Be Patient.** *When attempting something that has never been done, leaders should realize that their efforts might take time. Indeed, Nooyi went through several years of disappointing results at PepsiCo, before "Performance with a Purpose" began paying off. This does require a supportive board of directors, who will also have to exercise patience, even as investors are clamoring for faster results.*
   - **Communicate.** *Part of developing a vision is to communicate clearly to stakeholders a change story and a sense of urgency. Merely, having a vision is insufficient if people within the firm do not adopt it. The CEO must have a clear and consistent message and take actions (promotions, budgeting, etc.) to reflect the new priorities.*
   - **Achieve Quick Wins.** *Demonstrate the viability of the new strategy and get buy-in through achieving quick wins. This may necessitate setting some easy to achieve goals purely to demonstrate that the new strategy is producing results.*


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3. **Do you agree with Indra Nooyi's philosophy that "performance and purpose are intimately linked and you can't do one without the other"? Support your arguments. Apply the people, planet and profits model of sustainable strategy (see Exhibit 5.9).**

***Yes***. *Applying the three dimensions of the people, planet, and profits model of sustainable strategy. PepsiCo has outperformed expectations and produced good financial results (profits), while emphasizing social (people) and ecological (planet) performance as well. The latter two dimensions satisfy the broader stakeholder community and this is necessary for a firm's long-term success. The company's steadily increasing market valuation shows that investors view this positively.*

***No***. *"Performance with Purpose" is a promising long-term strategy that could put PepsiCo in a very favorable position with its stakeholders (especially its customers). However, shareholders want to see their investment grow by more than the industry average and certainly more than the company's direct competitors. Otherwise, there is an incentive for short-term investors to cash out and invest in a better-performing firm or a less risky asset. Even if the investor understands the long-term value of the strategy, there is a need for short-term results. (Fortunately, PepsiCo has consistently outperformed its competitors over the past several years, so even short tem investors should be happy with the success of their strategy.)*

4. **PepsiCo's investors require the company to grow about five percent or $3.5 billion a year. PepsiCo's top-line, however, remained flat for the last few years. Where would future growth for PepsiCo come from?**

*There are multiple options for PepsiCo to drive growth, including:*

- **Invest**. *Recognition that improved performance results from investment in initiatives to both increase revenues and reduce costs. In 2012, PepsiCo announced multiple initiatives to enhance shareholder value including major investment in its brands, investments to increase productivity, and the reduction of capital investment to improve return on invested capital (e.g., raising the hurdle rate for capital investment). The emphasis on brands appears to be paying off with PepsiCo now having 22 brands with sales over $1 billion.*
- **Go International.** *The North American market is largely saturated, so growth can be achieved by increasing PepsiCo's presence in emerging markets. Recognition of this is reflected in PepsiCo investing $5.5 billion in India for new products and manufacturing plants. China and Brazil represent other countries that PepsiCo could focus on with investments.*
- **Go Healthy.** *Consistent with social trends and "Performance with Purpose" PepsiCo could continue to invest in providing a healthier product line, or obtain growth from new, related products.*
- **Partner.** *Work with other companies to highlight its products and increase demand. For example, PepsiCo has collaborated successfully with Taco Bell to launch Doritos Locos Tacos.*

5. **Some activist investors are putting pressure on Indra Nooyi to split PepsiCo into two standalone companies, with one focusing on beverages (Pepsi, Gatorade, Tropicana); the other would focus on snack foods (such as the Frito-Lay brand). What is the idea behind this corporate strategy? Do you think this move would add value for shareholders? For consumers? Other stakeholders? Why or why not?**

Shareholders
*Some investors believe that separating PepsiCo's beverage and snack food businesses will allow each to streamline operating, marketing and advertising costs. Overheads would also be reduced. They also feel that the carbonated soft drink business is lagging behind snack foods, dragging down the latter. A stand-alone beverage firm would be able to function more effectively, with management focused on its success alone. Snack foods would be unleashed to perform even better. This would result in a net gain for shareholders.*


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*PepsiCo on the other hand believes that the synergies of a single corporate entity—cross marketing, bulk purchase of inputs and packaging materials, negotiating with the same buyers, etc. —outweigh any benefits that may be derived from this split.*


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Consumers
*If a split results in efficiencies, consumers may benefit from having some savings passed on to them. Separate firms, each focused on their own product line, might also develop new products that consumers find attractive.*

*A split may mean that cross promotions and other partnerships that benefit the consumer will no longer be available. If the split results in abandonment of "Performance with a Purpose," the push for healthier products may be weakened, hurting consumer health over the long term.*

Other Stakeholders
*A split may also impact other stakeholders. Buyers will now negotiate with two smaller firms, and will be in a stronger position. Communities could be affected by investment decisions, both positive and negative. A drive for efficiencies could negatively impact the workforce.*

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Bailey, Sharon. 2014. "An Investor's Guide to PepsiCo." *Market Realist,* December 12, 2014. http://marketrealist.com/2014/12/pepsico-company-overview/.

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PepsiCo. 2012. PepsiCo Announces Strategic Investments to Drive Growth: http://www.pepsico.com/live/pressrelease/PepsiCo-Announces-Strategic-Investments-to-Drive-Growth02092012

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Trefis Team. 2014. "Is PepsiCo Headed for a Split?" *Forbes,* August 28, 2014. http://www.forbes.com/sites/greatspeculations/2014/08/28/is-pepsico-headed-for-a-split/#29f5c0c4584a.


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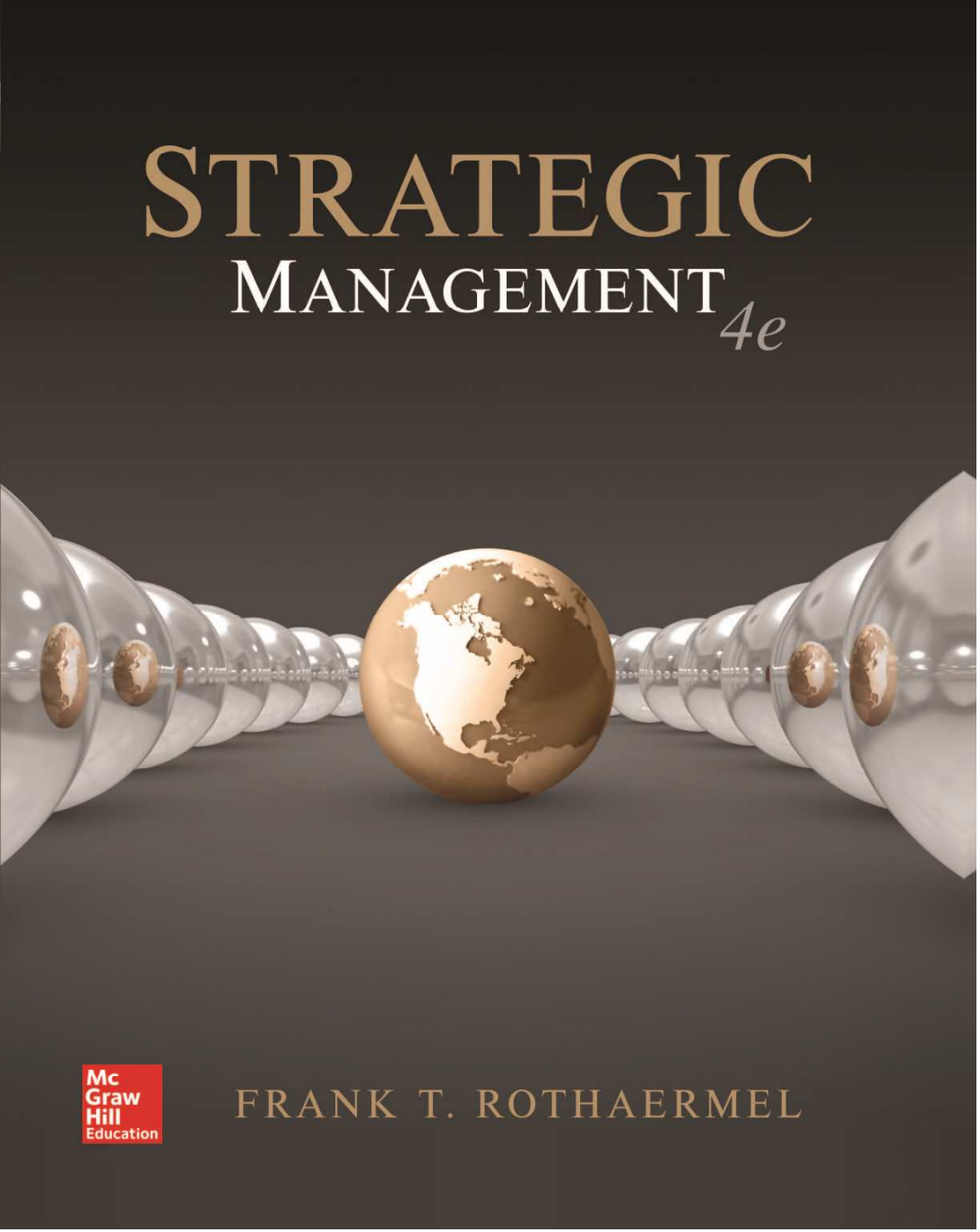


# CHAPTER 2

# Strategic Leadership

# Managing the Strategy Process

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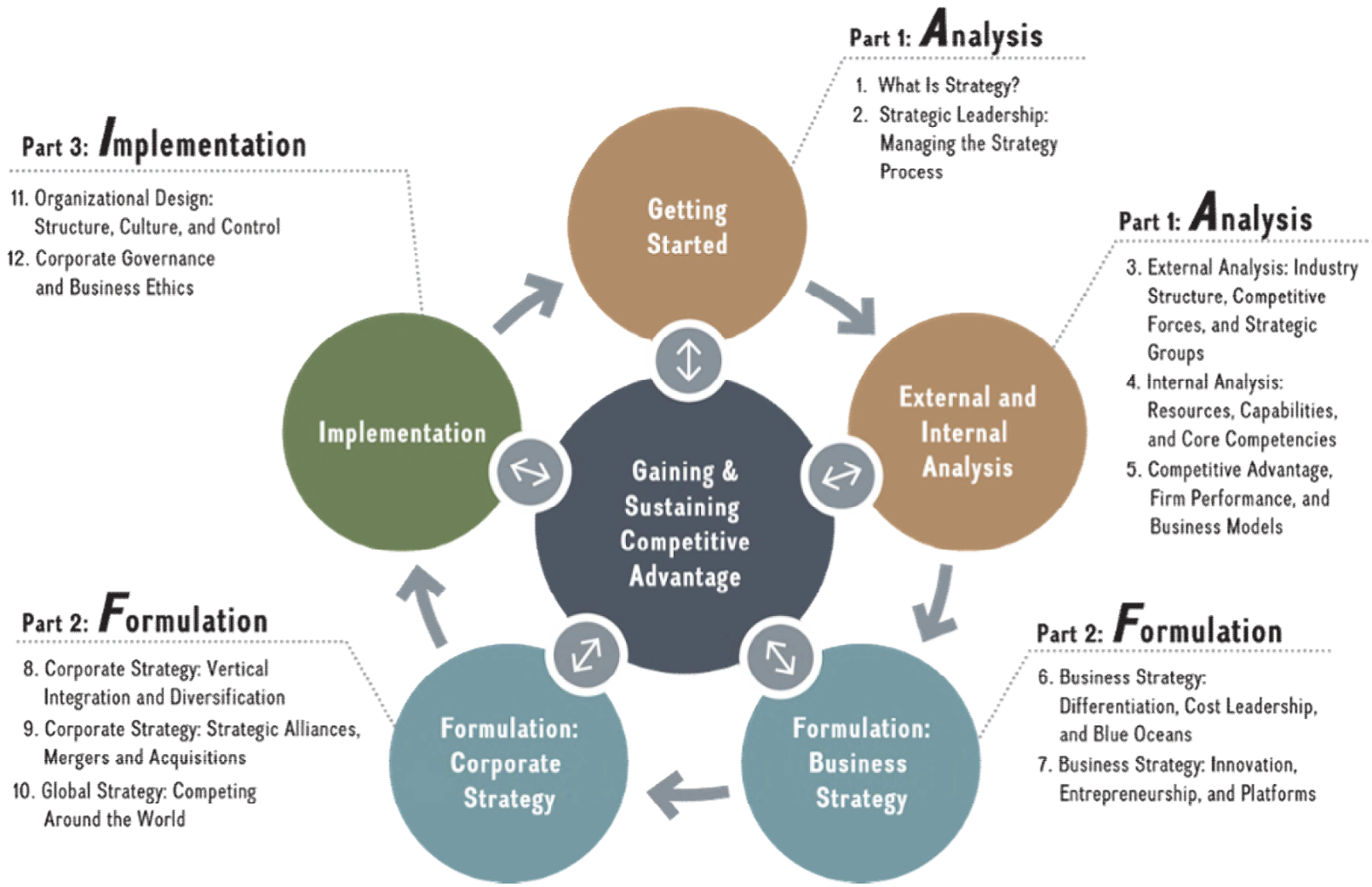
# The AFI Strategy Framework




Jump to Appendix 1 long image description



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# Learning Objectives

| | |
|---|---|
| LO 2-1 | Explain the role of strategic leaders and what they do. |
| LO 2-2 | Outline how you can become a strategic leader. |
| LO 2-3 | Describe the roles of corporate, business, and functional managers in strategy formulation and implementation. |
| LO 2-4 | Evaluate top-down strategic planning, scenario planning, and strategy as planned emergence. |
| LO 2-5 | Assess the relationship between stakeholder strategy and sustainable competitive advantage. |
| LO 2-6 | Conduct a stakeholder impact analysis. |

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# What Is Strategic Leadership?

Successful use of power and influence

Directing the activities of others

Pursuing an organization's goals

Enabling organizational competitive advantage

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# Leaders Can Positively Impact Performance

Mark Zuckerberg – Facebook

Elon Musk – Tesla and SpaceX

Jeff Bezos – Amazon

Oprah Winfrey – HARPO

Sheryl Sandberg – Facebook

Angela Ahrendts – Apple

Mary Barra – General Motors

Howard Schultz - Starbucks

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# Leaders Can Destroy Shareholder Value

Ken Lay – Enron

John Sculley – Apple

Bernard Ebbers – WorldCom

Richard Fuld – Lehman Brothers

Richard Wagoner – General Motors

Robert Nardelli – The Home Depot and Chrysler

Ron Johnson – JC Penney

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# What Do Strategic Leaders Do?

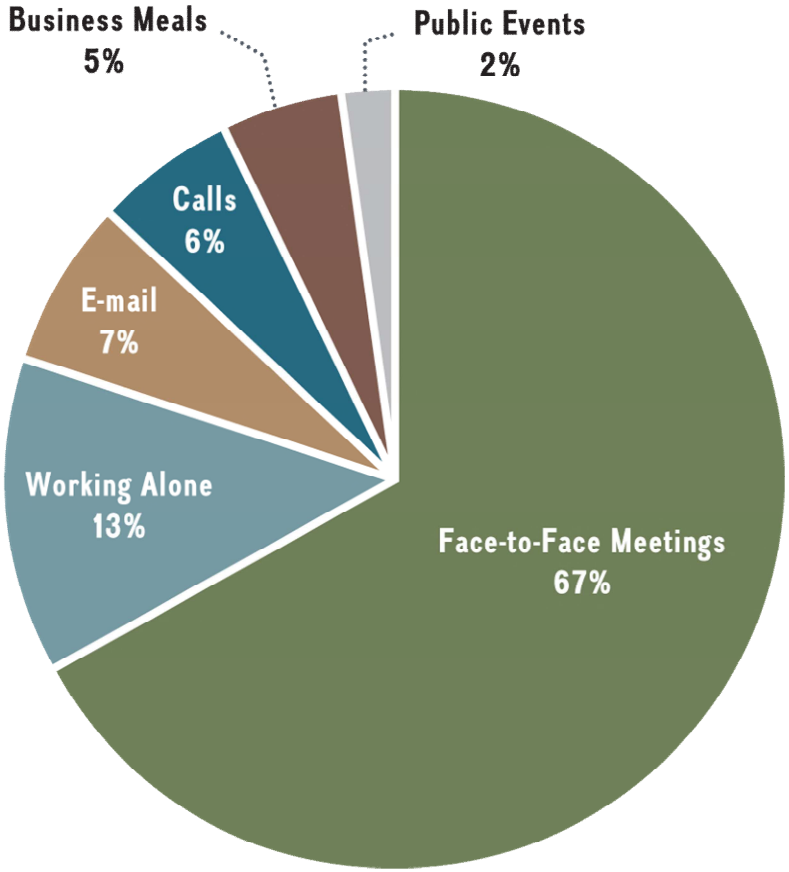


Exhibit 2.1

SOURCE: Data from O. Bandiera, A. Prat, and R. Sadun (2012), "Management capital at the top: evidence from the time use of CEOs," *London School of Economics and Harvard Business School Working Paper.*

Jump to Appendix 2 for long definitions

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# How Do You Become a Strategic Leader?

Leadership actions reflect:

- Age, education, and career experiences
- Personal interpretations of situations

Strong leadership: innate abilities <u>and</u> learning

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# Upper Echelon's Theory

Organizational outcomes reflect the values of the top management team.

Outcomes include:

- Strategic choices
- Performance levels

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# Great Companies

Based on the bestseller Good to Great

- Written by Jim Collins
- Over 1,000 companies were analyzed.

Great companies had things in common:

- Sustained competitive advantage
- Stock returns of almost 7x the general market
- Consistent patterns of leadership
  - Summarized in the Level 5 Leadership Pyramid

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# Level-5 Leadership Pyramid

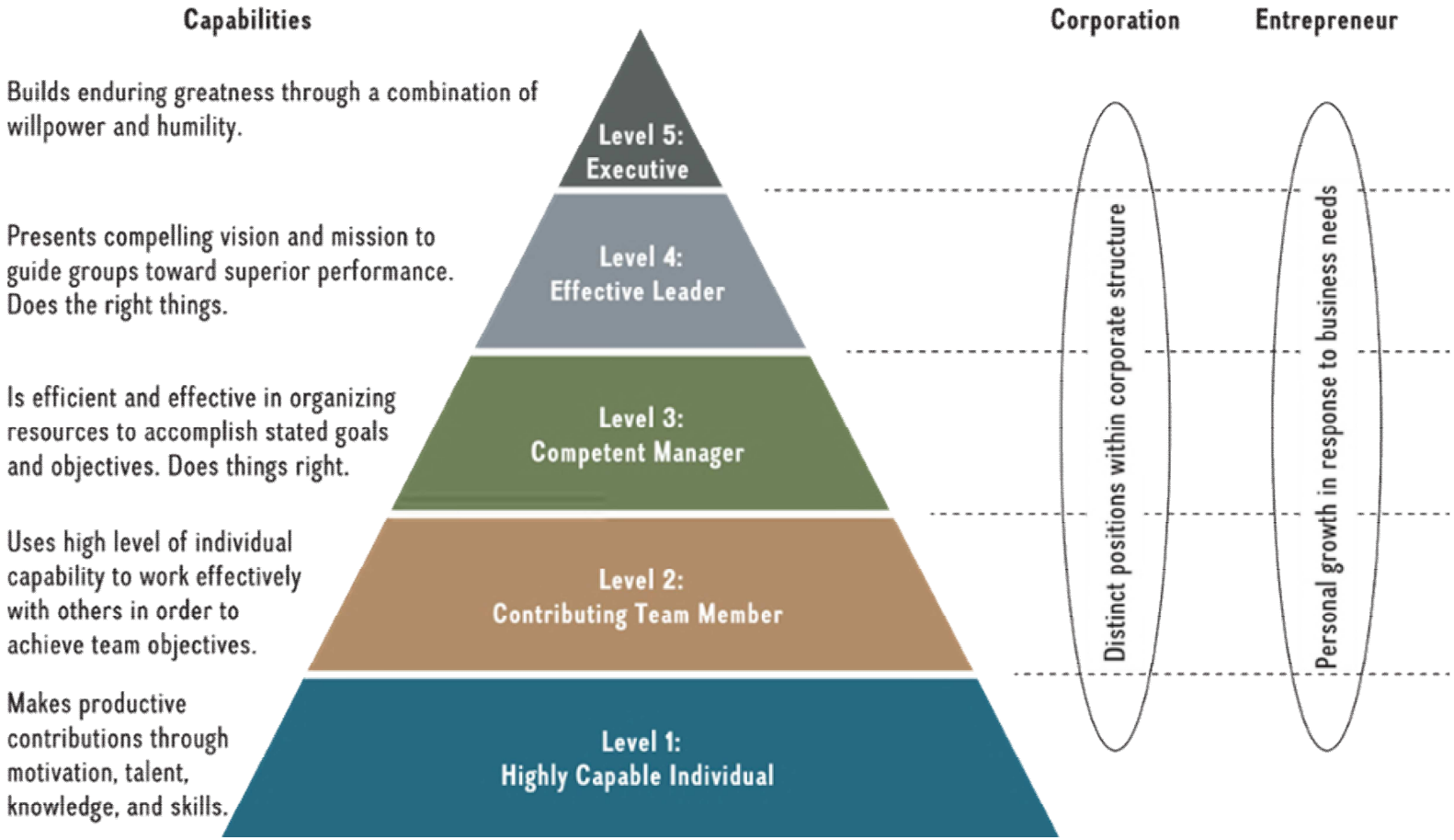


**Exhibit 2.2**

(Adapted to compare corporations and entrepreneurs) SOURCE: Adapted from J. Collins (2001), *Good to Great: Why Some Companies Make the Leap . . . And Others Don't* (New York: HarperCollins), 20.

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Jump to Appendix 2 long image description

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# Progression of Leaders Through the Pyramid

Each level builds upon the previous one.

Prior levels must be mastered before moving on.

Each level helps individuals develop the capacity for greater success.

A Level-5 executive:

- Works to help the organization succeed
- Helps others reach their full potential

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# The Strategy Process

## Strategy Formulation:

- The choice of strategy
- Where and how to compete

## Strategy Implementation:

- Organization, coordination, integration
- How work gets done
- The execution of strategy

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# The Strategy Process Across Levels

## Corporate Strategy

- Where to compete?
- Industry, markets, and geography

## Business Strategy

- How to compete?
- Cost leadership, differentiation, or value innovation

## Functional Strategy

- How to implement a chosen business strategy?

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# Formulation and Implementation Across Levels

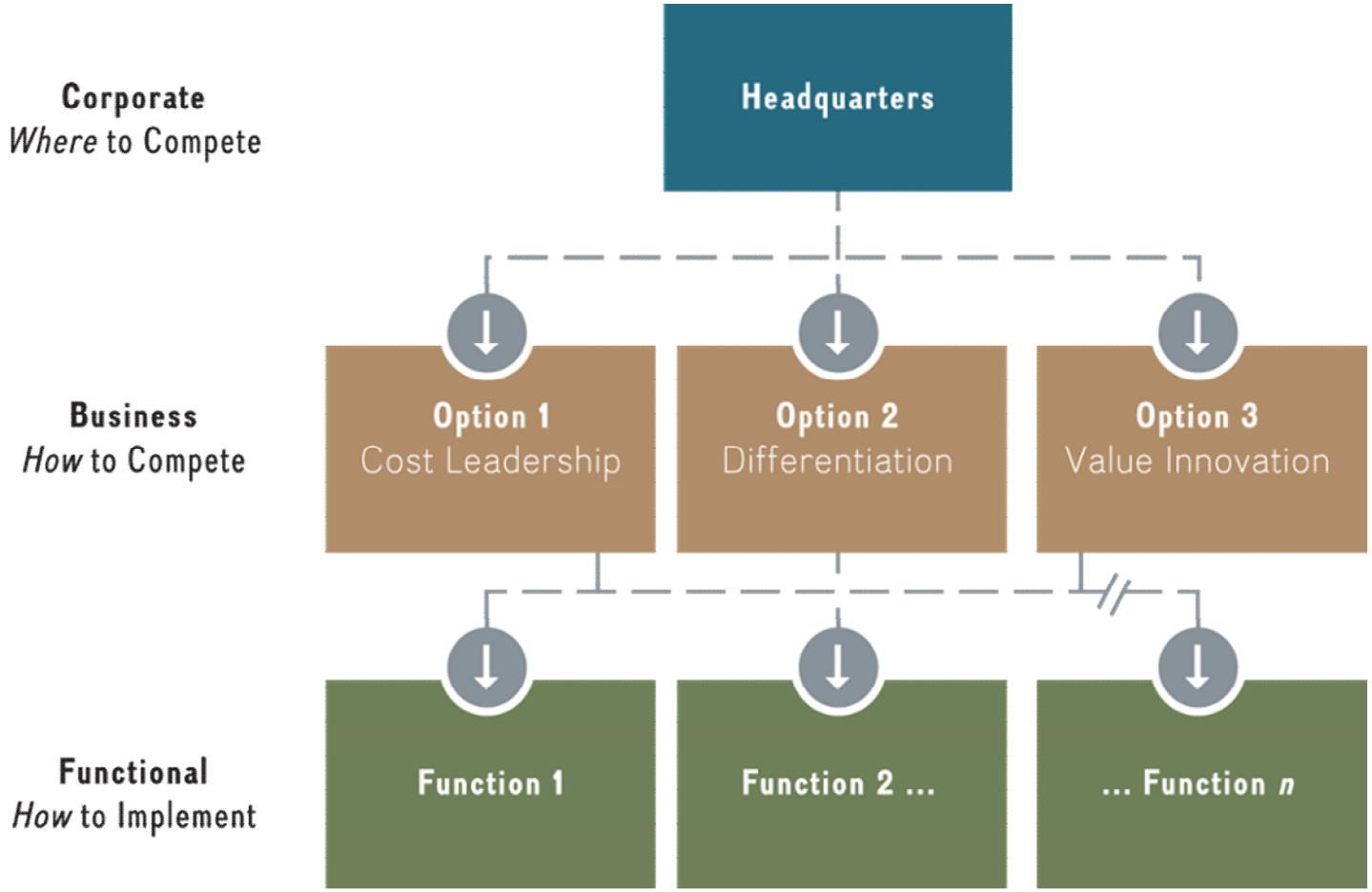


Exhibit 2.3

Jump to Appendix 4 long image description

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# Corporate Strategy

Decide in which industries, markets, and geographies their companies should compete.

Corporate executives:

- Create synergies across SBUs.
- Decide whether to enter or exit industries and markets.
- Set strategic objectives.
- Allocate scarce resources among SBU.
- Monitor performance.
- Make adjustments to the portfolio as needed.

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# Business Strategy

Standalone division of corporate

Profit and loss responsibility

Work with corporate to determine business strategy

- Cost leadership
- Differentiation
- Value innovation

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# Functional Strategy

Within each strategic business unit:

- Accounting
- Finance
- Human resources
- Product development
- Operations
- Manufacturing
- Marketing
- Customer service

Functional managers are responsible for decisions and actions within the function.

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# Three Approaches to Organizational Strategy

## Strategic planning

- A formal, top-down planning approach

## Scenario planning

- A formal, top-down planning approach

## Strategy as planned emergence

- Begins with a strategic plan, but is less formal

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# Top Down Strategic Planning (1 of 2)

Data-driven strategy process

Top management attempts to program future success through

- Analysis of:
  - Prices
  - Costs
  - Margins
  - Market demand
  - Head count
  - Production runs
- Five year plans and correlated budgets
- Performance monitoring

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# Top-Down Strategic Planning (2 of 2)

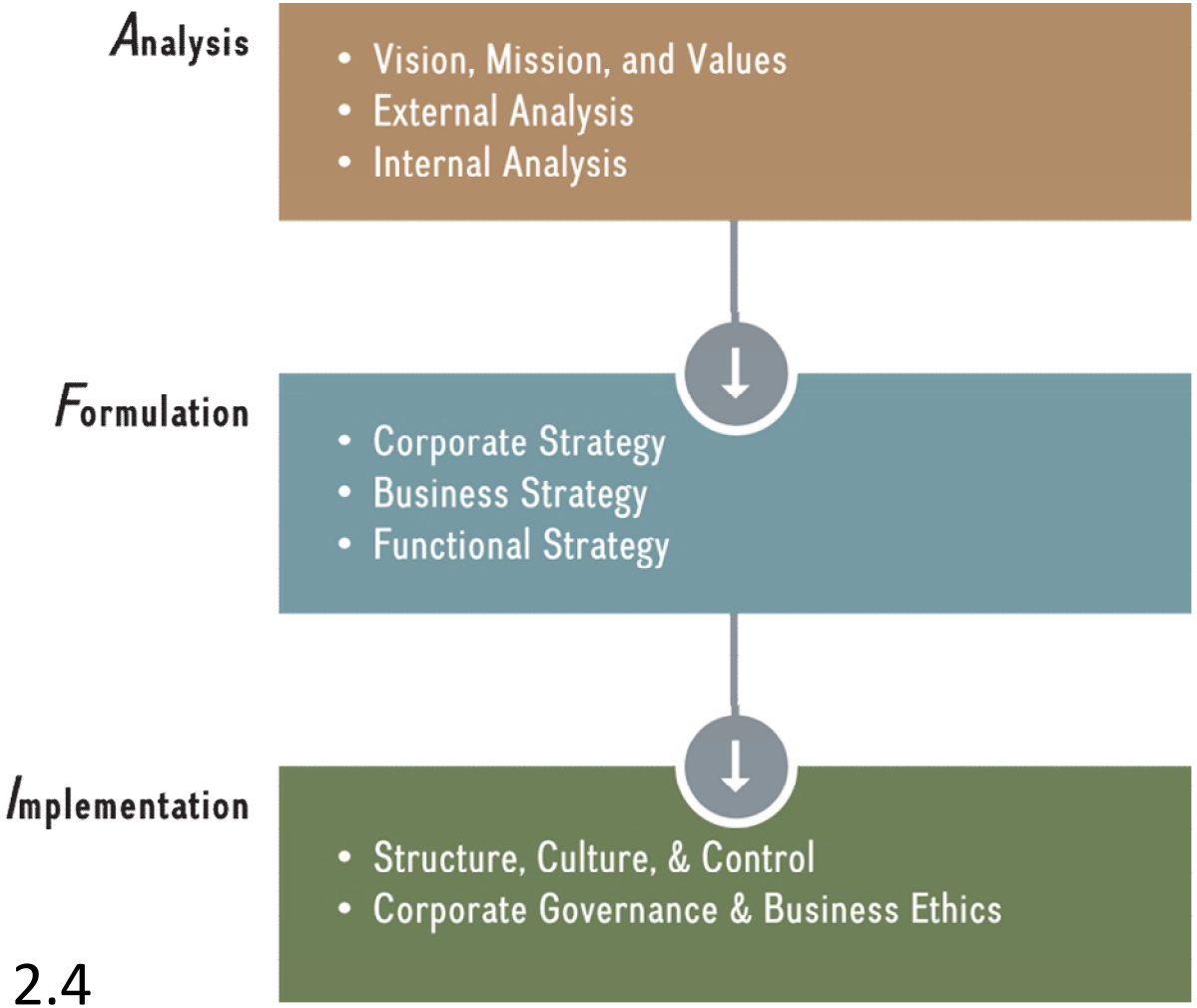


Exhibit 2.4

Jump to Appendix 5 long image description

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# Shortcomings of the Top-Down Approach

May not adapt well to change

Formulation separate from implementation

Information flows one-way

Leaders' future vision can be wrong

Example: Apple

- Steve Jobs predicted customers needs
- Apple didn't engage in market research
- Since Cook took over, their planning process has evolved

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# Scenario Planning (1 of 2)

Asks "what if" questions:

- Top management envisions different scenarios
- Then they derive strategic responses

Optimistic and pessimistic futures planned

Considerations can include:

- New laws
- Demographic shifts
- Changing economic conditions
- Technological advances

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# Scenario Planning (2 of 2)

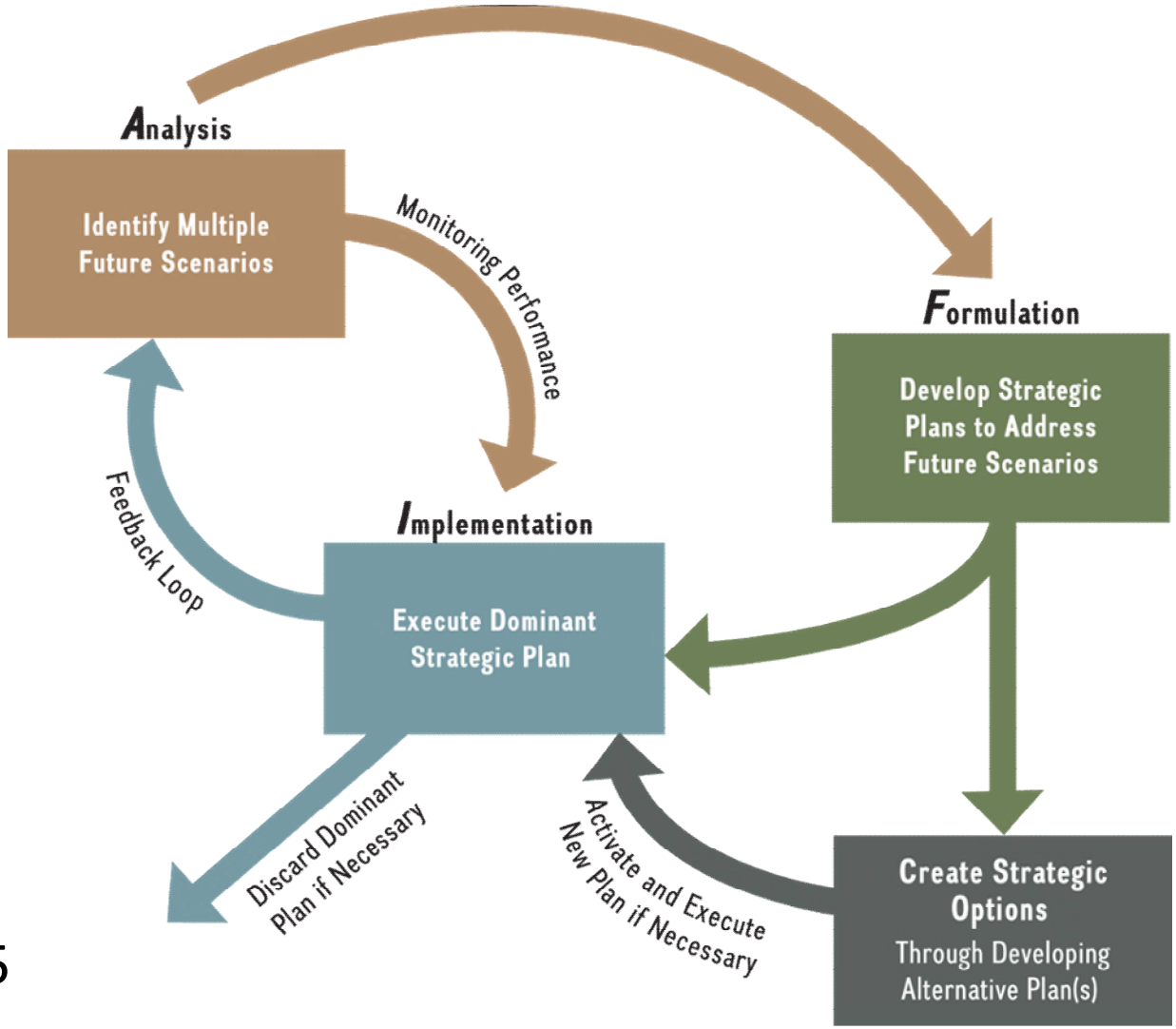


Exhibit 2.5

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Jump to Appendix 6 long image description

# Approaches to Scenario Planning

Obtain input from different levels and functions

- R&D, manufacturing, and marketing and sales

Determine how to compete situationally

- Example: UPS
- What if the price of a barrel of oil was $35, or $100, or even $200?

Attach probabilities to different future states:

- Highly likely vs. unlikely
- 85% vs. 2% likely

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# Black Swan Events

The high impact of a highly improbable event.

In the past, most people assumed that all swans were white.

- When they first encountered swans that were black, they were surprised.

Examples:

- Security breach of an IT system
- Accounting Scandals: Enron
- Real Estate Bubble: 2008 financial crisis

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# Questions to Ask in Scenario Planning

What resources and capabilities do we need to compete successfully in each scenario?

What strategic initiatives should we put in place to respond to each scenario?

How can we shape our expected future environment?

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# Strategy as Planned Emergence

## Top Down and Bottom Up

- Bottom-up strategic initiatives emerge
- Evaluated & coordinated by management

## Relies on data, plus:

- Personal experience
- Deep domain expertise
- Front line employee insights

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# Key Points About Strategy

Intended strategy

- The outcome of a rational and structured top-down strategic plan

Realized strategy

- Combination of intended and emergent strategy

Emergent strategy

- Any unplanned strategic initiative
- Bubbles up from the bottom of the organization
- Can influence and shape a firm's overall strategy

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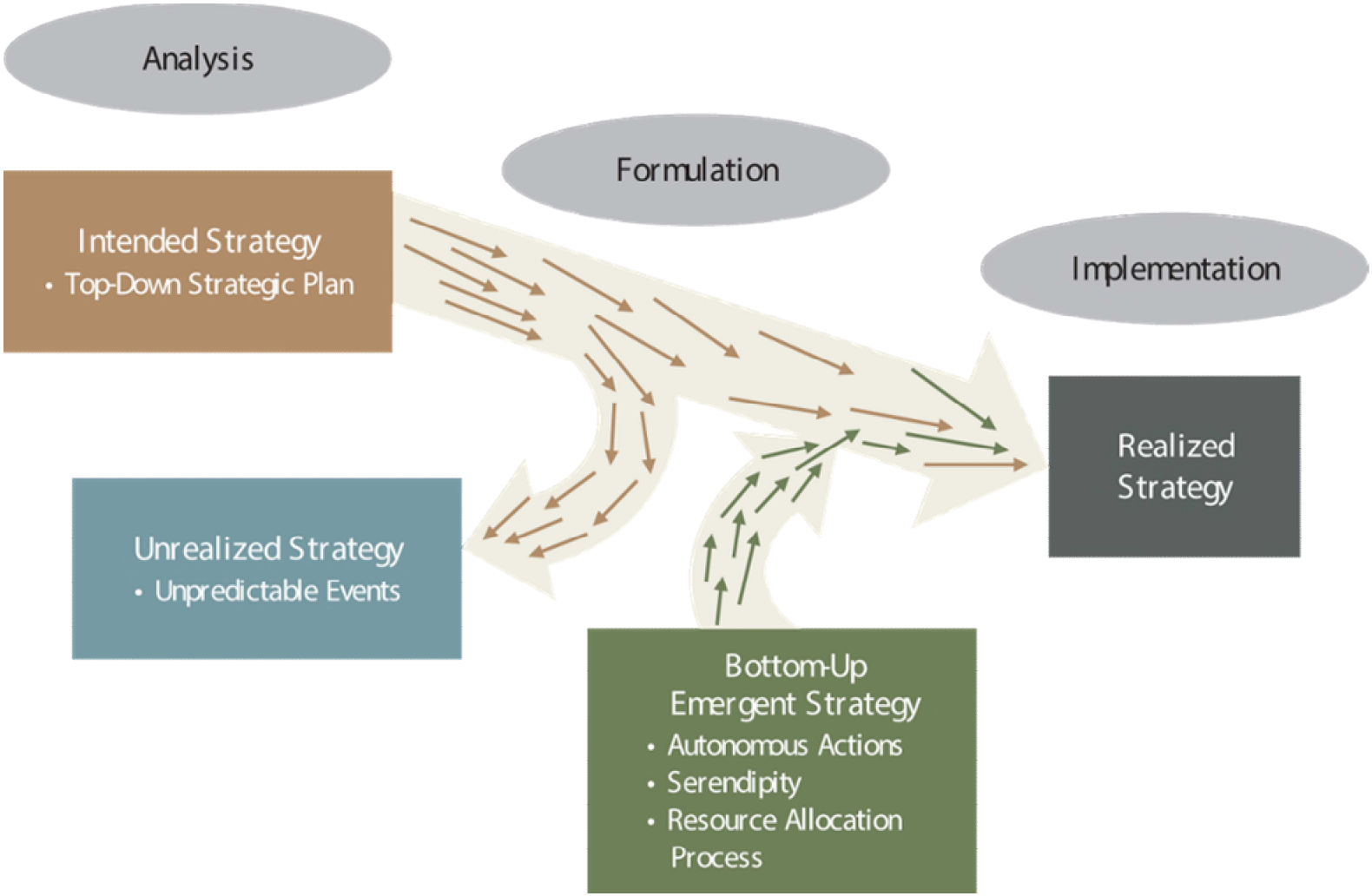
# Intended vs. Realized Strategy




Jump to Appendix 7 for long description

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# Strategic Initiatives

Any activity a firm pursues to explore and develop

- New products and processes
- New markets
- New ventures

Can bubble up from deep within a firm through:

- Autonomous actions
- Serendipity
- Resource-allocation process (RAP)

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# Autonomous Actions, Serendipity, and the Resource Allocation Process (RAP)

## Autonomous Actions

- Strategic initiatives undertaken by employees
- In response to unexpected situations

## Serendipity

- Random events, surprises, coincidences
- Has an effect on strategic initiatives

## Resource-Allocation Process (RAP)

- How a firm allocates resources based on policy
- Helps shape realized strategy

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# Companies with Good Strategy Are Valuable

Companies with a good strategy:

- Provide products or services to consumers at an affordable price
- Make a profit
- Can provide benefits such as:
  - Education, infrastructure, public safety, health care, clean water and air

Strategic failure is expensive

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# Stakeholders

Organizations, groups, and individuals

Can affect or are affected by a firm's actions

Have an interest in the performance and survival of the firm

Internal stakeholders:

- Stockholders, employees (including executives, managers, and workers), and board members

External stakeholders:

- Customers, suppliers, alliance partners, creditors, unions, communities, media, and governments at various levels

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# Internal and External Stakeholders in an Exchange Relationship with the Firm

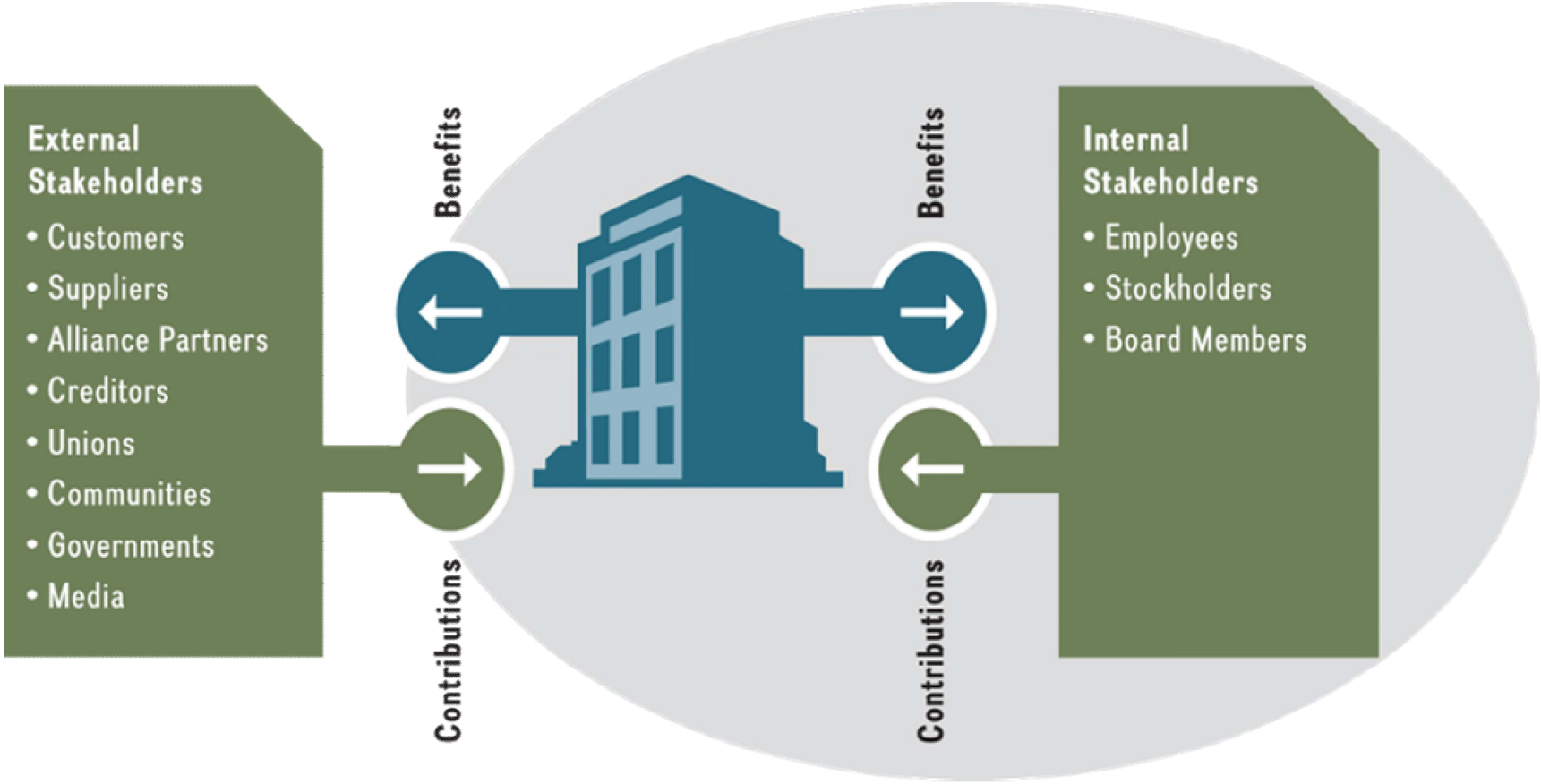


Exhibit 2.8

Jump to Appendix 8 long image description



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# Stakeholder Strategy

An integrative approach to managing a diverse set of stakeholders to gain and sustain competitive advantage

Stakeholder management benefits firm performance

- Stakeholders more cooperative
- Lower business transaction cost
- Greater adaptability and flexibility
- More predictable returns
- Stronger reputation

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# Stakeholder Impact Analysis (1 of 2)

A decision tool

Helps strategic leaders can recognize, prioritize, and address the needs of different stakeholders.

Important stakeholder attributes:

- Power: control over actions
- Legitimacy: valid concerns
- Urgency: require immediate attention

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# Stakeholder Impact Analysis (2 of 2)

Exhibit 2.9

Jump to Appendix 9 long image description



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# The Pyramid of Corporate Social Responsibility

**Exhibit 2.10**

SOURCE: Adapted from A. B. Carroll (1991), "The pyramid of corporate social responsibility: Toward the moral management of organizational stakeholders," *Business Horizons*, July-August: 42.

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Jump to Appendix 10 long image description

# Appendices
# Descriptions of Visual Graphics to Support Student Accessibility Needs

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# Appendix 1 The AFI Strategy Framework

The important inside circle is titled "Gaining and Sustaining a Competitive Advantage" that is at the very center of the image, with five different circles on the outside of it. Arrows go back and forth from the center circle to each of the five outer circles. The five outer circles are labeled: (1) Getting Started, (2) External and Internal Analysis, (3) Formulation: Business Strategy, (4) Formulation, Corporate Strategy, and (5) Implementation.

Each of these outer five circles have a brief description beside them to explain what the circle means:

Under the first outer circle titled "Getting Started," it says: Part 1, Strategy Analysis, "What is Strategy (Chapter 1)" and "Strategic Leadership: Managing the Strategy Process (Chapter 2)."

Under the second outer circle titled "External and Internal Analysis," it says: Part 1, Strategy Analysis, "External Analysis: Industry Structure, Competitive Forces and Strategic Groups (Chapter 3)," "Internal Analysis: Resources, Capabilities and Core Competencies (Chapter 4)," and "Competitive Advantage, Firm Performance, and Business Models (Chapter 5)."

Under the third outer circle titled "Formulation: Business Strategy," it says: Part 2, Strategy Formulation, "Business Strategy: Differentiation, Cost Leadership and Integration (Chapter 6)" and "Business Strategy, Innovation and Entrepreneurship (Chapter 7)."

Under the fourth outer circle titled "Formulation: Corporate Strategy," it says: Part 2, Strategy Formulation, "Corporate Strategy: Vertical Integration and Diversification (Chapter 8)," "Corporate Strategy: Strategic Alliances, Mergers and Acquisitions (Chapter 9)," and "Global Strategy: Competing Around the World (Chapter 10)."

Under the fifth outer circle titled "Implementation," it says: Part 3, Strategy Implementation, "Organizational Design: Structure, Culture and Control (Chapter 11)," and "Corporate Governance and Business Ethics (Chapter 12)."

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# Appendix 2 What Do Strategic Leaders Do?

This image is of a pie chart, which shows that CEOs typically spend, on average, 67 percent of their time in meetings, 13 percent working alone, 7 percent on e-mail, 6 percent on phone calls, 5 percent on business meals, and 2 percent on public events such as ribbon-cutting for a new factory.

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# Appendix 3 Level-5 Pyramid

This image shows a pyramid that progresses from Level 1 at the lowest part of the pyramid to Level 5 at the highest part of the pyramid. The levels as they progress are

Level 1: Highly Capable Individual

Level 2: Contributing Team Member

Level 3: Competent Manager

Level 4: Effective Leader

Level 5: Executive

Return to slide



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# Appendix 4 Strategy Formulation and Implementation Across Levels

This image shows several boxes in an organization-chart format. At the top level, is "Headquarters Corporate Strategy: Where to Compete?," below that box are three different boxes, Option 1 Cost Leadership, Option 2 Differentiation, Option 3 Value Innovation, each of which say "Business Strategy, How to Compete?." After choosing one of these options, the next level is labeled Business Function 1, Business Function 2, and Business Function n 4. Each of these four boxes say "Functional Strategy: How to Implement Business Strategy?"

Return to slide



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# Appendix 5 Top-Down Strategic Planning

This image depicts three boxes. The top box is titled "Analysis" and contains three bullets titled Vision, Mission, and Values, External Analysis, and Internal Analysis. The middle box is titled "Formulation" and contains three bullets titled Corporate Strategy, Business Strategy, Functional Strategy. The bottom box is titled "Implementation" and contains two bullets titled Structure, Culture and Control, and Corporate Governance and Business Ethics.

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# Appendix 6 Scenario Planning

The elements in the AFI strategy framework are placed in a continuous feedback loop, where Analysis leads to Formulation to Implementation and back to Analysis. This image elaborates on this simple feedback loop to show the dynamic and iterative method of scenario planning.

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# Appendix 7 Intended vs. Realized Strategy

This image shows a big arrow along a line that follows three phases of Analysis, Formulation and Implementation. At the beginning of this line is a box that says "Intended Strategy" which is a top-down strategic plan. Coming out of the intended strategy is unpredictable events, and feeding into the strategy is bottom-up emergent strategy including autonomous actions, serendipity, and the resource allocation process. This activity results in the realized strategy at the end of the graphic.

Return to slide



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# Appendix 8 Internal and External Stakeholders in an Exchange Relationship with the Firm

The graphic shows the flow of the relationship between stakeholders and the firm.

The external stakeholders are customers, suppliers, alliance partners, creditors, unions, communities, governments, and media

The internal stakeholders are employees, stockholders, and board members.

Benefits flow from the frim to both of these groups of stakeholders as the firm receives contributions from both.

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# Appendix 9 Stakeholder Impact Analysis

The graphic lists the steps of stakeholder impact analysis.

Step 1: Who are our stakeholders?

Step 2: What are our stakeholders' interests and claims?

Step 3: What opportunities and threats do our stakeholders present?

Step 4: What economic, legal, ethical, and philanthropic responsibilities do we have to our stakeholders.

Step 5: What should we do to effectively address the stakeholder concerns?

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# Appendix 10 The Pyramid of Corporate Social Responsibility

The pyramid's is economic responsibilities: gain and sustain competitive advantage.

The next level is legal responsibilities: laws and regulations are society's codified ethics; define minimum acceptable standard.

The next level is ethical responsibilities: do what is right, just, and fair.

The tip of the pyramid is philanthropic responsibilities: corporate citizenship.

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