Managing Your Business

Noordhoff Uitgevers

Irenee Dondjio & Robert Haafst

First Edition

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Managing Your Business

A Practical Guide

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Preface

The idea for this book was born in South Korea where, participating at the Konkuk University summer programme in 2011, Irenee was asked to design a business course for the summer programme. As a lecturer of Economics, Global Marketing, Maths, and Marketing at the Hague University, the Netherlands, Irenee realised he could combine all of these courses into one package, which he called Managerial Business. The course was well-received by both staff and students, and motivated him to compile the experience in this book, Managing Your Business (MYB).
In the arena that is modern-day business, mastery of Economics, Marketing, Financial- and Cost Accounting is crucial. Managing Your Business provides its readers with a clear understanding of business in general, specifically how the economy helps shape today's Marketing. A competent marketer should be able to set a good pricing strategy and decide on the right level(s) of production: aspects which both rely on a basic understanding of cost accounting. Marketers also benefit from the ability to read and understand balance sheets and income statements, which are essential in business. Lastly, mastering the basics of financial accounting helps marketers excel in their strategic planning.

Managing Your Business is intended to teach business decision-making to students in BBA, MBA and other Economic Degrees, and allows students to analyse, synthesise, and evaluate data from the various functional areas of business (e.g. Marketing, Finance, Accounting and Economics). Effective management requires appropriate decision-making abilities, long-term planning skills, human relations expertise, and motivational skills; Mind Your Business teaches students to understand and apply these four basic functions of management.
This book is intended for those who would like to acquire or improve their skills in strategic management, and to help business owners and entrepreneurs who are looking for a better understanding of their business and the environment in which they operate to comprehend, improve, and possibly expand their influence.

This book came to fruition with the helpful contributions of many people (Jochem Vreeke, participation in Chapter 4; Professor Sanjay Sharma and Soon-ok Heijmans, participation in Chapter 10; Professor Sunshine Cowan; Professor Dixon, participation in Chapter 5; Peter Heinen, participation in Chapter 3 and 4; Florence Akebe, participation in Chapter 3; Jimmy Jordan, Harrison Akoh, Etienne Nankeu, participation in Chapter 9; Peter de Vos, participation in Chapter 2), for which we would like to thank them all.
A special word of thanks to Hans Hoekstra for finetuning, and to Jan-Willem Tjooitink for proofreading.

This book is dedicated to our entire families, in particular our wives and daughters. Chapter 7 is dedicated to Toon Haafst, the father of one of the authors.

The Hague, 2016

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PART 1
The Internal Business Environment

The first part of this book looks at the concept of the company and how a company deals with its environment. Every company has a product it wishes to sell. In many cases, however, it will not be the only company selling this product; what every company needs are a competitive advantage and a certain uniqueness that appeals to its customers. Based on an analysis of the markets it operates in and an analysis of its own strengths and weaknesses, a company can determine a strategy for approaching the market. This strategy is used to derive a business model. Company strategy establishes which markets should be approached. A business model establishes what resources and unique proposals are needed to successfully sell products. The final step is the marketing plan, which establishes how the markets should be approached.
This chapter focusses its discussion on how companies determine strategies, business models and marketing plans, as well as on how a company manages one of its most important resources, namely human resources(HR), and how HR links to company strategy. The role of HR in adding to successful implementation of a strategy and marketing plan is also discussed.
Once a company has managed to cover the basics, it is time for the next step: accounting and finance. Accounting is needed because a company has to record its transactions; not just for tax purposes, but also because management wants an overview of how cash is spent and how much is earnt. In addition, a company needs to know how it can finance its activities.
In a nutshell, this part of the book explores the relationship between a firm's competitive advantage and its internal capabilities (or core competencies), as well as how a firm develops unique and superior resources and capabilities that are difficult for other firms to replicate.

Chapters included in part 1:

1 Business Model and Goal

Learning objectives

After studying this chapter, you should be able to define, understand, and assess:
- Mission
- Vision
- Mission and vision values in the planning process

Moreover, you should be able to understand:
- The differences between core and distinctive competencies
- The VRIO Model
- The importance and use of Business Model Canvas
- The company culture and structure

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1.1 Introduction

The success of companies relies mostly on the adequate utilisation and management of both internal and external resources and capacities. This chapter focusses on the internal factors, while the next chapters focus on the external ones. Internal analysis provides the tools needed to identify the strengths on which to build, and, equally importantly, the tools to recognise existing weaknesses. Both must be taken into consideration when formulating strategies. The internal analysis reflects a company's resources: its activities, objectives, policies, and plans.

Competitive advantage

Core competencies

Managers can use an internal analysis to find a company's competitive advantage. Basically, the competitive advantage is what one company has or does that is better than its competitors. Examples include offering lower prices for products, or understanding customers better than the competitors. Competitive advantages rely heavily on a company's core competencies.

Internal analysis

Internal strategic management audit

Internal analysis or an internal strategic management audit should start by identifying a firm's mission and vision. An audit begins by creating an understanding of strategy and performance. Auditing a firm helps assess the factors that affect the organisation's welfare. All organisations, regardless of size, nature, or scope of activities, need marketing, production/operations, finance/accounting, research and development, IT, and human resources to perform efficiently. Therefore, planning, executing, and managing these various functions is paramount an organisation's success. An internal strategic management audit begins by mapping and understanding a company's mission and vison.

Mission statement

Mission Statement

A mission statement describes an organisation's long term goals, or what it aims to achieve in business and often also in society. Mission statements therefore frequently contain elements such as 'market leader', 'product leader', 'most sustainable', 'most user-friendly', etc.

A major ferry cruise-line company, for example, could have the following mission statement: 'We are the most reliable ferry-cruise company in the industry with the lowest number of customer complaints and the highest number of on-time arrivals.'

A mission statement can help stakeholders decide whether or not they want to do business with an organisation. A mission statement should be no longer than three sentences. Most often, companies struggle in drafting their mission statement. They often confuse the concepts of 'vision' (why they exist), 'mission' (what they want to achieve), and 'strategies' (how they want to achieve both).
In the case of Nespresso, the mission would have been to successfully turn the vision into a profitable business line. For Nestlé's major stakeholders, this goal will have been made a bit more specific, but any further specifications would have been included in the defined strategies for their marketing, production and logistics; in other words: a specific new business model.

Samsung's website indicates the following: 'We do not have an official mission but express it through company's philosophy: At Samsung, we follow a simple business philosophy: to devote our talent and technology to creating superior products and services that contribute to a better global society.'

Two more examples of mission statements:
- Nike: 'To bring inspiration and innovation to every athlete in the world.'
- Starbucks: 'To inspire and nurture the human spirit — one person, one cup and one neighborhood at a time.'

In order to evaluate a mission statement, several key criteria must be adhered to.

The mission statement should:
- fit the current market environment
- be based on core competencies
- be motivational, and inspire employee commitment
- be realistic
- be specific, short, focussed and memorable
- state what the company wants to be remembered for
- be clear and easily understood

This list suggests that a mission statement actually consists of the first steps required to design the framework of a company; hence, it can even serve as some sort of rough guideline in future decision making. Looking closer, there emerges a possibility of combining several criteria into three generalised criteria, being:
- What would be the generalised target market for the company?
- What will the company provide to this market?
- How is the company going to stand out from the crowd?

These three criteria can be summarised this into three keywords: Market – Provision – Differentiation. This leads to a new definition of what a mission statement is:

> A mission statement sums up what a company aims to provide to a certain market, and how the company will differentiate itself from the competition. (Haafst, R. 2016)

Vision Statement

There exist many definitions of 'vision' in a business context. One might state that, through a vision statement, a company communicates its purpose and its reason for existing. A vision statement explains why a company does what it does. Most organisations are driven by a purpose, but this purpose is not always clearly defined. Employees may not even be aware of it. It is therefore crucial that an organisation devotes time to drafting their vision statement.

Vision statement

A company's purpose is not to be confused with business goals, such as 'profitability' or 'growth'. A vision means recognising a need in a specific customer segment and knowing how to address that need. From that vision, which also requires strong support among management/entrepreneurs as well as leadership and organisational skills to achieve, the mission and strategies will follow.

'If Apple was like everyone else a marketing message might be: We make great computers. They're user friendly. Want to buy one? …Here's how Apple actually communicates: everything we do, we believe in challenging the status quo, we believe in thinking differently. The way we challenge the status quo is by making our products beautifully designed, simple to use, and user friendly. We just happen to make great computers. Want to buy one?' (Simon Sinek – 'It all starts with why', Golden Circle)

In 1988, Nestlé had a vision of households wanting to experience a 'barista' type of coffee making and drinking in their homes. The company turned that vision into a totally novel solution: espresso machines using one-portion coffee pods, coined 'Nespresso'.

A vision statement can be seen as a tool to help managers verify whether a company is reaching its goals. If scheduled progress of action doesn't move a company toward its vision, the vision may need to be reviewed and adjusted.

Samsung's vision: 'Samsung is dedicated to developing innovative technologies and efficient processes that create new markets, enrich people's lives and continue to make Samsung a digital leader.'

Competencies

Core competency

A core competency is an activity central to the overall profitability and attractiveness of a company. It helps a company meet the critical success factors in particular market segments. Core competencies are the resources and capabilities needed to differentiate their products and services from those of their competitors, and should thus add (additional) value for a customer.

Resources

Resources are a company's assets. These assets come in three forms:
- Tangible assets,
- Intangible assets, and
- Human assets.

Tangible

Tangible assets are assets which can be seen, touched, felt, heard or smelled; examples are land, buildings, equipment, and customer databases.

Intangible

Intangible assets are those which cannot be seen or touched, such as brand loyalty. Resources are developed mainly due to company investments, and by building and utilising its capabilities.

Capabilities

Capabilities are the blend of skills and human assets in the current use of resources, such as through technology, brands and knowhow.

Misalignment of Resources and Capabilities

In 2013, a hospital in Kabul, Afghanistan bought a state of the art CT Scanner, worth just shy of $1 million. Proud as the hospital staff as, they claimed to now have the best radiology department in Asia. Part of the contract was that one user would be trained to operate the machine, following a train-the-trainer principle. In other words, following its installation, there was only one person in the country who actually knew how to operate this machine. After a few months, this person left the hospital, and in the meantime had not trained anyone else on how to operate the machine. The hospital, afraid of more people leaving the hospital as soon as a training was finished, was reluctant to provide training for another doctor. Eventually, this has resulted in the machine barely being used since 2013.
This is a clear example of misalignment of resources and capabilities. The hospital has the resources required for the best radiology department in the country, but lacks the capabilities needed to actually handle those resources.

Distinctive competency

One step beyond a core competency is the distinctive competency, which is a core competency in which the company outperforms its competitors. In other words, a competency that provides a company with a competitive advantage over its competition.

GE considers its core competency to be ‘the global recruiting and nurturing of the world’s best people’. According to Hamel and Prahalad, the core competences of any business are the ones which contribute to customer value or the efficiency of the delivery of this value, and those that are a foundation for entering new markets. Companies gain profits from their resources and capabilities (competences), which depend on factors such as the ability to establish a competitive advantage, to sustain that advantage, and to appropriate the returns on that advantage. Therefore, firms need to identify what could be potential as well as beneficial resources and competencies for their future and apply them effectively in their strategy. It has been found by Nahory, et al. (2016) that top-level managers viewing people as a strategic resource improves involvement of their employees. In other words, if employees feel they are valuable to and valued by the company, they will perform better and be more motivated. Of course, it is also up to the company itself to select the right people for the job; people who are willing to contribute their efforts and fulfil the firm’s goals. This competency can be very powerful strategically, because any firm’s capabilities are dependent on the skills and efforts of its employees. Challenging workers and giving them appropriate and encouraging rewards leads them to become better at their tasks, in the ending add value and profit to the business, as well as pushing it forward. (Nahory et al. 2016)

1.2 The VRIO Framework

VRIO framework

Barney and Hesterly (2006) designed the VRIO framework to be a suitable instrument for assessing a firm's internal environment. VRIO is an acronym for Value, Rarity, Imitability, and Organisation. Each of these keywords stands for a specific set of questions, which must be raised and answered in order to successfully determine a company's competitive internal environment. Unique to this model is the fact that it can be applied to every single sector or industry in the world. An excellent way of explaining this framework is by applying it to Apple.

Apple VRIO

Over the past 5 years, Apple shares rose by 255%, more than doubling the Nasdaq's return. This growth has been attributed the popularity of the Apple brand mostly for its star products: iPhone and iPad.

TABLE 1.1 VRIO Apple

Apple's VRIO ability on the closed ecosystem and brand appeal			
Valuable?	Rare?	Costly to imitate?	Can the company exploit it well?
yes	yes	yes	yes
Result: sustained competitive advantage			

Value

The term value revolves around the question of whether a certain capability or resource is, indeed, of value to the company. Value to a firm means that it allows a firm to either exploit an opportunity, or to lower the possible impact of a threat. A company should be careful, since its values that are not exploited to the full can instead become weaknesses. To make matters even more complicated, characteristics that are of value in one industry do not necessarily translate very well to another. Over the following chapters, this book will focus more on specific strengths, weaknesses, opportunities, and threats, using the so-called SWOT-Analysis. Generally speaking, an identified valuable resource or capability used to the fullest results in higher revenues, or lower costs. In other words, it creates a certain level of efficiency within the company.

Applied to Apple's example, this means that Apple products are mostly valuable due to their specific software and the high level of brand loyalty – and awareness.

Rarity

Secondly, following value, a company must establish whether or not the resources and capabilities to which it has access are rare. In other words: If a large number of firms have access to similar or the same resources or capabilities, then these do not constitute a rarity, allowing the competition to conceive of, and implement, the exact same strategy. If, on the other hand, the resources or capabilities are valuable and rare, a company can be said to have a competitive advantage for as long as their competitor cannot replicate these factors.

Competitive advantage

As only Apple can legally use their software (iOS), this software is considered a rarity. At the same time, the software is seen as one of Apple's USPs (Unique Selling Prepositions).

Imitability

Thirdly, a company must obtain an insight in to both cost structure and imitability. In other words, companies should be aware of cost behaviour of their resources or capabilities. They must establish whether costs are one-off or recurring events. Moreover, companies should evaluate whether costs are relatively high or low in order to sustain or develop that particular resource or capability.
Closely linked to but still separate from the cost factor is the matter of imitability. Companies should establish whether they (or their products) can be imitated easily by their competition. The higher the cost, the lower the probability of imitation. If a resource is both valuable and rare, and the probability of imitation is low, a company can be said to have a sustained competitive advantage.

Sustained competitive advantage

Apple's closed ecosystem and brand appeal are seen as its sustainable competitive advantages. In contrast to many other devices from their main competitors, like Samsung, HTC, LG, whose devices all run on Android (Google), Apple devices use iOS. Apple's brand name, hardware and software are hard to imitate; this is essentially due to Apple having protected their software (iOS) with several patents.

Organisation

Lastly, a company should also investigate its organisation, establishing beyond a doubt that the company is organised in such a way as to be able to effectively use and protect the value, rarity and imitability of its resources or capabilities. This involves looking into procedures, company policies, and compensation structures. If a company is successful, then it can acquire and hold a sustained competitive advantage.

Sustained competitive advantage

Is Apple organised to capture value from this competence? Very much so: Apple has trained managers and dedicated high skilled employees, who are proud to be part of one of the most renowned companies in the world. Therefore, they are more motivated and willing to work continuously on the innovation of products.

Table 1.2 provides an example of how to apply the VRIO framework, and the possible outcomes for a firm under changing circumstances.

1

TABLE 1.2 The VRIO framework, Adapted from J.B. Barney, 'Firm Resources and Sustained Competitive Advantage,' *Journal of Management* 17 (1991), pp. 99-120

Applying the VRIO Framework		
If the firm's resources are: Not valuable	→	The firm can expect: Competitive Disadvantage
Valuable, but not rare	→	Competitive Parity (Equality)
Valuable and rare, but *not* costly to imitate	→	Temporary Competitive Advantage
Valuable, rare, and costly to imitate	→	Sustained Competitive Advantage (if organised properly)

1.3 Business Model Canvas

Business model

Business Model Canvas

Whenever a company wants to develop a new business model in order to overhaul the company, or simply wants or needs to create a graphical representation of its existing business model, one available tool is the Business Model Canvas, or BMC for short. This business model is a representation of how a company delivers, creates and/or captures added value. This is important not only in terms of economics and financial statements, but equally so in cultural, demographic, or social terms. BMC is a simple but effective graphic capturing the business model, which can be described using the nine building blocks illustrated in table 1.3. BMC essentially builds on three principles. Contrary to traditional business plans, BMC focusses on what drives a business. BMC is also much easier to fine-tune as it can be drafted on a single page. Additionally, it provides managers with a swift and adequate way of understanding the business model, mission and vision of a company since all information is accessibly provided on one page.

TABLE 1.3 The Business Model Canvas

<table>
<tr><td rowspan="2">(Key Partners)</td><td>(Key Activities)</td><td rowspan="2">(Value Proposition)</td><td>(Customer Relationships)</td><td rowspan="2">(Customer Segments)</td></tr>
<tr><td>(Key resources)</td><td>(Channels)</td></tr>
<tr><td colspan="2">(Cost structure)</td><td colspan="3">(Revenue Streams)</td></tr>
</table>

These nine building blocks can be categorised into four segments, namely: Infrastructure, Customers, Supply, and Finances.

Infrastructure
Infrastructure consists of the three top left blocks: key partners, activities and resources.
The activities are the actual actions needed in order to maintain a competitive advantage or execute a company's value proposition.
The partners are all those partners in any capacity who may help a firm achieve its goals.
The resources are the company's basics, the core of what is, needed to add value for a customer. These factors should all be combined; or in other words, what are key partner activities, etcetera.

Supply
The supply is basically the combination of all products and services a company provides for its customers. Hence, the value proposition falls into this category. The value proposition may be split up in a qualitative part, defined as experiences and other non-quantifiable aspects, and the quantitative part, defined as efficiency, lead times, prices, etcetera. A company must therefore focus on what value is being delivered, what problems a company can resolve for its customers, and so on.

Customers
All aspects concerned with and involving customers belong to this category; in other words, customer relationships, segments, and channels.It is important to define in which segment a company operates, and if that is indeed the most profitable segment. In addition to that, the relationship with the customer must be defined. For example, a company may want to provide personal assistance for customers, or may rather have customers depend on self-service. Equally important is channelling, and establishing the best, or most cost effective way of channelling products and services to the customer.

Finance
The last category is company finances. Finance is split up into two blocks: the cost structure and the revenue stream. A company needs a good understanding on its cost structure; alternatively, it needs knowledge of how all costs are quantified. Moreover, an understanding of the most and the least expensive activities and resources is needed. Once the cost structure is understood, the revenue streams are next. Companies should establish how prices are set, and what effects a price cut or price increase might have on total revenue.

All of the above can be combined in the initial table, such as in the example found in table 1.4.

The following example of a BMC gives an idea of the business operations of a coffee capsule distributor. To process and distribute its coffee capsules to the Dutch market, Pearl Coffee works together with coffee bean traders, cups manufacturers, and packaging companies. Passionate and devoted coffee lovers who own a coffee cup machine can order the coffee cups via the website at any time. Pearl Coffee follows the JIT (just in time) principle. **Just in time**
The product is processed and delivered exactly when the customer needs it.

TABLE 1.4 BMC Pearl Coffee

Key Partners	Key Activities	Value Proposition	Customer Relationships	Customer Segments
Coffee beans traders Cups manufacturers Packaging	Coffee processing on demand Brand building Packaging and delivery	High customised quality and affordable coffee cups on demands	Email/newsletters Chat/self-portals	Passionate and devoted coffee lovers
	(Key resources) Web design Knowledge of coffee types worldwide. E-business		**(Channels)** Web sites Social media Email Chat/ self-portals	
(Cost structure) **Fixed costs** (machines, insurance, wages, utilities, marketing costs) **Variable costs** (cups, coffee beans, packing)		**(Revenue Streams)** Unit sale per set of 15 month subscription		

JIT

JIT is a theory established as a precursor to lean manufacturing. It revolves around the ideal of eliminating or reducing all sorts of 'waste' in the company. Waste should here be considered in the broadest sense of the word; hence, it includes inventories, defect products, over-production, waiting time, and waste of spill-over products. In essence, JIT aims to establish a manufacturing cycle in such a way that one manufactures exactly the amount of product required exactly when customers demand it.

Customers can customise their own coffees based on the extensive worldwide coffee variety provided. Pearl Coffee sells and advertises its product via social media. Communication with customers is done via emails and their website. Customer can choose monthly payments (subscription) or payment upon order.

1.4 Organisational Behaviour

The culture and structure of a company are its backbone. They refer to a system of shared assumptions, values and beliefs that indicate what type of behaviour appropriate or inappropriate. More often than not, company culture is referred to as the soft side of the company, while structure is defined as the hard side. There are numerous ways and hundreds of theories for describing the culture of a company. This book focusses on the 'cultural dimension theory' defined by Geert Hofstede. Various leadership and management styles are also discussed and considered. Lastly, the structures of companies are explained using Mintzberg's theories on the subject.

Any organisation, no matter its size, develops its own organisational culture over time. This culture is translated into the so-called corporate values. For example, the corporate values of Toyota are: Integrity, Customer-Focus, Teamwork and People Empowerment. Research shows that organisational culture can have a huge impact on a firm's performance and long-term effectiveness (Mintzberg, 1980). It also has a positive impact on staff performance and commitment.

In Practice

Just as the New York Times' scathing indictment of Amazon and its workplace culture hit the internet earlier this month – before the print edition was even in many readers' hands – Amazon's CEO Jeff Bezos sent a memo to his employees in an effort to contain the impact.
Perhaps admirably, he acknowledged the controversy and encouraged his employees 'to give this...article a careful read.' But that's where his success as a leader in a moment of organisational culture crisis ends. Bezos' attempt at damage control fails miserably precisely because it highlights the problems that created the vicious working environment that the Times describes: limited appreciation for the people delivering the company's success; half-hearted attempts to avoid a toxic culture rather than cultivation of a healthy one; and leadership that distances itself from its people rather than connecting and empathizing with them.
YSC (2015)

1.4.1 Structural Design

Organisational structure

Organisational structure can be very complex, as organisations can employ thousands of people working in different level and roles. In order to manage their results more effectively, businesses must have a clear organisational structure. A firm's structure is, in principle, the manner in which an organisation's workforce is structured and divided into specific job roles and responsibilities among the entirety of the workforce. A company structure that is not well-thought out not only makes communication within the company difficult, but may also hamper the company's visionary goals and management.

Organisational Design

Divided by labour

Differentiation

Coordinating

Company organisation must be thought of as an evolving process; a flow that, as the company grows bigger, must be guided in the correct direction in order to shape the company. Normally, an organisation is divided by labour. In other words, breaking a task into a number of simpler tasks and assigning these to specific jobs, departments, and levels. This process is also called differentiation, as different tasks call for different skills. Then, by coordinating, different specialists/departments/levels can be made to work together to fulfil desired goals in an organisation. Basically, the organisation should be viewed as a system or process operating within the following framework:

- Input – transformation – output
- Reacting and interacting with the environment
- Evolving over time
- Changing one thing leads to changing others
- 1 + 1 = 3

- Ever adapting systems to the environment
- No ‘single’ optimal solution
- Difficult to strike a ‘balance’
- Easily ‘out of balance’

Organisational design

Structural dimensions

Organisational design is important because it gives a clear insight into a firm’s strategy; whether, for example, a firm is more R&D focussed or more sales focussed. Additionally, a balanced design creates efficiency, and ensures an effective company. To describe and construct an organisational design, the structural dimensions must first be defined.

Structural Dimensions

The structural dimensions of a firm not only create its structure; they also assist leadership and management styles as shown in section 1.4.2, and culture as shown in 1.4.3. Structural dimensions can be split up into dimensions of division of labour and dimensions of coordination.

Division of Labour Dimensions:
- Horizontal Differentiation (Specialisation)
  - Functions/departments/BU/Divisions/regions
  - Outsourcing
  - Personnel ratios
- Vertical Differentiation (Hierarchy or Lines of Authority)
  - High or long lines
  - Low or short lines
- Professionalism
- Centralisation/Decentralisation
  - Vertical decentralisation
  - Horizontal decentralisation

Coordinating Dimensions:
- Formalisation or Standardisation
  - Input
  - Processes
  - Output
- Socialisation (unwritten Rules/Values)
  - Standardisation by culture
- Control (Formalisation/Standardisation) vs. Mutual Agreement
  - Control before (budget)
  - Control during
  - Control after (performance)

Differentiation

Span of control

First of all, the differentiation of the company must be considered; this is basically how the company is set up in terms of function. Therefore, the span of control of every manager must be defined. A large span of control means managing a lot of people, which in turn means a flatter organisation, and vice versa. The next step is deciding on a company set-up. The set-up of a company can be done efficiently in four different ways:
- Functional (specialisation)
- Divisional (grouping)
- Combined (grouping) and
- Matrix (grouping)

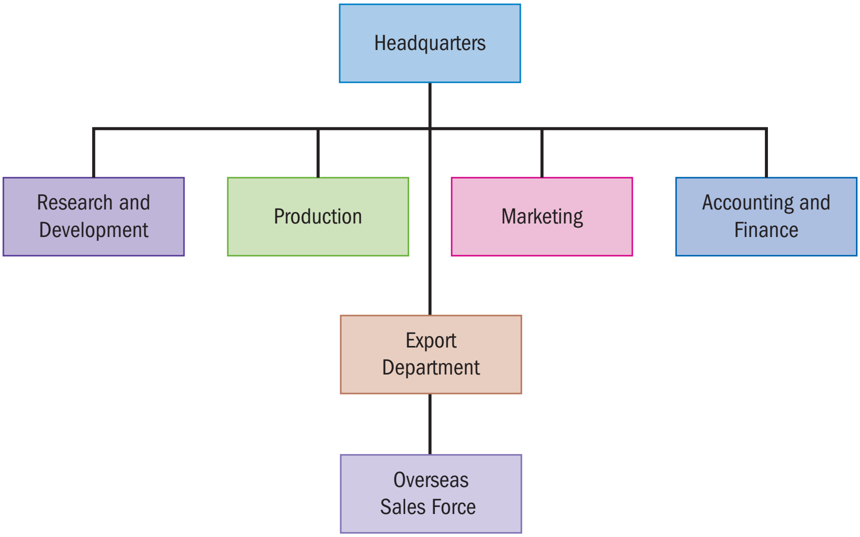
Each of these company set-ups, discussed below, contributes its own particular pros and cons.

Functional

Functional specialisation

Functional specialisation is applied by roughly 60 percent of organisations. It is done by grouping together all functions in the organisation. In doing so, people with the same specialties, skillset, abilities, and tasks are grouped together, creating efficiency and in-depth specialisation. Its downside is that it becomes more likely for communication across functional areas to deteriorate with employees having a limited view of organisational goals.

FIGURE 1.1 Functional Structure



Source: http //home.southernct.edu

Divisional grouping

Divisional grouping

Larger companies and conglomerates tend to use the divisional grouping structure. Divisions are arranged by product, type of client, or region. This results in a deep and thorough understanding of the product group or region, with managers becoming real experts in their respective areas of industry. Moreover, this setting ensures that the organisation is much closer to its clients. However, due to the duplication of functions it may be more expensive than a functional setting and, similarly, there is little insight into organisational goals.

Combined grouping

Combined grouping

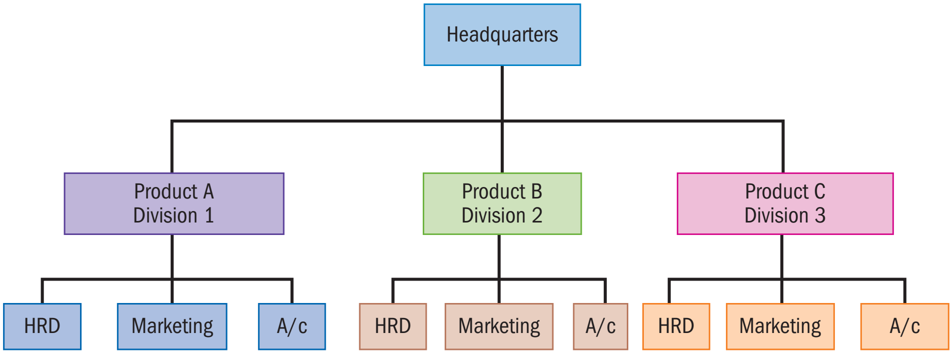
Combined grouping is done by arranging the top of the firm according to divisional structure, and the rest of the firm by functional grouping. The same pros and cons of functional and divisional grouping apply throughout the company.

Matrix Structure

Matrix grouping

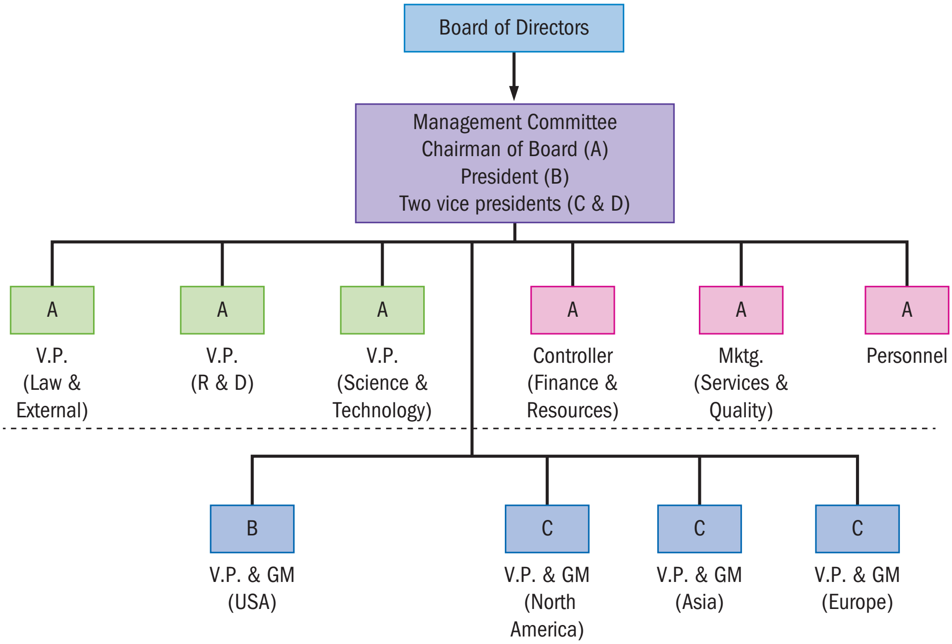
A matrix typed firm is arranged so that information and knowledge are easily transferred from one project to another. Furthermore, personnel is easily

FIGURE 1.2 Divisional Grouping



Source: http //book.transtutors.com

FIGURE 1.3 Combined Grouping



transferred from one department or division to another, which allows for flexibility, and creates economies of scale. On the other hand, matrix grouping is likely to result in having to spend a lot of time attending to meetings, as individual employees may be part of several units. On top of that, it may result in too much responsibility, and too little authority (half delegation), because individual roles and responsibilities are not necessarily clear.

Duality of command

On top of that, insufficient communication between units may result in a lack of synchronisation. Lastly, employees having two or more bosses may fall victim to power games, which is referred to as duality of command.

FIGURE 1.4 Matrix Structure

Project A (Team Leader)	Marketing Team (A)	Operations Team (A)	Finance Team (A)	HR Team (A)
Project B (Team Leader)	Marketing Team (B)	Operations Team (B)	Finance Team (B)	HR Team (B)
Project C (Team Leader)	Marketing Team (C)	Operations Team (C)	Finance Team (C)	HR Team (C)
Project D (Team Leader)	Marketing Team (D)	Operations Team (D)	Finance Team (D)	HR Team (D)

Source: http //s3-eu-west-1.amazonaws.com

It is important not overspecialise a firm. Overspecialisation can result in human diseconomies through boredom, fatigue, stress, poor quality, increased absenteeism, and higher turnover. Therefore, excessive specialisation may lead to disintegration. To counter the effects of overspecialisaton, a firm must hire extra personnel, and make use of integrating mechanisms, such as liaison officers, task groups and teams.

Over-specialisation

Disintegration

Integrating mechanisms

Vertical Differentiation

Vertical differentiation visually demonstrates the chain of command, which is the continuous line of authority that extends from the upper levels of an organisation to its lowest levels, and specifies who reports to whom. The more layers a company has, the more bureaucratic it will be, and the slower any call to action. However, the number of layers is not proportional to the size of a firm.

Chain of command

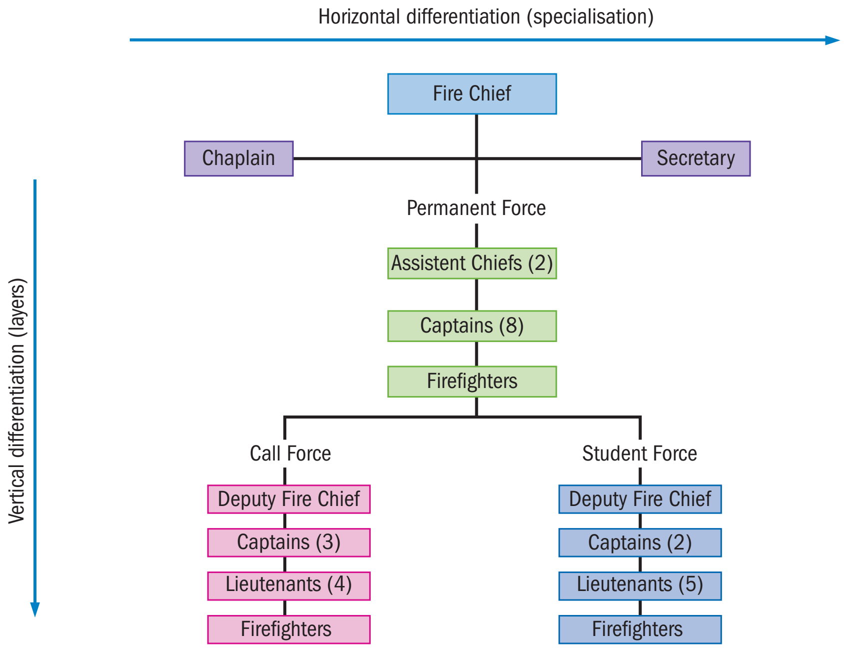
A result of creating too many layers is poor communication between departments; adding layers slows down decision-making efficiency significantly, which results in higher bureaucratic costs. Lastly, a firm runs a risk of falling subject to Parkinson's law.

Parkinson's law

Parkinson's Law

Following the British Navy's decision to decrease the number of ships by 68%, there was a notably swift increase in dockyard officials, by as much as 40%. In his studies into the phenomenon, Parkinson made particular note of the fact that the total amount of people employed within a bureaucracy rose by 5-7% per year 'irrespective of any variation in the amount of work (if any) to be done'. This was a result of the appreciation of rank by managers (admirals and such); the more subordinates each manager had, the greater 'their' empire. However, inspired by their chiefs, the subordinates wanted subordinates of their own. And added to that was the fact that officials tend make work for each other. More managers leads to more work; work expands so as to fill the time available.

FIGURE 1.5 Differentiation



Centralisation

Centralisation

Vertical decentralisation

Centralisation is the degree to which decision making is concentrated at upper levels in the organisation. For example, organisations in which top managers make all the decisions and lower-level employees simply carry out their orders. Vertical decentralisation refers to organisations where decision-making is pushed down to those managers closest to the action. Whether a company should centralise or decentralise depends on several factors. Increased centralisation is possible if the environment is stable and lower-level managers are not as capable of, or experienced in, making decisions as upper-level managers, or lower-level managers do not want to have a say in the decision-making. Increased centralisation is possible if an organisation faces either one of the following situations:

- The industry environment is stable.
- Lower-level managers are not as capable of making decisions as upper-level managers.
- Lower-level managers do not want to have a say in the decision-making.
- There is a possibility that the organisation is going to face a crisis or failure.

On the other hand, increased decentralisation is possible in one of the following scenarios:

- The industry environment is complex or uncertain.
- Lower-level managers are capable of making decisions, or lower-level managers want a voice in decisions.
- There is an open corporate culture, allowing managers to have a say in what happens.

Formalisation and standardisation
Standardisation or formalisation is frequently used either low level jobs (such as factory work), or for very specific complex jobs (such as piloting an aircraft). All processes and procedures are standardised, together with both output and input.

Standardisation
Formalisation

1.4.2 Leadership & Management Styles

Leadership

Leadership is important because, first of all, it influences subordinates. Added to that are the facts that leadership plays a critical role in ethical shortcomings, and that good leadership results in motivation, increased commitment, job satisfaction; leadership can be clearly linked to performance. Good leadership results in leaders who make a difference by being who they are. They have a positive impact. Leadership, however, is not a role, function, or position. Rather, it is about interpersonal relationships. Leaders have an influence, and without a leader people behave differently. Additionally, leaders can convince people they are acting of their own free will, with leadership being 'attributed' when results are shown. Good leadership results also garner a sense of loyalty, even a following. Thus, leadership is often situational.

Management

It should be understood that there is a huge difference between leadership and management. Leadership is the ability to influence a group towards the achievement of goals, while management is the use of authority inherent in designated formal rank to obtain compliance from organisational members. The differences between the two are explained in table 1.5.

TABLE 1.5 Leadership vs. Management

Leadership	Management
Coping with change Establish direction with a vision Align resources and inspire workers to complete the vision Leadership is doing the right things	Coping with complexity Bring about order and consistency Draw up plans, structures, and monitor results Management is doing the things right

Therefore, it follows that all leaders are managers, but not all managers are leaders. Every country has a different view of leadership. France, for example, has a more bureaucratic view of leaders, where individuals are task-oriented; a relatively autocratic system. The Nordic countries, on the other hand, view leaders as interpersonal, enthusiastic, sincere, informal, trustworthy, and inspirational.

Situational Leadership

Situational leadership model

The theory behind the situational leadership model reasons that history is full of leaders who did not succeed in their job because they apparently failed to comprehend the situation they were working in. Therefore, the style of leadership should be adapted to the situation, and must thus be contingent with the level of the followers' readiness. Leaders should look for the (un)willingness to take responsibility (commitment/motivation). Important in selecting leaders are the factors of enabling or having experience (competence), as these make it possible to train leaders to better fit their style to appeal to their followers.

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There are four main styles of leadership.

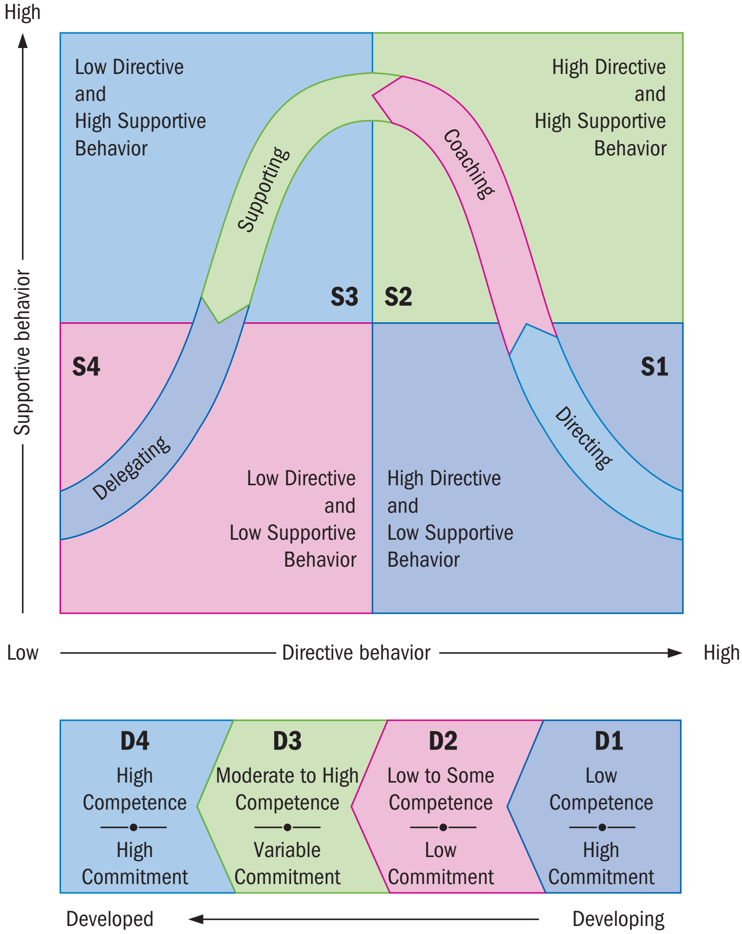
Telling Firstly, there is telling, which where the action and direction are solely dictated by the manager. The manager tells subordinates what to do, by when, where, why and how.

Selling Secondly, there is selling, which is a slightly more democratic way. Here, input from subordinates is used to actually support the subordinates, and thus the manager sells the concept of what needs to be done to his subordinates, thereby convincing them.

Participating Thirdly, there is participating, which is an even more democratic way. Input from subordinates is highly appreciated, and the decision making process is shared between manager and subordinate.

Delegating The last style is delegating. Here, although the manager is involved in the background, subordinates have responsibility of doing their work correctly, and thus have a high level of decision-making responsibility.

FIGURE 1.6 Situational Leadership



Source: www.kenblanchard.com

1.4.3 Culture

OCAI
Culture

According to OCAI (Organisational Culture Assessment Instrument) research, culture has a powerful effect on the performance and long-term effectiveness of all organisations. Culture impacts employee morale, commitment, productivity, physical health and emotional well-being. Furthermore, OCAI believes that culture is what makes an organisation unique – and what may keep it stuck in the past: today's world is complex, interconnected, driven by fast technological and social change. Therefore, organisations need to keep updating their mind-set and behaviours to survive.
OCAI also argues that culture is unique to every organisation – it involves 'everything': performance, competitiveness, innovation, satisfaction, retention, resistance to organisational change.
The OCAI is a validated tool for assessing current and preferred organisational culture, developed by professors Robert Quinn and Kim Cameron of the University of Michigan, who based it on the Competing Values Framework. It has been used by over 10,000 companies worldwide. The survey takes approximately 15 minutes.
OCAI provides online help for leaders, managers, Organisation Development consultants, Change practitioners, HR managers, and other professionals to assess and guide an organisation in changing their culture.

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How Strategy Shapes the Future

When executives develop corporate strategy, they nearly always begin by analysing the industry or environmental conditions in which they operate. They then assess the strengths and weaknesses of the players they are up against. With these industry and competitive analyses in mind, they set out to carve a distinctive strategic position where they can outperform their rivals by building a competitive advantage. To obtain such advantage, a company generally chooses either to differentiate itself from the competition for a premium price or to pursue low costs. The organisation aligns its value chain accordingly, creating manufacturing, marketing, and human resource strategies in the process. On the basis of these strategies, financial targets and budget allocations are set.

The underlying logic here is that a company's strategic options are bounded by the environment. In other words, structure shapes strategy. This 'structuralist' approach, which has its roots in the structure-conduct-performance paradigm of industrial organisation economics, has dominated the

FIGURE 1.7 Choosing the Right Strategic Approach

A structuralist approach is a good fit when:

- Structural conditions are attractive and the organisation has the recourses and capabilities to build a distinctive position
- Structural conditions are less than attractive but the organisation has the resources and capabilities to outperform customers

A reconstructionist approach is a good fit when:

- Structural conditions are attractive but players are well-entrenched and the organisation lacks the resources or capabilities to outperform them
- Structural conditions are unattractive and they work against an organisation irrespective of its resources and capabilities

When structural conditions and resources and capabilities do not distinctively indicate one approach or the other, the right choice will turn on the organisation's strategic mind-set.

Structuralist:

- The organisation has a bias toward defending current strategic positions and a reluctance to venture into unfamiliar territory

Reconstructionist:

- The organisation has an orientation toward innovation and a willingness to pursue new opportunities

Source: https://hbr.org/2009/09/how-strategy-shapes-structure

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practice of strategy for the past 30 years. According to it, a firm's performance depends on its conduct, which in turn depends on basic structural factors such as number of suppliers and buyers and barriers to entry. It is a deterministic worldview in which causality flows from external conditions down to corporate decisions that seek to exploit those conditions.

Even a cursory study of business history, however, reveals plenty of cases in which firms' strategies shaped industry structure, from Ford's Model T to Nintendo's Wii. For the past 15 years, we have been developing a theory of strategy, known as blue ocean strategy, that reflects the fact that a company's performance is not necessarily determined by an industry's competitive environment. The blue ocean strategy framework can help companies systematically reconstruct their industries and reverse the structure-strategy sequence in their favor.
Blue ocean strategy has its roots in the emerging school of economics called endogenous growth, whose central paradigm posits that the ideas and actions of individual players can shape the economic and industrial landscape. In other words, strategy can shape structure. We call this approach 're-constructionist.'
While the structuralist approach is valuable and relevant, the reconstructionist approach is more appropriate in certain economic and industry settings. Indeed, today's economic difficulties have heightened the need for a reconstructionist alternative. The first task of an organisation's leadership, therefore, is to choose the appropriate strategic approach in light of the challenges the organisation faces. Choosing the right approach, however, is not enough. Executives then need to make sure that their organisations are aligned behind it to produce sustainable performance. Most executives understand the mechanics of making the structuralist approach work, so this article will focus on how to align an organisation behind the reconstructionist approach to deliver high and sustainable performance.

What Is the Right Strategic Approach for You?
There are three factors that determine the right approach: the structural conditions in which an organisation operates, its resources and capabilities, and its strategic mindset. When the structural conditions of an industry or environment are attractive and you have the resources and capabilities to carve out a viable competitive position, the structuralist approach is likely to produce good returns. Even in a not-so-attractive industry, the structuralist approach can work well if a company has the resources and capabilities to beat out the competition. In either case, the focus of strategy is to leverage the organisation's core strengths to achieve acceptable risk-adjusted returns in an existing market.

Harvard Business Review (2009)

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Summary

- Mission and vision are both related a firm's purpose and aspirations. The mission statement communicates the firm's reason for existing, and the manner in which it aspires to serve its main stakeholders. A vision statement is intended to inspire and motivate a company's workforce by providing a potential aim, a direction the organisation is heading for. Competencies refers to a firm's abilities to carry out an activity well. They are consciously constructed and developed by firms through experience and learning. Core competencies are those activities central to a firm's profitability and competitiveness. Core competencies create and sustain firm's ability to meet the critical success factors of particular customer segments. Distinctive competencies are competitively valuable activities which enable a firm to outperform its competitors. Distinctive competencies provide the basis for competitive advantage, and are the foundation of a firm's strategy. They provide a sustainable competitive advantage because they are hard to copy.

- VRIO framework is a suitable instrument to assess a firm's internal environment. The acronym VRIO relates to four questions a firm must answer concerning all of its resources or capabilities in order to determine its competitive competencies. VRIO stands for Value, Rarity, Imitability and Organisation.

- The Business Model Canvas (BMC) is a handy tool that helps entrepreneurs and managers assess their business model. BMC essentially builds on 3 pillars, which are:
  - Focus (contrary to traditional business plan, BMC focusses on what drives a business);
  - Flexibility (it is much easier to fine-tune the model as it drafted on a single page); and
  - Transparency (BMC provides managers with a faster and (more) adequate way of understanding a company's business model, mission, and vision, since all of that information is provided on a single page).

Practical questions and assignments

1 What is a mission statement?

2 What is vision statement?

3 What is the importance of values to the content of mission and vision statements?

4 Where do the purposes of mission and vision statement overlap?

5 What is the difference between core competencies and distinctive competencies?

6 Briefly explain the use of the VRIO framework by applying it to a fictional company.

7 Briefly explain the Business Model Canvas by applying it to a fictional company.