# CIMA
Strategic Level – Paper E3
ENTERPRISE STRATEGY
(REVISION SUMMARIES)

<table>
<thead>
<tr>
<th>Chapter</th>
<th>Topic</th>
<th>Page Number</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Strategic Management</td>
<td>3</td>
</tr>
<tr>
<td>2</td>
<td>Mission, Objectives and Stakeholders</td>
<td>11</td>
</tr>
<tr>
<td>3</td>
<td>Environmental Analysis</td>
<td>15</td>
</tr>
<tr>
<td>4</td>
<td>The Position Audit and Corporate Appraisal</td>
<td>19</td>
</tr>
<tr>
<td>5</td>
<td>Strategic options</td>
<td>25</td>
</tr>
<tr>
<td>6</td>
<td>Marketing</td>
<td>33</td>
</tr>
<tr>
<td>7</td>
<td>Information Strategy</td>
<td>45</td>
</tr>
<tr>
<td>8</td>
<td>Corporate Social Responsibility and Ethics</td>
<td>61</td>
</tr>
<tr>
<td>9</td>
<td>Organisations</td>
<td>67</td>
</tr>
<tr>
<td>10</td>
<td>Change Management</td>
<td>73</td>
</tr>
<tr>
<td>11</td>
<td>Strategic Performance Measurement</td>
<td>85</td>
</tr>
<tr>
<td>12</td>
<td>Numerical skills for strategic evaluation</td>
<td>103</td>
</tr>
</tbody>
</table>
E3 revision summaries
Chapter 1
Strategic Management
Key summary of chapter

What is strategy?

**Strategy**

“A course of action, including the specification of resources required, to achieve a specific objective.”

CIMA: Official Terminology

Levels of strategy - Johnson and Scholes

- **Corporate strategy** (Where)
- **Business Strategy** (How)
- **Functional Strategy** (Who)

Arguments in favour of a strategic approach

- ✓ Strategy helps minimise risk
- ✓ Avoids short-term behaviour
- ✓ Improves stakeholder perceptions
- ✓ Encourages environmental analysis e.g. critical to react to change
- ✓ Evidence indicates performance can be improved using strategic approaches
- ✓ Integration and coordination of activities and processes

Arguments against a strategic approach

- ✗ Difficult to plan when environment changing, uncertain or complex
- ✗ Encourages conformity stifling innovation e.g. the corporate straightjacket
- ✗ Infrequently reviewed e.g. chosen long-term strategy may not keep pace with change
- ✗ Implementation often managed poorly
- ✗ Rational planning a complex methodology and costly for small businesses
Comparing and contrasting approaches to strategic formulation

<table>
<thead>
<tr>
<th>The Rational Planning process</th>
<th>Incremental approaches</th>
<th>Freewheeling Opportunism</th>
<th>Emergent strategies</th>
</tr>
</thead>
<tbody>
<tr>
<td>Top-down and centralised</td>
<td>Top-down and centralised</td>
<td>Top-down and centralised</td>
<td>Bottom-up and decentralised</td>
</tr>
<tr>
<td>Time horizon 2-10 years</td>
<td>Time horizon 6 months to 2 years</td>
<td>Time horizon day to day basis</td>
<td>Time horizon indefinite</td>
</tr>
<tr>
<td>Formal planning</td>
<td>Less formal planning</td>
<td>Informal planning</td>
<td>Informal planning</td>
</tr>
<tr>
<td>Complex and costly</td>
<td>Less complex and costly</td>
<td>Less complex and costly</td>
<td>More complex and less costly</td>
</tr>
</tbody>
</table>
The rational planning process

Top-down (centralised) and formalised approach to strategic planning. Originated from the USA e.g. the planning horizon for the organisation could be over 2-10 years.

**Advantages**
- For transformational or radical change
- Copes with the uncertain future by providing long-term plans
- Helps integrate and coordinate complex organisations

**Disadvantages**
- Rational planning can be too rigid and bureaucratic e.g. no use for the small business
- Rational planning can stifle innovation e.g. locked into plans
- No use for dynamic or uncertain environments e.g. plans quickly become ‘out of date’

The rational planning process

```
MISSION & OBJECTIVES → CORPORATE APPRAISAL → OPTION GENERATION → EVALUATION & CHOICE → REVIEW & CONTROL

ENVIRONMENTAL ANALYSIS

POSITION AUDIT

IMPLEMENTATION
```
### Incremental planning approaches (logical incrementalism)

Top-down (centralised) and less formalised approach to strategic planning. Smaller, gradual and more incremental adjustments to strategic plans e.g. every 6 months up to 2 years maximum.

<table>
<thead>
<tr>
<th>Advantages</th>
<th>Disadvantages</th>
</tr>
</thead>
<tbody>
<tr>
<td>✓ Less complex and long winded</td>
<td>✗ Too reactive, ‘muddling through’</td>
</tr>
<tr>
<td>✓ Better for uncertainty or rapidly changing environments</td>
<td>✗ Not suitable for transformational or radical change</td>
</tr>
<tr>
<td>✓ More frequent gradual adjustment e.g. easier to control and manage</td>
<td>✗ Lack of long-term direction e.g. ‘strategic drift’ may occur</td>
</tr>
<tr>
<td>✓ Greater frequency of planning to adjust plans to environmental change</td>
<td></td>
</tr>
</tbody>
</table>

### The entrepreneurial model (or freewheeling opportunism)

Henry Mintzberg referred to ‘freewheeling opportunism’ as an opportunistic strategy, dominated by the search for new opportunities, with bold and often high risk decisions that need to be made by the entrepreneur him or herself.

Freewheeling opportunism is a top-down (centralised), informal and short-term approach to strategic planning.

<table>
<thead>
<tr>
<th>Advantages</th>
<th>Disadvantages</th>
</tr>
</thead>
<tbody>
<tr>
<td>✓ Focus on exploiting product and market opportunities e.g. ‘never miss a good opportunity’</td>
<td>✗ Organisation too reactive, ‘muddling through’</td>
</tr>
<tr>
<td>✓ Less time consuming and complicated</td>
<td>✗ Not suitable for transformational or radical change</td>
</tr>
<tr>
<td>✓ Greater frequency of planning to adjust plans to environmental change</td>
<td>✗ Lack of long-term direction.</td>
</tr>
<tr>
<td>✓ Better for uncertainty or rapidly changing environments</td>
<td>✗ Relies heavily on the judgement and experience of the founder e.g. one single individual</td>
</tr>
</tbody>
</table>
**Emergent strategies**

Henry Minzberg, described emergent strategies as "patterns or consistencies realised despite or in the absence of conscious intention by senior management." Strategy emerges and is "unanticipated." Informal and bottom-up (decentralised approach) allowing strategic courses of action to be developed from both tactical and operational levels within the organisation.

<table>
<thead>
<tr>
<th>Advantages</th>
<th>Disadvantages</th>
</tr>
</thead>
<tbody>
<tr>
<td>✓ Quicker change or repositioning for the organisation e.g. lower strategic levels closer to the customer.</td>
<td>✗ Chaotic organisation that lacks control over planning</td>
</tr>
<tr>
<td>✓ Tactical and operational levels an extensive source of innovative ideas</td>
<td>✗ Lack of long-term direction.</td>
</tr>
<tr>
<td>✓ Greater motivation to other strategic levels</td>
<td>✗ Organisation too reactive, &quot;muddling through&quot;</td>
</tr>
<tr>
<td>✓ Supports culture of flexibility, learning and enterprise</td>
<td>✗ Requires entrepreneurial skills from staff which may not exist</td>
</tr>
</tbody>
</table>

**Comparing and contrasting RBV to the Positioning Approach**

<table>
<thead>
<tr>
<th>Resource Based View (RBV)</th>
<th>Positioning View (PA)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Similarities</strong></td>
<td></td>
</tr>
<tr>
<td>• Both ideas stem from the rational planning process.</td>
<td></td>
</tr>
<tr>
<td>• Both can use centralised (rational planning) or decentralised (emergent) approaches.</td>
<td></td>
</tr>
<tr>
<td>• Both aim to achieve competitive advantage e.g. ways to compete with rivals.</td>
<td></td>
</tr>
<tr>
<td><strong>Differences</strong></td>
<td></td>
</tr>
<tr>
<td>• Resource based approach</td>
<td>• Market based approach</td>
</tr>
<tr>
<td>• Inside out e.g. key internal resources for achieving success.</td>
<td>• Outside in e.g. best external opportunities to exploit.</td>
</tr>
<tr>
<td>• Organisation focuses on what it does best e.g. &quot;stick to knitting&quot;</td>
<td>• Organisation focuses on diversity and innovation.</td>
</tr>
<tr>
<td>• Emphasis on internal appraisal e.g. unique assets or core competences.</td>
<td>• Emphasis on external environment e.g. competition and customers</td>
</tr>
<tr>
<td>• Higher cost and time to exploit but long-term advantage.</td>
<td>• Less costly to exploit but short-term advantage gained.</td>
</tr>
</tbody>
</table>
Two contrasting leadership styles generally exist, democratic and autocratic. Democratic is based on democracy and social equality. Autocratic a bossy way and often aggressive and dominating.

<table>
<thead>
<tr>
<th>Huneryager and Heckman</th>
<th>Dictatorial</th>
<th>Autocratic</th>
<th>Democratic</th>
<th>Laissez faire</th>
</tr>
</thead>
</table>

E3 revision summaries
Chapter 2

Mission, Objectives and Stakeholders
Key summary of chapter

Stakeholders are those organisations or people that have an interest in the organisation, these interests varied and for many reasons. They can be a source of potential conflict for the successful accomplishment of an organisation’s strategy.

Mendelow’s stakeholder mapping model

Mendelow’s matrix is a way of prioritising stakeholders by subjective mapping of them, in order to understand and resolve any issues or conflicts that may exist. This model prioritises by mapping which stakeholders should more likely considered and therefore satisfied by the organisation.

- **Power** e.g. bargaining power, right or ability to exert influence over the organisation’s strategic aims and the general way it conducts itself.
- **Interest** e.g. interest in the activities or conduct of the organisation for varied reasons.

<table>
<thead>
<tr>
<th>Power over the organisation</th>
<th>Interest in the organisation</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Low</td>
<td>Low</td>
<td>Minimal Effort (priority four)</td>
</tr>
<tr>
<td>High</td>
<td>High</td>
<td>Keep Informed (priority three)</td>
</tr>
<tr>
<td></td>
<td>Low</td>
<td>Keep Satisfied (priority two)</td>
</tr>
<tr>
<td></td>
<td>High</td>
<td>Key players (priority one)</td>
</tr>
</tbody>
</table>
### Mission statements

Every organisation should have a mission, purpose or reason for being. This can be embedded within a mission statement. A mission statement describes in writing the basic purpose of an organisation and what it is trying to accomplish. A mission statement is a brief description of an organisation's fundamental purpose.

### Goals and objectives

#### Goals

What the organisation plans or intends to achieve. Normally converted to objectives which measurability and timescale. Long-term and sufficient to satisfy the mission statement.

**Critical success factors (CSFs)**

Key organisational goals that if achieved will make the organisation more successful.

#### Objectives

A measurable goal with a clearly defined timescale to achieve it. Objectives should be SMART (specific, measurable, agreed, realistic and time bound).

**Key performance indicators KPIs (performance measures)**

Objectives which have measurability and time scale.
Chapter 3

Environmental Analysis
Environmental (external) analysis

A study which considers potential environmental effects during the planning phase before an investment is made or an operation started (CIMA).

Environmental analysis tools

- PEST or SLEPT (social, legal, economic, political and technological).
- Porter's 5-forces (threat of new entrants, competitive rivalry, substitutes, bargaining power of suppliers and bargaining power of customers).
- Porters Diamond (favourable factor conditions, demand conditions, related and supporting industry and firm strategy, structure and rivalry).
- Competitor analysis. A systematic comparison of the organisation to competition within the same industry.

Using environmental models such as SLEPT analysis or Porter's five forces can give a diverse range of environmental information for an organisation. These models can be used to describe both the nature and source of information when conducting environmental analysis. The source of information is where the information can be found or where it originates from e.g. media, customers, websites or companies house. The nature of the information means to describe the information itself.

Game theory

A branch of applied mathematics that can be used in social sciences, in particular it can be applied to the theory of competition in terms of gains and losses amongst opposing rivals. A mathematical framework is used for analysing different choices that rational players can make, when their pay-off depends on the combination of their choices, as well as all other players choices.
Country risk

The financial or other risks of changes in the business environment of a country e.g. changes in the political, ethical, legal, market or economic environment. Such examples include introduction of trade barriers, regulatory changes to employment or competition law, or outbreak of war.

Country risk can also be referred to as political risk, however country risk is a more general term, for the diversity of environmental factors that can influence an organisation other than those which are just political.

Tools for analysing country risk

- **PEST or SLEPT** (social, legal, economic, political and technological).
- **Porter’s 5-forces** (threat of new entrants, competitive rivalry, substitutes, bargaining power of suppliers and bargaining power of customers).
- **Porters Diamond** (favourable factor conditions, demand conditions, related and supporting industry and firm strategy, structure and rivalry).

Political risk

Political risk is the risk that political or government action will effect the position and value of an organisation. The financial or other risk that a nations government changes its policies and procedures e.g. potential loss arising from a change in government policy regarding trade barriers such as foreign exchange controls, tariffs or import quotas.

Examples of political risk within Countries

- Outbreak of national war, civil war, unrest or riot.
- Nationalisation of industries
- Enforcement of international trade barriers
- New regulations or legislation introduced
- Restrictions on dividends or expropriation of assets out of a country.
- Political instability

Ways an organisation can influence a government

- Political donations
- Employment of lobbyists
- Appointment of civil servants or politicians as internal directors
- Attendance at annual conferences or political meetings
- Good relations with government upheld
- Advertising or promotion to influence legislation change or sway public opinion
- Unite with pressure groups that have common aims to the organisation
Chapter 4

The Position Audit and Corporate Appraisal
Key summary of chapter

Position audit
A position audit is a systematic assessment of the current strengths and weaknesses of an organisation and is a prerequisite for strategic planning and implementation.

- Resources
- Products, brands and markets
- Operating systems
- Internal organisation
- Current Results
- Returns to equity and debt holders

The 9Ms resource audit
- Men and women
- Management
- Money
- Make-up
- Machinery
- Methods
- Markets
- Material
- Management information
Value chain analysis

A value chain is ‘the sequence of business activities by which, in the perspective of the end user, value is added to the products or services produced by an organisation’ (CIMA).

The value shop is an alternative representation of value chain analysis and can be used more applicably for the professional firm or service organisation. Rather than just creating value by producing output from an input of raw materials in a uniform or standard way each client problem maybe unique, value is created by mobilising resources and deploying them for to solve specific problems. Within a service organisation the value creation process may deal with unique situations and the links between the primary activities may not be so visible.

Stabell and Fjeldstad (1998), five generic activities (primary activities) carried out by a value shop

1. Problem finding and acquisition
2. Problem solving
3. Choice of problem solution
4. Execution of solution
5. Control and evaluation
**Benchmarking**

“A continuous, systematic process for evaluating the products, services and work processes of an organisation that are recognised as representing best practice, for the purpose of organisational improvement.”

*(Michael Spendolini)*

**Types of benchmarking**

- Internal
- Best practice or functional
- Competitive
- Strategic

**The process**

- Selecting what you want to benchmark
- Consider benefits against the cost of doing it
- Assign responsibilities to a team
- Identify potential partners/known leaders
- Breakdown processes to complete
- Test and measure e.g. observation, experimentation or investigation/interview
- Gather information
- Gap analysis
- Implement changes/programmes/communicate
- Monitor and control
- Repeat regularly

**Business process re-engineering (BPR)**

Hammer & Champy (1993) defined the process of reengineering as "the fundamental rethinking and radical redesign of business processes to achieve dramatic improvements in critical, contemporary measures of performance, such as cost, quality, service and speed."

**The stages in a BPR exercise**

1. Identify processes to be re-engineered
2. Understand, break down and analyse the process
3. Identify change levers
4. Rationalise or eliminate process
5. Redesign process to operate in the most cost effective and efficient way
6. Reassemble, implement and manage change
7. Monitor and review
**Gap analysis**

Gap analysis is a long range and quantifiable planning technique

- Where the organisation is now
- Where the organisation will be
- Where the organisation wants to be

**Process of gap analysis**

1. Set long-term strategic objectives
2. Forecast likely performance given its current state of affairs
3. Current forecasts are frequently updated
4. Periodically compare revised performance to target performance and identify measurable gaps.
5. Further strategic development required when a gap exists
Scenario planning

A strategic planning method for the preparation of flexible long-term plans. Scenario planning involves testing business strategies against ‘alternative futures’ in an attempt to build plausible views, when operating in conditions of high uncertainty.

Process developed by Schoemaker

1. Develop scenarios e.g. examine environment, key trends and uncertainties.
2. Develop strategies to match each scenario.
3. Identify core competences that are required for each scenario.
4. Use of strategies developed if key trends and uncertainties turn out to be true.

The concept of foresight

Foresight has been described as the art and science of anticipating the future and planning prudently for it.

- Think tanks
- The Delphi model
- Scenario planning
- Brainstorming
- Visioning
- Morphological analysis

Corporate appraisal (SWOT analysis)

A corporate appraisal is a ‘critical assessment of the strengths and weaknesses, opportunities and threats (SWOT analysis) in relation to the internal and environmental factors affecting an entity in order to establish its condition prior to the preparation of the long-term plan.’ (CIMA)

- Strengths and weaknesses are normally internal (within the organization)
- Opportunities and threats are normally external (outside the organisation)

The TOWS approach

- SO Strategies e.g. match core competences or Strengths to Opportunities
- ST Strategies e.g. use Strengths to avoid Threats
- WO strategies e.g. take advantage of Opportunities by addressing Weaknesses
- WT strategies e.g. minimise Weaknesses and avoid Threats
Chapter 5

Strategic Options
### Michael Porter’s competitive generic strategies

<table>
<thead>
<tr>
<th>Competitive Scope</th>
<th>Cost Leadership</th>
<th>Differentiation</th>
<th>Cost Focus</th>
<th>Differentiation Focus</th>
</tr>
</thead>
<tbody>
<tr>
<td>Broad Target</td>
<td>Offering a product or service at the lowest price due to having the lowest cost per unit in the industry.</td>
<td>Offering a product or service with certain characteristics or features that are unique and distinct relative to the competition.</td>
<td>Market segmentation and cost leadership strategy pursued.</td>
<td>Market segmentation and differentiation strategy pursued.</td>
</tr>
<tr>
<td>Narrow Target</td>
<td></td>
<td></td>
<td></td>
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</tr>
</tbody>
</table>

**Cost Leadership**

Offering a product or service at the lowest price due to having the lowest cost per unit in the industry.

**Differentiation**

Offering a product or service with certain characteristics or features that are unique and distinct relative to the competition.

**Cost Focus**

Market segmentation and cost leadership strategy pursued.

**Differentiation Focus**

Market segmentation and differentiation strategy pursued.
The Ansoff matrix

<table>
<thead>
<tr>
<th>Existing Market</th>
<th>Existing Product</th>
<th>New Product</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Market Penetration</td>
<td>Product Development</td>
</tr>
<tr>
<td>New Market</td>
<td>Market Development</td>
<td>Diversification</td>
</tr>
</tbody>
</table>
Types of integration (merger or acquisition)

Related diversification

- Horizontal integration
- Backwards vertical integration
- Forwards vertical integration

Unrelated diversification

- Lateral integration or conglomerate diversification

Strategic options

- Internal development or ‘organic growth’
- Acquisition (takeover) or merger
- Joint venture
- Strategic alliance
- Franchise (licensing)
- Sales agents
- Manufacturing overseas
- Exporting
- Outsourcing
- Turnkey operations
- Do nothing
- Withdraw
- Consolidate

Divestment

- Liquidate assets
- Sell off products or brands as a going concern
- Management buy out (MBO)
- Management buy in (MBI)
- Demerger (sale)
- Rationalisation
Business process outsourcing (BPO)

A form of outsourcing, the contracting of operations and responsibilities of a specific business function (process) to a third-party service provider. Commonly referred to as ‘back office outsourcing’ because it involves the outsourcing of internal business functions e.g. finance, human resource management, legal, information technology, even the ‘offshore outsourcing’ of call centers by companies today.

Benefits of BPO

- Economies of scale
- Reduces the complexity of internal management
- Management can focus on its core competencies
- Greater flexibility of using the outsourcer
- Increase speed, improve efficiency and cut cost

Limitations of BPO

- Loss of strategic control
- Organisation more vulnerable due to over reliance
- Loss of competitive advantage
- Internal redundancy
- Risk to the security of information
- Failure of outsourcer to meet service levels

Offshore outsourcing

Offshore outsourcing is BPO contracted outside the company's country. Examples from the UK and US, have included overseas development of information technology e.g. programming or software development, customer call centers, processing insurance claims, and even research and development. In either case the process is performed in another country to where the product or service is actually developed or manufactured.

Offshoring is a similar term used when a process is performed in another country, but instead of a third party used, the process is provided by a foreign subsidiary.
Supply chain management

Strategies to achieve greater integration of the supply chain from raw material to the ultimate final sale and disposal of a finished product or service. Effective supply chain management can be crucial for an organisation to gain competitive advantage e.g. higher quality, lower cost, quicker delivery etc. A supply chain is an example of a supply network, raw materials, components, finished goods and services, are procured as a product passes through a chain of processes that supply one another and at each stage adds value to the customer in some way.

Strategic supply chain management

The strategic supply wheel illustrated by Cousin

- Portfolio of relationships e.g. high collaboration with suppliers
- Skills and competences e.g. develop skills internally
- Strategic performance measures e.g. monitor and control supply chain
- Cost-benefit analysis e.g. over strategic approaches
- Organisational structure e.g. support effective supply chain management

Supplier sourcing strategies

- Single sourcing e.g. source from one supplier only.
- Multiple sourcing e.g. source service from many suppliers simultaneously.
- Delegated sourcing e.g. purchasing decisions are outsourced.
- Parallel sourcing e.g. a combination of two or more of the above.

The three elements of supply chain management

- Responsiveness
- Reliability
- Relationships
IT to facilitate greater integration of supply chain

- Bar coding
- Electronic tagging
- Materials Requirement Planning (MRP I)
- Route masters
- Electronic Data Interchange (EDI)
- Extranet e.g. internet based EDI.
- Computer Aided Design (CAD)
- Electronic Funds Transfer (EFT) systems.

Business strategies to facilitate greater integration of supply chain

- Vertical integration
- Strategic alliances or joint ventures

Evaluating strategic options

The SFA (or FSA) criteria

- **Suitability** e.g. SWOT analyses and mission statement.
- **Feasibility** e.g. skills, core competences, finance and resources to achieve option
- **Acceptability** e.g. level of risk and financial return acceptable to stakeholders

RACES

- Resources
- Acceptably
- Coherence
- Effectiveness
- Sustainability
### Key summary of chapter

#### The marketing concept

<table>
<thead>
<tr>
<th>Marketing</th>
<th>The management process responsible for identifying anticipating and satisfying customer requirements profitably. Chartered Institute of Marketing (CIM)</th>
</tr>
</thead>
</table>

<table>
<thead>
<tr>
<th>The marketing mix (4 Ps)</th>
<th>A set of controllable variables an organisation has to influence a customers purchase decision for a good or service.</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Product</strong></td>
<td>The ‘package of benefits’ including guarantees, warranties and after sales service.</td>
</tr>
<tr>
<td><strong>Price</strong></td>
<td>The pricing element includes price promotions, discounts, and periods of credit, interest free credit and payment terms.</td>
</tr>
<tr>
<td><strong>Promotion</strong></td>
<td>The promotional mix or promotional plan is comprised of four subcategories: advertising, personal (or direct) selling, sales promotion and public relations.</td>
</tr>
<tr>
<td><strong>Place</strong></td>
<td>Place is where the product can be purchased from e.g. distribution channels.</td>
</tr>
<tr>
<td><strong>People</strong></td>
<td>Often referred to as the 5th P in the marketing mix, because staffs are the essential ‘human asset’ to support the marketing concept.</td>
</tr>
<tr>
<td><strong>Process</strong></td>
<td>How the service is delivered or how the sale of the good is managed.</td>
</tr>
<tr>
<td><strong>Physical evidence</strong></td>
<td>The tangible evidence that exists and that can be identified to the organisation.</td>
</tr>
</tbody>
</table>
Market research

A systematic investigation of markets and accumulation of relevant data

A process for market research

1. **Problem recognition**
2. **Define scope of data and information needs**
3. **Collect data and information** e.g. sampling, surveys, observation, interview etc
4. **Analyse and understand information** e.g. databases, summarise trends and results
5. **Report and conclude** for new marketing strategies

Sales forecasting methods

**Market forecasting methods for estimating current demand**

- Total market or industry potential
- Area market potential
- Market share
- Relative market share (RMS)

**Market forecasting methods for estimating future demand**

- Survey or sample of buyers intentions
- Composite of sales force opinions
- Expert opinions
- Past-sales analysis
- Market test methods
**Relationship marketing**

Relationship marketing is about devoting marketing resources to the maintenance of the existing customer base, as well as trying to attract new customers. Customer loyalty and retention has become critical to the long-term survival of organisations, relationship marketing aims to build excellent relationships with customers in order to retain their loyalty.

**Payne’s 6 markets model for relationship management**

Payne advocated that an organisation has six markets not just the ‘customer’ market when it comes to relationship marketing.

1. Customer market  
2. Referral market  
3. Supplier market.  
4. Recruitment market  
5. Influence market  
6. Internal market
Market Segmentation
The grouping of customers, with each sub-group or segment of customer having a common need, want or value. Each sub-group or segment will be affected by different targeting strategies; they would behave differently and respond differently to different tailored marketing mixes.

Advantages of market segmentation

✓ Match closer the features of a product to customer groups.
✓ Higher customer satisfaction or delight
✓ Brand loyalty and customer retention.
✓ More efficient use of marketing resources

Guidance for effective market segmentation (Kotler)

- **Substantial** e.g. segment sizeable enough to be profitable
- **Accessible** e.g. segment can be efficiently and effectively reached
- **Measurable** e.g. segment can be measured
- **Actionable** e.g. effective strategies are available to attract segment
- **Differentiable** e.g. the segment behaves and responds differently

Reasons not to engage in market segmentation

- The number of customers not big enough to earn a profit.
- Effective promotion mediums do not exist to create awareness economically.
- The size or strength of competition that already exists.
- Segment too subjective, complex and therefore difficult to measure.
- The firm lacks the core competences to compete.
- The market segment identified has no long-term future.
The strategic marketing process

The primary goal of any marketing strategy is to satisfy the strategic goals of the organisation e.g. competitive strategy must support the corporate strategy, mission and goals.

1. The mission statement and corporate objectives reviewed
2. Conduct a marketing audit
   - Review strategy and objectives of the organisation
   - Audit external marketing environment e.g. PEST or SLEPT analysis
   - Market analysis and segmentation for different customer needs and values
   - Competitive benchmarking of marketing mix practices
3. Evaluation and reporting of all market research and intelligence
4. Determine and evaluate competitive strategies
5. Detailed action plan created
6. Review and obtain feedback periodically
7. Regularly undertake marketing audit

The marketing environment

Environmental analysis is a process strongly linked to the creation of the marketing strategic plan for an organisation. Models such as PEST or SLEPT analysis and other derivatives of these e.g. PESTLE or SLEEPT or STEEPLE can be used for analysing the general or industry environment.

- S societal factors
- L legal factors
- E economic factors
- P political factors
- T technological factors

Two extra Es could include ethical and ecological factors. Other considerations to the above for a more comprehensive study of the environment would include a full analysis of customers, competition and markets.
Product positioning

Competitive positioning is about the organisation's role in the competitive market place.

- **Undifferentiated (or homogenous) positioning** is the targeting of an entire market with a single marketing mix.
- **Differentiated targeting** is the targeting of different market segments and a specific marketing mix for each segment.
- **Concentrated positioning** is the targeting of a single market segment only with a single marketing mix e.g. single segment focus.

Michael Porter’s competitive generic strategies

<table>
<thead>
<tr>
<th>Competitive Scope</th>
<th>Cost Leadership</th>
<th>Differentiation Focus</th>
</tr>
</thead>
<tbody>
<tr>
<td>Narrow Target</td>
<td>Cost Focus</td>
<td>Differentiation</td>
</tr>
<tr>
<td>Broad Target</td>
<td>Low cost</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Offering a product or service at the lowest price due to having the lowest cost per unit in the industry.</td>
<td>Market segmentation and cost leadership strategy pursued.</td>
</tr>
<tr>
<td></td>
<td>Differentiation</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Offering a product or service with certain characteristics or features that are unique and distinct relative to the competition.</td>
<td>Market segmentation and differentiation strategy pursued.</td>
</tr>
</tbody>
</table>
The characteristics of services

- **Intangibility** e.g. no material substance or physical existence
- **Legal ownership** e.g. difficult to return if faulty
- **Instant perishability** e.g. cannot be stored for future use
- **Heterogeneity** e.g. performed different each time
- **Inseparability** e.g. cannot be separated from the person who provides it

**Product (customer) portfolios and the product mix**

Product mix means the different products that the organisation makes or sells. The product portfolio can be managed using tools such as the product life cycle (PLC) theory and the Boston Consulting Group (BCG) matrix.

**Product or industry life cycle**

The product life cycle illustrates the succession of stages that a product goes through in terms of its sales or market share. The market environment in which a product is sold is always changing and therefore must be managed as it moves through a succession of different stages.

- Introduction
- Growth
- Maturity
- Decline

**The Customer Life Cycle (CLC)**

The Customer Life Cycle (CLC) is similar in theory to the Product Life Cycle (PLC), however, CLC focuses upon the creation and delivery of lifetime value to the customer (not product) during different stages of their life cycle e.g. identifying products or services that customers need, want or value throughout their life cycle stages. A customer lifecycle value (CLV) estimates the present value of the net cash flows likely to be received during a customers life time.

**The Boston Consulting Group matrix**

- Problem Child e.g. new product that poorly competes.
- Star e.g. new product that competes well.
- Cash Cow e.g. mature and established product that competes well.
- Dog e.g. mature and established product that poorly competes.

Product portfolio theory states that an organisation should have a well diversified portfolio of products. E.g. stars are essential for future success, cash-cows to harvest and support stars, the absence of question marks or dogs if possible.
Customer profitability analysis (CPA)

Relating specific costs to serving customers or groups of customers, so that their relative profitability can be assessed. Customer profitability analysis (CPA) focuses on cost reduction by understanding how customers consume different support resources e.g. processing, delivery, sales visits, telephone support, internet support etc. It allows an organisation to concentrate on the most profitable of its customers.

Direct product profitability (DPP)

DPP is a decision making tool that helps a food merchandiser by providing a better indication of the profitability of products on the supermarket shelves. DPP allocates direct product costs to individual products. These costs are subtracted from gross profit to derive at DPP for each product. The normal indirect costs attributed to products would be distribution, warehousing and retailing. DPP would ignore indirect costs such as head office overhead, only product specific fixed (indirect) cost would be analysed. e.g. shelf filling, warehousing and transportation

Distribution channel profitability (DCP)

DCP another ABC concept, is about relating specific distribution costs to serving customers or groups of customers, so that their relative profitability can be assessed. Typical supply chain channels today include the internet, e-mail, shops/branches, post, telephone, catalogues, other distributors etc

Activity based management (ABM)

Activity based management (ABM) is about satisfying customers whilst making fewer demands on internal resources. The aim is that once cost drivers are created, organisations can aim to reduce cost, by creating models for more effective planning and control.

Attribute costing

DPP or CPA can be taken one step further by using attribute costing, a method which applies cost-benefit analysis e.g. benefits from the value of customer utility or 'satisfaction' derived from different attributes of a product, compared to the cost of providing each attribute.

Strategies to improve customer or product profitability

1. Increase price
2. Increase volume sold
3. Reduce support activities that incur specific customer or product cost
4. Withdrawal e.g. discontinue selling
Branding

A trade name, symbol or logo synonymous or identifiable to an organisation, or its product or service e.g. Nike (and its ‘tick’ logo).

The merits of brands

- Can support new products and services
- Can create a premium price
- Can support franchising (licensing)
- Can have longer life cycle than products
- Can differentiate a product and strengthen customer loyalty

The five brand strategies of Kotler (1997)

- **Line extensions** e.g. new sizes, flavours etc launched under same product brand
- **Brand extensions** e.g. new product category launched under same brand
- **Multibrands** e.g. new brands launched in same product category
- **New brands** e.g. new product category launched or existing product relaunched
- **Co brands** e.g. complimentary brands combined for promotional strategic benefit

Brand accounting

Brand expenditure is not capitalised under IAS 38

The valuation of intangible brands

- The historical accounting cost
- The present value of the ‘price premium’ paid for the brand
- The present value of future estimated earnings from the brand
- The market price
**Ethics**
Morals about the right behaviour and way of conduct.

**Corporate Social Responsibility (CSR)**
Being aware of the impact of actions on others, and acting in the best interests of society

**Ethical considerations in marketing**

- Safe products and services
- Ethical products and services e.g. not tested on animals, fair trade, recycling, biodegradable etc
- Fair pricing and returns policy
- Full refund offered if customer unsatisfied
- Customers not misled e.g. information, sales staff and agents
- No text messaging or junk mail
The role of IT in supporting marketing

Marketing decision support systems (MDSS)

Databases, internet, extranet, intranet and e-commerce systems.
A coordinated collection of data, system tools, and techniques with supporting software and hardware by which an organization gathers and interprets relevant information from business and the environment and turns it into a basis for making management decisions.
(American Marketing Association)

Customer relationship management (CRM) systems

Devoting marketing and IT resources to the maintenance of existing customers, as well as strategies to attract new customers.

Examples of CRM systems

- **Face to face contact** e.g. meetings, phone calls, e-mail, online services etc.
- **Back office** e.g. booking, billing, invoicing and payment.
- **Analysis of customer trends** e.g. data warehousing and mining

Data warehousing and mining

**Data warehousing**
The input and storage of high volumes of data e.g. customer transactions such as time of day and type of goods purchased. Tesco collects data via its sales order processing systems using EPOS, bar-coding and magnetic stripe card (club card) technology.

**Data mining**
The process of extracting useful and perhaps previously unknown information from a large pool of information gathered within a data warehouse. It is also referred to as shopping basket analysis because it is heavily applied within the retail sector.

E-marketing and E-commerce

**E-marketing**
Marketing over the internet. Also referred to as i-marketing, web marketing and online marketing. The presentation of the organisation's brand, product and services over the internet, to help build strong customer relationships and brand loyalty.

**E-commerce**
The process of buying and selling goods and services electronically over the internet using website technology.
Chapter 7

Information Strategy
Key summary of chapter

Information
Data which has been processed in a meaningful way e.g. summarised, formatted, tabulated or filtered, so that it is understandable by its intended recipient.

Information system
A system of persons, data records and activities, manual or computerised, that process, collect and maintain information, to provide it to staff or other stakeholders.

The primary role of information systems is to support the business strategy and goals of the organisation. The business strategy and goals of the organisation should always be driving the information strategy of the organisation, never the other way around.

Characteristics of good information systems

<table>
<thead>
<tr>
<th>Quality</th>
<th>Strategic planning control</th>
<th>Operational</th>
</tr>
</thead>
<tbody>
<tr>
<td>TIME PERIOD</td>
<td>FORECAST &lt;------------------</td>
<td>HISTORICAL</td>
</tr>
<tr>
<td>TIMELINESS</td>
<td>IMMEDIATE&lt;------------------</td>
<td>DELAYED</td>
</tr>
<tr>
<td>OBJECTIVITY</td>
<td>SUBJECTIVE&lt;-----------------</td>
<td>OBJECTIVE</td>
</tr>
<tr>
<td>QUANTIFIABILITY</td>
<td>QUALITATIVE&lt;---------------</td>
<td>QUANTITATIVE</td>
</tr>
<tr>
<td>ACCURACY</td>
<td>APPROXIMATE&lt;----------------</td>
<td>ACCURATE</td>
</tr>
<tr>
<td>CERTAINTY</td>
<td>UNCERTAIN&lt;------------------</td>
<td>CERTAIN</td>
</tr>
<tr>
<td>COMPLETENESS</td>
<td>PARTIAL&lt;---------------------</td>
<td>COMPLETE</td>
</tr>
<tr>
<td>BREADTH</td>
<td>BROAD&lt;----------------------</td>
<td>SPECIFIC</td>
</tr>
<tr>
<td>DETAIL</td>
<td>LITTLE DETAIL&lt;---------------</td>
<td>HIGHLY DETAILED</td>
</tr>
</tbody>
</table>
Michael Earl reasons to have an IT strategy

- IT involves high costs
- IT is critical to the success of many organisations
- IT can be used as part of a commercial strategy to gain competitive advantage
- IT impacts upon customer service
- IT impacts upon all levels of manager
- IT could mean a revolution in the way information is created and presented
- IT involves many stakeholders

Nolan’s 6-stage hypothesis

- Initiation
- Contagion
- Control
- Integration
- Data administration
- Maturity

The three elements of IT strategy

- Information Systems Strategy (ISS) ÓWHATÔ
- Information Management Strategy (IMS) ÓWHOÔ
- Information Technology Strategy (ITS) ÓHOWÔ

Developing an IT strategy

1. Determine the business strategy, goals and objectives.
2. Define information needs and identify information sources.
3. Position audit and gap analysis undertaken for existing systems.
4. Heavy end user consultation and participation.
5. Change management and implementation
6. Review and control progress to ensure project objectives have been met
Earl’s Grid for assessing information systems

<table>
<thead>
<tr>
<th>Business Value</th>
<th>Technical Quality</th>
<th>Divest</th>
<th>Reassess</th>
</tr>
</thead>
<tbody>
<tr>
<td>Low</td>
<td>Low</td>
<td></td>
<td>Heavy user involvement to improve the value of information created and presented.</td>
</tr>
<tr>
<td></td>
<td>High</td>
<td>Divest</td>
<td>Reassess</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>High user involvement to improve the value of information created and presented.</td>
</tr>
<tr>
<td>High</td>
<td></td>
<td>Renew</td>
<td>Maintain and enhance</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Renew</td>
<td>Regular review and upgrade to maintain current position.</td>
</tr>
</tbody>
</table>

Divest: A costly and unused system.

Renew: Invest in a better IT infrastructure.

Maintain and enhance: Regular review and upgrade to maintain current position.
McFarlan’s grid or the ‘application portfolio’

<table>
<thead>
<tr>
<th>Strategic importance of planned IT systems</th>
<th>Strategic importance of current IT systems</th>
</tr>
</thead>
<tbody>
<tr>
<td>Low</td>
<td>High</td>
</tr>
<tr>
<td><strong>Turnaround</strong></td>
<td><strong>Strategic</strong></td>
</tr>
<tr>
<td>Limited importance today but predicted to become more strategically important in the future e.g. high potential for future competitive advantage. New and highly innovative systems normally at early stages of development.</td>
<td>The business depends on these systems for existing competitive advantage and will continue to do so in the future. Always at the heart of the organisations success with continuous redevelopment required.</td>
</tr>
<tr>
<td><strong>Support</strong></td>
<td><strong>Factory</strong></td>
</tr>
<tr>
<td>Not strategically critical and does not contribute significantly to the existing or future success of the organisation. Not critical and mainly exist for economic benefit e.g. increase efficiency and reduce headcount for data processing.</td>
<td>Currently viewed as strategically important and necessary for existing competitive success or advantage, but predicted that this significance in future is likely to disappear.</td>
</tr>
</tbody>
</table>
**Criteria for evaluating information systems**

- Quality of the information e.g. using ‘ACCURATE’ (see below)
- User acceptance testing e.g. surveys, interview, observation etc
- Actual costs and benefits of new system compared to budget
- Technical testing e.g. response time, performance and reliability
- Ease of recovery in the event of failure or malfunction

**Tools and techniques**

- User questionnaires, interviews and observation
- Testing using real and ‘dummy’ data
- Cost-Benefit (CB) analysis
- Benchmarking
- Post implementation audit and review
- Errors, complaints and queries reported
- The VFM or 3 Es approach

**Cost-Benefit (CB) analysis**

An economic evaluation technique which compares the costs associated with a proposed investment with the benefits that investment will return. Both tangible and intangible factors would be considered.

**Advantages**

- Considers the ‘intangibles’
- Useful technique for screening new projects

**Disadvantages**

- Uncertainty of estimating the future
- Placing a value on intangible benefits and costs
Post completion review and audit

Mistakes of management can be learned.

Techniques used to conduct a post completion audit

- End user satisfaction surveys
- Staff appraisals
- Exception reports e.g. time and cost
- Results from testing

The purpose

- To support continuous improvement
- To allow for the identification and implementation of corrective action

The value for money (VFM) framework

- Economy (cheap)
- Efficiency (quick)
- Effectiveness (good)

Qualities of good information

- A Accurate
- C Complete
- C Cost beneficial
- U User friendly
- R Relevant
- A Authoritive
- T Timely
- E Easy to use
Organising and managing information systems

**Centralisation of IT department or activities**

**Advantages of a centralised IT function**
- Economies of scale
- Better integration and compatibility of information systems
- Higher motivation of IT staff
- Can avoid duplication of effort
- Strategic view

**Benefits of in house developed information systems**
- Better understanding of information needs
- Strategic control
- Less risk to the security
- More effective support to end users

**Decentralisation of IT activities e.g. end user computing**

End-user computing is the direct hands on approach that end users have over the development and use of IT.

**Benefits of end user computing**
- Creativity and innovation
- Increases productivity of information systems
- End-user satisfaction ownership and motivation

**Limitations of end user computing**
- Lack of training and experience
- Lack of documentation
- Incompatibility of different systems
IT outsourcing (client-vendor relationships)

Examples include the outsourcing of system maintenance, development or data processing agreements with third party organisations, an entire IT department could be outsourced. IT outsourcing can allow management to start with a clean sheet and eliminate what they often see as an internal irritant.

### Advantages

- Save overhead
- Reduce the complexity
- Management can focus on its core competencies
- Flexibility of using outsourcer

### Disadvantages

- Loss of strategic control
- Over reliance
- Loss of competitive advantage
- Internal redundancy
- Risk to security
- Failure of outsourcer

### Management of vendors

- Policies, procedures and effective management
- Planned selection criteria
- Tender and visiting process
- References
- Contract agreements
- Penalties and cancellation terms

### Characteristics of a good service level agreement

- Terms and conditions
- Exit route for non performance
- Timescale of agreement
- Copyright and ownership
- Procedures for control
- Contact details

### Criteria for evaluating suppliers

- Invitation to tender documents
- Warranty and support
- Training assistance
- Cost and composite of cost
- Reliability and solid track record
### Management Information Systems

<table>
<thead>
<tr>
<th>Management Level</th>
<th>OPERATIONAL</th>
<th>TACTICAL</th>
<th>STRATEGIC</th>
<th>ALL LEVELS</th>
</tr>
</thead>
<tbody>
<tr>
<td>Information System</td>
<td>Transaction processing systems (TPS)</td>
<td>Decision support systems (DSS)</td>
<td>Executive information systems (EIS)</td>
<td>Expert Systems (ES)</td>
</tr>
</tbody>
</table>

### Emerging Information Systems

**Knowledge Management Systems (KWS)**

KWS are information systems that facilitate the creation and integration of new knowledge into an organisation. Many organisations now attempt to formalise systems for the gathering and dissemination of knowledge across the organisation. Knowledge management is the process of trying to collect, store and use knowledge within the organisation. Knowledge can be formalised by designing processes to create, store and use it to become explicit knowledge e.g. intranets, e-mail, databases, teams and social networking.

#### Types of KWS

- **Knowledge distribution systems** e.g. e-mail, scanners, e-fax, voice mail and document image processing (DIP). Groupware software packages like Lotus notes can help to manage e-mail, calendars, diaries and reminders.
- **Knowledge sharing systems** e.g. expert systems, databases, intranets and extranets.
- **Knowledge creation systems** e.g. computer aided design (CAD) and virtual reality systems (VR).

#### Benefits of KWS

- Help knowledge workers create new knowledge and expertise.
- Facilitates the sharing of information.
- Can reduce training time for new employees.
- Retention of knowledge e.g. if an employee leaves
- Could help gain competitive advantage
**Expert systems**

Software that behaves similar to the way a human expert would within a certain field of knowledge e.g. legal, medical, insurance or credit risk assessment. The expert knowledge, rules and facts are pre-programmed a memory to facilitate artificial intelligence by supporting decision making.

**Benefits of an expert system**

- Automated 'expertise' support for generalists.
- Speed of decision improved.
- Consistency of decision making
- Expert systems retain and acquire new knowledge

**Limitations of an expert system**

- Expensive to develop and maintain.
- Narrow and specific in focus.
- People can be more naturally creative than programmes.

---

**Enterprise-wide systems**

Also referred to as enterprise resource planning (ERP) or enterprise computing. Enterprise-wide systems are information systems that are used throughout a company or enterprise, to manage and coordinate resources, information and functions of a business. To be considered an ERP system, a software package must provide the function of at least two systems e.g. payroll and accounting functions if integrated.

ERP is the modern extension of MRP (material requirements planning, then later manufacturing resource planning) systems and CIM (Computer Integrated Manufacturing).

All functional departments are integrated into one holistic information system e.g. a central database. As well as integrating manufacturing, warehousing, logistics, and information technology, it would also include accounting, human resources, marketing and strategic management. SAP Business One is an example of an ERP software solution.

**Benefits of ERP systems**

- Speeds up enterprise wide exception reporting.
- Real-time data capture and reporting of financial results.
- Provides information for all levels of management.
- More effective planning and forecasting

**Limitations of ERP**

- Bespoke and expensive to develop and maintain.
- High switching cost.
- Industry prescriptions may not gain competitive advantage.
Customer relationship management (CRM) systems

CRM systems can automate many customer-related business activities and tasks. Customer loyalty and retention has become critical to the long-term survival of organisations, relationship management aims to build excellent relationships with customers in order to retain their loyalty.

Microsoft Dynamics CRM 4.0 is an easy to use customer management system that enables you to monitor and manage customers from their first contact all the way through to after-sales service. CRM software systems include customer contact management, sales automation, call centre applications and help desking. They allow departments to track customer information so that customers interacting with an organisation perceive the business as a single entity, despite interacting with a number of employees from different departments.

Benefits of CRM

- Increased loyalty of customers and free 'word of mouth'recommendation
- Organisation builds more knowledge and understanding about customers.

Web 2.0 tools

Web 2.0 tools refers to any computer application that is web-based and will support collaboration, interaction and sharing of information over the world wide web. Web 2.0 tools represent the second generation of software for the world wide web, moving away from static web pages to dynamic and shareable content. They enable people with no specialised technical knowledge to create their own websites, publish, create and upload audio and video files, share photos and information and many other tasks.

Examples

- Social-networking sites e.g. Twitter
- Video sharing sites e.g. YouTube
- Wikis e.g. a website that allows multiple users to create and modify web page content in a collaborative manner.
- Blogs e.g. a web site for regular entries of commentary, photos, files and descriptions, personal sites include MySpace UK and Facebook.

Benefits of Web 2.0 tools

- Facilitates creativity.
- Supports information sharing.
- Supports human collaboration e.g. virtual teams.
Electronic business (E-business)

Conducting business via electronic media e.g. telephone, fax machines, computers, video-teleconferencing etc. The internet supports E-business e.g. utilises information technology to support all the activities of a business, service its employees and other external stakeholders. Web 2.0 tools enable this to be done interactively.

E-commerce

The process of buying and selling goods and services electronically using website technology.

Benefits of e-commerce

✓ Improves marketing e.g. invitation to treat graphics and interactivity.
✓ Fulfil orders satisfactorily without human intervention e.g. electronic retailing (e-tailing) for automated ordering and payment
✓ Can monitor customer trends e.g. buying habits
✓ Encourage feedback from customers e.g. electronic surveys

Value added networks (VANS)

A VAN is a third-party network service provider which offers access to specialised services, normally for a fee e.g. Reuters. Customers either purchase leased lines or use dial-up to access the network. VANS can add value to an organisation’s products or services e.g. extranets, EDI and specialised knowledge databases, can all help those that subscribe to achieve mutual competitive advantage. VANS offer direct communication links to trading partners, mailbox services for further information and 24/7 message transmission.
The emergence of new forms of organisation

**Virtual or network firms e.g. dotcom companies.**

Network or virtual organisations rely heavily on external organisations or third parties for the delivery of their product or service.

A *virtual* organisation does not have a physical location. For example a collection of individuals that work from their home and the majority of the primary processes or activities of the organisation are outsourced to third party providers.

**Characteristics of virtual or network firms**

- High levels of outsourcing
- Relatively few physical assets e.g. lease rather than buy
- Relatively minimum full-time staff
- To the customer the organisation is perceived as one organisation

**Teleworking**

Teleworking (or telecommuting) is where staff employed by an organisation work from their home and communicate with the workplace via phone, fax, e-mail, intranet, extranet or any other telecommunications link.

<table>
<thead>
<tr>
<th>Advantages to employee</th>
<th>Disadvantages to employee</th>
</tr>
</thead>
<tbody>
<tr>
<td>✓ No commuting</td>
<td>✗ Room in your house for workspace</td>
</tr>
<tr>
<td>✓ Flexible working hours</td>
<td>✗ Family interruptions</td>
</tr>
<tr>
<td><strong>Advantages to employer</strong></td>
<td><strong>Disadvantages to employer</strong></td>
</tr>
<tr>
<td>✓ Saves office overhead</td>
<td>✗ Less loyalty from employees</td>
</tr>
<tr>
<td>✓ Larger pool of labour</td>
<td>✗ Staff training can be difficult</td>
</tr>
</tbody>
</table>
Virtual (or geographically dispersed) teams (GDT)

Virtual teams are groups or teams who are geographically dispersed but working and collaborating together. Virtual teams are not normally present in the same office, they are often working in different parts of the world and over different time zones.

Benefits of virtual teams

- Employer saves on staff office overhead
- Employer can recruit the best staff anywhere geographically
- Lower social cost to society from commuting

Limitations of virtual teams

- Cross-cultural management problems
- Time zones can cause delay in communication
- New methods of working maybe unfamiliar to those participating
- Isolation and lack of project team integration
- Group cultural norms can make teams very insular

IT to support virtual teams

Computer-supported Co-operative Working

Computer systems that support collaborative and the coordination of tasks and activities.

- Groupware
- Workflow management
- Internet, extranets and intranets
- E-mail, Video conferencing and Web 2.0 tools
- Knowledge work systems (KWS)

Groupware (collaborative software) supports multiple users on a network. Examples of groupware include Lotus Notes (or Lotus Domino) a client-server, collaborative application developed by IBM, or Microsoft Exchange. Features include quick notes, ideas and reminders, sharing of calendars, public folders, address books and schedulers to arrange meetings.

Workflow systems ensure less delay and greater efficiency of managing workflow. Image based workflow systems automate the flow of paper throughout the organisation by digitising paper based images. Form based workflow systems route text based documents around the organisation.
Key summary of chapter

Corporate Governance

The corporate governance framework is there to encourage the efficient use of resources and equally to require accountability for the stewardship of those resources. The aim is to align as nearly as possible the interests of individuals corporations and society”

(Sir Adrian Cadbury in 'Global Corporate Governance Forum' World Bank 2000)

UK corporate governance reporting and recommendations

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Cadbury and Greenbury report recommendations

- Split chairman and chief executive role
- Regular and more formal meetings.
- Directors remuneration clearly shown within the published accounts
- Pay awards to be decided by a remuneration committee using non-executive directors only
- Establish an audit committee using non-executive directors only
- Every company should have at least 3 non-executives directors

The Hampel report incorporated the recommendations from both the Cadbury and Greenbury Committees as well as amendments from the London Stock Exchange, it was published as the Combined Code in June 1998.

Benefits of good corporate governance

- Greater fairness and openness of directors
- Greater public confidence in companies
- Reduced risk for investors and other stakeholders
- Lower risk of strong CEO domination
- Transparency, timely and clearer communication of information
- Improves performance and leadership by the board
Summary of the principles for good governance

Directors responsibilities

- The Board should be effective to lead and control the company.
- Clear division of responsibilities between Chairman and CEO to ensure balance of power and authority.
- Board balance e.g. executive and non-executive roles.
- Supply of 'transparent' information.
- Timely and of appropriate quality of information.

Appointment of directors

- Formal and transparent procedures.
- Re-election e.g. all directors at regular intervals and at least every three years.

Directors Remuneration

- Level and make-up of remuneration should be sufficient to attract and retain but not more than necessary.
- A proportion linked to performance.
- Formal and transparent procedure fixing remuneration of each director.
- Disclosure e.g. details of the remuneration of each director.

Relations with Shareholders

- Dialogue with institutional shareholders.
- Constructive use of the Annual General Meeting (AGM).
- To communicate with private investors and encourage their participation.

Accountability and Audit

- Financial reporting e.g. balanced and understandable assessment of the company's position, performance and prospects.
- Maintain effective internal controls.
- Audit committee for maintaining an appropriate relationship with the auditors.
International perspective on corporate governance

This is of paramount practical concern for policymakers, managers, accountants and others since they are affected by the regulatory regimes and changes of regulations on a daily basis in their working environment.

Organisation for economic co-operation and development (OECD)

- Rights of shareholders e.g. one share equals one vote for all shareholders.
- Equitable treatment of shareholders e.g. protection of minority interests.
- Equitable treatment of all stakeholders.
- Accurate and timely information for users of published information.

US, the Sarbanes-Oxley Act (2002)

- Legal requirement for all companies with a US listing.
- Attempts to address auditor independence and corporate governance issues.
- Places restrictions on the nature of non-audit services that can be performed by auditors. Audit committees must approve any allowed additional services.
- Audit committee members should be independent, and are responsible for the appointment, remuneration and overseeing of external auditors.
- Audit committee must establish rules for the protection of whistleblowers.

South Africa, the King Report (2002)

- Broader stakeholder approach to governance.
- Considers social, environmental, economic aspects of company activities (HIV/AIDS impact, black economic empowerment, equal opportunities and human capital development)
- Accountability and independence of the board emphasised more.
- Delegation did not diminish ultimate responsibility of the board.
- Board is responsible for risk management processes including internal audit.
- Openness to all stakeholders
Ethics and social responsibility

**Corporate social responsibility (CSR)** is concerned with being aware of the impact of actions on others, and to act in the best interests of society.

**Ethics** is concerned with rules or morals about the right behaviour and conduct, it is one part of CSR

**Advice on how to be more ethical and socially responsible**

- Good public relations.
- Protection of the ecological environment
- Control energy consumption, waste and emissions
- Recycle all packaging material
- Support charities and the local community
- Good conditions of work provided for employees
- Embody ethical culture through a mission statement and training.
- Set and publish aims and objectives to achieve greater CSR.

Ethics for members of CIMA

The CIMA Code of Ethics for Professional Accountants sets out the fundamental principles of professional behaviour that members and students are required to follow. Other accountancy bodies and professions such as the ACCA, ICAEW and AAT, have similar standards of behaviour and conduct.

**Code of conduct for CIMA management accountants**

- Integrity
- Objectivity
- Professional competence and due care
- Professional behaviour
- Quality to the client
- Confidentiality
- Serve the public interest

**Code of conduct ensures**

- A positive global image to CIMA
- Protection for public interest.
- Prevention and limitation of malpractice.
- Repeat business in the long-term for CIMA and CIMA members
Key summary of chapter

**Private sector organisations**
Sub-sectors of the economy not directly controlled by the government or state e.g. private business and households.

**Examples**
- Private businesses
- Companies (corporations)
- Private banks and building societies
- Non-governmental organisations e.g. trade unions, charities, clubs etc

**Public organisations**
Sub-sectors of an economy, or organisations, owned and directly controlled by the state or government.

**Examples**
- Local authorities.
- State owned industries e.g. the UK post office.
- Public corporations e.g. the British Broadcasting Company (BBC).

**Characteristics of public organisations**
- Ultimately accountable to government.
- Goals and guidelines determined by government.
- Not-for-profit motive (NPO).
- Funded by the general public e.g. through taxation.

**Multinational Companies (MNC)**
A multinational corporation (MNC) can also be referred to as a transnational corporation (TNC) and a multinational enterprise (MNE). A global or international organisation which has production or service facilities in more than one country.
Emerging markets

An emerging market (or emerging economy) is a country in the early stages of development and often receptive to foreign investment. Emerging markets have very high growth rates in national product and yield enormous market potential. Examples of emerging markets include China and India considered to be two of the largest, also Mexico and Brazil, these nation's social or business activities are in the process of rapid economic growth and industrialisation. There are approximately 30 emerging markets in the world today.

Emerging market multinationals e.g. Korea's Samsung

Emerging market multinationals are changing the rules of the game, firms from developing countries are able to develop global competitive advantage, surviving local competition from their own unprotected economies and beating western multinationals.

The rise of emerging markets signals the greatest shift in global economic power since the industrial revolution. Emerging market economies are set not only to emerge, but also dominate the economic future of the world. Domestic companies from such countries as Brazil, Russia, India, Egypt and South Africa are successfully making progress in international trade and in every imaginable industry sector.

Characteristics of emerging multinationals

- Recognised as a global leader
- Has global presence
- Competitive in price, quality, technology design and management
- Can be benchmarked against the biggest and best in the world.
Comparing and contrasting organisational structures

<table>
<thead>
<tr>
<th>The small or entrepreneurial structure</th>
<th>The functional structure</th>
<th>The divisional structure</th>
<th>The matrix structure</th>
</tr>
</thead>
<tbody>
<tr>
<td>Informal, small organisation</td>
<td>Formal, bureaucratic,</td>
<td>Formal, bureaucratic,</td>
<td>Formal or informal</td>
</tr>
<tr>
<td></td>
<td>large organisation</td>
<td>complex group</td>
<td>teamwork</td>
</tr>
<tr>
<td>Founder driven with less bureaucracy.</td>
<td>Bureaucratic. Place for</td>
<td>Bureaucratic. Place for</td>
<td>Teamwork and</td>
</tr>
<tr>
<td></td>
<td>everything and everything in its place</td>
<td>everything and everything in its place</td>
<td>project focused</td>
</tr>
<tr>
<td>Communication in all directions</td>
<td>Vertical communication</td>
<td>Vertical communication</td>
<td>Communication in all directions</td>
</tr>
<tr>
<td>Power culture</td>
<td>Role culture</td>
<td>Role culture</td>
<td>Task culture</td>
</tr>
<tr>
<td>Customer focused</td>
<td>Process or activity focused</td>
<td>Customer focused</td>
<td>Project focused</td>
</tr>
<tr>
<td>Suits a dynamic and uncertain environment.</td>
<td>Suits a stable and certain environment.</td>
<td>Suits a dynamic and uncertain environment.</td>
<td>Suits a dynamic and uncertain environment.</td>
</tr>
<tr>
<td>Flatter and flexible structure</td>
<td>Tall and inflexible structure</td>
<td>Flatter and flexible structure</td>
<td>Flatter and flexible structure</td>
</tr>
<tr>
<td>Integrated</td>
<td>Specialised</td>
<td>Specialised</td>
<td>Integrated</td>
</tr>
<tr>
<td>Unity of command</td>
<td>Unity of command</td>
<td>Unity of command</td>
<td>Dual authority</td>
</tr>
<tr>
<td>Centralised decisions</td>
<td>Centralised decisions</td>
<td>Decentralised decisions</td>
<td>Decentralised decisions</td>
</tr>
</tbody>
</table>

Virtual or network firms e.g. dotcom companies.

Network or virtual organisations rely heavily on external organisations or third parties for the delivery of their product or service.

A virtual organisation does not have a physical location. For example a collection of individuals that work from their home and the majority of the primary processes or activities of the organisation are outsourced to third party providers.

Characteristics of virtual or network firms

- High levels of outsourcing
- Relatively few physical assets e.g. lease rather than buy
- Relatively minimum full-time staff
- To the customer organisation is perceived as one organisation

E3 revision summaries
Types of workforce flexibility

- **Functional flexibility** (task flexibility/multi-skilled employees) concerns breaking down traditional occupational boundaries and avoidance of over-specialisation.
- **Financial flexibility** aims to convert staff cost from fixed to variable cost.
- **Numerical flexibility** enables a firm to adjust rapidly to changing levels of demand by increasing or decreasing the number of employees.
- **Temporal flexibility** can be achieved by varying the hours worked by employees in response to changes in demand.

Lean production or the Toyota production system (TPS)

Lean production (also known as the Toyota Production System) is a manufacturing methodology originally developed by Toyota

"good thinking means good product"

Toyota Production System (TPS) was built on two main principles: Just In Time (JIT) and Jidoka e.g. continuous improvement of quality within the production system.

Lean production focuses on delivering resources when and where they are needed.

Lean production tools and techniques

- Getting things right first time
- Minimising inventory e.g. JIT stock control
- Minimising waste
- Flexible workforce practices
- High commitment to human resource policies
- Culture of commitment to continuous improvement
### Concepts that support lean production

<table>
<thead>
<tr>
<th><strong>Total productive maintenance (TPM)</strong></th>
<th>aims to shorten lead times by ensuring production and machine maintenance staff work closer together. Machine operators are empowered and trained in order to speed up routine servicing, fault diagnosis and maintenance of operating machinery.</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Just in time (JIT)</strong></td>
<td>requires that products should only be produced if there is an internal or external customer waiting for them. It aims ideally for zero stock e.g. raw materials delivered immediately at the time they are needed, no build up of work-in-progress in production and finished goods only produced if there is a customer waiting for them.</td>
</tr>
<tr>
<td><strong>Total quality management (TQM)</strong></td>
<td>is the process of embracing a quality conscious philosophy or culture within an organisation, it aims towards standards of near perfection and continuous improvement.</td>
</tr>
<tr>
<td><strong>Quality circles</strong></td>
<td>is an American idea, whereby a group of 5 to 8 employees, normally working in the same area, volunteer to meet on a regular basis to identify areas for improvement or analyse work related problems in order to find solutions.</td>
</tr>
</tbody>
</table>

### Information technology to support capacity planning

<table>
<thead>
<tr>
<th><strong>Flexible manufacturing systems (FMS)</strong></th>
<th>consist of several machines along with part and tool handling devices such as robots, arranged so that it can handle any family of products or parts for which the system has been designed and developed. These systems are highly computerised, automated and integrated.</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Computer aided design (CAD)</strong></td>
<td>automates the design, drafting and display of graphically oriented information early in the design process aids good production planning.</td>
</tr>
<tr>
<td><strong>Computer aided manufacturing (CAM)</strong></td>
<td>automates production e.g. robotic and programmable production cycles.</td>
</tr>
<tr>
<td><strong>Optimised production technology (OPT)</strong></td>
<td>helps to avoid the build up of unnecessary work in progress and supports a JIT environment e.g. resource planning centred around bottleneck resources (limiting factors) or the binding constraints that limit capacity.</td>
</tr>
<tr>
<td><strong>Materials requirement planning (MRP I)</strong></td>
<td>is an inventory control system which provides an automated list of components and materials required for the type and number of products entered. This allows better production planning and accuracy of inventory management.</td>
</tr>
<tr>
<td><strong>Manufacturing resource planning (MRP II)</strong></td>
<td>Evolved from MRP I. A system that incorporates not only material requirements, but all manufacturing resources such as different labour types, machine types and other manufacturing resources required for the type and number of products entered.</td>
</tr>
<tr>
<td><strong>Computer-integrated manufacturing (CIM)</strong></td>
<td>is manufacturing supported by computers. The total integration of computer aided design, manufacturing, quality control and purchasing in one centralised system.</td>
</tr>
<tr>
<td><strong>Enterprise-wide systems (ERP systems)</strong></td>
<td>also referred to as enterprise resource planning (ERP) or enterprise computing. Enterprise-wide systems are information systems that are used throughout a company or enterprise. A company-wide computer software system used to manage and coordinate all the resources, information and functions of a business.</td>
</tr>
</tbody>
</table>
Chapter 10
Change Management
Key summary of chapter

Change
A gradual evolution or sudden transformation, not normally within the control of the organisation, change often due to influences from the organisation's environment.

Change management
A structured approach to transition individuals, groups, departments, divisions etc from a current state to a desired future state. Other terms for change management include configuration management, change control or change leadership.

Internal ‘change triggers’
Internal factors within the organisation which cause change to be necessary e.g. new CEO, dissatisfaction of management or staff, reorganisation, rationalisation programmes, new information system etc.

External ‘change triggers’
External (environmental) influences which cause change to be necessary e.g. new competition, changes in strategy by the competition, new legislation, economic, technological, social changes in customer needs etc.

Models for analysing external change triggers
- PEST or SLEPT (general environment) e.g. social, legal, economic, political and technological.
- Porter’s 5-forces (task or competitive environment) e.g. threat of new entrants, competitive rivalry, substitutes, bargaining power of suppliers and bargaining power of customers.
**Greiner’s organisational growth model**

Greiner's Growth Model describes the different stages an organisation passes through over time as they grow in size. Larry E. Greiner originally proposed his model in 1972 with five phases of growth. A sixth phase was added further in 1998. Greiner explained the management problems that would be experienced over the different phases, each phase reaching a crisis or turning point. Organisations often have to change or reorganise at each of these phases, so if effectively planning for it, they can ensure smoother transition from one phase to another to avoid the chaos this may cause.

<table>
<thead>
<tr>
<th>Phase 1</th>
<th>Phase 2</th>
<th>Phase 3</th>
<th>Phase 4</th>
<th>Phase 5</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Young</strong></td>
<td><strong>Phase 2</strong></td>
<td><strong>Phase 3</strong></td>
<td><strong>Phase 4</strong></td>
<td><strong>Phase 5</strong></td>
</tr>
<tr>
<td>Growth through creativity</td>
<td>Crisis of leadership</td>
<td>Crisis of autonomy</td>
<td>Growth through delegation</td>
<td>Crisis of red tape</td>
</tr>
<tr>
<td>Small</td>
<td>Large</td>
<td>Large</td>
<td>Large</td>
<td>Large</td>
</tr>
</tbody>
</table>

**Size of Organisation**

- Growth through creativity
- Crisis of leadership
- Crisis of autonomy
- Growth through delegation
- Growth through coordination
- Crisis of red tape
- Crisis of ?

**Age of Organisation**

- Young
- Mature

---

E3 revision summaries
Stages in the change process ‘planned change theory’

1. Diagnose current problems
2. Create dissatisfaction with the existing state
3. Participation by those affected
4. Demonstrate support by senior management
5. Implementation of change.
6. Reward systems modified
7. Review and feedback obtained

Different reactions to change

- Acceptance
- Indifference
- Passive resistance
- Active resistance

Parameters for successful change

Wilson suggests the following parameters for how to consider change

- Scale e.g. scope and size of the program.
- Investment e.g. investment in resources defined in monetary terms.
- Timescale e.g. how long the process will take.
- Change e.g. the nature of the change required.
- Impetus for change e.g. the reasons for the programme of change required.
- Strategy e.g. the plan or strategy driving the change process.

Kotter and Schlesinger gave six methods of dealing with resistance to change

- Education and communication
- Participation and involvement
- Facilitation and support
- Negotiation and agreement
- Manipulation and co-optation
- Explicit and implicit coercion
Kurt Lewin - 3 stage (process) approach to managing change

- **Unfreeze**
  This process spells out the reasons why change needs to occur.

- **Behaviour change**
  This process identifies and crafts new norms, attitudes and beliefs.

- **Refreeze**
  This process reinforces new ways through reward and encouragement.

Lewin's *force field analysis* illustrates the forces that drive change and the restraining forces which push change back and prevent or hinder it from occurring. Lewin recommended weakening restraining forces as the popular strategy for managing change.

**Ideal position**

**Current state**

**Driving Forces**

**Restraining Forces**

**Practical techniques to reduce resistance**

- ✔ Bringing conflict into the open
- ✔ Top down commitment with clear vision of change
- ✔ Supporting positive behaviour
- ✔ Reward systems
- ✔ Communication and education
### Nature of change

<table>
<thead>
<tr>
<th>Management Role</th>
<th>Incremental</th>
<th>Transformational</th>
</tr>
</thead>
<tbody>
<tr>
<td>Reactive</td>
<td></td>
<td>Planned</td>
</tr>
<tr>
<td></td>
<td>Tuning</td>
<td>Planned</td>
</tr>
<tr>
<td></td>
<td>e.g. fine tuning or incremental change.</td>
<td>e.g. centralised, top-down, rigid and systematic approaches.</td>
</tr>
<tr>
<td></td>
<td>Adaptation</td>
<td>Forced</td>
</tr>
<tr>
<td></td>
<td>e.g. emergent.</td>
<td>e.g. when in crisis.</td>
</tr>
</tbody>
</table>
Types of change

Planned contrasted to emergent approaches to change

<table>
<thead>
<tr>
<th></th>
<th>Emergent Approaches</th>
<th>Planned Approaches</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Management Style</strong></td>
<td>Bottom-up and decentralised</td>
<td>Top-down and centralised</td>
</tr>
<tr>
<td><strong>Control of change</strong></td>
<td>Informal, decentralised and emergent</td>
<td>Tight control, rules and procedures</td>
</tr>
<tr>
<td><strong>Environment</strong></td>
<td>Dynamic, chaotic and uncertain environment.</td>
<td>Stable and certain environment.</td>
</tr>
<tr>
<td><strong>Change</strong></td>
<td>Flexible and adaptive</td>
<td>Slow and inflexible</td>
</tr>
</tbody>
</table>

**Step change**

Change that happens over a very short period of time and which makes a significant and radical difference to the organisation. Step change is when the trend line of performance makes a significant jump in direction, up or down, and stops being smooth. Step change is different from incremental change, which occurs gradually over an extended period of time.

**Transformational change**

Change that is radical, large scale changes to the strategy or operations of the organisation. Often transformational change involves major restructuring, reorganisation and/or cultural change necessary.

**Incremental change**

Change enforced gradually by management using a planned and consultative approach. This approach to change management would be used when no major restructuring or change of culture is necessary within the organisation.
Beer and Nohria

- **Theory E** (change based on economic value) e.g. hard and coercive approach to change, shareholder value as the only legitimate concern.
- **Theory O** (change based on organisational capability) e.g. soft and consultative approach to change, long-term need for the organisation to recognise the needs of all stakeholders, not just shareholders.

Contrasting Theory E and Theory O

<table>
<thead>
<tr>
<th></th>
<th>Theory O</th>
<th>Theory E</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Management Style</strong></td>
<td>Bottom-up Participative/Democratic</td>
<td>Top-down Autocratic</td>
</tr>
<tr>
<td><strong>Objective</strong></td>
<td>Develop organisational capabilities</td>
<td>Maximise shareholder value</td>
</tr>
<tr>
<td><strong>Control of change</strong></td>
<td>Informal, decentralised and emergent</td>
<td>Tight control, rules and procedures</td>
</tr>
<tr>
<td><strong>Change</strong></td>
<td>Flexible and adaptive</td>
<td>Slow and inflexible</td>
</tr>
<tr>
<td><strong>Reward</strong></td>
<td>Commitment and challenge</td>
<td>Financial incentive</td>
</tr>
</tbody>
</table>
### The learning organisation

According to Peter Senge, learning organisations are organisations that facilitate the learning by all its members and continuously transforms itself in order to cope with change. Rosabeth Moss Kanter, argued that segmentalist companies e.g. those which are organised by functions, lack creativity and entrepreneurial spirit. She argued that more integrative approaches would release more ideas from unconnected sources within the organisation.

### Organisational Development

Bennis defined OD as "a response to change, a complex educational strategy intended to change the beliefs, attitudes, values and structure of organisations so that they can better adapt to new technologies, markets and challenges, and to the dizzying rate of change itself." OD specialists are third party consultants and used for when chronic change or major transformation is needed or where severe problems in performance exist within the organisation. Often described as "change agents," OD consultants come from varied backgrounds with experience and training in organisational development, organisation behaviour, psychology, education, management or human resources. Many have advanced degrees and most have experience in a variety of organisational settings.

### Managing job reduction (or redundancy)

Redundancy occurs when the role that an employee performs no longer exists or is not required. This is a sensitive issue, the loss of motivation and morale of the entire workforce can be devastated when such news does occur not just those individuals affected by it.

**A process to manage job reduction**

1. Identify what changes will be necessary
2. Clear vision of change communicated
3. Educate and communicate the reasons
4. Participation encouraged by staff to aid change
5. Plan and determine how change needs to occur
6. Review and feedback obtained

**Ethical advice offered**

- Compulsory redundancy should be last resort
- A sensitive matter so plan for it
- Management must act as honestly and fairly as possible
- Selection methods used on a fair basis e.g. last in first out
A team is a group of individuals with complimentary skills and a commitment to a common purpose. They normally share a common sense of purpose; identity and social belonging and work interdependently toward a common goal often collectively sharing reward.

‘A collection or group of individuals who share a sense of common identity and contribute to the same common aim or purpose’.

<table>
<thead>
<tr>
<th>Advantages</th>
<th>Disadvantages</th>
</tr>
</thead>
<tbody>
<tr>
<td>✓ Dynamic and creative</td>
<td>✗ Inadequate leadership</td>
</tr>
<tr>
<td>✓ Flexible to change</td>
<td>✗ Unclear goals or objectives</td>
</tr>
<tr>
<td>✓ Improves staff morale</td>
<td>✗ Personality clashes</td>
</tr>
<tr>
<td>✓ Improves communication</td>
<td>✗ Group norms create ëinsular barriersë</td>
</tr>
<tr>
<td>✓ Group norms unify members</td>
<td>✗ Too many meetings to get things done</td>
</tr>
<tr>
<td></td>
<td>✗ Dual authority e.g. if a matrix structure exists</td>
</tr>
</tbody>
</table>

Bruce Tuckman’s stages of team development

<table>
<thead>
<tr>
<th>Forming</th>
<th>Storming</th>
<th>Norming</th>
<th>Performing</th>
</tr>
</thead>
<tbody>
<tr>
<td>ÔAn inefficient collection of individualsÔ</td>
<td>ÔOpen conflict, a highly defensive and emotional stage.Ô</td>
<td>ÔTeam conforming to norms with greater efficiency.Ô</td>
<td>ÔFully integrated team, development ceases.Ô</td>
</tr>
</tbody>
</table>
Charles Handy’s contingency approach to team effectiveness

A manager cannot in the short-term vary the ‘givens’ e.g. team size, members, aims and the challenges faced. Managers must use instead ‘intervening factors’ to maximise the output of a team to achieve greater group productivity and satisfaction.

Examples of ‘intervening factors’

- A good leader
- Clear and structured reward systems
- Clear establish aims and objectives
- Common processes and procedures
- Promotion of openness and trust
- Time for a group to integrate
**Key summary of chapter**

**Control theory**

<table>
<thead>
<tr>
<th>Feedback control ‘appraisal’</th>
</tr>
</thead>
<tbody>
<tr>
<td>Feedback is any process where part of the output of a system is measured and returned as input to regulate the systems further output.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Feed-forward control ‘prevention rather than cure’</th>
</tr>
</thead>
<tbody>
<tr>
<td>Feed-forward control would be a system that in a pre-emptive way, reacts to changes in its environment, normally to maintain some kind of desired state.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Hopwood’s three forms of control</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Social controls e.g. group norms, staff culture and social interaction.</td>
</tr>
<tr>
<td>2. Administration control e.g. management exception reporting systems.</td>
</tr>
<tr>
<td>3. Self control e.g. staff exerting self-control by modifying their own behavior.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Bureaucracy</th>
</tr>
</thead>
<tbody>
<tr>
<td>An organisation bound by an elaborate set of rules and procedures to tightly control it.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Reward</th>
</tr>
</thead>
<tbody>
<tr>
<td>Monetary reward is an example of extrinsic reward and considered as the most important of all hygiene factors according to Frederick Hertzberg.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Types of financial incentive schemes</th>
</tr>
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<tbody>
<tr>
<td>Performance related pay (PRP) systems</td>
</tr>
<tr>
<td>Bonuses</td>
</tr>
<tr>
<td>Profit sharing schemes</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Staff appraisal</th>
</tr>
</thead>
<tbody>
<tr>
<td>The review and assessment of an employee’s performance with the potential for improving effectiveness of performance through training and development.</td>
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</tbody>
</table>

<table>
<thead>
<tr>
<th>The aims of an appraisal system</th>
</tr>
</thead>
<tbody>
<tr>
<td>Reward</td>
</tr>
<tr>
<td>Performance</td>
</tr>
<tr>
<td>Potential for development</td>
</tr>
</tbody>
</table>
Examples of control in the workplace

- Job descriptions, grades and authority levels
- Span of control and scalar chain
- Organisational structure
- Standardisation of work procedures
- Rules and procedures
- Disciplinary procedures
- Reward
- Dress code
- Handbook
- Induction
- Training and development
- Recruitment and selection
- Contracts
- Staff appraisal

Classical school of management contrasted to human relations approach

<table>
<thead>
<tr>
<th></th>
<th>‘Classical School’ approach</th>
<th>‘Human Relations’ approach</th>
</tr>
</thead>
<tbody>
<tr>
<td>Theorists</td>
<td>Henry Fayol, Frederick Taylor, Max Weber</td>
<td>Elton Mayo, Abraham Maslow, Frederick Herzberg</td>
</tr>
<tr>
<td>History</td>
<td>Late 19th century</td>
<td>Early 20th century.</td>
</tr>
<tr>
<td>Management Style</td>
<td>Autocratic, lack of consultation.</td>
<td>Participative, democratic.</td>
</tr>
<tr>
<td>Motivation</td>
<td>Extrinsic Reward e.g. money.</td>
<td>Intrinsic Reward e.g. job enrichment.</td>
</tr>
<tr>
<td>Management Control</td>
<td>Carrot and stick approach.</td>
<td>Contented cows produce more milk.</td>
</tr>
<tr>
<td>Management Focus</td>
<td>Task planning and design</td>
<td>Human welfare and psychology.</td>
</tr>
</tbody>
</table>
Burns and Stalker

Characteristics of ‘organic’ verses ‘mechanistic’ organisations

<table>
<thead>
<tr>
<th>Management Style</th>
<th>Organic</th>
<th>Mechanistic</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Participative and democratic</td>
<td>Autocratic and lack of consultation</td>
</tr>
<tr>
<td>Control</td>
<td>Informal and decentralised</td>
<td>Formal and centralised</td>
</tr>
<tr>
<td>Communication</td>
<td>Lateral (all direction)</td>
<td>Vertical (up and down)</td>
</tr>
<tr>
<td>Change</td>
<td>Flexible and adaptive</td>
<td>Inflexible and slow to change</td>
</tr>
<tr>
<td>Structure</td>
<td>Flat chain of command e.g.</td>
<td>Tall chain of command and clearly defined roles</td>
</tr>
<tr>
<td></td>
<td>Matrix/Team/entrepreneurial</td>
<td></td>
</tr>
<tr>
<td>Environment</td>
<td>Dynamic/Uncertain</td>
<td>Stable/Certain</td>
</tr>
<tr>
<td>Outcome</td>
<td>Creative</td>
<td>Efficient</td>
</tr>
</tbody>
</table>

The concept of clan/cultural control

Hofstede’s dimensions of national culture

- **Power distance.** Extent to which people accept inequality of power.
- **Uncertainty avoidance.** Tolerance towards uncertainty or ambiguity.
- **Individualism /collectivism.** Collectivism strong affiliation towards one another e.g. strong and cohesive groups. Individualism individuals are expected to take care of themselves e.g. a strong need for individual success.
- **Masculinity/femininity.** Men's masculine values e.g. very assertive and competitive, are relatively different from women's feminine values e.g. modest and caring. Masculinity is a culture with a strong need for achievement, assertiveness and materiality. Femininity is a culture where relationships, modesty and quality of life are considered more important.
- **Long-Term Orientation.** Long Term Orientation e.g. perseverance, verses Short Term Orientation e.g. protection of reputation and traditions.

The 5 dimensions of culture can help management determine

- Leadership style
- Motivation incentives
- Organisational structure
- The degree of rules and procedures
Controlling subsidiaries

- Mission statement, goals and objectives.
- Performance measurement systems
- Systems for strategic planning and control
- Management appraisal process.
- Reward
- Culture

Goold and Campbell

Goold and Campbell identified three ‘styles of strategic management’

- **Strategic planning**  Senior management work closely with individual business unit managers to develop strategies for their business units.
- **Strategic control**  Senior management decentralise the development of strategic plans to business unit managers.
- **Financial control**  Control of strategy through a budget (financial) process e.g. financial controls and profit targets which business units are required to adhere to.

The divisional structure

A division is a distinct business set up within a larger company to ensure a certain product or market is handled and promoted as though it were a separate business.

<table>
<thead>
<tr>
<th>Advantages</th>
<th>Disadvantages</th>
</tr>
</thead>
<tbody>
<tr>
<td>✓ Quicker decision making</td>
<td>✗ High cost of head office</td>
</tr>
<tr>
<td>✓ Focus on product and market performance</td>
<td>✗ Duplication of functions (or departments)</td>
</tr>
<tr>
<td>✓ Ring fencing of financial results</td>
<td>✗ Reluctance to delegate by senior management</td>
</tr>
<tr>
<td>✓ More empowerment</td>
<td>✗ Lack of goal congruence</td>
</tr>
<tr>
<td>✓ Good training ground for managers.</td>
<td></td>
</tr>
<tr>
<td>✓ Frees up senior management time</td>
<td></td>
</tr>
</tbody>
</table>
The functions of a performance measurement system

- Publicise and communicate direction
- Control the organisation.
- Plan and allocate resources

Neely’s 4Cs in performance measurement (1998)

1. Check position
2. Communicate position
3. Confirm priorities
4. Compel progress

Recommended process to develop a performance measurement system

1. Senior management 'a clear vision of change'
2. Benchmark with other organisations
3. Participation by staff throughout the process
4. Targets/criteria should be set after consultation
5. Reward systems should be modified
7. Training for managers and staff
8. Review and monitor the new system
## Evaluating the performance of divisions

### The controllability principle
The controllability principle is concerned with assessing performance based upon measures that can be controlled only by a manager and omitting any items which are uncontrollable.

### Profit based methods for evaluating the performance of divisions

#### Operating profit (net profit) margin

\[
\text{Operating profit (net profit) margin} = \frac{\text{Profit before interest and tax (PBIT)}}{\text{Turnover}} \times 100\%
\]

#### Gross profit (sales) margin

\[
\text{Gross profit (sales) margin} = \frac{\text{Turnover less cost of sales (gross profit)}}{\text{Turnover}} \times 100\%
\]

Generally the gross profit or sales margin can also be referred to as the contribution to sales (C/S) ratio e.g. gross profit (sales less variable cost) ÷ sales.

#### Mark up

\[
\text{Mark up} = \frac{\text{Turnover less cost of sales (gross profit)}}{\text{Cost of sales}} \times 100\%
\]

#### Return on capital employed (ROCE)

\[
\text{Return on capital employed (ROCE)} = \frac{\text{Profit before interest and tax (PBIT)}}{\text{Capital employed}} \times 100\%
\]

ROCE is also referred to as return on investment (ROI) and return on net assets (RONA). ROCE measures profitability and shows how well the business is utilising its capital to generate profits.
Residual income (RI)

Residual income is the profit earned by a division less a ‘notional interest charge’ for the investment of finance within it.

<table>
<thead>
<tr>
<th>Profit before interest and tax (PBIT)</th>
<th>£</th>
</tr>
</thead>
<tbody>
<tr>
<td>Capital employed x head office % interest charge</td>
<td>X</td>
</tr>
<tr>
<td>Residual income</td>
<td>X</td>
</tr>
</tbody>
</table>

Residual income uses the same profit before interest and tax and capital employed value as the ROCE measure. Residual income is an absolute measure that deducts from profit before interest and tax, an imputed ‘notional’ interest charge using a cost of capital or return required.

Economic value added (EVA)

Economic value added was developed by Stern Stewart & Co and is a registered trademark. EVA is an estimate of economic profit, measured as Net Operating Profit after Taxes (or NOPAT) less the money cost of capital. MVA and EVA are strongly correlated.

\[
\text{EVA} = \text{Net cash operating profit after tax} - \text{(adjusted for accounting distortions e.g. add back depreciation)} - \text{Economic depreciation (based on market value or replacement cost of assets)} - \text{Amortised R&D, advertising, marketing, goodwill, brand or new product development cost} - \text{‘adjusted’ capital employed x cost of capital}
\]

Contrasting ROI, RI and EVA

<table>
<thead>
<tr>
<th>ROI</th>
<th>RI</th>
<th>EVA</th>
</tr>
</thead>
<tbody>
<tr>
<td>All measures support goal congruence for profit maximisation</td>
<td>Accounting based measures</td>
<td>Cash based measure</td>
</tr>
<tr>
<td>Historical accounting for non-current assets</td>
<td>Use of replacement cost</td>
<td></td>
</tr>
<tr>
<td>Long-term expenditure written off in the same financial period</td>
<td>Capitalises long-term expenditure and amortises</td>
<td></td>
</tr>
<tr>
<td>Relative measure</td>
<td>Absolute measures</td>
<td></td>
</tr>
<tr>
<td>No finance charge</td>
<td>Finance charge recognised</td>
<td></td>
</tr>
</tbody>
</table>
**Alfred Rappaport’s definition of shareholder wealth (value)**

Shareholder value = corporate (business) value – Debt

---

**Total shareholder return (TSR)**

\[
\text{TSR} = \frac{\text{Dividend per share} + \text{Growth in share price}}{\text{Market share price at the start of the period}} \times 100%
\]

The increase in the share price plus the value of any dividends paid or proposed.

---

**Market value added (MVA)**

MVA is an external measure of shareholder wealth, measured by taking the rise in the market capitalisation during a period less the increase in capital invested during a period by investors. If MVA is positive, then the firm has added shareholder value. MVA and EVA are strongly correlated.

---

**Value based management**

Value based management may often be referred to as shareholder value analysis (SVA). Value based management (VBM) is an approach which focuses on strategies and actions to create more value for shareholders. Value being measured by share price (market capitalisation), dividends and other principles such as RI or EVA.

Alfred Rappaport developed seven 'value drivers':

1. Sales growth
2. Operating profit margin
3. Cash income tax rate
4. Incremental fixed capital investment rate
5. Investment in working capital rate
6. Planning period
7. Cost of capital

**Managing VBM**

- Strategic selection of projects which create high shareholder wealth.
- Resource allocation and funding should have a recognised opportunity cost.
- Performance targets clearly communicated.
- Reward linked and correlated to performance targets.
- Change management to facilitate implementation.
- Review of VBM system for continuous improvement.
Multidimensional performance measurement

The balanced scorecard developed by Kaplan and Norton

The four perspectives of the balanced scorecard

- **Customer perspective** e.g. what must we do right for our customers?
- **Internal perspective** e.g. what must we excel at internally?
- **Innovation and learning perspective** e.g. how can we innovate?
- **Financial perspective** e.g. how do we satisfy shareholders?

### Advantages

- Long-term view of performance
- Non-financial as well as financial measures considered
- Performance measures can be 'tailor made'
- Monitor and control operations
- Communicate and publicise goals to all stakeholders
- Link to remuneration of management and staff

### Disadvantages

- Historical performance no guide to the future
- Manipulation performance measures
- Costly 'bespoke' information systems support BSC
- Conflict or 'trade off' between BSC perspectives
- Too many performance measures can distort the benefits

### A process to implement balanced scorecard (BSC)

1. A clear vision BSC communicated
2. Demonstration that senior management are committed to the idea
3. Education given to all managers and staff
4. Consultative meetings and presentations
5. Participation encouraged by all staff and management
6. Plan and determine how change needs to occur
7. Implement change
8. Reward and staff appraisal systems modified
9. Review and feedback obtained
The value for money (VFM) framework (the 3Es)

- Economy (Cheap)
- Efficiency (Quick)
- Effectiveness (Good)

The 6-dimensional performance matrix

Developed by Fitzgerald (1991)

Results

- Competitiveness
- Financial performance

Determinants

- Quality of service
- Flexibility
- Resource utilisation
- Innovation

The performance pyramid

Financial (ratio) analysis
The objective of financial statements is to provide information to all users of accounts to help them for decision-making. Note that most users will only have access to published financial statements.

The use of ratios
- To compare results over a period of time
- To measure performance against other organisations
- To compare results with a target
- To compare against industry averages

Limitations of ratio analysis
A ratio on its own is meaningless, accounting ratios must always be interpreted in relation to other information. Ratios based on historic cost accounts do not give a true picture of trends, because of the effects of inflation and different accounting policies. Investors’ ratios particularly have a disadvantage, because investment means looking into the future and the past may not always be indicative of the future. Comparing the financial statements of similar businesses can also be misleading.

Ratios can be grouped into 3 main areas

<table>
<thead>
<tr>
<th>1</th>
<th>Performance (profitability) – how well has the business done</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Return on capital employed (ROCE)</strong></td>
<td>( \text{Profit before interest &amp; tax (PBIT)} \times \frac{\text{Capital employed (CE)}}{100} )</td>
</tr>
<tr>
<td><strong>Operating profit margin</strong></td>
<td>( \frac{\text{PBIT}}{\text{Turnover}} \times 100% )</td>
</tr>
<tr>
<td><strong>Asset turnover</strong></td>
<td>( \frac{\text{Turnover}}{\text{Total assets}} \times \text{(number of times)} )</td>
</tr>
<tr>
<td><strong>Return on equity (ROE)</strong></td>
<td>( \frac{\text{Profit after tax, interest &amp; pref share divs}}{\text{Shareholder funds (equity)}} \times 100% )</td>
</tr>
</tbody>
</table>
## Position (liquidity) – short term standing of the business

<table>
<thead>
<tr>
<th>Metric</th>
<th>Formula</th>
</tr>
</thead>
<tbody>
<tr>
<td>Current ratio</td>
<td>( \frac{\text{Current assets}}{\text{Current liabilities}} ) (number of times)</td>
</tr>
<tr>
<td>Quick ratio</td>
<td>( \frac{\text{Current assets} - \text{inventory}}{\text{Current liabilities}} ) (number of times)</td>
</tr>
<tr>
<td>Gearing - equity</td>
<td>( \frac{\text{Debt capital}}{\text{Equity (shareholders funds)}} ) x 100%</td>
</tr>
<tr>
<td>Gearing – total</td>
<td>( \frac{\text{Debt capital}}{\text{Debt + equity (total capital)}} ) x 100%</td>
</tr>
<tr>
<td>Interest cover</td>
<td>( \frac{\text{Profit before interest &amp; tax (PBIT)}}{\text{Interest paid}} ) (no of times)</td>
</tr>
<tr>
<td>Trade payable days</td>
<td>( \frac{\text{Trade payables}}{\text{Cost of sales (or purchases)}} ) x 365 days</td>
</tr>
<tr>
<td>Inventory days</td>
<td>( \frac{\text{Inventory}}{\text{Cost of sales}} ) x 365 days</td>
</tr>
<tr>
<td>Trade receivable days</td>
<td>( \frac{\text{Trade receivable}}{\text{Sales}} ) x 365 days</td>
</tr>
<tr>
<td>Working capital cycle</td>
<td>( \text{Trade receivable days + inventory days} ) ( \text{+ trade payable days} ) ( = ) ( \text{working capital cycle (days)} )</td>
</tr>
</tbody>
</table>
### 3 Potential (investor) – what investors are looking at

<table>
<thead>
<tr>
<th>Metric</th>
<th>Formula</th>
</tr>
</thead>
<tbody>
<tr>
<td>Earnings per share (EPS)</td>
<td>Profit after tax</td>
</tr>
<tr>
<td></td>
<td>Number of shares</td>
</tr>
<tr>
<td>P/E ratio</td>
<td>Share price</td>
</tr>
<tr>
<td></td>
<td>Earnings per share</td>
</tr>
<tr>
<td>Dividend yield</td>
<td>Dividend per share x 100%</td>
</tr>
<tr>
<td></td>
<td>Share price</td>
</tr>
<tr>
<td>Dividend cover</td>
<td>Earnings per share</td>
</tr>
<tr>
<td></td>
<td>Dividend per share</td>
</tr>
</tbody>
</table>
Transfer Pricing

A transfer price is a price charged for goods or services provided internally between divisions or departments in the same group or company.

The common aims of transfer pricing systems

- Motivate managers
- Fair performance evaluation
- Promote autonomy
- Goal congruence
- To ensure optimal allocation of resources

<table>
<thead>
<tr>
<th>Change transfer price</th>
<th>Selling Division</th>
<th>Buying Division</th>
<th>The Group</th>
</tr>
</thead>
<tbody>
<tr>
<td>Increase transfer price</td>
<td>Profit increases</td>
<td>Profit Decreases</td>
<td>No change</td>
</tr>
<tr>
<td>Decrease transfer price</td>
<td>Profit decreases</td>
<td>Profit Increases</td>
<td>No change</td>
</tr>
</tbody>
</table>

International aspects to transfer pricing

- Exchange rates
- Import tariffs or quotas
- Taxation
- Worldwide prices and quality
- Other international legislation
Methods of transfer pricing

Cost based approaches
The pricing of products or services are based on their full or variable (marginal) production cost per unit.

Two-part tariff (two part charging) system
With a two-part tariff system the buyer is charged:
- A transfer price equal to the seller's variable (marginal) cost
- A fixed charge per period by the seller irrespective of the amount of units sold

Market based approaches
When the external market price is used as a transfer price, a seller will always be encouraged to sell because they would be indifferent between their charging policy for internal or external customers.

Dual pricing (or two prices)
Dual transfer pricing means setting one transfer price for the internal seller and another transfer price for the internal buyer.
- Internal seller  The transfer price received set at the external market price.
- Internal buyer  The transfer price paid set at the sellers variable (marginal) cost.
Opportunity cost pricing

Opportunity cost pricing is considered the most mathematically correct way of viewing transfer pricing. The reason is that it looks at transfer pricing issues from a group not divisional perspective and therefore promotes goal congruence.

Minimum price for a seller

<table>
<thead>
<tr>
<th>Full capacity</th>
<th>Spare capacity</th>
</tr>
</thead>
<tbody>
<tr>
<td>Market Price</td>
<td>Marginal Cost</td>
</tr>
</tbody>
</table>

Maximum price for a buyer

Maximum Price

The lower of?

The external market price for the internal product or service.

The net realisable value of the buyers final product.

So long as a maximum and minimum price range can be established it indicates that internal trade should take place, any transfer price set between the range will motivate both the internal seller and buyer to do so.
Key summary of chapter

### Investment appraisal techniques
- Payback
- Accounting rate of return (ARR)
- Net present value (NPV)
- Internal rate of return (IRR)

### Sensitivity analysis
Sensitivity measures the percentage change in a key input e.g. cash inflow or outflow needed, to make a project break even, in other words to have a project with a zero NPV.

\[
\text{Sensitivity} = \frac{\text{NPV of project}}{\text{PV of cash inflow or outflow}}
\]

### Expected values
Expected values calculate an 'average' return or an average financial calculation of some kind by the assignment of probabilities to the different returns possible. By doing so it recognises risk, something that may or may not occur.

### Limitations of expected values
- Expected values are no use for one off decisions
- Expected values calculate an average return not an outcome
- Expected values rely heavily on probability estimates

### Comparing projects of different time periods
#### The profitability index
A relative measure for a project of the NPV per £ invested.

\[
\text{Profitability index} = \frac{\text{Present value of cash inflows}}{\text{Present value of cash outflows}} = \text{decimal}
\]

#### Equivalent annual value (EAV)
The EAV is a yearly equivalent undiscounted cash-flow (assumed as an annual constant) calculated using an annuity factor for the life of the project.

\[
\text{EAV (using the annuity approach)} = \frac{\text{NPV of project}}{\text{Annuity for the life of the project}}
\]
Real Options as a tool for strategic analysis

Note: Complex numerical questions will not be set.

The technique of real options can be used when projects face a high degree of uncertainty. Real options analysis (ROA) applies put and call option valuation techniques to capital budgeting decisions, it is an extension of theory derived from the Black-Scholes model for valuing options, which won the 1997 Nobel prize for economics.

When applied to investment appraisal, ROA calculates mathematically ‘real options’ for such decisions as to contract, abandon, continue, expand or extend the project, it could also include the decision to switch and divert resources away to other alternative projects e.g. opportunity cost. ROA is useful for NPV projects because it forces decision makers to be explicit about the assumptions underlying their projections, it is also increasingly being applied as a tool for business strategy formulation.

Process by McKinsey & Company

1. Calculate NPV of the project without flexibility.
2. Use scenario planning to identify different ‘parallel’ universes that may occur.
3. Identify different ‘options’ that could be exercised over the life of the project.
4. Apply approaches similar to the Black-Scholes model for valuing each option.

Capital rationing

- **Soft capital rationing** ï internal or political reasons why funds capped.
- **Hard capital rationing** ï external or real reasons why funds are capped.
- **Divisible projects** ï can invest in ‘parts’ of projects.
- **Non-divisible projects** ï can only invest in all or none of the projects.

The process of investment decision making

The basic stages are:

- Spend forecast
- Projects identified
- Financially evaluate projects
- Consider qualitative factors
- Best options are chosen and approved
- Monitor and control project
- Deal with risk
- Post completion audit