

## 2 Literature review

“What are strategies and how are they formed in organizations?” Mintzberg (1978) asks in one of his articles. This chapter will respond to this question and give insight into topics related to strategy, strategy formation, strategic planning and strategic organization. It will provide the reader with the fundamental knowledge essential to understand the scientific course of this thesis. Past and current research findings and studies were selected carefully and are going to be reviewed and intertwined to a comprehensive summary of the most relevant issues.

The literature review is divided into three parts, which are again split up into subchapters, discussing and defining the most important aspects in the fields of interest of this study. The first part is concerned with strategy formation (see 2.1 Strategy formation). After a short introduction to strategy in general and strategic management, the *10 Schools of Strategy Theory* will be presented as well as Mintzberg's *5 Ps for Strategy Model*, as one example of the formation of strategies. The second part deals with strategic planning and related issues (see 2.2 Strategic planning). After a definition and general information, the strategic planning process is going to be explained as a base for the subchapters. Formal and informal strategic planning is put into focus and consequently strategic planning in different environments will be reviewed. Information about planning, plans and planners completes this second part of the literature review. The third part focuses on a company's strategic organization and structure (see 2.3 Strategic organization and organizational structure). After an introduction to organizational learning and how to think strategically, the concept of organizational ambidexterity is going to be explained. Insights on coordination mechanisms conclude this literature review. After reading this chapter, the reader will be able to understand the key issues of this piece of work and thus follow the further scientific investigation.

### 2.1 Strategy formation

At the beginning it is probably a good idea to talk first about strategy. Strategy is a widely used term. For the purpose of this piece of work, we will concentrate only on strategy in the field of business. It is necessary, however, to mention

that all kinds of strategy derived from military strategy. The concept of strategy dates back a long time ago, when the Chinese military general Sun Tzu is believed to have written his book "The Art of War", describing military strategies and tactics (Tzu, 1963; Mintzberg, 1994b; Cherp *et al.*, 2007). Consequently the word "strategy" has been in use for a long time and has also been used in different ways. One of the most influential people in the field of strategy and strategic planning, Henry Mintzberg, criticizes, that most definitions of what strategy really is, are too easy and lack comprehension (Mintzberg *et al.*, 1998). He argues that strategy requires a number of definitions, that is to say five definitions, the so-called *5 Ps for Strategy* (see 2.1.2 The strategy formation process) (Mintzberg, 1987a; Mintzberg *et al.*, 1998).

Nevertheless, Mintzberg (2003) tried to come up with one comprehensive definition of what strategy is, namely "a pattern of decisions in a company that determines and reveals its objectives, purposes, or goals, produces the principal policies and plans for achieving those goals, and defines the range of business the company is to pursue, the kind of economic and human organization it is or intends to be, and the nature of the economic and noneconomic contribution it intends to make to its shareholders, employees, customers, and communities..."

Due to an increasing environmental volatility and uncertainty (see 2.2.3 Strategic planning in a turbulent environment), the following impacts on organizations' strategic planning systems and strategy formation suggested by several studies: (1) Redistribution of strategic planning decision making authority, (2) Shorter planning horizons, (3) Less formality of planning processes, (4) A shift from detailed planning to strategic direction, and (5) Increased emphasis on performance planning (Grant, 2003).

(1) *Redistribution of strategic planning decision making authority*: Studies have shown that a turbulent environment encourages decentralization of strategic decision making authority from corporate to business level and reduces the role of staff planners compared to that of line managers (Lindsay & Rue, 1980; Grinyer *et al.*, 1986; Wilson, 1994). (2) *Shorter planning horizons*: As strategic planning is based on predictions, uncertainty about the future should shorten the planning horizon. While certain studies found no relationship between plan-

ning time spans and environmental stability (Lindsay & Rue, 1980; Javidan, 1984), Kukalis (1991) examined that in unpredictable markets with high levels of innovation and competition the planning horizons were comparably shorter. (3) *Less formality of planning processes*: Based on organizational theory, less stable environments demand less bureaucratization and more flexible decision making (Courtright *et al.*, 1989). Formality concerning the strategic planning process manifests itself in fixed timescales for the planning cycle, use of standardized methodologies, extensive documentation and written reports, and deployment of planning specialists. Kukalis (1991) observed that increasing change in the external environment causes an increase in the flexibility of planning practices; and Wilson (1994) showed that external instability led to greater informality. Contrary Lindsay & Rue (1980) pointed out that organizations tried to counteract uncertainty and unpredictability with greater planning efforts. (4) *A shift from detailed planning to strategic direction*: An increase in environmental turbulence did not only result in less formality and rigidity of the planning process, but also in less exactness and greater flexibility in the content of strategic plans. Instead of detailed plans of action, commitment to certain projects and resource deployment, the focus changed to more broadly defined goals. Organizations emphasize vision and mission statement to communicate and guide their strategies, and thereby create commitment to their long-term strategic intent and strategic goals (Grant, 2003). (5) *Increased emphasis on performance planning*: The organizations shifted their focus away from specific strategic decisions and forecasts towards performance targets. These targets might include financial targets, operating targets, safety and environmental targets, strategic milestones, and capital expenditure limits. Short-term profit targets were combined with strategic and operational targets in consistency with building longer-term competitive advantage measured by operational targets or strategic milestones (Grant, 2003; Brown & Eisenhardt, 1997).

Inside the company one can distinguish between two kinds of management: strategic management and operational management. Strategic management is what is done at the top of the organization's structure; everything else can be labeled as operational management. Nevertheless, both are linked strongly with each other. Strategic management sets the framework and guidance for the operational management. Strategic management and strategic planning there-

fore focus more on strategy than on operations (Steiner, 1997; Goodstein *et al.*, 1993). We can also find two types of important decisions within an organization, that is to say strategic decisions and strategically driven decisions. Making strategic decisions is a function of top and executive management, even one of the most important ones. They have to ensure that strategically driven decisions are implemented and applied properly. This process of the execution of a strategic plan is what we call strategic management; the day-to-day implementation of the strategic plan. Top management must be clear about, united and committed to their strategy. This commitment is one of the crucial factors in the implementation of strategy (Goodstein *et al.*, 1993).

The managerial emphasis in most organizations was once on operations and operational management. The main question used to be how to use scarce resources to produce goods and services, meeting the price range of consumers, which was supposed to consequently lead to profit maximization. This has changed over time. The efficient use of scarce resources is still an important issue for organizations, but due to turbulent and fast changing environments, it is vital for organizations to adapt properly to the internal and external environment (Steiner, 1997). With an appropriate strategy, a company can overcome inefficient use of resources. With the imperfect strategy, however, even a very good production and distribution performance is usually not sufficient. Ideally a company can design excellent strategies and implement them effectively and efficiently. Leadership and strategy are dealing with effectiveness, while management's responsibility is efficiency (Steiner, 1997; Ackoff, 1993). Leaders traditionally focus on effectiveness, on doing the right things, while managers concentrate on doing things right. Both topics are important and organizations can improve if focusing on the "right" issues (Ackoff, 1993).

### **2.1.1 Strategy formation theory**

In many organizations the framework for the formation and the implementation of strategies is a formal strategic planning system. Strategy does not necessarily have to be formulated through a formal system; formulation and implementation can be done to some extent or totally informal as well (Steiner, 1997). In a complex organization it is tremendously challenging, if not impossible, to plan and coordinate the process of strategy formation throughout the whole or-

ganization. It is almost impossible to put together all the information, such as internal decisions, the external environment, power relationships, technical and informational needs, information about competitors, and organizational behavior, at a precise moment (Quinn, 1978; Mintzberg, 1990).

Unlike suggested by Mintzberg (1990), explaining that managers are either totally sure or unsure about the future, however, these two extremes are rarely observable in the real business world (Schwartz, 1996; Ansoff, 1991). Especially in environments in which it is hard and challenging to predict the future, explicit strategy formulation is used to compensate for the unpredictability (Steiner & Schöllhammer, 1975). Assumptions, that the future will be just an extrapolation of the past, are too dangerous and can be overcome by precisely formulating a strategy (Ansoff, 1991).

There are altogether ten schools of strategy theories that seek to explain the 5 Ps and their correlations, which are classified and summarized in Table 1. Each of these schools has its own perspective on strategy and the strategy process and can be scaled into three groups: the first three schools are of a *prescriptive* nature, the following six schools are concerned with *describing* how strategies are made, and the remaining group being a hybrid is called *configuration* (Cherp *et al.*, 2007; Mintzberg, 1987a; Mintzberg *et al.*, 2003). It is important to add that various relationships do exist among the different definitions, and neither one relationship nor any single definition obtains priority over the others. Some of the definitions might be substitutes for each other or even a complement for each other. Not all plans are patterns, not all patterns are planned. Some strategies are more than positions and less than perspectives, and vice versa (Mintzberg, 1987a).

Summing up, there exist ten schools of thought, which represent ten different approaches to strategy formation. The relationships between them are varied. Some of the schools have their preferences, for example plan in the planning school, position in the positioning school, or pattern in the learning school. Although there may not be one simple and true definition of what strategy is, there are some general areas of agreement about the nature of strategy (Mintzberg *et al.*, 1998).

The 10 Schools of Strategy Theories	
Design school	Strategy formation as a process of conception. Strategy is a unique planned <i>perspective</i> conceived by senior leadership based on an ad hoc analysis of external and internal factors.
Planning school	Strategy formation as a formal process. Strategies are <i>plans</i> decomposed into programs resulting from formal planning procedures.
Positioning school	Strategy formation as an analytical process. Strategies are planned generic <i>positions</i> but also <i>plays</i> to defeat competitors. Positions are based on detailed analysis of markets and industry structures. Highly integrated corporate activity systems support focus on selected positions.
Entrepreneurial school	Strategy formation as a visionary process. Strategies are personal <i>perspectives</i> of visionary leaders conceived largely intuitively and adjusted when necessary.
Cognitive school	Strategy formation as a mental process. Strategies are mental <i>perspectives</i> reflecting 'constructed reality' in leaders' minds.
Learning school	Strategy formation as an emergent process. Strategies are unique <i>patterns</i> , constantly evolving as a result of learning by leaders and others in an organization.
Power school	Strategy formation as a process of negotiation. Strategies are political <i>patterns</i> and <i>positions</i> as well as <i>plays</i> . The micro-power school emphasizes internal politics as the basis for a strategy. The macro-power school considers strategy as a negotiated position and a play to defeat competitors.
Cultural school	Strategy formation as a collective process. Strategies are collective <i>perspectives</i> reflecting dominant ideologies, collective cognitive maps and narratives.
Environmental school	Strategy formation as a reactive process. Strategies are specific <i>positions</i> (ecological niches) developed as a result of evolutionary adaptations of organizations to ever changing and uncontrollable external circumstances.
Configuration school	Strategy formation as a process of transformation. Strategies can be formed by different processes depending upon the internal and external context (or stage in an organization's evolution).

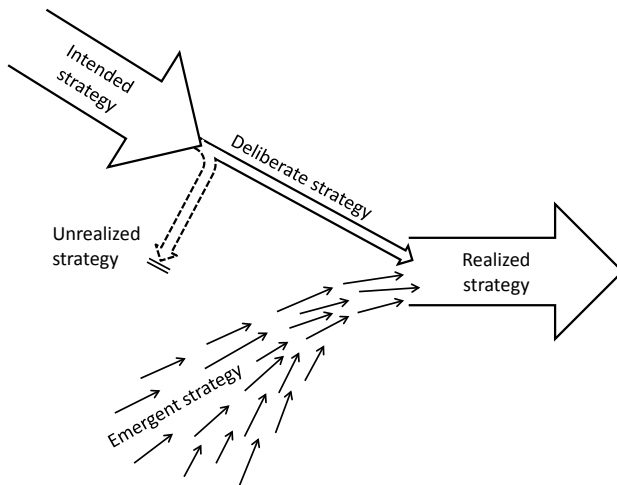
**Table 1: 10 Schools of Strategy Theories**

Source: Cherp *et al.*, 2007; Mintzberg *et al.*, 1998; Mintzberg *et al.*, 2003

### 2.1.2 The strategy formation process

Strategy formation can be made implicitly or explicitly. As already discussed, many different theories and schools of strategy theories exist. While many thinkers in this field suggest an explicit strategy formation as the most promising approach, Mintzberg and his design school model of strategy formation suggest an implicit strategy formation approach. He states that no formal strategic planning is used within an organization and that strategy should not be made explicitly, except under special circumstances. Mintzberg especially stresses the "emergent strategy", based on a trial and experience process, which he describes in his *5 Ps for Strategy Model* (Mintzberg, 1990; 1987a; Ansoff, 1991).

Asking someone for a definition about strategy, it is most likely that the answer will be that strategy *is a plan* or something similar; a plan to get from the current state to a projected state in the future, a defined goal and a guide to get there. This implies two essential characteristics about strategies: they are made in advance based on predictions and assumptions, and they are developed consciously and purposefully (Mintzberg *et al.*, 1998; Mintzberg, 1994b). Comparing this intended strategy with the strategy actually pursued over the past few years, there will be a difference between the intended strategy and the realized strategy. Strategy, therefore, *is a pattern*, looking at the behavior and performance in the past. It results from actions, not designs (Cherp, Watt, & Vinichenko, 2007). Companies develop strategies for the future and also evolve patterns out of their past (Mintzberg, 1987a).



**Figure 2: 5 Ps of Strategy**

Source: Author's illustration upon direct adoption from Mintzberg, 1987a

At the beginning we have the *intended* strategy, as shown in Figure 2. Parts of these intentions that are not realized are the so-called *unrealized* strategies. The *realized* strategy consists of the *deliberate* strategy, which contains the realized intentions, and of the *emergent* strategy, where patterns realized were not expressly intended.

Deliberate strategies are not necessarily positive and emergent strategies are not necessarily negative for an organization. Effective strategies have a combination of both, emergent and deliberate strategy, since all kinds of strategies combine some degree of flexible learning and some degree of control (Rea & Kerzner, 1997; Mintzberg, 1994a).

Completing the 5 Ps, strategy *can be a ploy*, a specific plan to outmaneuver an opponent or competitor; it *is a position*, meaning the positioning of an organization in the so-called environment or particular products in particular markets (strategy looks outside the company); and it *is a perspective*, taking into consideration its perception of the world, what is inside the heads of its strategist and the vision of the company (strategy looks inside the company) (Mintzberg, 1987a; Mintzberg *et al.*, 1998).

Mintzberg stresses especially what he calls the “emergent strategy” formation process, based on “trial and experience”. According to him, formulating an explicit strategy is more or less impossible in unpredictable environments, before the process of trial and experience has run its course. This process can be seen as a logical pattern of a historical sequence of successful trials (Mintzberg, 1990). This use of trial and error, however, might be tremendously expensive (Ansoff, 1991). For Mintzberg (1990) a company “has to make a number of mistakes until it gradually learns what works for it, if it ever does”, meaning that patterns of successive failures are automatically transformed into a successful instruction. This is contradicted by Ansoff (1991), who suggests that “repeated mistakes are [is] not a valid basis for recommending that others should follow the same path”.

## 2.2 Strategic planning

*“If you are failing to plan, you are planning to fail.”*  
(Tariq Siddique)

Drucker (1954) explained the strategic planning process as “the task of thinking through the mission of the business, that is, of asking the question ‘what is our business and what should it be?’ This leads to the setting of objectives, the development of strategies and plans, and the making of today’s decisions for tomorrow’s results. This clearly can be done only by an organ of the business that



can see the entire business; that can make decisions to affect the entire business; that can balance objectives and the needs of today against the needs of tomorrow; and that can allocate resources of men and money to key results.” Hopkins & Hopkins (1997) relate their definition of strategic planning to the strategy itself: “Strategic planning can be described as the process of using systematic criteria and rigorous investigation to formulate, implement, and control strategy, and formally document organizational expectations.”

Goodstein *et al.* (1993) define strategic planning as “the process by which the guiding members of an organization envision its future and develop the necessary procedures and operations to achieve that future.” This future state, the vision of the organization, provides both a direction in which the organization is supposed to move and the motivation to begin this move. It is important to add that this process must not be confused with long-range planning since this is usually simply an extrapolation of the current state and business trends. Especially when mixing strategic planning with strategic thinking, organizations and their leaders might confuse vision with quantitative analysis. Successful strategies, however, are visions and not plans (Goodstein *et al.*, 1993; Mintzberg, 1994b). Most planning processes are long-range plans rather than strategic plans. These long-range plans are made in the assumption that the future can be extrapolated from the past and the present. As this might work in certain cases, in general there will be significant, unforeseeable changes in the future that make an extrapolation pointless. A genuine strategic plan, therefore, should include a consideration of a variety of futures and develop different options to meet these different scenarios (Goodstein *et al.*, 2008).

The strategic planning process does not just plan for the future; it also “helps an organization to create its future” (Goodstein *et al.*, 1993). Envisioning the future is more than just anticipating it and preparing accordingly. It also means believing that some aspects of the future might be influenced and even changed by what an organization is doing now. Strategic planning is still more than just envisioning the future. It sets clear goals and objectives and how to reach them within a specified period of time. The targets must be realistic, objective and attainable, and have to be developed with the background of the designed and desired future state in mind. By doing so, they provide guidelines for all day-to-

day managerial decisions and should provide an organization with its core priorities (Goodstein *et al.*, 1993).

Strategic planning needs to answer three basic questions for an organization: Where are we going? What is the environment? How do we get there? Without any direction, the organization is drifting away from reaching its goals. Without knowing itself and its environment, it is exposed to threats and might miss opportunities. Without being aware of how to reach its goals and how to allocate the resources, the organization cannot enable the specific measures to reach the specific objectives. Therefore strategic plans should have an impact on day-to-day decisions and on the actual running of an organization (Gup, 1979; Goodstein *et al.*, 1993).

Top Management is mainly responsible for the strategy; strategic planning, however, is the function and responsibility of managers at all levels in an organization. Their involvement may vary significantly among different levels in this organization, their tasks and responsibilities and the type of organization itself (Steiner, 1997). The CEO is not, as often assumed, the only strategist within an organization. The CEO is, however, the initiator and maintainer of the development and operation of a strategic planning system. He or she (or a group of executives) is the person with the most influence within the organization and with the authority to make decisions and manage the business. CEOs have to understand that strategic planning is their responsibility and that they have to establish a climate in favor of strategic planning. They have to make sure that the design of the planning system is suitable to match the unique characteristics of the organization. (Andrews, 1987; Steiner, 1997).

McIlquham-Schmidt (2011) conducted a meta-analysis examining 88 individual studies concerning the relationship between strategic planning and corporate performance. His findings suggest that strategic planning does have a positive effect on the performance of an organization and confirm already existing management literature and other meta-analyses (Boyd, 1991; Miller & Cardinal, 1994; Capon *et al.*, 1994; Schwenk & Shrader, 1993): Strategic planning results in a better match between internal organizational conditions and external environment variables. Through this match the organization's vision and goals are

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