

SMALL FIRM STRATEGY IN TURBULENT TIMES

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ABSTRACT

The purpose of this paper is to suggest an approach to modifying firm strategy and tactics to cope with the demands of the current economic downturn and resulting challenges to profitability and growth. The approach is, broadly, becoming a focused differentiator, adopting Hersey's Situational leadership Model and adopting a Lean Management philosophy.

The target audience for this paper is Small and Medium Sized Enterprises (SMEs) - frequently privately held and often with fewer than 100 employees. These firms, in most cases, do not have sufficient resources to hire traditional management consulting firms but the reality is that what is described herein can be learned and applied at a very low cost.

This paper benefits from the work we have done with Jay Arthur (LifeStar) and Warren Miller (Beckmill Research). In the aggregate we have well over 75 years of experience working with and advising SMEs. We don't claim to be strategy experts but we have over the years seen the mistakes made by SMEs and we'd like to help you avoid some of those mistakes.

INTRODUCTION

Triggered by the burst of the housing bubble in late 2007, the United States entered the worst recession since the 1930s. Unemployment is currently at a twenty seven year high. Erosion of revenue and profits has plagued many firms and the very structure of a variety of industries has been impacted. The old strategy approach of positioning a firm within its industry is no longer completely adequate because of profound structural changes in many industries. What is needed for survival and some measure of success in a small firm is the appropriate positioning of the firm and an emphasis on operations excellence (Porter, 1996) under the guidance of Situational Leadership® (Hersey, 1997).

One definition of strategy is "A plan of action resulting from strategy or intended to accomplish a specific goal" (American Heritage, 1993). This general definition alludes to an important point and that is that the purpose of strategy is to accomplish an important goal or goals. The word "strategy" has as its root the Greek word "strategos" and that word is loosely translated in English (from Greek) as "the art of the generals". One of the first books describing the formulation and implementation of strategy was Sun Tzu's classic "The Art of Strategy" published some time during the Warring States Period (480-221 BC) (Wing, 1998). The Art of Strategy is really a series of tactical recommendations for conducting war. Although somewhat dated, it is interesting to note that this book is used as a strategy text at hundreds of schools around the world including the US Army's Command and General Staff College at Fort Leavenworth, Kansas.

It is difficult to estimate how many books, articles and monographs have been published about strategy over the last 2500 years, but it is safe to say that the number is well into the thousands. In "Strategy Safari", written by Mintzberg, Allstrand and Lampel in 1998, the authors comment that they

reviewed more than 2000 published studies on strategic management. Most of the published work on strategic management addresses the strategy problems (opportunities?) facing larger organizations. This is appropriate from a pedagogical perspective but it is not always helpful to the very small organizations that populate the business landscape. According to the Bureau of the Census, in 2002 more than 97% of all business firms in the United States had fewer than 100 employees. It is to the leaders and employees of these very small firms that this paper is addressed. Although some would argue that very small firms (fewer than 100 employees) don't really need to concern themselves with strategy as normally understood, I disagree - vehemently. If one "buys" the fundamental assumption that there is an important relationship between strategy and firm performance, then it's obvious that small firms need effective strategic management as much as large firms.

STRATEGY AND TACTICS

Pick up any strategic management textbook and you will find that strategy, in its most general sense, is visualized as a series of decisions resulting in plans that must be implemented to achieve whatever the organization's goals are. Many authors suggest that the starting point for the process is the articulation of a vision statement. Presumably, a vision statement defines, in fairly general terms, where the business organization wants to go in the future. In other words, the vision defines (loosely, in most cases) expectations regarding future markets to be served, products or services to be developed and some idea about the target customers.

Related to the vision is the idea of a mission statement. A mission is an articulation of what the company does currently in terms of products and services, markets and customers served. Some authors (and experts) see the vision and mission statements as "two sides of the same coin" and others see the vision and mission as distinct and quite different. The distinction is fairly unimportant from the small firm perspective.

I ascribe to a slightly different viewpoint regarding prescriptions about how to "do" strategy in a small organization. Jack Welch, in his recent book "Winning", talks about starting strategic management with a very careful decision about what he calls the "Big Aha" - a smart, realistic, relatively fast way to gain a competitive advantage (Welch, 2005). There are two fundamentally important considerations in this straightforward recommendation - the time dimension and something called competitive advantage. The time dimension is important and becoming more so all the time. Consider that Tom Peters in his groundbreaking book - "Thriving on Chaos" - back in 1988 talked about the critical importance of hustle. Successful firms tend to "out hustle" less successful firms in their industries by considerable margins. And this doesn't mean just compressing the delivery cycle. It means substantively shortening the time required to perform most operations - order placement, conflict resolution, billing, customer responses and new product development.

A competitive advantage means, essentially, what the label suggests - valuable and rare core competencies (Thompson, Strickland & Gamble, 2010). Core competencies that lead to significant competitive advantage are valuable, rare, difficult to imitate and essentially non substitutable. They are the things that we do that other firms with whom we compete are unable to do. Competitive advantages differ appreciably by industry but we illustrate the concept with the following examples - Honda and internal combustion engine design, Southwest Airlines and ticket pricing, Proctor and Gamble and

distribution of food products and the many smaller firms that thrive in highly competitive markets because they are better, faster or cheaper than their rivals.

Developing a competitive advantage, according to Porter (1980), means deciding to compete on the basis of low cost or differentiation. A low cost strategy generally means that facilities are large, production runs are long, controls are very tight, high degrees of automation are frequently employed and the major "focus" of the firm is to achieve the lowest costs in the industry in which it participates. An example of a low cost leadership strategy in retailing is obviously Wal*Mart. Toyota is an example of a manufacturing firm that achieves a low cost strategy by employing the Toyota Production System (Womack, Jones & Roos, 1990; Womack & Jones, 1996).

Differentiation is, in some ways, almost the opposite of low cost leadership. Differentiators carefully study their customers and potential customers to identify what special features, options and alternatives people are willing to pay competitive prices for. They then focus on providing these unique bundles of products and services which are generally sold in smaller volumes at higher margins. It is our position that the appropriate generic strategy for small firms is, almost always, focused differentiation. Small firms generally don't have sufficient resources - money, people or facilities - to compete on the basis of a low cost leadership strategy. As Tom Peters has said, "Don't try to compete with Wal*Mart on price or China on cost. (Peters, 2007).

One way to think about differentiation is to attempt to become a Purple Cow (Godin, 2003). Godin notes that the old "TV-Industrial complex" is no longer adequate in many industries. Firms - particularly SMEs -- need to transform their businesses by becoming remarkable. Think, if you will, of firms like early Starbucks, Jet Blue, Southwest Airlines, Outback Steakhouse and the new Volkswagen Beetle. These products and firms addressed a niche market and understood the customer's value propositions. They were very successful focused differentiators.

TACTICS

Once a conscious decision has been made to be a Focused Differentiator, the question then becomes, "How do we implement?" In this paper, we argue that Operations and the care and feeding of human resources are the critical functions that must be addressed. Operations, of course, are the conversion of inputs to outputs. Many real world examples of operations excellence are well-known - Toyota, Nucor Steel, Southwest Airlines and Springfield Remanufacturing Corporation (SRC).

Toyota (despite its recent difficulties with recalls) has fine tuned its production processes with the Toyota Production System - named Lean Manufacturing by Womack and Jones. Nucor Steel revolutionized basic steel making with continuous casting and became one of the most profitable (and largest) American producers. Southwest Airlines - the only profitable American airline - combines point-to-point route maps, open seating, no meals and one type of aircraft (Boeing 737s). SRC quickly rose to profitability after a leveraged buyout with an 89:1 Debt Equity Ratio by creating the Great Game of Business - Open Book Management. Over the last fifty years hundreds of tactics have been created to enhance productivity and efficiency. Such tactics as Lean Six Sigma, MBWA, TQM, Scenario Planning and a host of other "Best Practices" populate the landscape. What's missing is an organizing framework to implement the Focused Differentiation strategy. To implement, we suggest Situational Leadership® and a Lean Philosophy

SITUATIONAL LEADERSHIP®

It is axiomatic that the "right" leadership is likely associated with above average performance but one of the "knotty" problems lies in attempting to answer the fundamental question, "What kind of leadership?" A recent Google search yielded 138,000,000 "hits" for the term Leadership. Amazon.com currently lists over 59,000 leadership books. Clearly there are a host of competing theories of leadership. Paul Hersey's Situational Leadership (SL) Model ® provides a common-sense answer to that question and has been used by hundreds of the Fortune 500 firms (Hersey 1997). Hersey's Center for Leadership Studies in Escondido, California has taught SL to thousands of managers in three day sessions over the last twenty years.

One of the appeals of the SL Model is that it makes a great deal of intuitive sense. The model proposes that leader behavior should vary along two dimensions - directive behavior (task oriented) and supportive behavior (relationship oriented). The choice of which behavior to adopt should be a function of what Hersey calls follower readiness. Follower readiness ranges from "low" - unable and unwilling or insecure - to "high" - able, willing and confident.

I had personal experience using this model a number of years ago in the steel industry in Texas. We (Riverside Industries) were a manufacturer of galvanized transmission towers in Fort Worth. A substantial majority of our hourly workforce was young Hispanic men from the Rio Grande valley. These young men had grown up working in agriculture. Ten hour days and six day work weeks were common. They were willing to work hard but they were (when they first came to work with us) insecure because they did not have the requisite technical skills to do the job. They were for the most part what Hersey calls Readiness Level 1 and the recommended approach to leadership was "Telling." Over a period of several months they were taught to use basic hand tools and some of the simpler power equipment. This training was "on the job" training and it was, for the most part, conducted by fellow workers under the guidance of first line supervision.

Gradually these workers moved from Readiness Level 1 to Readiness Level 2 where the suggested "style" of leadership is "Selling." This means a heavy emphasis on supportive behavior and less emphasis on task behavior. Eventually, some of the workers at Readiness Level 2 moved to Readiness Level 3 where the emphasis should be (according to Hersey) on sharing ideas and facilitating appropriate decision making. It was from this group of workers that we were able to promote to first line supervision and the results were higher levels of productivity and related profitability.

Tom Peters (2005) proposes that in these crazy and chaotic times many of us have a tendency to fall back on a command-and control style of leadership. He argues that this is ineffective and that we should embrace a model of leadership that is loose, open and innovative - in other words Hersey's "Selling" and "Participating" styles of leadership. These styles of leadership comport well with flatter, decentralized forms of organizations.

One of my former employers - the United States Marine Corps - has moved strongly in this direction. Today we see NCOs and lower-level commissioned officers (Lieutenants and Captains) making decisions that were previously made at much higher levels in the hierarchy. They are doing that because the Corps has adopted the doctrine of maneuver warfare (Santamaria, Martino & Clemens (2004).

One can learn how to "do" Situational Leadership® by reading Hersey's book - The Situational Leaders (Hersey, 1997) but a better approach is to attend the three-day training session at Hersey's Center

for Leadership Studies in Escondido, California. More than ten million managers from over one thousand organizations have attended and have experienced higher levels of productivity and enhanced profitability. As Warren Bennis -eminent management scholar -- says, "Everybody nowadays is searching for excellence. Hersey's intriguing and concise book demonstrates how this can be done."

LEAN PHILOSOPHY

In 1990, James P. Womack, Daniel T. Jones and Daniel Roos published *The Machine that Changed the World*. This New York Times Best Seller described the five- year, \$5 million International Motor Vehicle Program (IMVP) at Massachusetts Institute of Technology which began in 1985. This world-wide research study included ninety vehicle assembly plants around the world and over a hundred component supplier plants. The purpose of the study was to determine the characteristics of what came to be known as Lean Manufacturing (LM). The results were mind boggling. Lean firms - particularly Toyota - were able to assemble cars in half the time of their American and European competitors with half the inventory and roughly half the floor space. Quality levels at Toyota (as measured by defects after assembly) were much lower. A Lean philosophy employs five principles: Value, Value Stream, Flow, Pull and Perfection (Womack & Jones, 1996).

Value

It is critically important that a firm give serious consideration to the question of how it creates value for its customers. It is not enough that the firm examine the value proposition from the perspective of the firm. It must also carefully consider what the customers consider valuable. An admittedly simple example follows. I routinely travel from my home in Joplin, MO to Fort Lauderdale, FL. The elapsed time for the flight (through the American Airline hub at Dallas) is approximately 6 hours including a two hour layover in Dallas. The actual trip time is about 9 hours because I have to drive to the Springfield, MO airport to catch a flight to Dallas. In bad weather, the trip can actually stretch to 10-12 hours of elapsed time. With the all-too-frequent flight cancellations on American Airlines, this frustrating itinerary can become an overnight experience. Granted, American's hub and spoke route map is probably valuable for American as they attempt to maximize aircraft utilization but it is most definitely not valuable for the traveling public.

Another common example of ignoring the customer in the value proposition is automated phone answering. I am probably not the only customer who has hung up in anger when faced with an interminable list of push button options to get to speak to a "live" human being. I recall one example a few years ago that really got my attention. I was teaching a class at the Army's Command and General Staff College at Fort Leavenworth and needed to speak to someone in the Provost Marshal's office. I did not know the extension and was forced (by the automated phone answering system) to talk to personnel in five different offices. I eventually got to a "live" human being in the Provost Marshal's office but this took the better part of a half hour and all I could think of was, "I wonder what would have happened if I was calling in to report a terrorist threat!" The two preceding examples illustrate a very important issue. An organization must understand value as perceived by the customer. It is not unusual for a firm to understand what creates value from its perspective but to miss important value attributes of goods and

services from a customer perspective. It must be remembered that successful Focus Differentiation (the generic strategy we recommend for SMEs) mandates that we really understand what the customer's need, wants and desires are and, most importantly, what they will pay for.

It is common for many SMEs to have an implicit set of ideas about what their customers value. Unfortunately, this is not always accurate and comprehensive. I recommend that SMEs perform a customer survey at least annually among existing and potential customers. The technique is well-described in Warren Miller's new book - Value Maps (Miller, 2010)

The Value Stream

The Value Stream is a process map of all the steps (and delays) in designing, producing and distributing products and services to customers. The purpose of the value stream is to eliminate all possible delays and those steps in the process that do not add value - what the Japanese call muda. The value stream mapping process underlies what Hammer and Champy called Business Process Reengineering (Hammer & Champy, 2005) and Peter Drucker described this as "A new and systematic approach to structuring and managing work." I have used value stream mapping very successfully with clients like the Army Ammunition Plant (Parsons, Kansas) and Masonite Corporation (Pittsburg, Kansas). In every case we were able to eliminate significant process delays and non-value adding activities. The "bottom line" was that we were able to enhance efficiency and overall profitability. Value stream mapping can also be used effectively to enhance repetitive administrative functions in service organizations. Although there are many software products available to draw value stream maps, I recommend the low cost and common sense approach described by Jay Arthur in Six Sigma Simplified. The only tools required are a pen and a pad of Post It Notes (Arthur, 2004).

Flow

Once the Value Stream has been drawn, you will have a graphical representation of each step in the value stream and all of the intermediate delays and distances between steps. The idea then is to optimize the value chain by eliminating those steps that do not add value and minimizing the distance and time between steps. It is useful to think of this as eliminating "bottlenecks" (Goldratt, 1990). The net result of this activity is to move from vertical thinking where our focus has historically been optimizing individual functions to horizontal thinking where our focus is on optimizing cross functional activities.

Admittedly, refining the value chain can be challenging. People will not always agree, initially, on what all the activities are or on what the sequence of activities is. One way to illustrate that point is to ask two or three friends to draw the value stream for the activities involved in going to work in the morning. Presumably there would be great similarity in the steps in the value chain and roughly the same amount of time. Reality is there are substantial differences. Those of us who did some of our early growing up at places like Parris Island can roll out of bed when the alarm goes off and be in the car headed to work in as little as ten or fifteen minutes. That is not characteristic of all people. It is not unusual to find many folks who need a half an hour to an hour to get going in the morning. One very useful website which provides many tools for enhancing the value chain is Quarterman Lee's strategosinc.com.

Pull

Pull refers to an inventory management philosophy invented by Toyota and commonly called "Just in Time. (JIT)" As opposed to traditional in process inventory management, JIT requires downstream activities to "pull" products from upstream activities only as needed. The net results of implementing a pull philosophy are smaller batches (less inventory), significant reductions in floor space and better quality.

Reductions in floor space are achievable because of smaller in process batches and better quality results because the system cannot tolerate in process defects.

Perfection

Perfection is the fifth principal of a Lean Philosophy. It essentially means optimizing every element in the value chain by applying Six Sigma methods. Six Sigma was created by Bill Smith - an engineer at Motorola - in 1985. Six Sigma "migrated" to Allied Signal and then to General Electric (GE). Jack Welch (former Chairman of GE) reported in the 1999 Annual Report that Six Sigma added an incremental \$2 Billion in profits to GE's bottom line (Box, 2005). Not surprisingly, the applications of Six Sigma proliferated widely during the 90s.

Getting started with Six Sigma can be an expensive proposition. Innumerable classes are offered that can cost as much as \$25,000 per student. A better approach, I believe, is to purchase Jay Arthur's Q1 Macros. At \$139 this Excel-based software provides all of the Six Sigma tools that you would ever need. Anyone familiar with Excel can use the software and many tutorials and examples are provided.

The focus with Six Sigma is to specifically identify a product, an operation or a process which exhibits an unacceptable level of defects and then to dramatically reduce the level of defects by employing a four-step process - Focus, Improve, Sustain and Honor (Arthur, 2003). This approach is attractive because it requires a small number of techniques as opposed to Total Quality Management or traditional approaches to Six Sigma.

Although originally developed to improve quality in manufactured products, Six Sigma has been recently employed in the healthcare field. It can also be used in repetitive administrative task so it's quite useable for most service industry firms.

CONCLUSION

There is little doubt that the US is in a recession. Unemployment is at a twenty seven year high. Home foreclosures are at record highs as are personal bankruptcies. The Dow Jones Industrial Average is approximately 30% below where it was in December, 2007. SMEs have suffered the economic downturn for nearly three years now and unfortunately some are predicting a "double dip" recession. Clearly these are turbulent times. What is needed for many firms is new strategy and supportive tactics. The following are recommended:

Step One: become a Focused Differentiator. This means identifying a market niche and discovering what differentiating features and options for goods or service are particularly appealing to customers.

Step Two: Adopt Hersey's Situational Leadership® Model. Adapt your leadership style to the readiness of your followers. This means moving from a command and control style to a participative style as followers develop over time.

Step Three: Adopt a Lean Philosophy. Understand your customer's value propositions and then optimize your value chain.

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Such traditional strategy formulation often pays lip service to the perspectives of the capital markets, to changing industry structures, and to the forces at work in the environment. But in reality, a "visionary" corporate strategy is often an internally driven reflection of what the company wants the world to look like. But suppose we no longer believe that the future is foreseeable. What if defining and achieving an enduring competitive advantage is really just a conceit that must be abandoned? Second, it paces the company's evolution by alternately shifting the balance of organizational initiatives between static efficiency-based "local search" strategies, chosen in times of stability or economic slowdown, and dynamic efficiency-based "long jump" strategies, adopted during periods of major environmental turbulence. The Lujan story clearly illustrates the important role of corporate strategy in a firm that must undergo radical transitions as a result of major environmental changes. Turbulent environments are those characterized by high levels of dynamism, complexity and uncertainty (Crossan, Nanjad and Vera, 2001). The idea of dynamics at the "edge of chaos" (Brown and Eisenhardt, 1998; Marion, 1999) gained particular currency. Small firm strategy in turbulent times. In Proceedings of the Academy of Strategic Management (S. 2-9).Google Scholar. Box, T., & Miller, W. D. (2011). Small firm competitive strategy. In Proceedings of the Academy of Strategic Management (S. 13-17).Google Scholar. Bruch, H., & Ghoshal, S. (2003). SWOT analysis: It's time for a product recall. Long Range Planning, 30(1), 46-52.CrossRefGoogle Scholar. Homburg, C. (2012).