Strategic Management – The Competitive Edge

Professor R Srinivasan
Department of Management Studies
Indian Institute of Science Bengaluru

Lecture 20

Case Analysis-Contd.

So welcome to this session, we were looking in the last class on how a case study should be developed, what should it have? So some aspects I am giving you. A case study, one of the important aspects when this case study method was introduced was to look at real life case studies, that is what has happened in organizations and what is the type of decision making that has been done by the managerial team or the concerned manager, how did he arrive at the decision? He might have his own reasons to arrive at that type of a decision, but he would have given sufficient justification for arriving at that decision, it is possible in spite of all that, the decision went awry.

As long as the objective is clear, and it is not detrimental to the organization, that is the objective of taking the decision is clear and it is beneficial to the organization the manager should not be held accountable even if the decision goes awry.

So suppose you take 10 decisions in as many times it is possible that 5 or 6 might go wrong, only 5 or 4 might be on the track; fine fair enough, go ahead, as long as the objective of the manager was to help the organization then there is no need to pick holes in the decision making of the manager. So what most of the software companies are doing now, as I told you in the previous class also, they are trying to learn from all these exercises, they are trying to see what has been the learning inputs from this decision making.

So all this is stored in the knowledge bank of the company. So the knowledge bank of the company gives a lot of inputs to the incoming youngsters and managers. So it tells them this was the type of project which was taken up and this was the type of decisions that were made, this is where the problems came and if they were overcome, how they were overcome, it will be a very good exercise for posterity. So this is where the case study method is considered to be a very good experience.

So in fact, now, a little further has been done with the case study that is, they are doing simulation exercises, what is the simulation exercises? So in the organization, the students are divided into teams, they are given roles and they are asked to make decisions depending on the type of situation that was encountered, how will the students make the decision? So there is a learning in this also.

Many times many of my students in fact, I have found them to be extraordinarily intelligent. So they would ask the question, suppose the manager had taken the decision in this manner, would it not have been beneficial to the organization? Quite possible, but at that point of time he took the decision in his considered wisdom, he might have taken all the ifs and buts and then said okay I am taking this decision .

Now, the case study itself should have the following aspects, one is the origin, history and growth of company over time; so you should know about a company before you analyze it. For example, the Mysore sandals soaps now, is going by the name of Karnataka soaps and detergents limited the company started by the Maharaja with the guidance of Sir MV and also a chemist who was sent abroad for specialized training to make the sandal soap. So out came this product sandal soap at that point of time when nobody knew what is sandal soap.

So the smell of sandal and the soap; the formula for this product is still a very guarded secret even after so many decades. So it is the product which is taking the company forward. So when you look at a company you should know what is the history it has, so that gives you an idea of how much inputs have gone or how much trials have gone into making the company. So you might be analyzing the case of the company so many decades later, but when they established it, the way they went through the trials.

Similarly if you take the case of Infosys, terrific problems in the beginning, not 1 or 2. So many times the founders were toying with the idea of closing the company. Started in 1981, its first fortune 500 client came sometime 5 years later, but that was the turning point for the company; so afterwards it did not look back. Some 5 years later further, a wonderful offer was made to the company founders to sell the company for a huge sum at that point of time, but it did not materialize the company still went with the founders and this is doing very well even to this day.

So this is where you learn a lot from this origin, history and growth of company over time. And should also give the analysis of the organization how it has done for example, Infosys developed what is called a PSPD model,etc. So what is that model, how did it come about all those types of things, nature of external environment.

Then the SWOT analysis, this is something very important; when you take up any company, you should do a SWOT analysis, present the corporate strategy, present the business strategy with respect to the different business units, some more of that we will discuss when in the coming sessions.

So the organization structure and control systems and the type of recommendations that you are

making for the company all this should come in the case study. To make these recommendations there may be some issues which might have been raised in the case study. So the case study might raise some issues saying that these are the types of issues that has come about in the company, then how would you really go about handling this or tackling these issues. So these are the types of things which one should have with respect to the company.

Now, on the SWOT list, I want you to go to my book on case studies. I am reading from that book. The table 1 on page 3 gives you a SWOT checklist, what does it tell with respect to the company? Internal strengths, so many questions are asked, does the company have many product lines, broad market coverage, manufacturing competence, good marketing skills. So as I told you, the distinctive competence of Hindustan lever is in its marketing skills, the distinctive competence of manufacturing is with Tata Steel, the manufacturing skills competence is with Tata Steel.

Then good inventory management, R&D, Information System competencies, good human resources, brand equity, this is very important in the marketplace. A product coming from the house of Tatas always enjoys the brand equity that it is a quality product. When it is a quality product, it is very probable that it will have higher acceptance in the market. So even a ubiquitous product like salt, if it is coming out from the house of Tatas, then by the name of this Tata salt it carries an edge over other similar products in the market.

Then cost advantage, appropriate organizational structure, appropriate control systems, ability to manage strategic change, kindly note that all these organizations especially in the present liberalisation era, they should be able to manage strategic change, if they are not able to do that it is probable that they will find themselves extinct sooner than they thought. Well-developed corporate strategy, good financial management, these are all the checklists for developing internal strengths.

For weaknesses, what are the checklists you should have? Instead of many product lines, it may be narrow product lines, rising manufacturing costs, poor marketing plan, poor materials management, inadequate human resources, loss of brand name, lack of corporate direction, lack of corporate control, poor financial management, inappropriate organizational structure and control systems, high conflict politics, others.

So in most of these public sector units, you will find politics is a quite an important element, so you do not know to whom you are really barge into, how connected he is politically. Suppose you want to take a decision and the decision irks him, he will put all stumbling blocks in your taking the decision; so this is happening in most of the public sector units also.

Another bane of the public sector units is putting a bureaucrat to head the unit; he will be most of the times ignorant of the company, how it is working. So the most important thing to manage a public sector company is to have a person from inside, grow from inside to become the managing director or whatever, he will be knowing the ins and outs of the company, he knows where the troubles are likely to come and he can act or he can do this troubleshooting much better than the bureaucrat.

In fact, most of the problems which we are facing in many of the public sector units is if you really see may be attributed to the interference from the bureaucracy. So this is something which companies have to be wary of.

Potential environmental opportunities, then the type of opportunities that is New markets, businesses, Cost or differentiation advantage, profitable new acquisitions, brand name, capital in new areas, R&D skills in new areas, vertical integration, can it can be both forward and backward, diversification & others.

Then on the threats, attack on core businesses, increase in domestic competition, increase in foreign competition, change in customer taste, new forms of industry competition, barriers to entry, new or substitute products takeover, slowdown in the economy, lower market rate and others. So these are the types of issues that you normally encounter with respect to SWOT analysis; as a manager, you should be able to come out with this type of checklists.

So suppose, you find it difficult, let us say to impartially analyze your organization, then you can have these services of an external consultant, he can always show the mirror to you, where you have gone wrong. So in fact, I remember with respect to a public sector organization in Bangalore, a well-known business consultant was hired to suggest changes in the organization structure, this company is a well-known company in the public sector, was small at that point of time, but was doing reasonably well.

So what did this well-known consultant at that point of time suggest to the company? He suggested that dismantle the existing organization structure in entirety, so dismantle it totally.

So the company was in a state of shock, what is this consultant trying to tell? Suppose, the entire organization structure is disbanded, how will the new organization structure come about? So this was a type of question which the top echelons of the company had at that point of time. And to which the, this eminent consultant gave the answer. He said the new organization structure comes like a phoenix, what do you mean comes like a phoenix, phoenix is a bird which comes back to life even after coming out of fire, so that type of scenario.

In other words, he was trying to tell the company bosses, the senior bosses, trial by fire to the organization. So this petered down to lower levels in the company and many of the unions, the stronger union said do not allow that consultant to come inside the company at all. So the next day he should be thrown out from the gate only, so all those types of things happened.

But anyway, what was the net outcome of all this, the company did go through an organizational change exercise as suggested, though not fully, by the consultant, but more or less, they took important suggestions which the consultant gave and did effect changes in the organization structure.

And the company right now, if you look at it, in 2022, it is a very important public sector unit, still doing well, not having the problems of its elder brother whom they used to consult every other day. So whereas the elder brother went into so many hiccups, after liberalization process, this younger brother survived and is doing well. So I am not naming the companies; so it is for you to make your good guess on that.

Now, with all this, let us look at the type of ratios I gave you in the last class, the key financial ratios, which you can, which you should with respect to your company calculate. So under the heads of profitability, leverage, activity, liquidity, and other ratios.

Now, go back to the book on case studies; page number 4 gives you the summary of key financial ratios, how they are calculated, and what they show, I am reading a few of them. One with respect to profitability, gross profit margin, how do you calculate this gross profit margin: Sales minus cost of goods sold divided by the sales revenue.

Now, what it shows- indication of the total margin available to cover operating expenses and yield profits. So this is very important in a business as you know, you are not doing a business for charity, you are producing a product to make profits. So if your profit margin comes down, then your survival in the market itself is under threat.

Now, the gross profit margin does not take into account the taxes. So there you come into the operating profit margin: profit before taxes and interests divided by sales revenue. So what it shows? An indication of the firm's profitability from current operations without regard to interest charges. Then you come to the net profit.

Then how do you calculate the return on total assets? It can be calculated in 2 ways, one is profit after taxes divided by total assets or profit after taxes plus interests divided by total assets. What does it tell you? A measure of the return on total investment in the enterprise.

So suppose you are putting so much money let us say the stakeholders of the company are putting that investment, naturally they expect some return. So naturally they expect the return better than the bank rate of interest, so the operations should be able to give them that type of return, if it is not giving them that type of return, very unlikely that they will really okay this type of scenario.

Then what is the type of stockholders equity return, how do you calculate that? It is profit after taxes over total stockholders equity. What is that? It is a measure of the rate of return on the stockholders investment in the enterprise. So you are a stockholder then how much do you want? What is the type of return you are getting?

So if you really see in the present context, the LIC came out with an IPO and that IPO has been oversubscribed. The percentage of dilution which the government of India wanted to do was at a higher rate initially, but when they really came out with the IPO, it was a very small percentage of dilution which they effected and for that, this issue was oversubscribed many times. So what does it tell you? It means to say the confidence of the prospective investor in the initial public offering.

So the return on common equity that is profit after taxes minus the preferred stock dividends divided by the total stockholders equity minus the par value of preferred stock. So what does it tell you? A measure of the return rate of return on the investment that the owners of the common stock have made in the enterprise.

Then the earnings per share it gives you the earnings available to the owners of the common stock.

Liquidity ratios in the marketplace, you have the current ratio, the quick ratio, and the inventory to net working capital. So what does this current ratio give you? It is current liabilities over current assets.

Indicates the extent to which the claim of the short term creditors are covered by assets that are expected to be converted to cash. Normally, you expect this current assets to current liabilities at 2: 1. Suppose you have put 1 rupee as investment, what is the maximum liability you can have? Only 2 rupees not more than that. So if your current assets are taking care of the current liabilities, suppose there is a demand by the creditor, give back my 1 rupee, suppose it is taking care of that, then the company does not have to bother.

So a quick ratio same as the current ratio but minus the inventory. Suppose you got some finished products, but which are still not been able to get cash or that is not converted to cash, so

that gives a measure of the firm's ability to pay off short term obligations without relying on the sales of inventories. Without the sale also you can clear off this current liabilities.

So inventory to net working capital that is inventory divided by current assets minus current liabilities gives the extent to which the firm's working capital is tied to the company inventory.

So this is the type of liquidity ratios which you have to look at with respect to organizations.

Then you have the leverage ratios, you have to look at debt to assets gives the measures the extent to which borrowed funds are being used to finance the firm's operations. Debt to equity, provides a measure of the funds provided by creditors to that provided by owners. Then times interest earned measures the extent to which earnings can decline without the firm becoming unable to meet its annual interest costs. Then fixed charge coverage, so this fixed charge coverage more inclusive indication of the firm's ability to meet all its fixed charge obligations.

So then what is the activity ratios: inventory turnover that is sales revenues divided by inventory of finished goods, when compared to industry averages, it provides an indication of whether the company has excess or inadequate inventory of finished goods, so this is where so many concepts came especially the Japanese concepts that is the just in time inventory.

So it was it was one of those companies from the south it has the advantage of being very close to Bangalore, its production facilities also in Mysore, so draws heavily on Bangalore's infrastructure and its capabilities, so it is able to have a very good inventory management in the whole process. Similarly, the other company which you can think of in the same belt is Ashok Leyland; then the fixed assets turnover, a measure of the sales productivity and utilization of plant and equipment.

Then the total assets turnover, a measure of the utilization of the firm's assets. A ratio below the industry average indicates the company is not generating enough volume of business given the size of its assets investment. Accounts receivable turnover, that is annual credit sales divided by accounts receivable gives a measure of the average length of time it takes the firm to the sales made on credit, that is annual credit sales over accounts receivable.

Then average collection period indicates the average length of time the firm must wait after making a sale before it receives payment. Other ratios are with respect to dividend yield on common stock, gives a measure of the returns on to the owners received in the form of dividends. Price earnings ratio gives faster growing or less risky firms tend to have heavier price earnings ratios than those slower growing or more risky firms.

Then the dividend payout ratio indicates the percentage of profits paid out as dividends. Then the cash flow per share that is after tax profits plus depreciation divided by the number of common shares outstanding gives a measure of the discretionary funds over and above expenses available to the firm.

So this is a very good summary which is given in this book. As I told you, both these books will be very helpful to you in understanding this subject and also to do well in your exams, and also in your professional career as well, so kindly purchase these books. So repeating: the sixth edition of Strategic Management, and the seventh edition of Case studies in Marketing- The Indian context, both published by Prentice Hall available to you with almost all the leading booksellers.

We will stop here for this session. In the next session, we will look at 1 or 2 case studies from the real context, so not exactly the case studies, I have given a few case studies in the book on strategic management also. I may not be looking at them, I may be looking at a public sector company which was very strong, but failed in this liberalisation era, so that is the first one which I will be looking at.

And if time permits, we will also look at one more company's strategy which I have been discussing that is the Gillette company, how it has been successful to have a distinct competitive advantage in the marketplace with respect to its product that is the Mach 3 blade. So we will stop here, we will continue in the next session. Thank you.