

## **Chapter 2 Leading Strategically**

### **KNOWLEDGE OBJECTIVES**

1. Define and explain strategic leadership.
2. Explain how vision and mission create value.
3. Define the meaning of a top management team and the value of having a heterogeneous top management team.
4. Explain the importance of managerial succession.
5. Define human capital and social capital and describe their value to the firm.
6. Describe an entrepreneurial culture and its contribution to a firm.
7. Explain the importance of managerial integrity and ethical behavior.
8. Discuss why firms should have a control system that balances the use of strategic controls and financial controls.

### **CHAPTER OUTLINE**

*Focusing on Strategy: Changes in Corporate Governance Have Reformed the Role of the CEO in Strategic Leadership*

**ESTABLISHING THE VISION AND MISSION**

**DEVELOPING THE TOP MANAGEMENT TEAM AND SUCCESSION**

Top Management Team

Management Succession

**MANAGING THE RESOURCE PORTFOLIO**

*Understanding Strategy, Learning from Failure: Trying to Make Yahoo! Competitive Again*

**BUILDING AN ENTREPRENEURIAL CULTURE**

*Understanding Strategy, Learning from Success: General Mills Creates Wealth with a Focus on Healthier Products*

**PROMOTING INTEGRITY AND ETHICAL BEHAVIOR**

**USING EFFECTIVE CONTROLS**

**SUMMARY**

**KEY TERMS**

**DISCUSSION QUESTIONS**

**STRATEGY TOOLBOX**

*Mini-Case: Strategic Leadership Made the Difference at Priceline.com***EXPERIENTIAL**

**EXERCISES**

**ENDNOTES**

**Lecture notes: Chapter Introduction:** This chapter emphasizes the importance of strategic leadership actions for the organization's survival and success. While strategic leaders are, generally, in upper-level organizational positions, today's business climate warrants involvement of people throughout the organization. Anyone inside and outside of a firm who may be responsible for designing strategic actions and ensuring they are carried out in ways that move the firm toward their vision is acting as a strategic leader.

*Focusing on Strategy*

**Changes in Corporate Governance Have Reformed the Role of the CEO in Strategic Leadership**

This feature conveys the changing role of strategic leaders. Division of the role of chairman of the board and CEO along with changes in corporate governance prompted by the Sarbanes-Oxley Act have created a new breed of chairpersons. This has raised questions of who is responsible for strategic decision making and brought about a decrease in CEO power while increasing the need for power sharing among board members and the CEO. With such partnering arrangements and more involvement of all employees, strategy becomes even more dynamic.

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This section applies to Knowledge Objective 1.

- **Strategic leadership** involves developing a vision for the firm, designing strategic actions to achieve this vision, and empowering others to carry out those strategic actions.
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**FIGURE 2.1**  
**Strategic Leadership Actions**

This figure applies to all Knowledge Objectives.

The figure outlines the strategic actions necessary for strategic leadership.

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**ESTABLISHING THE VISION AND MISSION**

This section applies to Knowledge Objective 2.

- Most strategic plans are designed for a 3-to-5 year time period.
- Visions look forward 10 to 20 years.

- The mission of the firm flows from the vision and is more concrete.
  - An effective strategic leader develops a vision and inspires stakeholders to commit to achieving it.
  - Shareholders are critical stakeholders.
  - If shareholders do not support the vision they may pressure the board of directors to change it or find new strategic leaders.
  - Employees are critical stakeholders because they must implement the strategy.
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*TABLE 2.1*

**Fortune's Most Admired Companies Ranking**

This table applies to Knowledge Objective 1.

This table lists Fortune's rankings of most admired companies.

**Teaching notes:** While the rankings can be subjective, the instructor may use the list to stimulate discussion as to what strategic leadership actions have made these companies successful. Instructors and students may also compare these companies to list of least admired companies in order to examine the differences in strategic leadership.

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**DEVELOPING THE TOP MANAGEMENT TEAM AND SUCCESSION**

TOP MANAGEMENT TEAM

This section applies to Knowledge Objective 3.

- A *top management team* is the group of managers charged with the responsibility to develop and implement the firm's strategies.
- Top management teams are usually composed of officers of the company with titles of vice president and higher.
- *Homogenous teams* are made of people who think alike and have similar backgrounds.
- Drawbacks of homogenous teams are the tendencies to
  - overlook important issues
  - make errors in judgment
  - lack all the knowledge and information needed to make good decisions
- The main advantage of homogenous teams is quick consensus.
- *Heterogeneous teams* have members with different backgrounds, e.g. experience, education.

- Heterogeneous teams tend to
  - take longer to make decisions
  - make better decisions

**Lecture notes:** Companies may benefit from the diversity provided by a heterogeneous management team. Using Nissan as an example, the instructor may stimulate discussion of what diversity in management provided to the company. It should also be emphasized that as strategy must continually be created and recreated, top management teams must continue to be developed.

## MANAGEMENT SUCCESSION

This section applies to Knowledge Objective 4.

- Strategic leaders must develop people who can succeed them.
- CEO successions can be
  - from inside the firm (the majority of successions)
  - from outside the firm
- Inside succession
  - motivates employees to work hard in hopes of opportunities for promotion for good performance
  - unlikely to result in drastic changes in strategies
- Outside succession is more likely when
  - the board wants changes in strategy
  - the organization is performing poorly
  - opportunities or threats in the external environment require strategy adjustment

## MANAGING THE RESOURCE PORTFOLIO

This section applies to Knowledge Objective 5.

- **Lecture note:** This section focuses on organizational resources and how best to utilize these resources for effective strategic leadership. Tangible resources (buildings, manufacturing plants, offices, machinery, computers, etc.) require intangible resource (human capital, social capital, and organizational capital) input. Strong human and social capital provide a base of financial capital. This is an appropriate time to emphasize the value and extent of human capital and how many firms fail to recognize the long term impacts of devaluing human capital. Students should understand that all firms have varying levels of resources and cannot do everything well. The instructor should explain how firms may make up for resource deficiencies and how firms may utilize the resources they have. Discussion of the impact on the balance scorecard may be useful.

- Resources are the basis for a firm's competitive advantages and strategies.
- Tangible resources include
  - buildings, manufacturing plants, and offices
  - machinery and computers
- Intangible resources include
  - human capital
  - social capital
  - organizational capital (e.g., organizational culture)
- **Human capital** is the knowledge and skills of people working for the firm.
- Human capital is the source of intellectual property.
- Human capital requires continuous investment in knowledge and skills
- Learning comes from
  - training
  - experience
  - failure
- Strategic leaders
  - develop skills throughout the workforce
  - motivate employees to use their skills to implement strategies
  - reward employees for using their skills
- **Social capital** includes all internal and external relationships that help the firm provide value to customers and ultimately to its other stakeholders.
- **Internal social capital** refers to the relationships among people working inside the firm.
- **External social capital** refers to relationships between those working with a firm and individuals and organizations outside the firm.
- **External social capital**
  - provides access to resources
  - helps firms enter new markets
  - forms links with reliable suppliers
  - locates partners for joint ventures
- Strong ties in external relationships require
  - trust
  - reciprocity
- Weak ties serve
  - information roles
- Effective strategic leaders have well-developed relational skills.
- Financial capital is important and is affected by human and social capital.

*Understanding Strategy, Learning from Failure*

**Trying to Make Yahoo! Competitive Again**

This case applies to Knowledge Objectives 1 and 5.

This case illustrates how strategic leaders manage the resource portfolio. The information provided focuses on new CEO Carol Bartz's changes and resource usage in order to make Yahoo! competitive again. With Bartz at the helm, Yahoo! has partnered with Microsoft for increased operating margins, focused company resources on making acquisitions in content, and improved its positioning. With problems with positioning in its content area, competitiveness with rivals remains strong. Will Yahoo! remain competitive?

**Critical thinking questions:**

1. What strategic leadership contributions has Carol Bartz made to Yahoo!? (Knowledge Objective 1)

**Answer:**

Carol Bartz has taken actions toward a vision for the company. This is illustrated by 1) working out the partnership with Microsoft which increased operating revenues and reducing costs, 2) focusing resources on making acquisitions in content, 3) eliminating businesses, and 4) using resources to improve positioning and building Web page counts.

2. Using information provided in the case, briefly evaluate Yahoo!'s resources and capital. (Knowledge Objective 5)

**Answer:**

Human Capital: Problem---Bartz's competitive background is not in content. She was the CEO of Autodesk, a producer of sophisticated design and engineering software such as AutoCAD.

Tangible Resources: Problem—perhaps excessive given the fact that some businesses have already been eliminated

Social Capital: Good---Yahoo! appears to be able to establish external relationships with other companies like Microsoft to offer value to customers. However, there is no evidence of furtherance of these initiatives. Also, there is no evidence of their internal social capital position.

Financial Capital: Good—Substantial cash on hand is evident.

3. How could the balance scorecard approach help Yahoo! to remain competitive?(Knowledge Objective 8)

**Answer:**

The balanced scorecard provides a framework for simultaneously evaluating strategic and financial controls. By examining financial factors, customers, internal business processes, and learning and growth, the stalled growth companies would have a heads up on combating problems with strategic and financial controls, breakdown in information systems, premature decision making, and any deficiencies in human capital.

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## **BUILDING AN ENTREPRENEURIAL CULTURE**

This section applies to Knowledge Objective 6.

- An entrepreneurial culture encourages employees to identify and exploit new opportunities.
    - encourages creativity
    - encourages risk-taking
    - tolerates failure
  - Payoff for innovation in high-technology industries is often low.
  - Pressure for return on research investments leads to acquisition of firms which have new products far along in development process.
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*Understanding Strategy, Learning from Success*

### **General Mills Creates Wealth with a Focus on Healthier Products**

This case applies to Knowledge Objective 6.

This case discusses General Mills' entrepreneurial culture. General Mills, with a succession planned CEO, has developed new innovative products. By linking bonuses with health and wellness objectives, encouraging risk taking and creativity, and experiencing some failure along the way, General Mills' growth and profits have stemmed from their attempt at innovation and establishing an entrepreneurial culture.

**Critical thinking questions:**

1. What do think stimulated General Mills' innovation and entrepreneurial culture? (Knowledge Objective 6)

**Answer:**

It may be that the transition to a new strategic leader brought an innovative spirit prompted by human and social capital that weren't present. Another possible catalyst may have been a pressure to receive returns from research investments. From the case, General Mills did examine market research and made decisions accordingly. If and when Kendall Powell decides to leave General Mills, is it doomed to become less innovative? What could be done to resist that event? (Knowledge Objective 4)

**Answer:**

This could be considered a managerial succession issue. Powell needs to find and develop someone who can step into his shoes and maintain the innovative culture. Organizational cultures, typically, are not self-sustaining if top management is not actively supporting them.

2. How are cultures "rebuilt"? (Knowledge Objective 6)

**Answer:**

From the case, it seems that establishing expectations of behavior, setting up suitable reward systems for the behavior, having leaders who model the behaviors of the desired culture, and bringing in employees who already display the behavior (e.g., acquiring other firms with the desired culture) are tactics used. Another step would be to create a system for building human and social capital.

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## PROMOTING INTEGRITY AND ETHICAL BEHAVIOR

This case applies to Knowledge Objective 7.

- Strategic leaders
  - develop standards for behavior of employees
  - serve as role models
  - determine the boundaries of acceptable behaviors
  - set tone for organizational actions
  - ensure that ethical behaviors are expected, praised, and rewarded
- **Opportunistic** managers make decisions that are in their own best interest rather than the firm's best interest.
- **Corporate governance** begins with board of directors overseeing managerial actions.

- Independent outside board members are considered more objective.
- **Related-party transactions** involve paying a person who has a relationship with the firm extra money for reasons other than his/her normal activities on the firm's behalf.
  - Sarbanes-Oxley Act is focused on related-party transactions.
- Fraudulent and unlawful acts by managers (white-collar crime) result in negative outcomes for firms.
- Unethical leaders eventually fail.
- Only leaders with integrity and respected values sustain effective outcomes over time.

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## USING EFFECTIVE CONTROLS

This case applies to Knowledge Objective 8.

- Controls
  - ensure standards are met
  - prevent employees from misusing the firm's resources (fraud and opportunism)
  - guide managerial and strategic decisions
- Financial controls focus on shorter-term financial outcomes, including profit.
- Strategic controls focus on content of strategic actions.
  - take longer term view
  - best employed under conditions of uncertainty
  - determine acceptable risks
- **Balanced scorecard** provides a framework for evaluating the simultaneous use of financial and strategic controls.
- Four foci of balanced scorecard
  - financial factors
  - customers
  - internal business processes
  - learning and growth

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## SUMMARY

## KEY TERMS

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## ANSWERS TO DISCUSSION QUESTIONS

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1. What is strategic leadership? Describe the major actions involved in strategic leadership. (Knowledge Objective 1)

**Answer:**

Strategic leadership is the process of developing a vision for the firm, designing strategic actions to achieve the vision, and empowering others to carry out these strategic actions. Other major actions involved in strategic management are developing the management team and managerial succession, managing the firm's resource portfolio, building an entrepreneurial culture, promoting integrity and ethical behavior, and using effective controls.

2. How do a vision and a mission create value for a company? (Knowledge Objective 2)

**Answer:**

Through the vision and the mission of the firm, strategic leaders inspire stakeholders (especially employees) to commit to achieving them. This commitment is crucial to effective implementation, without which value cannot be created by the firm.

3. What is a top management team? Why does a heterogeneous top management team usually formulate more effective strategies? (Knowledge Objective 3)

**Answer:**

The top management team is the group of managers charged with the responsibility to develop and implement the firm's strategies. A heterogeneous top management team approaches problems with different education and experience backgrounds. This helps them bring recognize important issues and avoid errors in judgment that can occur when the top management team members all think alike.

4. Why is it important to develop managers for succession to other managerial jobs? (Knowledge Objective 4)

**Answer:**

Eventually, every manager will leave the firm, and there must be competent managers to replace them. If top management positions are filled from inside the firm, lower level managers are motivated to try to perform well in hopes of

being promoted. If management positions are filled from the outside, it has the advantage of being more likely to bring about a drastic change in strategy if the firm is performing poorly.

5. What do the terms human capital and social capital mean? What is the importance of human capital and social capital to a firm? (Knowledge Objective 5)

**Answer:**

Human capital includes the knowledge and skills of those working for the firm. Social capital includes all internal and external relationships that help the firm provide value to customers and ultimately to its other stakeholders. Human capital is the basis for learning and employee performance within the firm. Social capital allows the firm to run smoothly internally and also gives access to resources outside of the firm. Both human and social capital are key to organizational success.

6. How can a strategic leader foster an entrepreneurial culture, and why is such a culture valuable to a firm? (Knowledge Objective 6)

**Answer:**

A strategic leader can foster an entrepreneurial culture by encouraging employees to identify and exploit new opportunities. In such a culture, the strategic leader encourages creativity and risk taking but also tolerates failure. An entrepreneurial culture is valuable to a firm because it has major effect on employees' actions, profitability, and can increase chances of success.

7. Why are managerial integrity and ethical behavior important to a firm? (Knowledge Objective 7)

**Answer:**

Managerial integrity and ethical behavior are important to a firm because they can be serious and extremely costly for a firm and for the person lacking integrity and behaving unethically. Extraordinary unethical behavior can even lead to a firm's demise.

8. Why should strategic leaders develop a control system that balances strategic controls and financial controls? (Knowledge Objective 8)

**Answer:**

Controlling financial outcomes is important while simultaneously looking to the longer term and evaluating the content of the strategies used.

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**INSTRUCTORS' NOTES FOR STRATEGY TOOLBOX**

This feature applies to Knowledge Objectives 1, 2, and 8. When presenting this to students, there are two key points to drive home. First, this tool is meant to provide focus on the most critical aspects of strategic management. Often CEOs and other Top Management Team Members become focused on too many different areas, especially operational issues. This tool ensures that the most important, strategic issues are addressed. Second, the tool can be generalized to leadership of a division, product line, or even a student organization. Many of the concepts within this textbook are generalizable by design.

Ask the students to think of a student organization they belong to (or especially are part of the leadership thereof). Ask them do a CEO Strategy Checklist to see how well strategic the organization is and compare results within the class. Share with them that the same situation is in place in many very large organizations (strategy process not done well).

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**INSTRUCTORS' NOTES FOR MINI-CASE**

**Strategic Leadership Made the Difference at Priceline.com**

This case applies to all the Knowledge Objectives.

This case outlines CEO, Jeffrey Boyd's leadership in Priceline.com's turnaround, from being near bankruptcy, to being victim of the September 11, 2001 terrorist attacks, to having a bright future in poor economic times.

**Questions:**

1. What did Jeffrey H. Boyd, CEO of Priceline, and his management team do to turn around the business to make it profitable after downturn in 2001? (Knowledge Objectives 1, 2, and 58.)

**Answer:**

First of all, Boyd had a vision for changing Priceline's future. Secondly, Boyd diverted attention and focus on airline tickets to rebuilding Priceline's brand around hotel bookings and expansion into Europe. He, also, cultivated stronger relationships with important brands such as Marriott and Starwood and gained control of TravelWeb, a joint venture owned by major hotel chains. Further, Boyd lowered the fee that it received from hotels for facilitating bookings relative to other travel agents/brokers. Moreover, the Boyd team obtained William Shatner as a company spokesperson for television ads and continued to focus more on European investments and acquisitions.

2. What aspects of strategic leadership found in this chapter are emphasized in the mini-case on Priceline.com? (Knowledge Objectives 1 and 2)

**Answer:**

The real emphasis is on how Jeffrey Boyd developed a vision for Priceline, designed strategic actions to obtain the visions, and how he utilized other people and departments to carry out the strategic actions.

3. If you were the CEO of Priceline, what challenges would you need to overcome in the future given the knowledge you have gained through studying the concepts in this chapter? (Knowledge Objective 1, 2, and 8)

**Answer:**

There are several challenges: 1) the need to revise the vision and mission, if necessary, in new competitive environments. 2) A continued review of the strategic actions covered in Figure 2.1 to make sure these processes are in place and are consistent with one another and the organization's vision and mission. 3) The use of the balanced scorecard approach might serve to keep Boeing "on track" and not over-emphasizing some goals at the expense of others.

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## INSTRUCTORS' NOTES FOR EXPERIENTIAL EXERCISES

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### Exercise One: Building an Entrepreneurial Culture

This exercise applies to Knowledge Objective 6.

The purpose of this exercise is to examine whether some firms identified as innovative by *Fast Company* magazine engage in the types of activities suggested in the chapter

discussion of “Building an Entrepreneurial Culture.” To complete this exercise, students should read the section of the chapter about Building an Entrepreneurial Culture and evaluate whether the firm engaged in the actions suggested in the chapter (for example taking risks and tolerating failure). Specific questions are provided for the group to answer. The instructor should emphasize to students that they must give concrete examples of what the company does to encourage and exploit new opportunities and to encourage risk taking. In addition, the exercise allows students to go beyond the chapter material to see whether companies employ other practices to build their entrepreneurial cultures. Companies are chosen from a leading business magazine known for identifying exceptional companies. Most of these companies are known to students and should provide for a stimulating analysis.

### **Exercise Two: Codes of Ethics**

This exercise applies to Knowledge Objective 7.

First, have a brief discussion delineating the difference between ethics and legality. Students should grasp that actions that are often viewed as unethical could still be legal (e.g., omitting verbal discussion of written specific details of a business deal that would likely influence decision making). Conversely, some actions that might be illegal (e.g., breaking into someone’s home while they are away) might not be considered unethical by some in certain instances (e.g., to provide shelter to a group of hikers that have been lost for days in blizzard conditions).

The website [www.e-businessethics.com](http://www.e-businessethics.com) is run by The Center for Business Ethics and Social Issues at Colorado State University, and is directed by Dr. O. C. Ferrell, an often published authority on business ethics. This Center “... provides a source of information on business ethics, corporate citizenship and organizational compliance.” The “Ethics Links” assigned to students provides many links to other ethics centers and government agencies, as well as to Codes of Conduct and/or Codes of Ethics for professional associations and organizations, specific businesses, and so on. You may wish to choose specific codes for assignment, reading, study and discussion. Also check out the many other links, but of particular interest may be the “PowerPoint” link, which provides a plethora of information on corporate citizenship behavior, professionalism, ethics and corporate reputation, teaching ethics, etc. The site also provides information on books, case studies and articles dealing with various aspects of ethics.

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## **ENDNOTES**

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