Basic Strategy Concepts

Learning Objectives

After reading and studying this chapter, you should be able to:

• Explain the difference between the strategic initiatives and operating activities of a health care organization.
• List the numerous benefits that an organization receives from the practice of strategic planning and management.
• Understand the different types of competition that make strategic planning necessary.
• Distinguish the several different organizational levels at which strategic planning and management can take place.
• Recognize the ability of a person to engage in “strategic thinking.”
• Differentiate between “incremental” and “revolutionary” strategies, as well as “intended” and “actual” strategies.
• Describe in a basic way the fundamental steps in a good strategic planning and management process.
• Explain the concept of “strategic direction” and the critical role that it plays in the strategic planning process.
• Understand how strategic management often goes wrong, due to both management failures and inherent organizational barriers.
• Identify the powerful environmental forces that affect organizational efforts at strategic planning and management.
Alice, in conversation with the Cheshire Cat:

“Would you tell me, please, which way I ought to go from here?”

“That depends a good deal on where you want to get to,” said the Cat.

“I don’t much care where—” said Alice.

“Then it doesn’t matter which way you go,” said the Cat.

“—so long as I get SOMEWHERE,” Alice added as an explanation.

“Oh, you’re sure to do that,” said the Cat, “if you only walk long enough.”

—Lewis Carroll, Alice’s Adventures in Wonderland

It might not seem to make much sense to do a lot of long-range strategic planning and management in an industry like health care where the ground rules are changing constantly and so many of the options depend ultimately on reimbursement rates set by the Centers for Medicare and Medicaid Services (CMS) in Washington, D.C., or on federal and state health care laws and regulations. Or in the biotechnology industry, which depends so much for its funding on the whims of venture capitalists or congressional appropriations for the National Institutes of Health. Yet, even in these fluid, often chaotic environments, meaningful strategic planning and management is not only possible, it is essential for an organization to survive and, then, thrive.

DEFINITION OF THE CONCEPT OF “STRATEGY”

It is best to begin a conversation about strategic management by coming to an understanding of what “strategy” is and what it is not.

THINK ABOUT THIS: Have you ever used the term “strategy” in conversation? Exactly what did you mean by it? Some people claim to have a strategy for mowing the lawn or shopping for a new car. Are those really strategies or are they some kind of “plan”? What is the difference between a strategy and a plan, and does it really matter?

In the true business management sense, strategy is distinguished by several key dimensions.

- A strategy aims to steer the direction of the overall organization. It affects the long-term well-being of the organization.
- A strategy has a long time horizon, usually measured in years rather than months or weeks. A typical strategic plan may set goals to be achieved five or more years in the future.
- A strategy has an impact that is more likely to be felt throughout the entire organization rather than within a single component of the organization.
A strategy builds on and exploits to the fullest extent the organization’s resources and abilities.

A strategy aims to create the best possible fit between the organization and its mission, on one hand, and the organization’s external environment, on the other hand.

Strategic decisions require major resource commitments and are difficult to reverse.

A strategy is distinguished by the strength of the organization’s commitment to it and reluctance with which it considers changing it.

For those organizations in a competitive environment, a strategy is frequently aimed at gaining an advantage over competitors.

In order to focus its resources and energies, an organization or business unit normally will pursue only a few distinct strategies at one time, perhaps no more than six or seven.

A strategy is future oriented and marked by uncertainty and risk.

A strategy calls upon the organization to do something that it is not doing now. This inevitably requires change, sometimes profound, in many aspects of its operations.

A successful strategy is the result of an integrated/collaborative effort by many parts of the organization.

What is regarded as long term will depend on the organization and the industry or market in which it operates. It may mean five years or longer for a small community hospital located in a modest-sized city in rural Kansas, where it faces no competition. In contrast, a large teaching hospital surrounded by several other teaching hospitals in a vibrant, highly competitive market for hospital care in Boston or Los Angeles may find it hard to think much further than two years into the future.

THINK ABOUT THIS: Is there any reason that a component of the overall organization cannot have a strategy or a strategic plan? Is it possible for both a teaching hospital and its department of orthopedic surgery to have strategic plans? What advantages might this offer? What problems could it present? Might a surgeon working in that department have a personal strategic plan?

It may be easier to understand the concept of “strategic” planning by contrasting it with two other forms of planning—“operational” and “tactical.” A strategic plan is concerned with the widest scope of organizational activities, frequently encompasses the broadest geographic area, affects and involves the largest number of employees (often everyone in the organization), costs the largest amount of money (usually millions...
of dollars), and takes the longest period of time (several years) to implement. An operational plan deals with activities of narrower dimensions, impacts subgroups of the workforce (a single department or professional category), involves the expenditure of more modest sums (tens or hundreds of thousands of dollars), and typically takes no more than a year to carry out. A tactical plan is at the lower end of the planning continuum: it embraces activities affecting smaller segments of the organization, may require the participation of very few people (one or two, or a small ad hoc task force), entail quite modest expenditure (sometimes no additional outlay at all, perhaps hundreds or thousands of dollars at most), and stretches over a few days or weeks.

A health maintenance organization (HMO) based in Ohio may adopt a strategic plan that sets an objective of expanding from its present market base in the northern part of the state around Cleveland and Akron further south into Columbus and eventually Cincinnati over the next two years. Its synchronous operating plan may be to enroll at least 25,000 new members in Columbus over the next year. As a tactical step toward achieving that goal, the HMO’s marketing department may carry out a direct mail and television advertising campaign during the month of October.

When the planning and implementation process is executed expertly, the efforts at the strategic, operational, and tactical levels merge into a seamless continuum of forward-looking activity intended to ensure the survival and growth of the organization. Fulfillment of the tactical plans contributes to meeting the objectives of the operational plans, which in turn advance the end purposes of the strategic plans.

THINK ABOUT THIS: Does an organization that does not face competition need to have a strategic plan? Examples are NFP organizations and government agencies. What benefits would a strategic plan bring to them? Do they in fact have competitors?

Perhaps more than any other industry, health care delivery and financing is performed by a diverse collection of for-profit (FP), not-for-profit (NFP), governmental, and quasi-governmental organizations. 60 percent of the hospitals are organized as NFP corporations, in addition to which the federal government agency Veterans Administration operates well over 1,200 hospitals, clinics, and other facilities. Many states and cities own and run public hospitals and clinics. Some of the oldest, largest, and best-known HMOs are NFP: Kaiser Foundation Health Plans, Harvard Pilgrim, and Group Health Cooperative of Puget Sound, among others. All the Blue Cross/Blue Shield health insurance companies are NFP entities. The largest health care payer in the country is the Medicare program administered by the federal Centers for Medicare and Medicaid Services (CMS). In
many states, the state-level Medicaid financing program accounts for the largest portion of the state budget. The health care industry can also be considered to include the large number of federal, state, county, and municipal agencies concerned with regulation of and reporting on the activities of hospitals, insurers, managed care organizations (MCOs), physician practices, and health care professionals. Do not forget the NFP organizations that accredit provider entities (Joint Commission on Accreditation of Healthcare Organizations or JCAHO, National Committee for Quality Assurance or NCQA). There are numerous associations representing the various health care professions, and others seeking cures for the most common diseases.

The professional management of all these organizations demands a strategic mindset and the preparation and execution of a strategic plan. Many of them face a form of competition that must be confronted in a systematic fashion. Government agencies compete with each other for a share of the overall budget and for the attention and support of taxpayers. NFP organizations fight constantly to win the hearts and minds of potential donors, either individual or institutional.

However, strategic action is about more than responding to the competition. It is necessary to constantly adapt the organization to the changes taking place in its external environment. Imagine how unsuccessful a hospital built in 1955 would be if it had made no adjustments during the wave of managed care that swept the industry in the 1980s and 1990s. In fact, many hospitals did not see the need for change quickly enough or lacked the resources to carry it out, and subsequently closed down or were acquired. Internal organizational changes also may drive strategic action. For instance, a medium-sized physician group practice may have depended for much of its past growth and reputation on a highly accomplished, well-known oncologist who has announced that he will be retiring within two years. Immediate steps will be necessary to either replace him (a daunting task) or strategically refocus the group.

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**PURPOSE OF STRATEGIC MANAGEMENT**

Every organization in existence is engaged in some current activities designed to create products or services for sale, delivery, or distribution to its customers, clients, patients, or beneficiaries. This is true for a pharmaceutical company selling its drugs to retail drug chains, a durable medical equipment (DME) manufacturer selling its parenteral nutrition pumps to managed care organizations, electronic medical record (EMR) system vendors selling their software and hardware solutions to physician group practices, an NFP hospital selling its clinical services to patients, a small biomedical research firm licensing its drug discovery patent to a...
large pharmaceutical company, an NFP health care advocacy group lobbying legislators on universal coverage for uninsured people, a municipal public health agency offering newborn immunizations to residents of low-income neighborhoods, or a state Medicaid agency providing health care coverage to medically needy disabled adults. The willingness of the customers to accept, demand, receive, or pay for the goods and services can shift over time—as a result of changes in their desires and preferences or the availability of superior product and services from competing organizations.

An organization employs strategic management to continually adapt itself to these changing circumstances. The adaptation may involve altering virtually any aspect of the organization’s operations—the products and services it creates, the way in which it creates them, and the customers to whom it offers them.

The organization generally makes these adjustments for any of three reasons:

• to satisfy and reward its stakeholders,
• to pursue and fulfill its mission, and
• to survive.

In the case of a profit-driven corporation, the primary stakeholders are the equity shareholders, the legal owners of the corporation, and the lenders and bondholders, sources of debt capital. If corporate performance does not deliver the performance expected by these groups, they will be reluctant to provide the capital the organization relies on to fund its operations and strategies.

In the case of an NFP corporation, the stakeholders receiving the greatest attention are charitable contributors and the debt capital providers. The performance results sought by the two groups are different. The lenders and bondholders want to feel secure in the principal and interest payments on their loans, just as debtors for FP corporations do. The donors give money in support of a defined cause or mission, and they wish to see it carried out as fully as possible. If either group is dissatisfied with the organization’s performance, it can withhold its funds.

The key stakeholders of public entities like government agencies are the general population of the jurisdiction in which they operate. The citizens’ wishes and expectations for agency performance are interpreted by the legislative and executive branches of government, which provide funding and direction. Citizens’ unhappiness with that performance can lead to reductions in funding and, in extreme cases, dissolution of the agency.

All of these organizations must keep their primary stakeholders uppermost in their minds as they constantly manage and adjust their operations. In order to satisfy its stakeholders, an organization must engage itself in some focused undertaking, rather than a set of random, aimless activ-
This enterprise is defined as the organization’s “mission”—its reason for existing and operating. The mission provides the contextual basis for the organization’s strategies. The operational adjustments that they entail are designed to keep the organization’s resources, activities, and efforts focused on the mission. Many equity shareholders and debtors of for-profit corporations are not particularly concerned with what the mission is as long as it is pursued competently enough to provide them with the rewards they are seeking.

Beyond the rational strategy motives of pleasing stakeholders and carrying out a mission, most organizations are also driven by an almost primal impulse simply to survive. Even when stakeholders have given up and the mission has become untenable, some organizations struggle to keep going. An example is a community hospital in a small city, most of whose patients have been redirected to a larger teaching hospital in a city twenty miles away. The local residents prefer the convenience of a nearby hospital, but the revenues are insufficient to support it. In a strictly rational health care system, this hospital would not continue to operate. Yet, almost everyone associated with it—board of directors, managers, and employees—will go to great lengths over a number of years to try to keep it alive.

Even if an organization faced no competition at all, it could count on the world around it changing—both the internal and external environments. New laws are enacted (Health Insurance Portability and Accountability Act, or HIPAA), consumer demographics shift (aging, ethnicity), a key employee retires (researcher, physician, executive). It would be necessary to implement strategies to make appropriate operational adjustments to accommodate these changes (new compliance policies and procedures, additions to and deletions from product and service lines, new hires and redefining job assignments). It would be imperative that these adjustments be made with all due haste, but the pressure to do so would not be extreme.

Virtually every organization also must deal with some kind of competitors. Competition is an accepted feature of corporate life for profit-driven organizations. A good example is pharmaceutical companies vying with each other to sell their individual variations of a drug to treat particular diseases. NFP corporations also engage in competition. It is not uncommon for FP and NFP hospitals to coexist and compete in the same markets; the same is true of managed care organizations. Competition occurs even when all the providers of a product or service line in a given area are NFP. In Boston, three major teaching hospitals, Brigham and Women’s Hospital/Massachusetts General Hospital, Beth Israel Deaconess Medical Center, and Tufts–New England Medical Center compete vigorously with each other and with several smaller NFP hospitals. Even public government agencies may engage in a form of competition—not
so much for customers, but for the attention of legislators and political leaders.

In addition to their competition in the marketplace for customers, organizations also engage in a different form of competition in the marketplace for financial capital. Equity investors buy shares of stock in companies whose financial performance meets their return on investment (ROI) criteria. Money lenders make loans to, or buy the bonds of, FP and NFP entities with high credit ratings that ensure their ability to make interest and principal payments. Wealthy citizens and charitable organizations make donations to NFP organizations that are doing the best job of supporting a cause that they value. Legislators appropriate tax revenues for the budgets of government agencies whose work meets the needs of their constituents.

The way that an organization succeeds in the competition with its rivals is by doing something that gives it an advantage in the eyes of the consumers of its products and services, and the sources of its capital—a “competitive advantage.” An advantage is not worth much if it lasts only a few weeks. Ideally, an organization wants to create a “sustainable competitive advantage” that will persist for as long as possible, at least months if not years.

If an organization is going to achieve an advantage over its rivals, it will come through things that it does—the activities performed by its employees. The organization will gain no advantage if it does exactly what its rivals do—creating the same products and services by the same methods, distributing them through the same channels, and selling them at the same prices. Instead, an organization must distinguish its activities from those of its competition. It has three generic choices:

- It can perform activities that are different from its competitors’ activities.
- It can perform the same activities as its competitors do but in different ways.
- It can perform the same activities at lower cost than its competitors.

The purpose of formulating and implementing a new strategy is to engage the organization in performing activities that are different from those of its competitors in at least one of these three ways.

### LEVELS OF STRATEGY

Good managers observe their competition all the time and speculate on what particular strategy those organizations are following. In fact, strategic planning and management may be occurring at three or more different levels in an organization. It will look like a cascading hierarchy of strategic
initiatives that build and depend upon each other. Ideally, each level fits into and is guided by the one above it.

Corporate or Organization-Wide Strategy

The highest-level strategy work encompasses the entire organization. The scope and nature of that work is a reflection of what the organization does and how it is structured to do it. Consider the Hospital Corporation of America (HCA). At the end of 2006, HCA was composed of 179 hospitals and 104 freestanding surgery centers in 21 states. During 2006, HCA reorganized those nearly 300 facilities into East, West, and Central groups.

Strategic activity at this level is concerned primarily with managing the portfolio of businesses and groups of businesses that compose the corporation and securing financial capital for allocation to them. It may also define the values that will be practiced throughout the organization, provide varying degrees of direction to the specific strategies adopted by the groups and facilities, facilitate the sharing of resources and capabilities among the groups and facilities, and offer strategic support services to them. Corporate-level strategy is explained in greater detail in Chapter 7.

Strategic Business Unit or Product/Service Line Strategy

Most companies start out—or start up—by offering a single product or service within a single market. If the product or service is well received in the marketplace, the company will thrive and grow. Many businesses continue operating in this fashion, at this scale (one or a few products in a single market), for many years. As long as their stakeholders are satisfied and they are not overwhelmed by competing businesses, there is nothing wrong with this approach.

At a certain point, however, in order to maintain the growth, increase returns to stakeholders, and resist competitive threats, the company will take steps to diversify and expand into other products or services and other markets. Eventually, the company will conclude that it cannot direct the operations and strategies for multiple products competing in multiple markets with a single management team. It will reorganize itself (or actually organize itself for the first time), at first perhaps into several distinct, though not autonomously governed, product or service lines managed by separate sets of managers. The product/service lines often then evolve into strategic business units (SBUs) with significant degrees of autonomy. Each is run by a strong management team that reports to a relatively small corporate headquarters office. Together, the SBUs make up the parent corporation’s “portfolio.”

These original SBUs are the results of internal development within the corporation. Further along the corporation’s strategic path, it may choose to add SBUs to its portfolio through acquisition or merger.
An SBU is distinguished by several features.

1. It serves a discrete external market or market niche different from that of any other SBU.
2. It offers unique product or service lines that are different from those of any other SBU.
3. It is usually a separate structural component of the parent company—a division, group, subsidiary, or department.
4. It is operated as a profit center by the parent company, meaning that the SBU has its own mission, objectives, and strategies and its management is responsible for bottom-line performance.

Strategy at the SBU level is explained in greater detail in Chapter 8.

Functional Area Strategy

Each SBU is further subdivided into functional areas, which make their individual specialized contributions to the unit’s operations and strategic initiatives. Traditional functional areas include marketing, manufacturing or production, research and development, human resources, and finances. The functional areas found in a hospital are more likely to be something like medical staff departments (specialties like medicine, surgery, and obstetrics and gynecology), nursing, ancillary services (radiology, clinical laboratory, and pharmacy), support services (medical records, housekeeping, and food service), financial (admitting, billing, and claims filing), and legal (compliance, payer contracting). Sometimes, every SBU will contain all the necessary functional areas for it to carry on its operations. It may have all the characteristics of an independent, freestanding business, except that it is not a separate legal entity and relies for investment capital on its parent. Alternatively, certain of the functions may be provided by the parent for all the SBUs in its portfolio. For example, a hospital that is offering and marketing a unique package of women’s health services will rely on the food service, claims processing, radiology or pathology service, and pharmacy service functions used by other clinical areas of the hospital.

Word Usage Note: Throughout this book, the term “corporation” will always refer to a for-profit entity composed of multiple SBUs. The terms “business,” “company,” “firm,” “entity,” and “organization” will be applied, depending on the context, to individual SBUs, independent freestanding units, and any other type of strategy-making legal structure, either for-profit, not-for-profit, or public. Where the text discussion is relevant only to one type of organization (say, for-profit rather than not-for-profit), that will be made clear.
These functional areas frequently will prepare and execute their own strategic plans that support the strategies of their respective SBUs. These plans are the responsibility of the departments and workgroups that make up the functional area.

STRATEGIC THINKING OR STRATEGIC MINDSET

Do you have a “strategic mindset”? Can you think “strategically”? It is not surprising that these qualities are common, virtually mandatory expectations of executives as they rise higher and higher in an organization.

Strategic thinking is an ability constantly to view an organization’s operations, issues, and problems in a very broad situational and environmental context and with a very long time perspective. A department manager with a strategic mindset will, while thinking about the challenges in the department, keep in mind their impact on other departments and the overall health of the organization. In determining the causes of problems, the manager also will look outside the department and even outside the organization, to customers, competitors, and the entire external environment. This attitude, this mental outlook, is a form of “systems thinking” that recognizes the interconnections between a project or problem in a single department and many other people, departments, organizations, and environmental forces.

A strategic thinker also constantly projects his understanding and analysis of issues well into the future. She may be measuring the effects of actions occurring now on events three or four or more years from now.

It is not an easy task to contemplate simultaneously an almost infinite number of influences and dependencies on the problem at hand, as they transform and evolve over years. Furthermore, this ability does not occur naturally in most people and frequently requires rigorous development.

In the explanations about why managers, with their MBA degrees, and physicians, with their MD degrees, clash so often when they must work together in hospitals and managed care organizations, the point is often made about their very different professional mindsets. The physician is trained to concentrate his attention on the patient in front of him and to mobilize all available resources to resolve the patient’s medical problems in the shortest time possible. The ultimate measure of success is clinical outcomes. The value of this training is particularly obvious in the emergency department or the operating room. The manager is trained to think about markets composed of thousands of customers, the coordination of numerous functional areas and departments, the threats posed by competitors, and the long-term future of the organization. The ultimate measure of his success is fiscal outcomes. This perspective reaps its greatest
rewards when preparing annual financial statements, meeting with Wall Street analysts, or trying to impress shareholders.

It is not surprising that people with such different work culture backgrounds would be in conflict. However, it is also true that many managers never truly develop a strategic mindset. In the lower echelons of the organization, supervisors and junior managers must focus almost exclusively on the current operations within their organizational scope of authority—a department, an office, a task force, or a unit. Their sole responsibility is to keep that component operating as smoothly and efficiently as possible on a day-to-day basis. They are not expected to think strategically and normally do not have the time to do so.

As managers are promoted through the organization, their duties take on an increasingly strategic nature. They become less concerned with the short-range, routine operations of a particular department and look further into the future, to other units within the organization, and outside the organization to forces in the external environment. By the time a manager reaches the position of CEO, she spends her entire working day on strategic issues. The shift in work focus from operational to strategic could be pictured as shown in Figure 1.1.

It is a challenge not only for individual mid-level managers but also for the organization as a whole to find an appropriate balance between current operations and long-term strategy. The actual work of a health care organization is carried out in the present: treating patients, filling prescriptions, performing diagnostic tests, researching new drugs, and processing claims—the multitude of activities that fulfill its mission. The purpose of strategic thinking is to prepare the organization for the actual work that it will carry out in the future and move it toward realization of its vision. The work activities that provide value to stakeholders (like
customers and shareholders) today may not be the activities that do so two or three years from now.

**INCREMENTAL VERSUS REVOLUTIONARY STRATEGY**

Formulation and implementation of a new strategy is a statement that an organization intends to make some sort of change in its operations. The change can vary greatly in the extent to which it is a departure from the current state of operations. The degree of change can range along a continuum from incremental to revolutionary. For instance, a physician practice may decide to begin introducing its patients to alternative medicine options. A modest, incremental first step would be to place literature in the waiting room describing acupuncture, yoga, and herbal medicine. At the more revolutionary extreme, the practice could hire an acupuncturist and a yoga teacher, and start promoting itself as a holistic healing center. Strategy planners must be conscious of how much they are asking of the organization and its people; it has implications throughout the strategic management process.

- An incremental change is more likely to be carried out satisfactorily; revolutionary change may stir greater resistance that slows or prevents success.
- A revolutionary strategy may be necessary to give the organization a breakthrough in gaining a sustainable competitive advantage over its competitors. To be incremental when a revolution is called for could be a mistake.
- In contrast, a well-conceived incremental strategy that leverages a unique resource, competence, or value activity may be more effective than a dramatic, high-risk, mistargeted revolutionary strategy.
- The type of strategy must be consistent with an organization’s culture. A firm with a tradition of risk avoidance probably should not attempt a revolutionary strategy.
- The chosen strategy type must be backed by sufficient resources, particularly financial. A revolutionary strategy may require more working capital to sustain it until the strategy succeeds and finances reach the break-even point.

**INTENDED VERSUS ACTUAL STRATEGY**

Books on strategic management sometimes make it seem like a pretty cut-and-dry process. An organization does a nice, thorough job of examining itself, its markets, and its competitors and uses its best judgment in formulating a few good strategies. If it can implement them properly, most
of them will be successful and produce something close to the intended results. In practice, it rarely works that way.

What happens is that even with a deliberate, structured, and forceful strategy-making process, other factors come into play that can produce different outcomes.

- Assumptions about the external environment, including competitor actions and customer preferences, cease to be valid due to unanticipated changes. Management decides that it no longer makes sense to proceed with the strategy, or it chooses to make significant modifications in the strategy.
- Strategic support that was expected from important stakeholders, such as suppliers, investors, or legislators, is not forthcoming. The strategy must be cancelled or overhauled.
- If strategies are implemented at all, it is through many small routine actions, decisions, and behaviors on the part of individuals and sub-units within the organization. Most of the time, these activities are carried out without the close oversight of a strategist and without close attention to the strategic plan. Nonetheless, they can have the cumulative effect of subtly moving the organization in a definite strategic direction. That direction may be a little bit or a lot different from the intended direction.
- One of the most influential lower-level decisions in shaping an organization’s strategic movement has to do with the allocation of resources. There is always competition among individuals, projects, programs, and departments for the limited amounts of money, space, time, equipment, personnel, and influence available. The way those resources are distributed may not follow the strategic plan closely or at all. However, they do contribute unintentionally to a strategic momentum.
- All organizations are characterized by a unique collective personality or “culture,” often described as “the way things are done around here,” an undocumented set of values, customs, beliefs, and habits. When employees need to act and make decisions under the conditions of uncertainty and ambiguity that prevail in rapidly changing environments, they often instinctively fall back on traditional patterns and practices that they know best. Unconsciously, that can create its own strategic direction.
- Strategies are carried out by people and, wherever people come together to work toward a common end, internecine politics come into play. Rather than the result of a dispassionate, objective dialogue, strategy often is determined by biased, passionate bargaining. The participants bring different educational backgrounds, professional cultures, experience bases, and values and mindsets to the
negotiations. Their hidden agendas may be to protect a personal power base, enhance a department’s status, increase a budget, or simply protect and maintain traditional practices. The strategic welfare of the organization may be a secondary consideration.

The net result of these forces is that several different kinds of strategy development paths can occur within an organization. First, there is the strategy intended by the planners and executives. It is based on careful analysis of prior history, current circumstances, and projected future developments. It is a description of how the managers would like things to turn out in an ideal world. Then there is the implemented strategy, the one that the firm puts into operation. Because the implementation is not well conceived, does not receive the necessary resources or attention, or is not competently executed, the resulting strategy can be significantly different from what was intended. In the end, the actual strategy that is pursued and impacts the marketplace can be even more at variance with the original intention. This may be due to changed environmental conditions, customer preferences, or competitor behaviors. There is also a category of strategies that simply “emerge” or develop without much prior planning in the course of the firm’s operations. These emergent strategies may be conscious, spontaneous responses to new opportunities or threats that show up in the normal course of events, after the formal strategic plan has been prepared. Sometimes, they arise almost unconsciously as managers and employees make instinctive, often small adjustments to subtle shifts in the world around them. Finally, there are the planned and intended strategies that never actualized. Changed circumstances or failed assumptions may render the strategy irrelevant, or the organization may fail to implement the strategy competently or at all.

STRATEGIC PLANNING AND MANAGEMENT PROCESS

Traditionally, the process of making business strategy was described as strategic planning and management (SPM), or even simply “strategic planning.” Those phrases are significant. One of the most daunting parts of the process is the preparation of the strategic plan. It often receives such a disproportionate share of corporate attention and energy that the management step is overlooked or never really carried out. In fact, it might be better to use the term “management” to describe the entire ongoing process of directing an organization’s available resources and competencies in the preparation and execution of strategic plans that move the organization closer to achievement of its chosen vision. It is important to be clear about the full range of tasks that go into making successful strategy for an organization.
These are the fundamental steps in the process. They may be referred to by different names. They are rarely performed sequentially, one after the other, fully completing one step before moving on to the other. Some steps may be carried out simultaneously or jointly with other steps. Some organizations may prefer to reorder the steps slightly, putting one later or earlier in the process. Each organization tends to develop its own unique way of making strategy. What is important is that certain strategic management activities are performed; how they are structured or designated is less important. These steps are explored more fully in the remaining chapters of this book.

Mission—what the organization is doing right now.
Vision—what the organization wants to be doing five or ten years from now.
Values—behavioral principles which employees will follow in performing their duties.
Grand strategic objectives—a few, broad organization-wide thrusts that will move it toward its vision.
Specific organization-wide strategic plans (at corporate and SBU levels)—complex, systematic, expensive, long-term programs for achieving the strategic objectives.
Benchmarks, metrics, targets, goals within those plans—standards by which strategic plans and performance are judged.
Functional area strategic plans—coordinated plans in support of the organization-wide strategic plans.
Action plans—more detailed, shorter-term sets of activities designed to carry out the organization-wide and functional area strategic plans.
Implementation of strategic (corporate, SBU, and functional area) and action plans—actual performance of the steps and activities described in the plans.
Monitoring and adjustment of plan implementation—constant measurement of plan progress coupled with appropriate fine-tuning.

**STRATEGIC DIRECTION**

If strategic planning and management is about moving an organization in a rational “strategic” direction, how does the organization decide what that direction is? Can it go in two or more strategic directions at once? How many possible strategic directions are available to a particular organization? When an organization decides on a strategic direction, how does it describe it? Where is it found in the organization’s documents? Do you
know what the strategic direction is of organizations for which you have worked?

It is possible for a business to implement very successfully a strategy that does not move it one bit closer to realization of its vision. In fact, the strategy may move it farther away from that vision. The business may be better off with no strategy than one that is misdirected (Figure 1.2).

Quite often, a business will be in the process of implementing five or six distinct strategies at one time. Ideally, they should all work in unison to move the business along a desired path. Without careful thought, it is easy for strategies to conflict with one another and reduce their respective chances of success (Figure 1.3).

The penalties for pursuing strategies that are not aligned with some vision for a future state are that the business never arrives at a place that it truly wants to be. It never accomplishes goals that have been chosen deliberately by its executives and managers. For all its efforts, the business does not deliver optimal value to its stakeholders. In the process, it wastes financial resources, human energy and focus, and the most valuable commodity of all—time. Ultimately, for all these reasons, it may fail as a competitive entity.

Every forward-looking organization must define a strategic direction for itself. That is traditionally accomplished through the preparation of four documents or statements: a mission, a vision, a code of values, and
a set of a few long-term strategic objectives. The content of these statements and their method of preparation are explained in Chapter 6.

### HOW ORGANIZATIONS BENEFIT FROM PRACTICING STRATEGIC PLANNING AND MANAGEMENT

A great many benefits accrue to organizations that practice SPM. Most would not be as successful as they are without it. Some examples include:

- By engaging in SPM, an organization is taking an aggressive, proactive approach to maintaining and growing its operations. This is in contrast with organizations that simply let things happen to them and try to react as best they can. This constitutes an active versus a passive approach to an organization’s welfare.
- No one can accurately predict the future. Some organizations let the future happen to them, others make an effort to influence their futures, but SPM is a powerful tool that helps organizations actually create the future that they most desire.
- The plan and its execution increase the likelihood that the organization will actually arrive at that desired future, the place where it wants to be.
- The process of preparing a strategic plan forces the organization to develop a clearer sense of its strategic vision. In fact, when organizations begin doing strategic planning, they frequently realize for the first time that they can and should have a strategic vision.
- The motivating effects of a well-founded strategic initiative with carefully gauged “stretch” goals result in higher levels of organizational and individual achievement than would be possible under “status quo” operations.
- The preparation of a strategic plan and the management of its implementation require that an organization focus on what is strategically important. It is easy to become so immersed in the tactical and operational details of running an organization that one loses sight of broader, longer-range concerns like strategic direction.
- To prepare a meaningful strategic plan and keep it relevant, an organization is compelled to acquire a better, more comprehensive understanding of its environment. This is particularly critical when that environment is evolving rapidly—as it is in health care and the biotechnology field.
- Every organization—for-profit, non-profit, or government—is limited in the resources that it has to carry out its current operations and plans for the future. The resources include money, people, space, skills, time, and commitment. Common sense says that the
organization that employs its resources more efficiently will do better than the organization that is sloppy and wasteful in its resource utilization. The discipline of SPM allocates resources to the activities that contribute most to the organization’s mission, ensuring the most efficient use of those scarce resources.

- The existence of a strategic plan coupled with organizational commitment to its implementation stimulates and energizes the people carrying out the strategy. A strategic plan provides a greater sense of purpose to their work that goes beyond their routine operational duties. It often shows the way that employees can satisfy their personal goals through achievement of the organization’s goals. A plan can be a powerful motivating force.

- The strategic planning and implementation process encourages imagination, innovation, and forward thinking in response to an ever-changing external environment.

- A well-conceived strategic plan establishes metrics for success that can be used to plot and evaluate the progress and performance of the organization and its people. The objective, time-limited goals in a strategic plan may be incorporated into pay-for-performance compensation schemes.

- The effect of a well-executed strategic plan is to orchestrate and synchronize the efforts of disparate people and units scattered throughout the organization. This results in higher levels of achievement than would be possible without a coordinated, inspired focus on the future.

- The future is an unpredictable, sometimes scary place. Strategic planning and management secures a desirable future for the organization and its stakeholders.

■ HOW STRATEGIC MANAGEMENT GOES WRONG

Strategic thinking and the practice of strategic management do not come naturally to many senior managers. It is not surprising, therefore, that their efforts to make strategy sometimes run into problems that limit their effectiveness. When that happens, both they and the entire organization can become disaffected from the process. It is worth anticipating and preempting problems.

*The firm takes a passive reactive approach to external events, rather than an aggressive proactive one.* Organizations with a passive, almost submissive attitude about the world in which they operate frequently do no strategic planning at all. When they do embark upon strategic initiatives, they are often reacting impulsively to a development in the general environment or a threatening move by a competitor. In the latter case, the
firm is allowing a competitor to dictate its strategies. An essential element of strategic management is the desire of an organization to take charge of its future, to do all that it can with its resources and capabilities to carry out its mission.

The strategic plan is created at the top of the organization and handed down without further input from other parts of the organization. Sometimes, a special strategic planning unit handles most of the preparation before handing the plan off to senior management for approval. This approach misses out on two opportunities. First, many people throughout the organization can provide valuable inputs to the planning process based on their contacts with customers, suppliers, competitors, and other stakeholders in the course of their day-to-day work. Their knowledge and opinions help ensure a plan that is responsive to its environment. Second, it is the masses of employees below the level of senior management (and the strategic planning unit) that will be responsible for carrying out the plan. Experience shows that they will implement the plan more effectively and enthusiastically if they have been involved in its creation. The importance of their participation cannot be overestimated.

Management fails to build a consensus around the plan before trying to implement it. Even if senior management insists upon creating the strategic plan entirely within the executive suite, optimally effective implementation depends on some degree of buy-in from other employees and other stakeholders who may have a role to play. If these people were not involved in the formulation of the plan, an aggressive effort should be made to “sell” it to them and solicit their support. This usually requires numerous small-group meetings throughout the organization, including extensive Q&A, as well as a willingness to make some adjustments to the plan in response to feedback received.

The strategic initiative begins and ends with the plan; little attention is given to actual implementation. This sometimes happens because the managers involved exhaust themselves in the planning activity and have no energy left to do the things necessary to put it into effect. They also may not understand the additional steps required—breaking down broad goals into narrower actionable tasks, setting time deadlines for completion, delegating primary authority to specific individuals, allocating appropriate resources, constantly measuring progress, and making small and large adjustments. The plan may be broadcast to the organization and its execution left to employees who are more concerned with their immediate operational tasks. The strategic plan is forgotten.

The planning process gets stuck in “analysis paralysis.” There is an infinity of information that can be gathered about an organization, its customers, its competitors, and the general environment. It is easy to get so lost in data collection and analysis, always seeking just one more report or making just one more calculation, that the plan is never completed, let
alone implemented. Experienced strategists know when to halt the quest for greater knowledge and precision and move on to translating the information at hand into actionable plans.

The organization follows the plan unquestioningly throughout its term, which may be as long as five years, despite substantial changes in the organization’s external and internal environments. By the second or third year, the assumptions on which the plan is based may be invalid and its objectives no longer relevant to the organizational mission. Instead of moving the organization closer to its desired future, the plan may have moved it further away and wasted resources in the process.

Because of low risk tolerance and a fear of failure, the strategic planners set modest, unambitious goals. A good strategic plan stretches the firm and its people. How far depends on the industry in which the firm competes. When the competition is particularly intense, when the external environment is changing rapidly, bold, even audacious strategy is called for. These are the conditions that currently prevail throughout the health care industry. Undemanding strategic goals are less likely to capture the imagination of employees; they will be less motivated to work toward achievement of the goals. As a result, the firm may fall behind the competition and fall behind in pursuit of its vision.

There is a lack of top management support for the strategic planning and management effort. In most organizations, initiatives with far-reaching agendas like strategic management do not go very far without the explicit support of managers at the highest level. Their apparent disinterest sends an implicit message to employees and other stakeholders that the organization does not intend to engage systematically with the competition or its own future. If senior managers responsible for the long-term future of the firm are not enthusiastic about strategic thinking, employees responsible for carrying out any plans that emerge will be no more motivated.

Strategic planning is conducted separately from or totally without functional area planning. The practical details of implementing a strategic plan are laid out within the functional areas of an organization (e.g., marketing, production, clinical services, finance). The area managers should be consulted during the planning process to be sure of their ability to carry out the plan’s directives. It is most critical to involve those managers familiar with the firm’s access to the financial resources called for by the plan. It is not uncommon for each functional area to back up the overall strategic plan with a strategic plan of its own.

The plan fails to address crucial strategic issues because they seem too difficult or too numerous. As a firm analyzes itself, its markets, competitors, and the general environment, a few especially critical issues will emerge. They may be based on a competitor’s announced new strategic initiative (e.g., local teaching hospital will build a new women’s health center), changing demographics in the market area (e.g., population aged
25–34 is declining), or proposed new state legislation (e.g., state governor backs a plan for statewide universal health coverage). A responsible strategic plan will acknowledge such issues and offer some response. Management may choose not to because either it does not fully comprehend the issues or there seem to be too many to cope with. It is better to make a mediocre attempt to answer the challenge than to ignore it. If the number of critical issues is overwhelming, some probably are not as critical as others and the list should be prioritized.

The strategy implementation phase lacks flexibility and responsiveness to subsequent changes in the environment. A well-researched strategic plan is based upon the best possible projections of how competitor and customer behavior are likely to evolve in the future, and of events and trends likely to occur in the general environment. Many of the plan assumptions will turn out differently, sometimes so much so that the strategies, as originally conceived, are no longer relevant. In some cases, they may be rendered counterproductive. An essential piece of strategy implementation is the ongoing monitoring of conditions that might impact the strategy, coupled with a willingness to make minor or major compensating adjustments in the strategy itself. It would be a rare strategic plan that, two or three years into its implementation, did not have to be radically altered. This is particularly true in the tumultuous health care and biotechnology industries.

The plan does not address or focus on the most critical issues. The plan is a thoughtful, well-structured document that is implemented with great effect. The problem is that it does not tackle some of the core strategic issues facing the organization. Some of them may be too difficult or too painful to even think about, so they are bypassed in favor of less-stressful, less-perplexing issues. In contrast, in an attempt to be thorough, the plan may attempt to cope with far too many issues. They cannot all be critical. The result is that none of them, including those most important to the business’s future, get the attention and the resources they deserve.

#### BARRIERS TO STRATEGIC MANAGEMENT

If SPM is such a good idea, why do so many organizations fail to practice it? These are some of the reasons.

- Organizations have poor reward structures, no positive reinforcement. Businesses do not formally recognize success in performing strategic planning and management. Some might not even be able to define “success” at the strategic level. If a firm is aware of when it has succeeded strategically, managers do not notice the people who contributed to the success. And, if managers can see that some
people are making a difference in moving the firm into the future, they simply do not reward them, monetarily or otherwise for their efforts. There are no incentives for spending time on strategic matters or doing well at them.

- Organizations are focused on operational or tactical activities or, even worse, on crisis management. Historically, the management of
health care organizations, most of them not-for-profit in noncompetitive environments, was concerned exclusively with relatively routine operational matters. Some managers have never made the transition from that more benign milieu to the current industry situation that demands constant attention to markets, competitors, and the future. Health care management, in general, has become more complex, more intense, and more demanding. It is easy to get so caught up in trying to keep a hospital or a physician practice running on a day-to-day basis that there seems little time left to indulge in the luxury of long-term thinking and planning.

- Organizations fail to appreciate the delayed link between strategic planning and management efforts now and concrete operating results in the future. In a culture constantly seeking immediate, certain gratification, and in businesses with predominantly short-term horizons, strategic management has two unpopular aspects. It is concerned with creating effects in the future and, because it is impossible truly to predict the future, those effects are uncertain. The subjects of strategic decision-making are dealt with on a timescale measured in years. Decisions made today will produce changes so far in the future that some people lose patience and interest. Under such conditions, engaging in strategic management seems pointless.

- If an organization has no prior experience with strategic management, at least some of its members will have to acquire new skills and comprehend new concepts. A few people must develop the ability to think strategically. For those nearly overwhelmed by their current responsibilities, there is no desire to make the effort to learn.

- When an organization feels that it is doing quite well currently, and perhaps has been successful for a number of years, there may be a tendency to believe that it is doing all the right things. Strategic management then seems superfluous. The firm’s leaders are content with the way things are and assume that they will never change. Or, they become overconfident in their ability to adapt and improvise in response to any challenges that may appear.

- At the other extreme, some executives believe that their organizations are operating in environments that are changing so rapidly that any attempt to look and plan ahead will be made irrelevant by unanticipated circumstances and conditions. An attitude like this would not be surprising in the turbulent climate of today’s health care industry.

- Managers have had unhappy prior experiences with strategic management. It is possible that managers in health care have worked previously for organizations that did practice some form of strategic
planning. However, the experience may have been so dysfunctional, unpleasant, or nonproductive that they assume that all strategic management initiatives are similar and avoid repeating them.

- Some managers without prior experience or education in strategic planning and management believe that it can or should offer a 100 percent probability of success and, when they learn that the outcome cannot be ensured, refuse to engage in the process at all.
- By definition, strategic management sets out to create fundamental changes in an organization structure or operations. A few managers with a vested interest in the status quo may fear the loss of money, status, or power, and will purposely avoid strategic management and even attempt to sabotage the process.

For all these reasons, organizations choose not to invest the time, the money, or the personnel that even a modest strategic planning effort would require.

### FOCUS ON THE HEALTHCARE AND BIOTECHNOLOGY INDUSTRIES

The scope of this book is the planning and management of strategy in particular industries—those associated with the delivery and financing of health care in the United States. The term “health care” is interpreted in its broadest sense to include the following, among others:

- Managed care organizations
- Health maintenance organizations
- Preferred provider organizations
- Independent practice associations
- Solo physician practices
- Small group practices
- Large group practices
- Academic physician practices
- Multi-specialty group practices
- Teaching hospitals
- Community hospitals
- Specialty hospitals
- Integrated delivery systems
- Health plans
- Health insurance companies
- Community health centers
Taken together, these industries account for expenditures approaching one-fifth of the gross domestic product of the United States.

There are several reasons for devoting a book to an explanation of the practice of strategic planning and management by organizations in these particular industries. The strategic challenges that they face and the competitive milieu in which they operate are strikingly different from those in other economic sectors. In few other industries do federal, state, and local government agencies play so significant a role through regulation, financing, and direct service delivery. In few other industries are the choices of which products and services to buy, the payment for those products and services, and the consumption of those products and services carried out by different people. More than in any other industry, the structures, products and services, practices, and costs of health care and biotechnology are the subject of close scrutiny and constant debate by the media, politicians, scholars, executives, professionals, and members of the public. Even though many of the strategy concepts and principles are generic, it is more useful to explain them in terms and contexts familiar to the health care and biotechnology executives who must employ them.

### ENVIRONMENTAL FORCES THAT AFFECT STRATEGY-MAKING IN THE HEALTHCARE AND BIOTECHNOLOGY INDUSTRIES

It is worth acknowledging some of the significant forces in the external environment that influence the strategies that health care organizations choose to adopt—or are virtually compelled to adopt if they wish to survive. These forces are present in every area of the organizations’ external environment. Because of the constant ferment in the health care industry, some of these forces may weaken or disappear completely within a few years while others will become stronger and more influential. New environmental forces with impacts on health care strategies will emerge. The process of assessing and monitoring a firm’s general external environment is discussed in Chapter 3.

**Legislative/Political.** At both the federal and state levels, legislators are introducing bills designed to provide various forms of universal health
care coverage. It is particularly noteworthy that a number of states have seized the initiative to create individual statewide universal plans. Some have been enacted and are being implemented. Many of the candidates in the 2008 presidential election, primarily on the Democratic side, are speaking openly about the need for sweeping national health care reform. Regardless of who is elected, proposals for significant changes in the financing and structure of the health care system are likely to be on the legislative agenda of the next administration. There will continue to be more regulation of health plan activity—concerning abusive treatment of patients or providers, disclosure of policies (denial of coverage, provider financial incentives), publication of prices for common services and procedures, mandated coverage of specific services, and protection of patient privacy interests. Ongoing legislative efforts can be expected to try to slow the steadily rising national health care budget.

Economic. Though the rate of growth waxes and wanes, the national health care budget continues its inexorable climb. Although more money available for spending on health care might seem like a good thing for health care organizations, the trend also increases the likelihood of more limitations on reimbursements under Medicare and Medicaid because of their budget constraints.

Social/Demographic. The baby boomer cohort continues to work its way through the population, increasing the numbers of elderly requiring the expensive health care services that come with aging. Contributing to this trend is the slow, steady improvement in life expectancy of Americans. The ethnicity of the overall population and, therefore, prospective patients is becoming more diverse. The education level of the population also is increasing; this has special implications for the changing role of patients under “consumer-driven health care.” The income disparities within the population are growing, affecting the ability and willingness of patients to pay for their care. That trend is leading to a three-tiered system of access to care: privately insured patients, publicly insured patients (Medicare, Medicaid), and uninsured patients. Patients often experience forced mobility from one health plan to another, and from one provider to another, as employers change their mix of health plans and patients change their jobs. The proportion of the population that is either underinsured or completely uninsured increases steadily. There are critical shortages of nurses and primary care physicians, coupled with physician surpluses in certain geographic areas and in certain specialties.

Technological. The introduction of new clinical technologies that has typified the health care industry for at least two decades continues apace in areas like drug design, imaging, minimally invasive surgical procedures, genetic mapping and testing, gene therapy, and vaccines. The momentum is even greater for medical information technologies such as electronic medical record (EMR) systems, computerized physician order entry (CPOE)
systems, automated practice guideline prompts, integrated clinical/cost analyses to demonstrate cost effectiveness, electronic claims filing and processing, and telemedicine. For provider organizations, the availability of these new technologies offers strategic opportunities to gain competitive advantage although often at substantial costs. For the developers and vendors of these technologies, the markets for their products seem to have promising futures.

Industry (competitive). New models of drug discovery and development have created a major new industry composed of small and startup biomedicine and biotechnology companies that research products (often no more than one per firm) that are licensed or sold to major pharmaceutical companies for the ultimate market introduction. The trend of consolidation among health plans, among hospitals, and among group practices into networks and systems continues in response to unrelenting cost pressures and heightened competition. The principles of professional business management that are applied in most other industries are steadily working their way into the day-to-day running of health care organizations. Those businesses that embrace these concepts rather than resist them will reap the benefits sooner and gain at least temporary competitive advantage over their rivals. The principles are often first introduced by entities organized as for-profit corporations and their executives with prior experience in predominantly for-profit industries. The for-profit ethos is transforming managerial decision-making and organizational cultures in the health care industry.

Study Questions

1. If a health care organization, such as a hospital, carefully formulates and implements a strategic plan, exactly what differences can it expect to see in four or five years?

2. Try to describe the type of organization that would have no good reason for carrying out strategic management.

3. Under what circumstances should an organization attempt to execute a “revolutionary” strategy, and when should it be satisfied with “incremental” strategy?

4. Draw a diagram of the strategic planning and management process described in this chapter. Elaborate upon the process, inserting additional steps and sub-steps, and drawing lines to show the connections between the steps.

5. Do some Internet research on health care/biotechnology companies that have had substantial, public business problems in the last few years, and try to identify the possible strategic causes of those problems.
What apparent mistakes in either the planning or implementation of strategy led to the problems?

6. Choose a very large corporation in any part of the health care or biotechnology industries, and identify the individual SBUs that make up the corporation. What are the features that distinguish those SBUs from a department or division?

**Learning Exercise 1**

There is an organization that does research and development in the area of new drug discovery. It was founded four years ago and recently licensed the patent for its initial research output to a large pharmaceutical company. It is now in the very earliest stages of work on two additional research projects in related areas. Up until now, the decisions about the scientific focus of the firm’s research efforts have been made by the researchers involved. The patent licensing decision seemed like an obvious way to bring in the significant new financial resources that the firm now enjoys. However, there remains within the firm some general uncertainty about the future.

You have been hired as a consultant by the organization's board of directors to persuade top executives that strategic planning and management is a worthwhile pursuit. The executives have expressed some of the reasons described in this chapter for avoiding any strategic activities up until now. Think of a rational, constructive response to each of those barriers.

**Learning Exercise 2**

The purpose of this exercise is to design a simple instrument to help you determine whether another person is able to “think strategically.” Prepare a series of about ten questions that explore the various dimensions of strategic thinking as explained by this chapter. The answers to the questions may be brief open-ended essays, multiple-choice, assignment of scores or ratings, or anything else that seems appropriate. You may want to test it on a few classmates. When you have it in a final form, administer the instrument to people (friends, relatives, colleagues, coworkers) whose attitudes about strategy are unknown to you. On the basis of their answers, make a judgment about their ability to practice “strategic thinking.” How do you feel about the results that you have achieved? Does this exercise give you a better understanding of strategic thinking, either in yourself or in others?
References


