STRATEGY AND STRATEGIC MANAGEMENT

For the past decade, Texas Health has been executing a strategic plan called the Ascent to the Summit. As the organization nears the end of that climb with a stronger strategic footing in place, the THR Promise continues to unify and strengthen us as we move into a journey toward becoming a high-reliability organization transforming the way healthcare is delivered. . . . In the past decade, Texas Health has shifted from an acute care hospital company to an integrated health system. In 2009, Texas Health Physicians Group was formed, creating a base of employed physicians who work with Texas Health on numerous objectives. Today, the group includes more than 830 physicians, physician assistants, nurse practitioners, and medical professionals dedicated to providing safe, quality care for its patients. The Texas Health Physicians Group's primary care and specialist network represents more than 50 medical specialties, with more than 250 locations spanning 11 North Texas counties. . . . Because of our culture, Texas Health was recognized in 2015 as the number one healthcare organization to work for in the United States by *Fortune*. We also were recognized as the number two workplace for women and the number three workplace for diversity in the nation, with one-third of our nurses from ethnically diverse backgrounds. We're proud to say we reflect the diversity of the communities we serve.

—Barclay Berdan, 2016, "Climbing the Healthcare Summit"

Learning Objectives

After reading this chapter, you will

- comprehend that *strategy* has many definitions, and its meaning depends on one's perspective;
- understand the role of strategy in moving a healthcare organization to achieve its goals, increase its business, and improve its performance;
- recognize the use of prospective and emergent strategies; and
- be aware that business strategies evolve over time as a result of changing circumstances and managerial modifications.

Strategy—integral to all businesses and life today—has different meanings to different people. Academics and consultants have suggested many diverse definitions. Little agreement on its meaning can be found in the business world, and it has been notoriously difficult to define (Luke, Walston, and Plummer 2004; Murray, Knox, and Bernstein 1994). For some, strategy is developing a formal plan. For others, strategy involves crafting a process or means for outwitting a competitor. Yet others see strategy as a way of doing business, positioning an organization, and determining competitive differences from a prospective or an emergent viewpoint (Mintzberg, Ahlstrand, and Lampel 1998; Porter 1985). Strategy tends to be a bit of all of these perspectives in that it involves processes and end goals but also constant adaptation to shifting conditions and circumstances in a world dominated by chance and uncertainty.

This text focuses on the importance of strategic thinking and strategic decision making. As the Texas Health Resource story in this chapter demonstrates, strategy is critical for organizations. At its foundation, strategy is about organizing information better to make better decisions. This text examines the fundamental components of strategy and methods for its implementation from both theoretical and practical perspectives. Theory is important to understanding strategy; as the great German general Carl von Clausewitz (1976, 141) stated, "Theory . . . becomes a guide to anyone who wants to learn about war from books; it will light his way, ease his progress, train his judgment, and help him avoid pitfalls." However, theories can provide only so much guidance, as we live in a world of incomplete information and often-limited knowledge of our competitors' strategic intentions and purposes. Likewise, strategies frequently emerge from the unintended, almost accidental results of decisions, as our earlier decisions commonly restrict the path of our choices and impose policies and actions that leaders initially would not have chosen (Murray, Knox, and Bernstein 1994).

Theoretically, an organization's established mission and vision should drive strategy formulation. The organization should first define what business it is in and what it wants to become and then establish goals, objectives, and tactics to achieve its mission and vision. This prospective approach is common to management-directed strategic planning. From this point of view, strategy establishes a path and direction toward an end state or outcome. In formal prospective planning processes, leaders often elaborately analyze the environment, set goals, and lay plans to achieve those aims. The strategic plan becomes management's action plan for running its business and operations. A management-driven organization's strategy addresses

- how management intends to grow the business,
- how the organization competes and collaborates with other organizations,

- how the functional components of the business relate and coordinate with each other,
- which services and programs the organization will emphasize and allocate greater resources to relative to other projects, and
- what the relationships and culture among employees will be.

This book primarily takes this perspective and elaborates on methods for better understanding and articulating organizational influences, purpose, and direction. Strategy and strategic thinking are important for all types of organizations. The text applies general business strategies to healthcare and examines their application to this growing, critical field.

History of Strategy

Derived from *strategos*, the Greek word signifying the planning of a military campaign, *strategy* literally means "the art of the general." The concept of strategy has been discussed for thousands of years, primarily with respect to aspects of war. Strategy was refined and articulated to further military purposes. Military campaigns encouraged the training of leaders to win battlefield conflicts. Millennia ago, generals recorded their experiences so that they could pass on their wisdom. Some of the first recorded strategy instruction originated in China during the period between 500 BCE and 700 CE and included significant treatises on warfare. The most familiar is Sun Tzu's *Art of War*, which has become one of the most important books on military strategy (Sawyer 2007). Sun Tzu taught the importance of positioning in military strategy—establishing objectives based on environmental conditions and the subjective beliefs of one's opponents.

Centuries later in the Mediterranean, modern military strategy developed under such leaders as Philip II (382–336 BC), Alexander the Great (356–323 BC) of Macedonia, and Hannibal (247–183 BC) of Carthage. Philip II demonstrated how infantry, cavalry, engineers, and primitive artillery combine to form a trained, organized, and maneuverable fighting force. Later, Philip II's son Alexander and the great Carthage general Hannibal advanced military strategy by organizing open communication and supply lines, surprise tactics, better use of cavalry, and unity of command (Van Der Merwe 2002).

In 70 CE, Sextus Julius Frontinus, the Roman governor of Britain who subdued the hostile tribes in Wales, wrote a theoretical treatise on military science called *Stratagems*, which included a collection of examples of military strategies from Greek and Roman history. *Stratagems* did not exclusively denote acts of military ingenuity for the ancient Greeks and Romans but suggested a pattern of thinking to guide strategic behavior (Wheeler 1988).

The notion that strategy applied mostly to military warfare endured until the advent of the Industrial Revolution, when companies grew to a size that warranted more coordination and direction. In the early twentieth century, the need for explicit strategy was highlighted by executives at large companies, such as Alfred Sloan of General Motors and Chester Barnard of New Jersey Bell, who wrote about how to better organize and lead (Barnard 1968; Sloan 1963).

Today, strategy and strategic management are widely accepted. Courses about strategy are core in business schools, and strategic management is an integral part of leadership training. Teaching strategy can be a difficult task, involving both instruction on how to craft future-directed plans and, at the same time, development of intuitive insight and the ability to learn, adapt, and change (Burns 2002).

Strategy in Healthcare Today

The concept and importance of strategy expanded to healthcare in the 1970s. One factor motivating this expansion was the conversion of many hospitals and insurance companies, including health maintenance organizations, from not-for-profit to for-profit status. This change in ownership increased the level of competition among healthcare organizations.
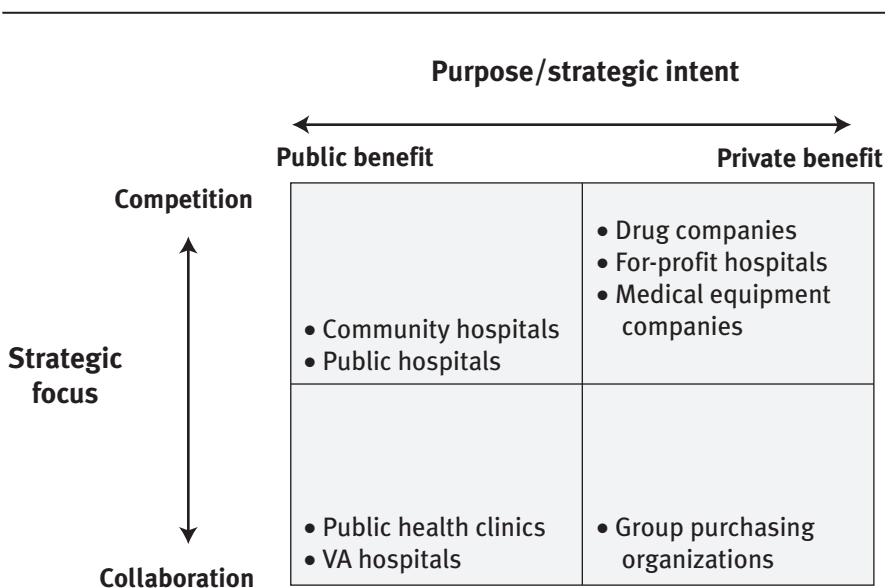
Stimulated by governmental reimbursement changes and incentives, many national for-profit hospital companies, including Humana, Hospital Corporation of America, National Medical International, and American Medical International, aggressively sought to acquire hospitals across the country. These acquisitions dramatically changed the nature and behavior of local healthcare delivery and competition. For example, private, for-profit hospitals accounted for only 6.3 percent of US hospitals in 1975 (Gray 1986). As corporations formed extensive hospital chains, this percentage increased and competition grew; today, private, for-profit hospitals account for about 21 percent of US hospitals (American Hospital Association 2016). Likewise, physician practice continues to evolve. In 2000, about 24 percent of physicians worked for hospitals or integrated delivery systems (Medical Group Management Association 2005). However, by 2015, 38 percent of physicians were employed by hospitals or integrated delivery systems (Physicians Advocacy Institute. 2016). As for-profit healthcare organizations became more prevalent and consolidation has occurred, the level of rivalry increased throughout the healthcare landscape, motivating organizations to adopt more competitive strategies.

Some maintain that there should be no difference in the application of strategic principles between the healthcare field and other sectors. While the general principles and techniques discussed in this book are relevant to healthcare, the field is distinct from many other sectors and a much higher

percentage of its organizations are created for community or public benefit (often referred to as *not-for-profit organizations*). This difference in purpose or mission does not lessen the importance of applying strategy and its principles but should motivate more cooperative strategies to achieve missions.

As shown in exhibit 1.1, the purpose and mission of a healthcare organization should influence the emphasis it places on competitive versus collaborative strategies. Competition involves the effort of two of more parties seeking the rewards of a certain fixed contest. For example, a race or sports event may involve two or more teams that seek to win the contest. Likewise, companies submit bids for construction or other contracts, and only one contractor wins the job. As the story in exhibit 1.2 explains, competition involves outperforming one's competitor, which sometimes creates negative consequences for at least some members of the community. However, the dominant purpose of strategy in general business has been to gain competitive advantage at the detriment of competitors (Denning 2013). A common competitive strategy is to attract market share from competitors and, if possible, drive competitors out of the market. As a result, the community's access to products and services constricts and costs often increase.

Cooperative strategies, on the other hand, build on synergies and community good. As discussed in chapters 5 and 6, many healthcare organizations are now seeking to collaborate through cooperative strategies. Cooperation better uses community resources by reducing duplication and allows separate organizations to contribute their best competencies to achieving strategic goals.

EXHIBIT 1.1
Healthcare Organizations by Strategic Intent and Focus

Purpose/strategic intent

Public benefit — Private benefit

	Public benefit	Private benefit
Competition	• Community hospitals • Public hospitals	• Drug companies • For-profit hospitals • Medical equipment companies
Collaboration	• Public health clinics • VA hospitals	• Group purchasing organizations

Strategic focus

EXHIBIT 1.2
The Difference
Between
Competition and
Collaboration

A salesperson had taken a client to the north country to camp and fish. They had taken off their shoes and were wading in a stream to cool their feet when a huge bear emerged from the trees and came charging toward them. The client, in his bare feet, ran fearfully out of the stream and up the rock-covered slope. He looked back and saw the salesperson quickly putting on his shoes. The client cried out to the salesperson that he must hurry because the bear was almost upon him. The salesperson said, "I'm okay. I don't have to outrun the bear—I only have to outrun you!"

Organizations' emphasis on competition and cooperation varies. Drug, medical equipment, and for-profit hospital companies typically demonstrate much more competitive strategies, while healthcare organizations working for the greater public benefit, such as public health clinics and the US Department of Veterans Affairs medical centers, use more collaborative strategies. Community hospitals, especially those in markets that include for-profit organizations, often adopt a more mixed strategy of competition and collaboration.

Why Study Healthcare Strategy and Strategic Management?

Healthcare organizations hire leaders to make decisions. Strategy and strategic management provide a solid framework for better decision making. Leaders ultimately have the responsibility and authority to make decisions and act. A key premise of successful leadership is that leaders must be good thinkers and deciders. For example, President Barack Obama was recognized by the magazine *Modern Healthcare* as its most influential person for three separate years during his presidency because of his actions on healthcare reform (Meyer 2016). Strategy and strategic management help leaders be mindful of the critical facts they need to consider to be better deciders. They must understand the purpose or, as is often the case, the mixed purposes of their organization and internal and external conditions, and they are charged with creating and implementing a strategic framework to accomplish the organization's purpose(s).

Leaders who think strategically allocate resources and minimize threats more effectively so that their organizations sustain mission advantage and perform better. Such thinking motivates leaders to proactively shape and craft the organization's business and inspires its delivery. Strategy is the road map and game plan for success. Unlike many other strategy texts, this book demonstrates that good strategy is only part of a successful equation. Good implementation must be added to good strategy to achieve excellent strategic outcomes. Both the creation and implementation of strategy are core functions of healthcare leaders.

Good strategy + Good strategy implementation =
Excellent strategic outcomes.

The importance of strategy in healthcare also is increasing because of the shift to value-based and patient-centered care in some states, which will require a complete restructuring of how healthcare is "organized, measured, and reimbursed" (Porter and Lee 2013). Change in healthcare is now driven by advancing technologies, demographic shifts, political debates, and global forces that directly affect the cost, access, and quality of healthcare. As these changes unfold, healthcare organizations require new, innovative strategies that may shift their direction and form new strategic thrusts. The following discussion highlights some of these changes and some strategies that have arisen as a result.

Healthcare Technology

Healthcare technology—especially diagnostic tools, information technology, and pharmaceuticals—has advanced rapidly in the past century. Radiological equipment, including computed tomography, magnetic resonance imaging, positron emission tomography, and ultrasound, has opened new diagnostic avenues. Radiologists' work has evolved from just reading X-rays to performing interventional procedures, operating outpatient facilities, and treating diseases that previously required major surgery. Hospitals and physician groups have reacted strategically by establishing centers for interventional radiology to compete with physician specialists, such as surgeons and cardiologists, who have traditionally provided these services. In addition, advances in molecular imaging will change needed services, as it will enable physicians to detect and treat disease at the cellular level.

Prescription drugs contribute an increasing burden to the cost of healthcare. The overall use of prescription drugs rose from 51 to 59 percent of the adult population between 1999 and 2012, with 15 percent of the overall population and 40 percent of adults 65 and older using five or more medications (Firger 2015). Because patents are time limited (the patents for seven of the ten most widely used prescription drugs expired in 2012–2016 (Anderson 2014), pharmaceutical companies' survival is tied directly to continuous research, discovery, and innovation. In 2015, global pharmaceutical research and development costs reached $150 billion (Statista 2017a). Yet big pharmaceutical companies spent more on marketing than research (Swanson 2015) and prescription drug prices have skyrocketed, with the cost of common brand-name drugs jumping 128 percent from 2008 to 2014 (Johnson 2015). In response to the changing environment—including declining drug-discovery success rates, expiration of blockbuster drug patents, cost and pricing pressures, and the subsequent rise of cheaper alternatives—drug companies have shifted their efforts toward greater consumer marketing, a focus on efficacy, targeted

mergers, cost cutting, and research on biotech and therapeutic specialties, focusing on specific disease areas and populations (Deloitte 2016).

Advances in genomics and genetics may also transform much of medicine in the future. Developments in gene testing, gene therapy, and pharmacogenomics are now beginning to improve care for patients with AIDS and some cancers, and many predict they will have profound impact on healthcare in the coming decades (Wadhwa 2014).

Demographic Shifts

Demographic shifts occurring across the world are affecting the healthcare delivery system. Birth rates are falling in most countries, and populations are aging rapidly. In 1970, women had on average 4.5 children worldwide. By 2014, the birth rate had fallen to 2.5 children per woman. At the same time, global life spans have increased from 64.8 years in 1990 to about 70.0 years today (United Nations Population Fund 2017). While lower overall, birth rates in the United States remain higher among minority populations, and minority youth segments of the population are growing (Adamy 2016). This increasing diversity is driving innovative strategies and forcing healthcare organizations to be agile and adapt to the cultural and demographic needs of their constituents. Culture, race, ethnicity, and primary language have been shown to be associated with access-to-care issues and compliance with prevention and treatment of disease. As a result, many organizations emphasize culturally sensitive, linguistically appropriate care to ensure equity and quality across patient groups. Progressive health systems must take the lead in addressing these needs (Ubri and Artiga 2016).

The demographic trends in the United States will require different healthcare services. By the year 2050, almost one-third of the US population will be Hispanic, yet only 5 percent of physicians come from this group. Our citizens are getting older, as well as more racially, ethnically, and geographically diverse. People 65 years and older will grow from 14.5 percent of the American population in 2014 to almost 22 percent by 2040, and many will have multiple chronic diseases. These changes are creating significant challenges for healthcare planning in the United States, including deficits in geriatric care, fulfillment of ethnic needs, and treatment of chronic disease (Administration on Aging 2016). Globally, the number of people older than 65 is projected to grow by 1.6 billion and almost 16 percent of the population by the year 2050, while the number of young children will decline to approximately 7 percent of the total population (He, Goodkind, and Kowal 2016).

Political Forces

Political forces have a significant impact on healthcare. Legislation can substantially shift money, power, and regulation. Legislative bodies across the world continue to struggle to design laws that will curb the cost of healthcare while improving quality and access.

The politics affecting healthcare in the United States continues to be very significant. The Patient Protection and Affordable Care Act (ACA) signed into law by President Obama on March 23, 2010, triggered a seismic shift in the healthcare provider and payer communities with regard to organizational structure and operational work flows. The law provided greater drug coverage for seniors, diminished denial of insurance for preexisting conditions, mandated greater coverage of preventive services, shifted to a value-based orientation, and changed the mechanisms of provider payment. Value-based care sought to reimburse providers for the value patients received and not just quantity of services, which promoted approaches such as bundled payments and accountable care organizations. However, political representatives elected in 2016 have declared that this law will be overturned in 2017 and indicated an aversion to many of this law's components and results. What portions of the law will be retained and what will be changed remains highly uncertain (Bazzoli 2016).

Global Forces

Global forces affect all aspects of our lives today. Competition has broadened to include global players in healthcare. Patients increasingly are turning to new global alternatives to meet their healthcare needs, such as purchasing medications from other countries and seeking care abroad. Medical tourism is increasing steadily as US residents and others go to South America and Asia for surgeries and procedures that are more costly in their home country. Up to 750,000 US residents go abroad for medical care each year (Centers for Disease Control and Prevention 2016b).

Changes in the global healthcare market and politics are also affecting the number of foreign nationals who come to the United States for healthcare. For decades, the United States has attracted medical tourists because of the perception that it delivers the best healthcare in the world. In 2008, more than 400,000 non-US residents sought healthcare services in the United States, accounting for almost $5 billion in revenues and about 2 percent of total US healthcare services rendered that year. As global providers improve the quality of their care, this influx of patients may decline. The number of foreign patients coming to the United States has already fallen substantially since 2001, and the numbers of US residents traveling abroad for care could soon reach 23 million, spending almost $79 billion for services provided at international locations (Deloitte Center for Health Solutions 2008; Lee and Davis 2004; Patients Beyond Borders 2016).

Prospective and Emergent Strategies

Most large organizations engage in some type of planning process to analyze and design means to prospectively address the aforementioned issues and

then produce some form of written document to guide their future decisions. This forward planning is called *prospective* or *prescriptive strategy*. This activity includes the general designing, planning, and positioning efforts of businesses to craft strategies for sustained competitive advantage.

A retrospective analysis of strategy, on the other hand, looks backward to see what actually happened. Constant experimentation and adaptation to new market conditions produce patterns identified retrospectively as *realized* or *emergent strategy*. Most organizations' strategy evolves incrementally over time, even in organizations that do prospective planning. This process also helps organizations understand their competitors' strategies. Chapters 2 and 7 discuss how understanding competitors' strategies contributes to an environmental analysis and to developing and forming more effective organizational strategies and tactics. Organizations often modify their plans, and the end results may vary significantly from those anticipated. Companies and individuals may abandon established strategies or introduce new initiatives. Furthermore, a retrospective analysis can help organizations better understand the effects of environmental factors and is important during times of upheaval and in industries subject to significant uncertainty and change.

Both prospective and emergent views have merit; all strategy has both planned and unplanned components (Moncrieff 1999). Emergent strategy is more important in settings where greater environmental uncertainty and event randomness cause prospective strategies to be of little value in setting organizational direction. Emergent strategies may result from random choices, luck, the experience and reasoning of executives, or incremental decisions made by internal or external stakeholders. Scholars suggest that both deliberate action and nonlinear thought are needed for an organization to establish routines and processes while maintaining flexibility and ability to adapt (Burns 2002; Ghoshal and Bartlett 1995; Mintzberg, Ahlstrand, and Lampel 1998).

As shown in exhibit 1.3, **prospective strategy** can help to align an organization's actions with its mission and vision that will produce more relevant, appropriate outcomes (provided all goes according to plan). In addition, prospective strategy enables organizations to predict resource needs, identify and plan for major capital expenditures, recruit personnel, and attract other resources.

Planning for the future is a critical function of leaders. Healthcare organizations, such as pharmaceutical companies and hospitals, frequently invest millions in strategic projects involving buildings, equipment, and new hires that may take three to five years of development and effort before the new services, programs, or products become functional. Critical resources must be prospectively identified, accumulated, and organized so that they are available when needed. Likewise, prospective plans provide direction for proper resource allocation. Understanding what the future should look like allows leaders to

Emergent strategy
A pattern of actions that develop over time and become an organization's strategy *de facto*. This type of strategy is identified by examining decisions that were made and the patterns that occurred as a result. Also called *realized strategy*.

Prospective strategy
A planning function that forecasts an organization's future situation and designs means to guide an organization's future decisions.

Prospective Strategy	Emergent Strategy
Align actions with mission/vision	Understand competitors' strategies
Predict resource needs	Evaluate own strategy
Allocate capital and personnel to projects	Enhance organizational learning
Position organization in competitive space	Adapt to uncertain environments

EXHIBIT 1.3
Value and Purpose of Prospective and Emergent Strategies

set aside appropriate capital and personnel prospectively for their strategic efforts. In addition, as Porter (1996) suggests, strategy directs an organization to choose a set of activities that will deliver a unique set of results. This prospective role actively guides an organization to differentiate itself to gain and maintain mission advantage.

On the other hand, as Winston Churchill (1931, 6) once stated, "There is always more error than design in human affairs." An emergent view of strategy acknowledges that prospective plans are often not translated into action, and designs frequently contain errors that prevent implementation. Many organizations do not begin with a defined strategy; as in Humana's case (see exhibit 1.4), their strategy and market position emerge through trial and error. Looking back, organizations can see how their strategy formed and understand the actions that created it. However, few would have predicted in the 1970s that Humana would have become one of the largest health insurance companies in the United States.

An emergent perspective allows an organization to view its competitors' patterns of action and better understand their strategies. As discussed in chapter 2, knowing competitors' strategies helps an organization predict how it may react to strategic moves and better informs its prospective strategy. An organization may gather much more strategic information by observing its competitors' behavior and actions than it would by reading their written plans. Examining one's own strategy retrospectively is critical to learning from organizational successes and failures and providing feedback for future plans.

Strategy in many industries is emergent by nature; many avenues must be tried before a successful strategic direction is found. For example, in the past, pharmaceutical companies continuously searched for the next new blockbuster drug, and their discoveries drove their strategy. Chemical-driven experimentation dominated drug research. They tested hundreds of chemicals before finding one that might be effective for treating a disease. Today, their strategy is more prospective. Much of today's biomedical drug discovery is a process of first understanding how genes and proteins interact for a specific disease and then choosing a drug molecule to test. By using genomic markers to predict drug

Humana is one of the larger insurance companies in the United States, but it was not always in this business. In fact, its strategies and focus evolved over time. In 1961, David Jones, Wendell Cherry, and others formed a partnership that grew to own seven nursing homes, going public in 1968. At the advent of Medicare, they decided to expand their for-profit company, Extendicare, into the hospital business. By 1972, they had divested their nursing homes and decided to concentrate on the growing hospital market.

Humana soon became one of the leading hospital companies. Reflecting its new direction, Extendicare was changed to Humana Inc. in 1974. Through the next two decades Humana grew more than 80 hospitals in the United States and abroad. Humana was known for its centralized measurements and controls, and it sponsored innovative treatments, such as the first artificial heart. It also vertically integrated by creating the Humana Health Care Plan in 1984. The insurance arm was to help feed patients to Humana's hospitals, but by the 1990s, it seemed to create conflicts among the different divisions.

Humana again changed its strategies and focus. In 1993, the organization spun off its hospitals into a separate company called Galen Health Care Inc., which was shortly thereafter sold to Humana's for-profit competitor, Columbia/HCA. The company was left with only its health insurance business portfolio, which it has leveraged to achieve a $32.3 billion market capitalization in 2016. That year, Aetna offered to purchase Humana for $37 billion (Aetna 2015; E*TRADE 2017).

response, pharmacogenomics researchers can lower the cost of drug development and shorten drug development times (Cook, Hunter, and Vernon 2009; Thomson Reuters 2011).

Thus, organizations prospectively plan deliberate strategies and also realize emergent strategies retrospectively. Implementation of deliberate and emergent strategy may be influenced by many factors, including those shown in exhibit 1.5. Factors that influence the type of strategy an organization adopts include level of certainty, speed of change, degree of proactivity, clarity of mission, and time perspective. As exhibit 1.5 indicates, the greater the environmental uncertainty and change, the less clear the purpose or mission of the organization, and the shorter the time perspective, the more likely an organization will function from an emergent strategy.

Levels of Strategy

Strategy occurs at different levels in an organization. In today's world corporations, strategy is often divided into corporate, business, and functional levels. Most organizations—when they attain a large enough mass—create corporate

Deliberate strategy	Emergent strategy

←————————————————————————→
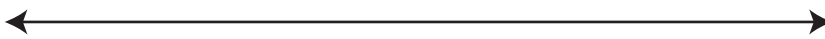
– Low uncertainty	– High uncertainty
– Slow change in:	– Fast change in:
* Consumer preferences	* Consumer preferences
* Technology	* Technology
– Written plans/proactive	– No plans/reactive
– Clear mission	– Unclear mission
– Lengthy time frame	– Short time frame

structures with strategic business unit (SBU) subcomponents. As shown in exhibit 1.6, the corporate level—which consists of top executives, corporate staff, and generally a board of directors—is the apex of decision making in an organization. This corporate structure oversees the strategy for the complete organization. However, as discussed in chapter 12, the primary function of corporate strategy is to define the mission and overall strategic goals of the organization, allocate capital funds to the different SBUs, and decide which businesses to enter or exit.

For example, Merck & Co., Inc., is one of the largest pharmaceutical companies in the world, with approximately 68,000 employees, and it has robust corporate and SBU strategic planning and management. As shown in the organizational chart in exhibit 1.7, Merck's corporate structure in 2012 consisted of five large divisions: manufacturing, animal health, research laboratories, global human health, and consumer care. At the divisional level, the executives consider major acquisitions and divestiture. For example, in 2009,

Corporate
Strategy

Business Unit
Strategy

Functional Strategy

Merck acquired Schering-Plough, another large pharmaceutical company, for $41 billion to create a more diverse portfolio of products and accelerate Merck's international growth (Reuters 2009). This acquisition was conceptualized, organized, and driven by **corporate-level strategy**. Likewise, Merck's mission and vision drive and derive from its corporate strategy (Merck 2017a):

Corporate-level strategy
The overall strategic scope and direction of a corporation. The primary function of corporate-level strategy is to allocate capital funds to SBUs and decide which businesses to enter or exit.

> **Vision:** To make a difference in the lives of people globally through our innovative medicines, vaccines, and animal health products. We are committed to being the premier, research-intensive biopharmaceutical company and are dedicated to providing leading innovations and solutions for today and the future.

> **Mission:** To discover, develop, and provide innovative products and services that save and improve lives around the world.

However, the Merck SBUs' business-level strategies focus on specific product lines, as demonstrated by the Merck Animal Health business unit (exhibit 1.8). At the SBU level, strategy focuses on more specific development projects, such as animal vaccines, pharmaceuticals, and diagnostics. Managers at this level usually receive the latitude to develop the best strategies for their areas of responsibility as long as those strategies fit into their corporate directives. Managers translate general statements of direction and intent from the
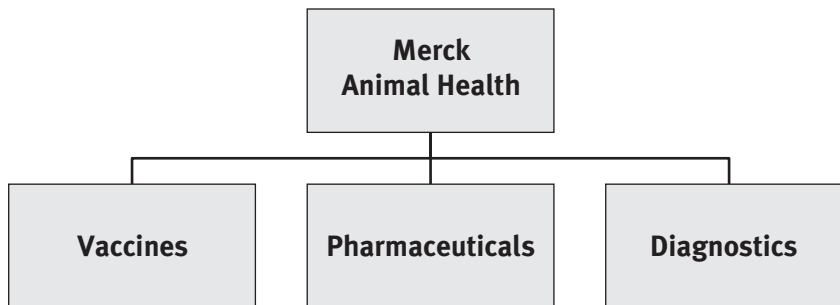
EXHIBIT 1.7
Merck & Co., Inc., Corporate Structure 2012
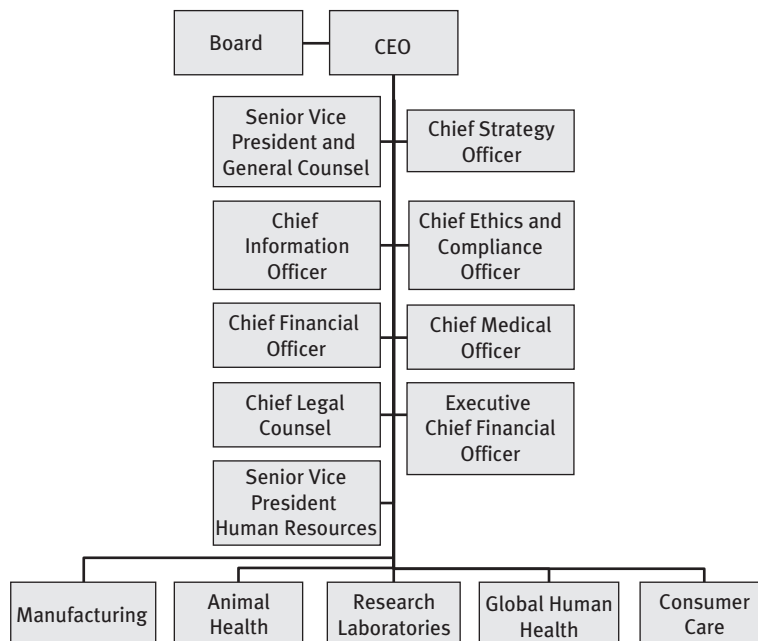
Source: Merck (2017c).

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                    ┌─────────────────┐
                    │     Merck       │
                    │  Animal Health  │
                    └─────────────────┘
        ┌────────────────┬───────────────┐
┌───────────┐   ┌─────────────────┐   ┌─────────────┐
│  Vaccines │   │ Pharmaceuticals │   │ Diagnostics │
└───────────┘   └─────────────────┘   └─────────────┘
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Source: Merck (2017b).

EXHIBIT 1.8
Merck & Co., Inc., Animal Health Division (SBU level) 2012

corporate level into concrete strategies for their individual businesses. Thus, while corporate strategy spans multiple businesses, **business-level strategy** focuses on a defined, specific business under the umbrella of corporate direction.

The functional level is the operating division, department, or project level. Here is where the rubber meets the road and the implementation of plans succeeds or fails. **Functional-level strategy** must support the business and corporate strategies. At this level, product or service line may be the drivers behind strategies. For example, Merck's Animal Health business unit (see exhibit 1.8) has a product-driven functional strategy that integrates research, marketing, production, and distribution to sell its products successfully. Hospitals may establish service line–driven functional strategies to promote their areas of specialty, such as oncology, cardiology, and obstetrics.

Each level's strategies must align with those of the other two. Misaligned plans may contradict the others' efforts and fail. Corporate strategies should cascade down the organization and be reflected in the lower levels' strategies and actions.

Business-level strategy
The strategic scope and direction of strategic business units (SBUs). SBUs focus on specific product/service lines while under the umbrella of corporate direction.

Functional-level strategy
Strategic scope and direction at the operating division, department, or project level. This type of strategy is driven by product or service line.

Text Overview

As shown in exhibit 1.9, this text explores in depth the concepts and tools needed to think strategically and develop and implement a strategic plan. Chapters 2 through 5 focus on strategy concepts; the remainder of the book seeks to answer the following questions:

- What is the purpose of the organization? (chapter 6)
- How well is the organization achieving its purpose? (chapters 7, 8, 9)
- What plans should the organization make to achieve its purpose more closely? (chapters 10 and 11)

- How should the organization act to better implement its strategies? (chapters 12, 13, 14)
- How can the organization tell if its strategies are having the desired effects? (chapter 15)

Building on the critical concepts presented in chapters 2 through 5, the text examines the process of creating and maintaining strategies. Good strategy development begins with an understanding of why an organization exists and where it wants to go. Chapter 6 explores how stakeholders and executives formulate an organization's strategic intent, including its values, mission, and vision. Next, an organization must look at its environment to understand the challenges it will need to overcome to achieve its strategic intent. Chapters 7 and 8 describe methods of analyzing the external and internal environments, and chapter 9 provides critical tools for strategic financial analyses.

EXHIBIT 1.9
The Text's
Structure

Core Concepts of Strategy (Chapters 2–5)	
• Market structure	• Growth strategies
• Business models	• Strategic alliances
• Generic and specialized strategies	

What Is the Purpose of the Organization? (Chapter 6)	
• Stakeholders	• Mission
• Values	• Vision

How Well Is the Organization Achieving Its Purpose? (Chapters 7, 8, 9)	
• External environmental analyses	• Financial analyses
• Internal environmental analyses	

What Plans Should the Organization Make to Achieve Its Purpose Better? (Chapters 10, 11)	
• Creation of strategic plans	• Creation of marketing plans
• Creation of goals and objectives	• Creation of business plans
• Creation of project charters	

How Should the Organization Act to Better Implement Its Strategies? (Chapters 12, 13, 14)	
• Proper organizational structure	• Strategic thinking and strategic management
• Strategic change management	

How Can the Organization Tell If Its Strategies Are Having the Desired Effects? (Chapter 15)	
• Engaging the right people	• Gantt charts
• Monitoring strategic efforts	• Strategy's interface with budgets

The book then shifts to the question of how organizations create strategic plans to better achieve their strategic intent. Chapter 10 explains how to engage key stakeholders in the planning process and outlines the structure and creation of strategic planning documents, including project charters and marketing plans. Chapter 11 discusses the use and creation of business plans. Chapters 12, 13, and 14 examine the organizational structure, change management, and strategic thinking critical to implementing strategy successfully. Chapter 15 concludes the text with a discussion on means of implementing and evaluating the strategic effort.

> "The better conceived a company's strategy and the more competently it is executed, the more likely that company will be a standout performer in the marketplace" (Thompson, Strickland, and Gamble 2010, 17).

Chapter Questions

1. What is a prospective strategy?
2. What is an emergent strategy?
3. Why is it important to understand the difference between prospective and emergent strategies?
4. Why is there an imperfect matchup between prospective and emergent strategies?
5. What might interfere with the realization of a prospective strategy?
6. How might you manage the balance between design and emergence strategizing processes in an organization?
7. What are the major factors that distinguish levels of strategies in an organization?

Chapter Cases

Case Studies
In the case studies section at the end of this book, read "The Virulent Virus." Create teams of three to four students. Each team should reach a consensus and recommend a decision. This case encourages teams to explore risk preferences, environmental pressures, and differences in decision making and is an excellent activity for the first day of class.

(continued)

Repeal of Obamacare?

The ACA, signed into law in 2010, substantially changed the direction and strategies of most US healthcare organizations. The US Department of Health & Human Services was given the responsibility of implementing many of the provisions that sought to "expand coverage, emphasize prevention, improve the quality of health care and patient outcomes across health care settings, ensure patient safety, promote efficiency and accountability, and work toward high-value health care." The law instituted healthcare exchanges to facilitate purchasing insurance and banned lifetime dollar limits and discrimination based on preexisting conditions (Assistant Secretary for Planning and Evaluation 2016).

The law was designed to motivate care coordination and integration across the continuum of care by transitioning to a population health and value-based care focus. Healthcare organizations responded, among other ways, through mergers and acquisitions. Physicians merged into mega–group practices. Pharmaceutical and insurance companies consolidated (Singer 2016). Hospitals acquired other hospitals, as well as physician practices and insurance businesses. Providers opened accountable care organizations, which were established to take capitation that could function next to traditional fee-for-service models. Healthcare insurers merged to counterbalance the growing market power of hospitals. In sum, changes happened in and across all sectors in the healthcare field. Much of the consolidation has been blamed on the ACA, and in early 2016 these changes seemed inevitable (Gluck 2016).

However, few predicted the election of Donald Trump in the fall of 2016 and his effect on the direction the healthcare sector has taken. Trump signaled that on his first day in office he would "work immediately on repealing Obamacare" (Koronowski 2017). A full or even partial repeal of the ACA would have significant impact on the strategies of healthcare organizations. Although we may not know what the repeal means for some time, and the final shape of the healthcare field under a Trump administration may gradually evolve, most Americans support coverage guaranteed regardless of preexisting conditions yet oppose a mandate. The ACA also cut $700 billion from Medicare provider reimbursements, which will probably not be restored by Trump's reforms (Kapur 2016). Whatever the results, the political winds of change have roared through a healthcare sector that now must review and revise its plans.

Questions

1. Why does politics have such an important impact on strategy in the healthcare sector?
2. Why were healthcare organizations merging under the ACA? Why might these strategies need to be revisited under a Trump administration?
3. How does this case demonstrate the difficulty in only having a prospective strategy?

Chapter Assignment

After reading chapter 1, read the 1996 article by Michael Porter titled "What Is Strategy?" from *Harvard Business Review*, volume 74, issue 6, pages 61–79. After reading these materials and discussing them in class, write a one-page (single-spaced) paper on what strategy is to you and provide three examples of different types of strategies exhibited by healthcare organizations.