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Strategic Audit and Ownership Strategy

Mike Franz Wahl[1]

ABSTRACT

In the new global economy, ownership has become a central issue for organizational performance. Ownership strategy is where corporate governance meets strategic management. Highlighting a knowledge gap in the field of corporate governance, the author is asking the central research question: "how to develop an ownership strategy?" The main purpose of this paper is to answer this original question and develop a better understanding about ownership strategies. Theoretically there is evidence to indicate that there is a link between strategic audit and ownership strategy. Analyzing firm cases from Estonia allows concluding that the strategic audit is useful for developing systemically ownership strategies, which in turn could be a realistic alternative for complete contracts. The use of strategic audits gives the business owner an opportunity to analyze his own actions and behavior, learning, managing knowledge, and finally clearly expressing his will in the form of an ownership strategy.

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1.0 INTRODUCTION

Agency theory (Alchian & Demsetz, 1972; Eisenhardt, 1989; Jensen & Meckling, 1976) is still the most popular theoretical approach in corporate governance, being concerned with relationships between owners and directors. While the agent (director, manager) has been asked by the principal (owner) to carry out a specific duty, the agent may not act in the best interest of the principal once the complete contract has been signed (Jensen & Meckling, 1976). In practice it is impossible to write such complex contracts, and they would be probably impossible to monitor. Ownership strategies could substitute complete contracts.

Highlighting a knowledge gap in the field of corporate governance, investigating that although some research has been carried out on importance of ownership in strategic management (Wheelen & Hunger, 2012), understanding corporate owners classes and types (Wahl, 2006, 2011, 2012), also conceptualizing ownership strategies (Collin, 2000; Luoma, 2011; Wahl, 2012), and strategy development (Grant, 1991) no studies have been found which

[1] Tallinn University of Technology, Estonia. E-mail: mike.wahl@ttu.ee

proposing how to develop actually an ownership strategy. Therefore the author is asking the central research question: "how to develop an ownership strategy?"

The main purpose of this paper is to answer this original question and develop a better understanding about ownership strategies. Theoretically there seems to be some evidence to indicate that there is a possible link between strategic audit and ownership strategy. Analyzing the chosen cases (n = 123), using text mining software, is showing that the strategic audit is useful for developing systemically an ownership strategy, which could be a realistic alternative for complete contracts. This gives the owner an opportunity to analyze its own actions and behavior, learning, managing knowledge, and finally clearly expressing his will.

The present paper is organized as follows. Section 2, "Theoretical framework: Ownership strategies in strategic management" begins by defining the key constructs that underscore the developing an ownership strategy from a holistic perspective. Relevant theories and evidence relating to the constructs are reviewed focusing on developing a research gap and central research question. Section 3, "Research methodology and data analysis" tells us about the philosophic assumptions and research design. The technical findings, results, interpretative analysis of meaningful relationships are explained. Section 4, "Conclusions and policy implications" concludes by describing the main insights and locating potential for the further research.

2.0 THEORETICAL FRAMEWORK: OWNERSHIP STRATEGIES IN STRATEGIC MANAGEMENT

2.01 OWNERSHIP AS A RELATIONSHIP BETWEEN THE OWNER AND THE OWNED TARGET

Ownership strategy is where corporate governance meets strategic management. An owner of a corporation is supplying equity capital, which is the main risk capital, and as compensation, the owner demands the residual from the firm, and in main stream agency theory, the owner and the corporation are assumed to have profit as the sole goal (Collin, 2000). However, enlightened ultimate owners have actually various goals. They know what results they want to have from the company in the long run – diverse personal, social, political, and economic values, and succeeding in a dynamic environment only if they invest those same values (Wahl, 2012). Therefore ownership is seen as a relationship between the owner and the owned target, having personal, social, political, and economic value dimensions. Successful ownership requires not only owners' resources, capabilities and will but also proficiency.

2.02 STRATEGIC MANAGEMENT

While corporate governance is concerned with the implementation of proficient owners' will (Wahl, 2012). The goal of strategic management should be creating and capturing values. Values have been a central concept in the social sciences since their inception (Schwartz, 2012). Cardinal values wealth, order, truth, transcendent, virtue, and beauty are values that are fundamental to rest of the moral system, the values from which all other values spring (Zetterberg, 1997). Basic values are deeply rooted, abstract motivations that guide, justify or explain attitudes, norms, opinions and actions (Schwartz, 1992) in the analysis they can provide predictive and explanatory power. Ownership values are classified in personal, social, political, and economic values (Wahl, 2012). Stakeholder theory (Freeman, 1984) begins with the assumption that values are necessarily and explicitly a part of doing business. It asks managers to articulate the shared sense of the value they create, and what brings its core stakeholders together. It also pushes managers to be clear about how they want to do business, specifically what kind of relationships they want and need to create with their stakeholders to deliver for their purpose. Stakeholder theory concerns values and beliefs about the appropriate relationships between the individual, the enterprise, and the state (Tricker, 2009). The "enlightened shareholder value" approach represents an attempt to strike a balance between shareholders' primacy and corporate stakeholders' interests (Andreadakis, 2011).

Strategic management is a set of decisions and actions that determines the long-run performance of a corporation. In this process, the interrelated activities internal and external environment scanning and strategy formulation, implementation, and evaluation result in a set of strategies the organization. Early efforts ranged from defining strategies as integrated decisions, actions, or plans designed to set and achieve organizational goals to defining strategy as simply the outcome of the strategy formulation process (Wheelen & Hunger, 2012). Here defining strategy as a series of goal-directed plans and activities that align "match" a business's structure (chain of command), culture (behavior, attitudes, norms, value judgments, and values), and resources (tangible and intangible assets, skills, competencies, knowledge) with the opportunities and threats in its environment.

In strategy literature, strategy can be classified on four levels: functional, business, corporate, and ownership. On lowest level are functional strategies, which are concerned with coordinating the functional areas of the organization, so that each functional area upholds and contributes to individual business-level strategies and the overall corporate-level strategy. Business-level strategies are similar to corporate strategies in that they focus on overall performance. In contrast to corporate strategies, however, business strategies focus on only one rather than a portfolio of businesses. On the highest level are the ownership- and corporate strategies, addressing the entire strategic scope of the company.

2.03 OWNERSHIP STRATEGY

The concept of ownership strategy is indicating that different ownership objectives demands different strategies (Collin, 2000). Owners are distinctive and may have their own agendas – their own ownership strategy. In the classic three-level hierarchy of strategies, the role of owners is distant, passive, and is not anticipating different types of owners. Actually there are considerable differences between the different profiles, styles or types of owners. However, owners are not a homogenous group with similar interests and similar abilities, but rather individuals with individual interests and abilities (Luoma, 2011). Wahl's (2006) nine class classification system covers features of corporate owners, but classification systems are differentiated from typologies. Several of the important criteria of theories meet typologies; therefore Wahl (2011, 2012) constructed an ownership typology, which helps to explain behavior of the most important actor in corporate governance. It is improving understanding about the owners' role and behavior at the individual, firm, and societal level (Wahl, 2012).

It is stated that beyond functional-, competitive-, and corporate strategy there is a fourth dimension, a level of an ownership strategy. Long-term success means accomplishing the mission, organizational development requires a consistent vision, and has an ownership strategy based corporate strategy at heart. Ownership strategy is here defined as the choice of direction of the firm as a whole and the governance of its business, and product or service portfolio. A further definition given by Collin (2000) is that ownership strategy is the composition of the mix of governance mechanisms in order to ensure the fulfillment of the aims of the owned organization (Collin, 2000). Ownership strategy is also defined as an expression of the will of the company's owners; it clarifies what owners want in terms of rights, resources, risks, responsibilities and returns (Luoma, 2011). The interest (will) and capacity of the owners constitute the ownership strategy, defined as the actual composition of the mix of corporate available governance mechanisms the owner have made in order to make it possible for the company, ultimately the top managers, to fulfill the aims of the company; the collection of governance mechanism influences the efficiency of the company (Collin, 2001).

By combining owners' will on one document, the ownership strategy gives one clear message from principals to agency instead of several signals. The implementation of an ownership strategy is enabling to improve communication both among owners and between owners and management. (Luoma, 2011) The most important contribution made by an ownership strategy is perhaps not its capacity to predict, but to prescribe, or at least to be an efficient basis for analyzing an owner, or for an owner to analyze its own actions (Collin, 2001) and behavior. Experience and institutional factors (e.g. quality of corporate governance, enforcement of property rights) are the most important determinants of the ownership strategy (Delios & Beamish, 2001).
In a publicly listed company with dispersed ownership structure there is no need for an ownership strategy, but in companies with concentrated ownership structure it can be seen as a practical tool for corporate governance (Luoma, 2011).

2.04 STRATEGY DEVELOPMENT

Already during the 1980s, the principal developments in strategy analysis focused upon the link between strategy and the external environment. Later the link between strategy and the firm's resources actualized. Most research into the strategic implications of the firm's internal environment has been concerned with issues of strategy implementation and analysis of the organizational process through which strategies emerge. There has been a resurgence of interest in the role of the firm's resources as the foundation for the strategy. The knowledge-based theory (Kogut & Zander, 1992) of the firm considers knowledge as the most strategically significant resource of the firm, an outgrowth of the resource-based view of the firm (Barney, 1991). This knowledge is embedded and carried through multiple entities including organizational culture and identity, policies, routines, documents, systems, and employees. The ability to sense and then seize new opportunities, and to reconfigure and protect knowledge assets, competencies, and complementary assets is dynamic capability (Augier & Teece, 2009), achieving a sustained competitive advantage needs dynamic capabilities. Dynamic capabilities directly impact the competencies and resource base of the firm, which in turn is the source of the firm's competitive advantage (Ambrosini & Bowman, 2009).

At the corporate strategy level, theoretical interest in economies of scope and transaction costs has focused attention on the role of corporate resources in determining the industrial and geographical boundaries of the firm's activities. (Grant, 1991) There are five stages in this framework for a resource-based approach to strategy formulation: analyze resources, appraise capabilities, analyze competitive advantage, select strategy, and identify resource gaps. This framework uses resources and capabilities as the foundation for a firm's long-term strategy because they provide direction for firm strategy and serve as the primary source of firm profit. The essence of strategy formulation is to design a competitive strategy that makes the most effective use of core resources and capabilities. (Grant, 1991)

Strategy formulation is developing and choosing appropriate strategies, as guided by the situation analysis (Wheelen & Hunger, 2012), including corporation's vision, mission, objectives, and policies. The most exploited situation analysis is SWOT; this is a framework for strategic planning, standing for strengths, weaknesses, opportunities, and threats. Performing a SWOT analysis involves describing and analyzing a firm's internal capabilities its strengths and weaknesses relative to the external opportunities and threats of the competitive marketplace. Organizations are advised to take strategic actions to preserve or sustain strengths, offset weaknesses, avert or mitigate threats, and capitalize on opportunities. (Grant, 1991) But an opportunity has no real value unless a company has the capacity to take advantage of that opportunity (Wheelen & Hunger, 2012). Main critics to SWOT are that this analysis generates lengthy lists, uses no weights to reflect priorities, using ambiguous words and phrases. The same factor can be in two categories. There is no obligation to verify opinion with data or analysis. It requires only a single level of analysis with no logical link to strategy implementation. Therefore the author proposes to use instead of SWOT the strategic audit, where generating a strategic factors analysis summary (SFAS) Matrix.

Auditing is the instrument of the owners and the state in order to ensure the legality of the corporation (Collin, 2000). The proposed strategic audit is providing a rich dataset and the opportunity to move from a narrow, specialized view that emphasizes functional techniques to a broader, less precise analysis of the overall corporation. Its strengths include a real world orientation and the ability to focus on developing decision making skills. Overall, there seems to be some evidence to indicate that there is a possible link between strategic audit and ownership strategy, namely the best tool to develop a strategy seems to be the strategic audit. In the next section the author analyzes cases using text mining software Leximancer, showing that strategic audit is useful for developing systemically an ownership strategy.

3.0 RESEARCH METHODOLOGY AND DATA ANALYSIS

Research philosophies tells us about the philosophic assumptions the authors have about the world, the nature of knowledge and knowing, the role of values, and how to go about studying the phenomena. Current work is based on constructionism. Here using interpretive ontological assumptions that the world is complex and dynamic and is constructed, interpreted and experienced by people in their interactions with each other and with wider social systems. People experience reality in different ways. Reality is constructed by people based on beliefs, feelings and experiences; multiple local and specific "constructed" realities exist (Hine & Carson, 2007). An interpretive epistemological assumption is that knowledge is based not only on observable phenomena, but also on subjective beliefs, values, reasons, and understandings. The researcher is a "passionate participant" in the world being investigated.

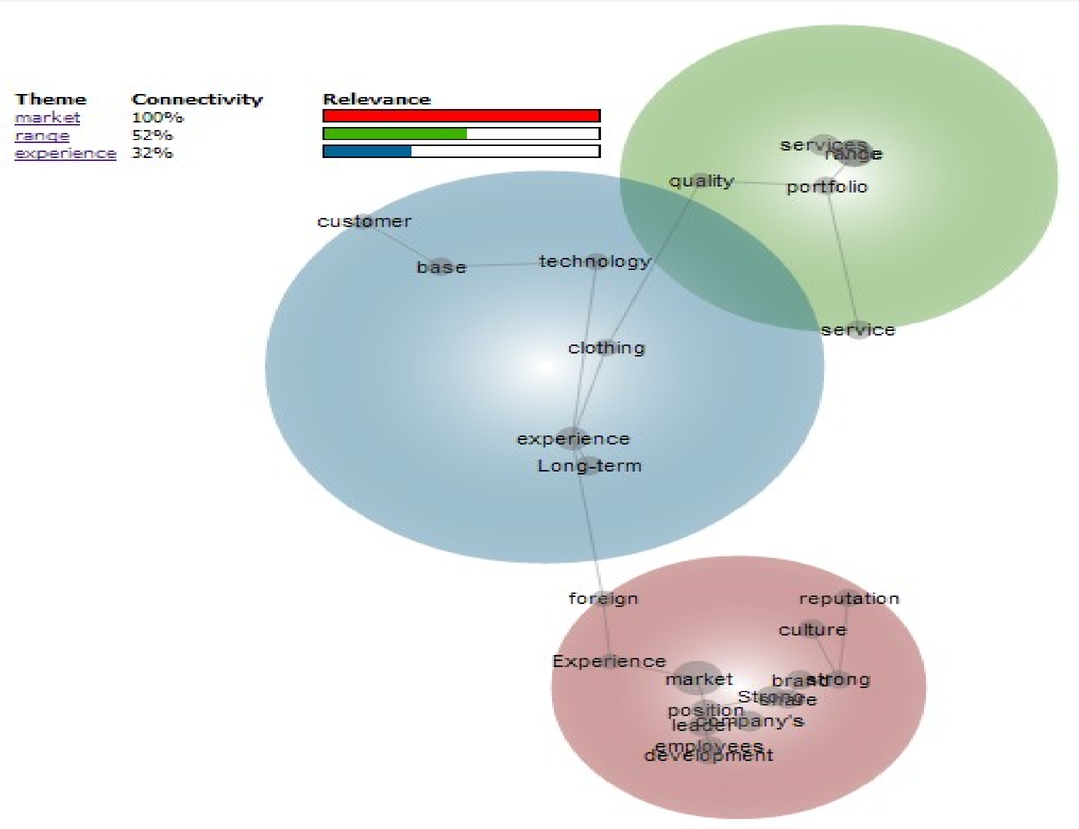
Research design turns the central research question into a project that considers strategies, choices and time horizons. The chosen research strategy is case study, using mixed methods, and it can be categorized as an explanatory, cross-sectional research project. Case study strategy is an empirical inquiry that investigates a contemporary phenomenon within its real-life context, especially because the boundaries between phenomenon and context are not clearly evident (Yin, 2009). Case studies provide a rich understanding of a real life context; using and triangulate multiple sources of data. The chosen research strategy is case study, using mixed methods, and it can be categorized as an explanatory, cross-sectional research project. Techniques and procedures are miscellaneous material or data collection and analysis methods. The data type constrains the presentation, summary and analysis techniques that can be used.

The outcome of the ownership strategy is always unique and firm-specific. Every strategic audit were starting with a careful study of the firm, using the strategic audit worksheet. Next step included doing outside research, calculating common size financial statements, and key ratios, if appropriate. Here also describing the basic corporate governance mechanisms of the corporation. Owners and managers are the people who are primarily tasked with the strategic management process if the corporation is to have long-term success in accomplishing its mission. The advanced analysis started with the external (EFAS), and internal (IFAS) factor analysis, concluding in a comprehensive strategic factor analysis summary (SFAS). After working out strategic alternatives and recommendations, an implementation, evaluation and control process of organizational learning is following. Organizational success is related to growth and development.

All collected material and data from firms in Estonia is entered into a MS Excel 2010 case database. All chosen firms, cases (n = 123) are thoroughly described and coded. Material is entered as a matrix and recorded using numerical codes. Codes are entered for all data values. Existing coding schemes enable comparisons. Data is checked for errors, cleaned, pre-processed. Thematic case analysis and case contrasts were done before analysis of empirical regularities.

For computer analysis Microsoft Excel and Leximancer were used. Text is more than a collection of words, it tells a story. Ideas, concepts, and relationships are buried in the words. Leximancer is text mining software that can be used for content analysis of collections of textual documents and to visually display the extracted information. The information is displayed by means of a conceptual map that provides an overview of the material, representing the main concepts contained within the text and how they are related. It supports processing text from a number of different formats (e.g. CSV, Plain Text, DOCX, PDF) and languages (e.g. English, German, Finnish, Russian), it analyses automatically texts to identify the high level concepts, delivering the key ideas and actionable insights needed with powerful interactive visualizations and data exports. Helping to understand of what text is really saying. (Leximancer, 2014) The Leximancer is transforming lexical co-occurrence information from natural language into semantic patterns in an unsupervised manner. It employs two stages of co-occurrence information extraction – semantic and relational, using a different algorithm for each stage. The algorithms used are statistical but they employ nonlinear dynamics and machine learning. (Smith & Humphreys, 2006) Leximancer enables to navigate the complexity of text in a uniquely automated fashion, it identifies 'concepts' within the text – not merely keywords but focused clusters of related, defining terms as conceptualized by the author. Themes are the colored circles that group clusters of concepts.

Figure 1: Leximancer concept map for the examined categories and subcategories of strengths



Source: Author's illustration

Figure 2: Leximancer concept map for the examined categories and subcategories of weaknesses

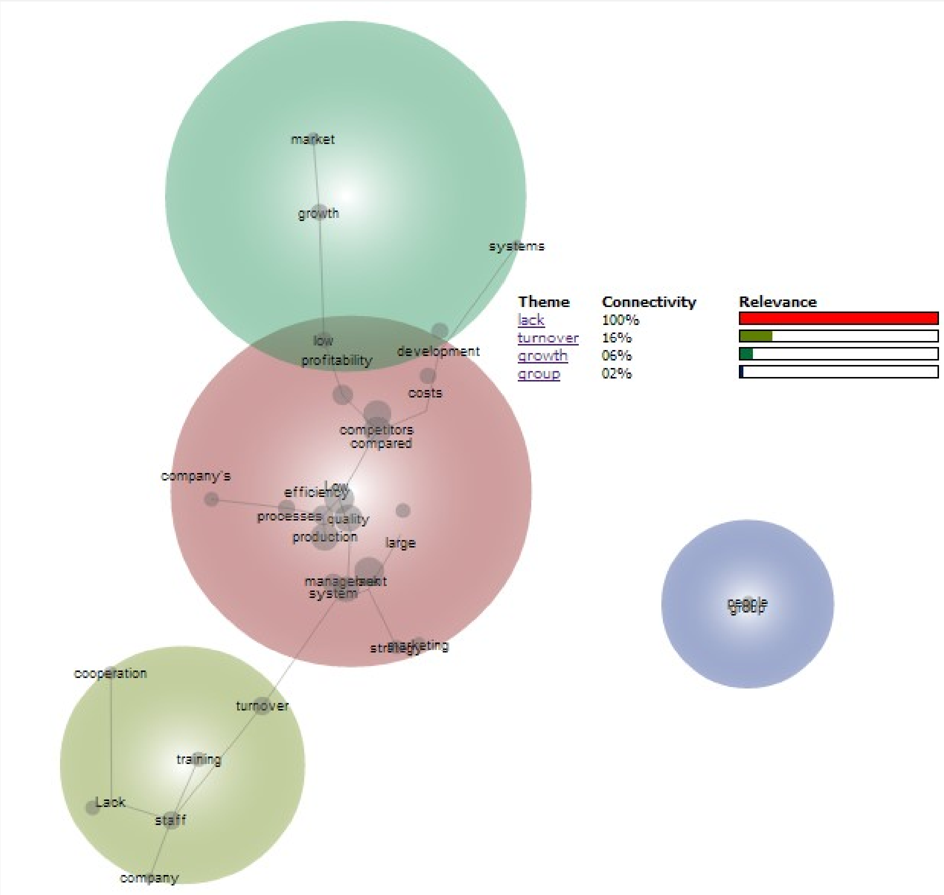
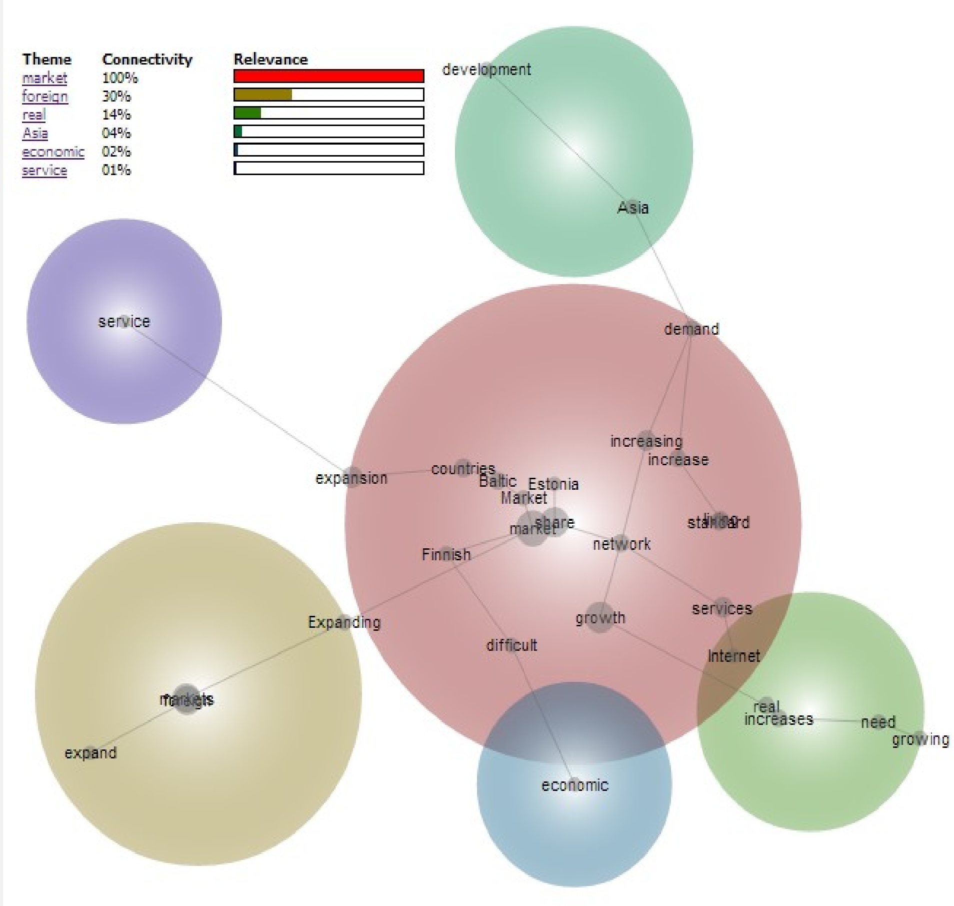


Figure 3: Leximancer concept map for the examined categories and subcategories of opportunities



Source: Author's illustration

Internal factors, strengths (Figure 1) are divided in three themes; they are market, range, and experience. The themes are heat-mapped, meaning that hot colors (red, orange) denote the most important themes 'market', and cool colors (blue, green), denote those less important 'range' and 'experience'. The Thematic Summary includes a 'connectivity' score to indicate the relative importance of the themes. Connectivity scores for market (100%), range (52%), and experience (32%).

The Concepts are presented in a compelling, interactive display so that it is possible to visualize and interrogate their inter-connectedness and co-occurrence, this is as important as the concepts themselves. The insight dashboard report is a useful way of encapsulating the quantitative correlations between selected dependent segments and the observed text concepts, along with the supporting textual evidence for better understanding. (Leximancer, 2014).

Internal factors, weaknesses (Figure 2) are divided in four themes; they are lack, turnover, growth, and group. The most important theme is 'lack', and less important themes are 'turnover', 'growth', and 'group'. Connectivity scores are shown for lack (100%), turnover (16%), growth (6%) and group (2%). External factors, opportunities (Figure 3) are divided in six themes; they are market, foreign, real estate, Asia, economic, and service.

The most important theme is 'market', and less important are 'foreign', 'real estate', 'Asia', 'economic' and 'service'. Connectivity scores are shown for market (100%), foreign (30%), real estate (14%), Asia (4%), economic (2%) and service (1%). External factors, threats (Figure 4) are divided in six themes; they are price, materials, economic, service, competition, and market. The most important theme is 'price', and less important themes are 'materials', 'economic', 'service', 'competition' and 'market'. Connectivity scores are shown for price (100%), materials (68%), economic (13%), service (4%), competition (3%), and market (2%).

The examined categories and subcategories of the most important strategic factors for developing an ownership strategy should be not only described but also "understood" and "explained", therefore the meaningful relationships that form the basis of the empirically founded themes were analyzed. SFAS summarizes an organization's strategic factors by combining relevant external factors (EFAS) with the internal factors (IFAS). The strategic factors could be corn stones for every strategy.

4.0 CONCLUSIONS AND POLICY IMPLICATIONS

The conducted research allows making conclusions and recommendations. The central research question set by the author „how to develop an ownership strategy?" has been answered. The main purpose to develop a better understanding reached.

In conclusion it can be stated that the main practical implication of the current research is the understanding, that a strategic audit is useful for developing systemically an ownership strategy. Interpreting the results, it is important to keep in mind that the case database consists only few competitive case studies (n = 123). It is recommended that further ownership research should include general systems theory, which is not explicitly used as a theoretical framework in corporate governance. Developing a new conception of ownership strategy could be a future scientific problem to solve. Methodologically the research is valuable while used modern text analytics Leximancer for an innovative way to present, and to garner deeper insight from texts. Practically, in order to stay sustainable and be able to develop further there is a need for professional corporate governance and also enlightened proficient ultimate owners. The proposed use of strategic audit gives the owner an opportunity to analyze its own actions and behavior, learning, managing knowledge, and finally clearly expressing his will in the form of an ownership strategy. This could be a realistic alternative for complete contracts. Corporate governance has become a major topic in the world of business, politics, and academia, in Estonia and throughout the world. It has important implications not only for business, but for the wider economy and society.

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