



Studies in Management and Accounting for the

FOREST PRODUCTS INDUSTRIES

DEVELOPING A STRATEGIC PLAN FOR A FOREST PRODUCTS COMPANY: A CASE STUDY

**Steven S. Bremner
Arthur Andersen & Co.**

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INTRODUCTION

Over the period since the Second World War, strategic planning has become a well-accepted practice in both large and small American businesses. However, forest products companies generally have not been leaders in adopting strategic planning. This is largely due to the fact that much of the industry was historically production oriented, and focused on ways of increasing productivity, improving recovery and minimizing production costs, while strategic planning has found acceptance among marketing-oriented businesses.

The production-oriented business approach of small- and medium-size forest products companies worked relatively well during the peak home building years in the 1960s and the 1970s. However, the decline in construction of single-family homes and continuing unfavorable trends in forecasts for housing construction during the remainder of the current decade are causing an increasing number of companies to question whether the "efficient production strategy" which served them so well in the past can continue to be viable.

Because of this uncertainty, growing numbers of forest products companies are developing formalized planning processes to evaluate the strategic alternatives available to their businesses and to determine new courses of action for the future.

This monograph outlines an approach that many companies have followed in developing a strategic plan. A case study approach is used for purposes of illustration. The "Biota Company" is typical of many medium-size forest products companies; it should be understood that it represents a composite derived from a number of companies.

Also, the approach which is suggested is oriented toward small-to medium-size forest products companies (i.e., non-integrated producers, usually with annual sales ranging from \$10 to \$200 million). Large horizontally or vertically integrated companies often have complex planning requirements which require these companies to develop sophisticated formal planning systems. In small- and medium-size companies, however, elaborate

planning processes may be counter-productive. Here, the planner's major task is to make sure that management has real understanding of why the company needs to develop strategic plans and of its own planning responsibilities.

CASE BACKGROUND

The Biota Company is a medium-size manufacturer and distributor of both commodity and specialty Western wood products with annual sales of approximately \$80 million. The Company has a dimension lumber mill geared toward processing medium-quality, mid-size logs to produce commodity lumber products used in home construction. The mill was rebuilt several years ago and is considered by Biota to be "better than average" in terms of productivity and lumber recovery. Annual capacity is approximately 55 MMBM. The second, older mill is a cutting mill which saws high-quality, old-growth timber to produce high value specialty products. The Company markets its commodity products primarily through office wholesalers, although a small percentage of its products are sold directly to retail customers. Most dimension lumber is shipped via rail or truck and sold in Western U.S. markets. A considerable portion of the grade mill's production is export quality and is sold through wholesalers to foreign markets. The remainder is sold domestically both through wholesalers and (in the case of certain industrial specialty products) directly to manufacturers.

In addition to selling its own production, Biota occasionally buys lumber from other manufacturers and resells it. The Company also has several building materials distribution centers located in the Midwest which were purchased several years ago. These distribution centers operate semi-autonomously, buying a portion of their wood through Biota's office wholesaling group.

The Company has little fee timber and is essentially dependent on public timber sold by the United States Forest Service and various state agencies. On several occasions, the Company has purchased timber and exported the logs to Japan.

The Company is privately held, and the family ownership was very pleased to see its investment in the business prosper during the '60s and '70s. In particular, the late '70s were extremely profitable due to several favorable log export sales. However, beginning in 1979, the decline in both export and domestic markets for the Company's products caused a severe reversal in performance, shaking both the owners' and management's confidence that the approaches which had served them so well in the past would continue to be effective in the future. Accordingly, the Company determined that it needed to rethink its business direction and to develop new strategies to cope with the changing economic environment.

DEVELOPING A STRATEGIC PLAN

A. ORGANIZING THE PLANNING PROCESS

The Company developed a planning team made up of key members of management who would be most affected by strategic decisions and who would be responsible for implementing the Company's new plans. The members of the planning team included: President; Vice President of Marketing; Vice President of Finance; Vice President of Timber and Logging; Manager of Distribution Centers; and Manager of Sawmill Operations.

To assist the members of the planning team in accumulating financial and other numerical data and documenting plan findings, the Company assigned a support staff consisting of the Company's controller and a production supervisor from one of the Company's mills. The planning staff members worked on the plan on a part-time basis for the duration of the project. The Company also retained a consulting firm in this initial planning effort to assist in organizing and directing the planning process.

The president of the Company established the basic requirements for the plan. The planning period was set at five years. The scope of activities covered included all the current operations as well as potential new businesses development. The Company decided to document its plans in a summary report containing the key plan findings and financial projections; however, consistent with the informal style of the business, this planning document was designed to be written in an outline format with as little narrative as possible.

A work plan was developed which specified how the planning project would be organized and the responsibilities of each individual. The work plan identified a schedule for preparation and completion of the plan, as well as time budgets for

each member of management, the support staff and the consultants. In this first planning effort, a substantial commitment of management time was budgeted to allow for lack of familiarity with the planning process and to provide time for training in planning skills.

B. REVIEW THE KEY FACTORS IN THE EXTERNAL ENVIRONMENT

The support staff and consultants developed background material to be used by the management team in preparing the plan. Much of the data were publicly available from government agencies, industry trade associations, market research services and econometric data reporting services. In addition, the Company also prepared planning data based on its own financial and operational records. The types of data which Biota felt were important for planning purposes include (among other factors):

1. The type, size, species, quality and ownership pattern of timber in the Company's natural working circle.
2. A profile of the Company's own timber contracts that summarized price, contract expiration date, volume, quality and potential markets.
3. Log recovery, product yield, production rates and cost data for each mill.
4. Current and projected long-term demand and pricing levels for selected wood products.
5. Order of magnitude costs of capital investments in mills and other operating equipment being considered by the Company.
6. Data on foreign and domestic markets, distribution channels, product acceptance and consumer trends.
7. Trends in government regulations, public forest management policy and forecasted timber availability.
8. Forecasted interest rates and inflation trends.

Based on this data, the planning staff prepared summaries of the key factors in the external environment which needed to be considered by the management team in developing a strategic plan. A list of planning assumptions also was prepared, which indicated the Company's realistic assessment of how these external factors were expected to change over the planning period, and their potential impact on the business. Perhaps more important than the specific forecasts, however, was an identification of the external issues which represented the most significant opportunities or threats facing Biota.

Two brief one-page scenarios were prepared, outlining possible courses that the economy could take over the planning period. A favorable scenario outlined a period of declining inflation and interest rates accompanied by a gradually rising level of the economy with housing starts recovering to average 1.6 to 1.8 million units per year. An unfavorable scenario described another possible future: one in which both inflation and interest rates stay at high levels, employment remains flat, the economy stagnates and home building continues to suffer, resulting in housing starts of only 1.2 million units per year.

The alternative scenarios, together with the summary of key external factors and planning assumptions, were then sent to the management members of the planning team. Each member was instructed to review the planning data and assumptions about the future course of the economy, and to consider these factors in the planning process.

C. ASSESSING THE COMPANY'S STRENGTHS AND WEAKNESSES

The planning staff interviewed Biota's management to identify the Company's major competitors and to identify the competitor's successful business strategies. Next, the team prepared brief profiles of each major competitor's strategies, financial results, operational data, and strengths and weaknesses. In the course of its business, Biota had become quite familiar with its major competitors, thus, much of the information needed to evaluate its competitors was readily available. The objective of this task was to help identify the key factors that relate to long-term success in the forest products industry.

As head of the planning team, the president instructed the other members to consider the Company's present capabilities and resources including mills, distribution centers, products manufactured and distributed, personnel, financial position and access to timber. Each member of the planning team was asked to develop his own independent assessment of Biota's strengths and weaknesses.

A full-day meeting was held during which the team members discussed their own assessments of the Company's position. Not surprisingly, there were significant differences between each manager's list of strengths and weaknesses. As the result of this meeting, the team reached a consensus (with some direction from the president) on the Company's major opportunities and its major

problems. This realistic assessment of the Company's capabilities and limitations was a key part of the planning process. In essence, the remainder of planning was devoted to finding ways to overcome the weaknesses and to emphasize the Company's strengths.

Based on the outcome of the planning meeting, the planning staff prepared a brief statement that summarized Biota's view of its position in the wood products industry. The position document contained six basic sections:

- A summary of the key factors for long-term success in the wood products industry.
- A summary of Biota's position in the industry vis-a-vis its competitors in terms of sales, growth, profitability, access to timber, and other key data.
- Profitability and sales growth for each of the company's operating divisions.
- An assessment of the capabilities, resources and limitations of each of the Company's major functional areas (e.g., manufacturing, marketing, finance).
- A summary of the major strengths and weaknesses of the Company.
- A brief conclusion as to the relative attractiveness of the wood products industry and the market segments which the Company serves.

D. DEVELOP BUSINESS OBJECTIVES AND GOALS

In a second full-day meeting, the planning team developed its statements of missions, objectives and goals. This began by writing a statement of the Company's "business mission," or a broad definition of the primary business of the Company in terms of the markets served, product lines, distribution channels and sales territory. Management was surprised to find that the development of a statement of its mission was difficult; the Company's commodity product manufacturing operations did not appear to be consistent with its general orientation toward marketing specialty lumber and its exporting business. In addition, the distribution centers were unrelated to the Company's other operations. After some discussion, the planning team decided that consistent with the Company's past history and its desired position in the industry, its mission should be "to manufacture and market high value wood products through wholesalers and directly to industrial buyers to meet the special needs of domestic and foreign customers."

Based on this statement of mission, the planning team went on to define "objectives," or general statements of what Biota needed to do in order to accomplish its business mission. For example, one of marketing's objectives was "to increase export sales of the Company's own manufactured products." Objectives were developed for each of the Company's functional areas including finance, timber and logging, manufacturing and distribution centers.

Once the objectives had been set, the planning team developed "goals" relating to each objective, or specific measurable targets which must be achieved in order to meet the objectives. For example, one of marketing's goals related to the above objective was "to increase sales of metric dimension lumber 50% by December 1983."

During this phase of the planning process, it became apparent that several of the goals and objectives of individual members of the planning team were in conflict. For example, marketing's objective was to increase sales realization per MBM by identifying markets for high-value products. Production's objective was to increase mill productivity and overrun. However, the high-value products which the Company preferred to market require greater care in manufacturing and, consequently, increased productivity or overrun was not immediately compatible with marketing's goals. Resolving these conflicts required the planning team to re-examine the Company's long established ways of looking at the business. Indeed, this was one of the principal benefits of planning: to build management's awareness of common objectives and to ensure that the Company worked together as a team to meet these objectives.

E. DEVELOP BUSINESS STRATEGIES

Concurrently with the development of objectives and goals, the planning team worked to develop alternative "strategies," or specific action plans intended to achieve these goals. Strategy development was approached in two stages. First, at a planning meeting, the members of the planning team developed a list of all possible strategies that could be used to accomplish each goal. The initial list was prepared based on the Company's existing strategies. This was supplemented by the apparently successful strategies of competitors and by new strategies which the Company developed in a "brainstorming" session. The intent in preparing this initial list was to be as comprehensive as possible, including all workable strategies whether good or bad.

Once the list of alternative strategies had been developed, the next step was to analyze the alternatives to see:

- What level of risk was involved.
- What resources needed to be committed.
- What time would be required.
- Whether the strategy would meet Biota's objectives and goals.
- Whether the strategy was consistent with the Company's financial resources.
- Whether the strategies were compatible with management's and the owners' personal styles and desires.

Relatively few strategies needed to be evaluated in detail, since many strategies could be eliminated based on the above criteria. The evaluation of the remaining strategies was a lengthy and difficult project that required the staff members on the planning team to pull together detailed information on each apparently viable strategy and to assess its financial implications.

At a follow-up planning meeting, the team reviewed the results of the analysis of proposed strategies. Management found that the process of selecting strategies also caused a re-evaluation of the objectives and goals which had been developed. For example, one of the Company's objectives had been to increase flexibility to respond to customer requests for specialty products. A related goal was to meet most customer requests within a brief period of time. One strategy which the Company considered involved maintaining inventories of certain specialty wood products; however, when the Company determined the cost of implementing the strategy, it decided that the goal was unrealistic and that it needed to find other ways of satisfying its customers.

Also, in weighing the alternative strategies, the planning team tried to consider how its plans would be affected by unfavorable contingencies. Biota had to balance its desire to meet its objectives with the level of risk it was prepared to assume. The strategies were evaluated considering the two economic scenarios prepared at an earlier stage of the planning process. Sometimes, a strategy which appeared to be superior under a favorable scenario was discarded as unacceptably risky should events unfold according to an unfavorable scenario.

Of necessity, the planning team re-evaluated and modified the selected strategies to arrive at a workable set of strategies, consistent with the Company's expectations about the future, its resources and other constraints.

F. PREPARE THE PLAN REPORT

In this final planning stage, the planning staff assembled the sections of the strategic plan report which had been developed during the planning process, and wrote brief narratives which integrated the report into a cohesive, finished document. In addition, the controller and accounting staff prepared summaries of quantitative data which represented the expected results of Biota's plans. The majority of this quantitative data was financial and included pro forma income statements, balance sheets, cash flow and other financial measures of the plan. Other nonfinancial data regarding key production, marketing and other operational statistics also were quantified. Last, a brief executive summary was added to highlight the major items in the plan report. Copies of the final, five-part plan then were distributed to all Biota managers responsible for implementing the plan. The plan's Table of Contents is shown in Appendix A.

IMPLEMENTATION

In order to successfully implement its strategies, Biota needed to develop systems to monitor and control its progress in achieving the plan. This was done by modifying Biota's existing budgeting

process to serve as its principal control system. The strategic plan provided Biota with many of the objectives, goals and strategies required to develop each operating unit's annual plans and budgets. In effect, these shorter term plans became more detailed subsets of the strategic plan, which had to be achieved in order to attain the Company's goals and objectives.

The individuals responsible for developing operating plans and budgets were given responsibility for developing programs to implement the Company's strategies. Subsequently, the budget review process was used to ensure that all the strategies called for by the strategic plan would be implemented. During the year, monthly and quarterly reviews of actual progress against operating plans and budgets provided feedback on the Company's ability to implement its strategies and to fulfill the strategic plan. Lastly, to close the loop in its control system, Biota modified its managers' compensation to provide for bonuses if the business's goals and objectives were successfully met. This use of salary incentives was a significant factor in convincing the Company's managers that Biota intended to follow through with its plans.

APPENDIX A
THE BIOTA COMPANY
STRATEGIC PLAN
1983 - 1988

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MONOGRAPHS PUBLISHED TO DATE

"The Rush to LIFO: Is it Always Good for Wood Products Firms?" issued in December 1974 and published in condensed form in the April 1975 issue of Forest Industries. This monograph was revised and reissued in January 1976.

"Accounting and Financial Management in the Forest Products Industries: A Guide to the Published Literature," issued in June 1975. (A supplement to this monograph was issued in March 1977 and January 1981.)

"A Decision Framework for Trading Lumber Futures," issued in October 1975.

"Capital Gains Tax Treatment in the Forest Products Industries," issued June 1976.

"Measurement Difficulties in the Log Conversion Process," issued June 1976.

"Capital Budgeting Practices in the Forest Products Industry," issued March 1978.

"A Reporting and Control System for Wood Products Futures Trading Activities," issued July 1978.

"Selected Issues of Financial Accounting and Reporting for Timber," issued November 1978.

"Pool Log Transfer System," issued August 1979.

"Fundamentals of Financing Major Timber Acquisitions," issued February 14, 1980.

"LIFO Inventories in the Forest Products Industry," issued July 1980.

"Accounting Controls for a Forest Products Firm," issued January 1981.

"Log Inventory Controls," issued April 1981.

"Accounting Treatment for Wood Products Futures Trading Activities," issued October 1981.

"A Reporting and Planning System for a Wood Products Operations," issued November 1981.

"Boise Cascade's Productivity Improvement Program," issued January 1982.

"Information Systems Planning in Weyerhaeuser Company," issued August 1982.

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