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The classification and comparative analysis of the methods available for developing the financial strategy of a company

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Abstract

This work deals with the classification and analysis of the methods available for developing the financial strategy of a company available both in Russia and abroad. The focus of this article is the well-known methods, as well as the little-known ones. The author gives her own classification of these methods and highlights advantages and disadvantages of these groups of methods. This analysis is important for the research and practical developments in the field of financial strategy. The work briefly reviews the ability of each group of methods prescribed by financial strategies to determine the economic behavior of companies.The author provides the system of these methods as part of their practical use.

Keywords: financial strategy, developing financial strategy, classification, comparative analysis;

1. Introduction

The paper contains the analysis of the methods available for developing the financial strategy of a company, which is relevant because many businesses are aware of the need for strategic planning of their financial activity in the conditions of continuous adaptation to the changes of the external and internal environment. It starts by the concept of a strategy and definitions of financial strategy followed by the methods recently available for the development of a company's financial strategy with the focus on their classification. The article reviews several classifications widely used in management underlining the advantages and disadvantages of each group of strategies.

2. The research

2.1. Definition of financial strategy

There are three types of strategies in the strategic management: corporate, functional strategies and strategies of individual business units. Financial strategy, along with marketing, production, human resources and innovation strategies relates to the functional strategies that are detailing the corporate strategy and supporting the strategies of individual business units with the resources. It is worth mentioning that the functional strategies are closely related to each other. So financial strategy has a strong link with the production, credit and innovation strategies, as evidenced by T.V. Klintsova [7].

Nowadays many companies are aware of the need for strategic planning of the financial activity in the conditions of continuous adaptation to the changes of the external and internal environment. E.O. Kokareva and T.V. Geniberg define a strategy as a long-term action plan of a firm, which aims to achieve the set of goals resulting from the external and internal firm's audit and based on the available resources [8].

There are many definitions of financial strategy. Some of them are the following.

I.A. Blanc defines a financial strategy as one of the most important types of functional strategies of the enterprise that provides it with all the basic directions to develop its financial activities and relations through the formation of long-term financial goals and the most effective ways to achieve them, their adequate adjustmentsьto the changing environmental conditions [3].

For V. Belashev, N. Gorickaya and G. Kleiner a financial strategy is a general plan of action to provide the necessary financial resources to a company and their effective use. Thus, G. Kleiner highlights the notion of "a financial-investment strategy" [14].

Other Russian researches such as N. Sokolova and T. Egorova view it as system decisions and planned directions of long-term activities for achieving the goals and financial objectives to ensure optimal and stable operation of the economic structure within the current reality and the expected results [11].

NASDAQ defines a financial strategy as practices a firm adopts to pursue its financial objectives [4].

Ruth Bender, Keith Ward in their work "Corporate financial strategy" [2] define it as having two components. Firstly, it relates to raising the funds needed by an organization in the most appropriate manner. Its second aspect is in managing the employment of those funds within the organization, including the decision to reinvest or distribute any subsequent profits generated by the organization.

The studied material enabled me to give a workable definition of a financial strategy that reflects my vision of this topic. I view the financial strategy as a one of the company's functional strategies aimed at achieving its long-term financial goals, optimal and stable operation in conditions of uncertain and risky external environment, which contains the system of management and financing these goals through the formation, coordination, distribution and use of financial resources and management system staff associated with these resources.

2.2. Classification of the methods for developing the financial strategy

During the work, I collected information on various methods available for the development of a company's financial strategy. These techniques have been then classified into six groups according to their underlying approach:

• Matrix techniques typified by J. Franshone and I. Romano matrix and V.B. Akulov's method;

• Methods based on the concept of residual income such as the EVA (Economic Value Added) model;

• Methods of portfolio analysis used for BCG matrix (Boston Consulting Group); the strategic management concept of Arthur D. Little; McKinsey and Co. Matrix; Shell matrix and I. Ansoff's matrix;

• Methods based on financial performance (so called the coefficient's method) including the method of M. Sorokin; Altman's model; Dupont's formula; and O.V. Nesmachniy's method;

• Rating approach underlying M.L. Dorofeev's method;

• Methods of mixed type such as the matrix of possible strategic directions of financial development by I. Blanc; the method presented by T.V. Geniberg, N.A. Ivanova and O.V. Polyakova; Z.F. Aminova's approach; A.V. Vorobyov and V.M. Ivanov's method; M.V. Gorelkina and N.N. Pogostinskaya's approach; A.A. Peshkova's method; P.V. Karpov's method; and L.V. Averyanova's method.

The analysis of various works has shown that foreign researches widely use the matrix method for the development of a financial strategy. It allows them to create a model of the organization at present and its desired position in future. This approach describes the different possible states of the organization through the inside and outside review of its place, role and capabilities. Currently, one of the most famous foreign matrix approaches is a matrix of financial strategies by J. Franshone and I. Romano [12], which helps one to attribute the organization to one of the matrix quadrants conventionally through the calculation of its major indicators such as the economic performance, the financial performance and the result of financial and economic activity. The matrix approach in Russia is represented by Akulov's method [1]. The researcher develops the approach presented by J. Franshone and I. Romane to create a matrix of strategies that adds the ability to analyze the dynamics of strategies.

Unlike it, another foreign approach identified as a separate group is a method based on the concept of residual income. It is typified by the EVA model that applies Alfred Marshall's residual approach [13]. The strategy uses the business value assessment where the value of the company is discovered through its book value increased by the present value of its future surplus value. This model serves as a tool for measuring the surplus value created by investments and assesses the quality of management decisions.

The methods of portfolio analysis are quite common in management, especially in foreign practice. Like the matrix techniques, all techniques of this group employ their analysis. However, the analysis of portfolio investments that determines the most profitable business combination or different strategic areas of the company management occupy a leading position here. The methods differ in the types of indicators for business valuation. Foreign representatives of portfolio methods are Boston Consulting Group matrix, the strategic management concept of Arthur D. Little, McKinsey & Co matrix, Shell matrix and Ansoff's matrix [5]. In Russia the portfolio methods are mostly used to create new synthetic approaches.

The next group worth reviewing is based on the financial performance (known as the coefficient's method). In this group financial indicators have dominant roles. So, the basis of DuPont formula is the factor analysis which views the return on equity through the influence of various factors and, accordingly, develops a strategy based on the growth of this indicator. Altman's model also considers several financial indicators that affect the level of probable loss of solvency and, therefore, the strategy originates from reducing the risk level. The Russian representative of this group is M. Sorokin, who offers to classify the financial performance by user groups and by business solutions areas. In this technique the strategy is based on the business value assessment and maximization through financial and non-financial solutions. Another Russian representative is the method presented by O.V. Nesmachniy who offers a comprehensive model of financial strategy where the main tool is the system of balanced indicators adapted to Russian realities.

Another group is a set of the rating approaches. The method of M.L. Dorofeev stands out in this group. This approach develops a matrix method adding there a ranking score of companies. It represents a set of the analytical results of the various financial and non-financial indicators determined by experts [9].

The last but not the least group includes the techniques of a mixed type using several methods to develop financial strategies. The best-known method among them is the matrix by I. Blanc that determines the financial strategies depending on the phase of the enterprise life cycle, different financial indicators and the dominant spheres through the matrix approach. A method of T.V. Geniberg, N.A Ivanova and O.V. Polyakova [6] synthesizes BCG portfolio approach and DuPont formula with the focus on the financial strategy based on the estimates of the company's sustainable growth. Aminova's approach, however, applies a dynamic analysis of the company's assets and liabilities. M.V. Gorelkina and N.N. Pogostinskaya, in their turn, use a variety of financial indicators and take into account the system of opportunities and threats provided by the environment. A similar procedure is used by A.V. Vorobyov and V.M. Ivanov [10], but they add the financial resource potential. Unlike them, P.N. Karpov’s method consists of eight steps combined into three phases. As for L.V. Averyanova, she uses the SWOT analysis complimented with a selection of the relevant financial indicators. Another researcher, A.A. Peshkova adds a special method for calculating the rational path of sustainable development that facilitates the choice of the reasonable market alternatives through identifying the growth rate of a firm's financial potential.

2.3. Comparative analyses of financial strategies: advantages and disadvantages

Now that we have reviewed different taxonomies, let's look at the advantages and disadvantages of each group's strategy presented in Table 1.

Table 1. Comparative analyses of financial strategies: advantages and disadvantages

Methods	Advantages	Disadvantages
Matrix techniques	The potential wide range of users	The life cycle stage of a company is not considered; The subjectivity of determining the strategic position of company
Methods based on the concept of residual income	A clear method of calculation; The influence of numerous factors taken into account	The life cycle stage of a company is not considered; A large number of edits (160 pieces)
The methods of portfolio analysis	Convenient to compare different businesses	The recommendations are mostly general
Methods based on financial performance	Convenient to compare different businesses	Not universal; A limited number of sources taken into account
Rating Approach	Recommendations for further development of the company and its current state; Use of financial and non-financial analyses	Subjective; Not all the features of the external environment and its changes taken into account
Methods of mixed type	Scopes for modifying models; Easy to find a suitable method for a particular business	Either a limited or too general application area; No developed technology to implement the financial solution

Apparently, each group has its strong and weak points. It is the general view of groups. Inside each, there can be some differences. So let us have some insights to find out the advantages and disadvantages of these methods to understand differences among them.

Therefore, the advantage of J. Franshone and I. Romano matrix, except those already listed in the table of matrix techniques is that it is possible to analyze dynamics in financial condition and prospects of the company's solvency. The disadvantage is that it may be difficult to determine the location of the businesses in the matrix quadrants in a particular period. Another matrix approach of this group, Akulov’s method, makes it ~~is~~ possible to analyze strategies in the dynamics.

The methods of portfolio analysis have some differences inside the group too. For example, another advantage of BCG matrix is that it identifies possible priorities choosing marketing, production and financial decisions on various activities, competition strategies, and the formation of the business portfolio of the company. In addition, this approach offers an overview of the demand and competitiveness of the company. The disadvantages are that the whole matrix is meaningless if there is no possibility of growth and there is no average parameter values, as everything is divided only into 4 groups. At the same time, one more advantage of McKinsey and Co. matrix is that it uses average values and a wide set of variables.

Sorokin's approach as one of the methods based on financial performance has some additional advantages, namely it considers the financial indicators through the financial condition of the solution spheres. The advantage of DuPont formula is that it is easy to calculate and make an analysis. Its disadvantage is the fact that it uses only indicators of the accounting report without other data sources taken into account.

The methods of mixed type face most differences among the approaches. Thus, the method of A.V. Vorobyov and V.M. Ivanov provides a detailed view of the phased implementation methodology, but it is very specific being created for waterway transport.

The model uses only the accounting report indicators and, hence, lacks the reliability of model results. The matrix of possible strategic directions of the financial development by I. Blanc, on the other hand, takes possible changes of individual factors and the environment into account. The advantage of the method provided by T.V. Geniberg, N.A. Ivanova and O.V. Polyakova is the distinction between the financial policy and the firm's policy on financing its activities. Its major disadvantage is the lack of a mathematical model to calculate the transitions from one quadrant to another.

Conclusion

In conclusion, it should be noted that the choice of the method for developing the financing strategy of a company depends on many factors, namely, the type of business, the company's life cycle, the production and product distribution specifics, external environmental factors, and, obviously, the goals set by the top managers of the company.

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