Directional Policy Matrix (DPM)

Idea In Short

The Directional Policy Matrix (DPM) is a framework that organizations can use to classify and categorise their business activities in terms of their strengths, capabilities or market position, and the way they perceive markets for attractiveness.

The Shell Directional Policy Matrix (DPM) is an extension of the Boston Consulting Group (BCG) Matrix. It is a valuable tool that helps organizations determine their preferred segments.

Origin

The Shell Directional Policy Matrix (DPM) is a traditional tool for portfolio analysis. It was originated to analyze qualitative variables present in the Strategic business Units (SBUs), which also need to be included in corporate planning. The origin of this toolkit was to:

1. Offer a comparative overview between SBUs, and
2. Provide more intelligent tools than only financial forecasting or financial return predictions

The idea of the Shell DPM foundation was to overcome the bias or predisposition towards financial returns. After the awakening of matrix tools for portfolio analysis, most multinationals, or when international corporations with multiple SBUs took the BCG or GE Matrix, then many corporations decided to refine it and adapt it for their specific needs. The concept of directional policy matrix got off and, that led to the emergence of Shell DPM. In the 1970s, The Royal Dutch Shell Group (as a parent company) approved that one of its companies, the Shell International Chemical Company Ltd., design a tool that could include qualitative and quantitative considerations in addition to the financial yardsticks. The Shell group wanted to systematize a new tool, called Shell Directional Policy Matrix (DPM). This specific concept DPM was conceptualized as a technique to build future corporate plans to identify:

1. The main criteria by which the prospects for a business sector or business units may be judged to be favorable, i.e., with high profit and growth potential for the industry or unfavorable
2. Those by which a company´s position in a sector may be judged to be strong or weak.

The Directional Policy Matrix

The Directional Policy Matrix measures the attractiveness of a segment and the capability of the organisation to support that segment.

Directional Policy Matrix

	Prospects for sector profitability		
Company's Competitive Capability	Unattractive	Average	Attractive
	Disinvest	Phased Withdrawal	Double /
	Phased Withdrawal	Custodial Growth	Try Harde
	Cash Generation	Growth Leader	Leader

Through a DPM, an organization will understand the segment it should invest in and the direction it should take. The directional policy matrix organizations determine whether decisions made in the day-to-day running of the organisation are in it's best interest.

Attractiveness Of A Market Segment

This includes criteria of market growth rate, market quality, industry situation and environmental considerations. On each of these variables an SBU or product is given from one to five stars. For instance, the variable - market quality might be judged on the basis of several criteria, such as pricing behaviour, past stability or profitability of that sector. The qualitative or quantitative evaluation of market quality is then converted into a rating from zero to four. The same procedure is followed for each of the other three variables, so the overall score on sector profitability is the total of the ratings on all four variables. Evaluating the attractiveness of a segment should include, but not be limited to, these variables:

- Size of the segment (number of customers, units or sales)
- Growth rate of the segment (a very important variable)

- Profit margins of the segment to the sales organisation
- Ongoing purchasing power of the segment
- Attainable market share given promotional budget, fragmentation of the market and competitors' promotional expenditures
- Required market share to break even

Organisational Capability

The same approach is used here, except that the company''s capabilities are assessed on the basis of market position, product research and development and production capability. These are further divided into sub-variables applicable to any particular industry. Shell emphasized that, regardless of the strategy that is eventually chosen, the aim is that is should be resilient, i.e. viable in a diverse range of potential futures. Hence, each strategy ideally should be evaluated against all future possible scenarios. Evaluating the capability of the organisation to meet the needs of the segments should include, but not be limited to, these variables analysed against the competition:

- Competitive capability of the organisation against the marketing mix (product/service, place, price and promotion)
- Access to distribution channels
- Capital and human resource investment required to serve the segment
- Brand association of the organisation in the eyes of the segment
- Current market share/likely future market share

The Matrix

Along the horizontal axis are prospects for business sector profitability, and along the vertical axis is a company's competitive capability. Business sector profitability includes the size of the market, expected growth, lack of competition, profit margins within the market.

Business Sector Profitability

Business sector profitability includes the size of the market, expected growth, lack of competition, profit margins within the market and other favorable political and socio-economic conditions.

Competitive Capability

On the other hand company's competitive capability is determined by the sales volume, the products reputation, reliability of service and competitive pricing. As with the GE-McKinsey Matrix, the location of an SBU in a cell of the matrix implies different strategic decisions. However, decisions often span options and in practice the zones are an irregular shape and do not tend to be accommodated by box shapes. Instead they blend into each other.

Zones

Each of the zones in Shell's Directional Policy Matrix is described as follows:

Divest

SBU's running in losses with uncertain cash flows. Theyshould be divested as the situation is not likely to improve in thenear future. These liquidate or move thee assets.

Phased Withdrawal

SBU's with weak competitive position in a lowgrowth market with very little chance of generating cash flows. Theyshould be phased out gradually. The cash realized should be investedin more profitable ventures.

Double Or Quit

Gamble on potential major SBU's for the future.Either invests more to use the prospects presented by the market orelse better to quit the business.

Custodial

SBU's are just like a cash cow, milk it and do notcommit any more resources. The corporate has to bear with thesituation by getting help from other SBU's or get out of the sceneso as to focus more on other attractive business.

Try Harder

SBU's could be vulnerable over a longer period oftime, but fine for now. They need additional resources to strengththeir capabilities. The corporate try harder to exploit the businessprospects thoroughly.

Cash Generator

Even more like a cash cow, milk here forexpansion elsewhere. SBU's may continue their operations, at leastfor generating strong cash flows and satisfactory profits. Nofurther investments are made.

Growth

Grow the market by focusing just enough resources here.These SBU's need funds to support product innovations, R&Dactivities etc.

Market Leadership

Major resources are focused upon the SBU. Itmust receive top priority.

Summary

TThe Directional Policy Matrix (DPM) helps evaluate organisations' strategic options against two composite dimensions - business strengths and market attractiveness. The DPM, therefore, enables organisations to conduct an analysis of their portfolio of products or areas of operation. It is a way of categorizing and prioritizing opportunities. The tool can be customized to unique content and made relevant to the individual strategic position of an organization in its market place. The grid plots market attractiveness against organizational capability; this allows management to appropriately prioritize resources and strategic investments.