

Competitive Strategies and Risk

Lecture Objectives

Review the concept of competitive advantage, explain its importance.

Define competition & describe how a firm's competitors can be determined.

Explain how resources & capabilities can lead to competitive advantage

Explain the relationship between competitive advantage and competitive strategies

Lecture Objectives (Cont'd)

Discuss Porter's generic competitive strategies

Describe the new perspectives on competitive strategies

Describe how a firm's competitive strategy is implemented

Discuss the various competitive postures and actions firms can take to defend or attack rivals

COMPETITIVE ADVANTAGE AND HOW IT IS OBTAINED

- Competitive Advantage
 - What sets an organization apart -- competitive edge
 - Controlling or having something others do not have
 - Doing something better than other organizations
 - Doing something other organizations cannot do
 - Competitive strategies are designed to exploit an organization's competitive advantage
 - Implies there are other competitors also trying to develop competitive advantage & attract customers
 - Competitive advantage can be eroded easily (& often quickly) by rival's actions

Understanding the Competitive Environment

- What is competition?
 - When organizations battle for some desired object or outcome
 - Customers
 - Market share
 - Survey rankings
 - Needed resources
 - Hypercompetition
 - A situation of intense and continually increasing levels of competition in today's business environment

Understanding the Competitive Environment

- Who are our competitors? -- 3 Perspectives
 - (1) Industry perspective
 - Identifies competitors as firms that are making the same products or providing the same service
 - Describes industries according to number of sellers & the similarities or differences in the products or services
 - The number of sellers & level of product-service differences will affect how intensely competitive the industry is

Who are our Competitors?

(2) Marketing perspective

- Competitors are firms that satisfy the same customer needs
- Intensity of competition depends on
 - How well the customer need is understood or defined
 - How well different firms are able to meet that need

Who are our Competitors?

(3) Strategic Group Perspective

- Competitors are firms that follow similar strategies
- Strategic group is a set of firms competing within an industry that have similar strategies & resources
- An single industry could have a few or several strategic groups depending on what strategic factors are important to different group of customers

Who are our Competitors?

- Strategic Group Perspective (cont'd)
 - Firms in same strategic group have **two or more** competitive characteristics in common
 - Sell in same price/quality range
 - Cover same geographic areas
 - Be vertically integrated to the same degree
 - Have comparable product line breath
 - Emphasize same types of distribution channels
 - Offer buyers similar services
 - Use identical technological approaches

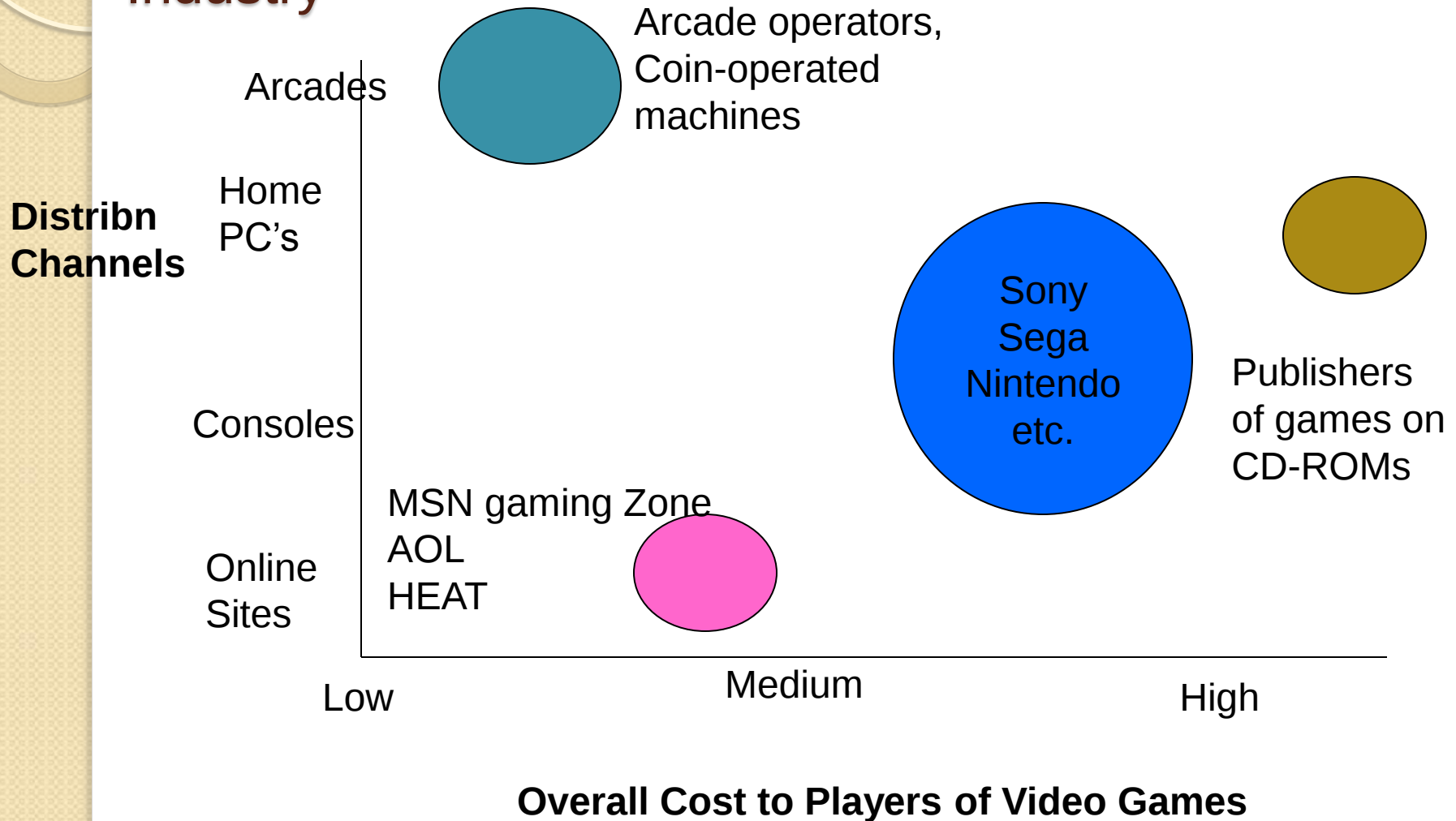
Who are our Competitors?

- Strategic Group Perspective (Cont'd)
 - Constructing a strategic group map
 - Identify competitive characteristics that differentiate firms in an industry from one another
 - Plot firms on a two-variable (X-Y) map using pairs of these differentiating characteristics
 - Assign firms that fall in about the same strategy space to same strategic groups
 - Draw circles around each group, making circles proportional to size of group's respective share of total industry sales

Who are our Competitors?

- Strategic Group Perspective (Cont'd)
 - Guidelines for constructing SGM
 - Variable selected as axes should **not** be highly correlated
 - Variables chosen as axes should expose **big differences** in how rivals compete
 - Variables do **not** have to be either quantitative or continuous
 - Drawing sizes of circles **proportional** to combined sales of firms in each strategic group allows map to reflect relative sizes of each strategic group
 - If more than two good competitive variables can be used, several maps can be drawn

Strategic Group Map of Competitors in Video Game Industry



Resources, Capabilities & Competitive Advantage (CA)

- Every firm has resources & work processes
 - Systems to do whatever it's in business to do
- **But** not every firm is able to
 - Effectively exploit its resources & capabilities
 - Obtain resources & capabilities it needs
- Some firms are able to “pull it together” & develop distinctive capabilities, others don't
- Competitive advantage implies gaining the edge on others – using resources & capabilities
- As firms strive for sustainable CA, stage for competition is set - intense, moderate, low

Competitive Advantage & Competitive Strategy

- What is competitive strategy?
 - Consists of business approaches to
 - **Attract** customers by fulfilling their expectations
 - **Withstand** competitive pressures
 - **Strengthen** market position
 - Exploits competitive advantage by
 - finding ways to use resources & capabilities to set firm apart from competitors

PORTER'S GENERIC COMPETITIVE STRATEGIES

- Competitive advantage come from one of two sources:
 - Having the **lowest cost** in the industry
 - Possessing a product or offering a service that is **perceived as unique** in the industry
- Another important factor is the scope of the product-market (broad or narrow)
- Mix of these factors provide basis for
 - Cost leadership strategy (low-cost strategy)
 - Differentiation strategy
 - Focus strategy

PORTER'S GENERIC COMPETITIVE STRATEGIES

		Competitive Advantage	
		Low Cost	Differentiation
Market Scope	Broad	Cost Leadership	Differentiation
	Narrow	Focus (Low Cost)	Focus (Differentiation)

Cost Leadership Strategy

- **Objective:**
 - Gain sustainable competitive advantage over competitors, using **low-cost** (not price)
 - Produce for broad customer base
- **Basic Theme (Keys to Success):**
 - ***Low-cost relative to competitors***
- Low cost implies **OVERALL LOW COST**
 - Not just low manufacturing or production cost
 - Product quality cannot be ignored

Characteristic of Cost Leaders

- Champion frugality
- Strict attention to production controls
- Rigorous use of budgets
- Little product differentiation
- Limited market segmentation
- Emphasis on productivity improvements
- Distinctive capabilities found in manufacturing & materials management

Successful Pursuit of Cost Leadership Strategy

- Every strategic decision is aimed at keeping cost as low as possible
- Efficiency is sought in all areas of operation
- All functional strategies & capabilities are directed at efficiency
- Doesn't have deep & wide product lines
- Market products aimed at “average” customer
- Little or no product frills or differences

When Cost Leadership Works Best

- Price competition is vigorous
- Product is standardized or readily available from many suppliers
- There are few ways to achieve differentiation that have value
- Most buyers use product in same ways
- Buyers incur low switching costs
- Buyers are large and have significant bargaining power

Competitive Strengths of Cost Leadership Strategy

- **RIVAL COMPETITORS** - compete using low price
- **BUYERS** - nullify power to drive down prices
- **SUPPLIERS** -Flexibility to cope with input cost increases
- **POTENTIAL ENTRANTS** - More efficient (through EOS) & pricing power
- **SUBSTITUTE PRODUCTS** - Potential use of low price

Drawbacks of Cost Leadership Strategy

- Being overly aggressive in cutting price
- Low cost methods are easily imitated by rivals
- Becoming too fixated on reducing costs and ignoring
 - Buyer interest in additional features (tastes)
 - Declining buyer sensitivity to price
 - Changes in how the product is used
- Technological breakthroughs open up cost reductions for rivals

Differentiation Strategy

- **Objective**
 - Offering products/services **perceived as unique** over the brands of rivals in an industry
- **Keys to Success**
 - Offer products/services that ***create value*** to customers
 - Offer products/services ***not easily matched*** or ***easily copied*** by rivals
 - ***Not spending more*** to differentiate the firm's products or service than the ***price premium that can be charged***

Differentiation Themes

- *Unique taste* -- Dr. Pepper
- *Special features* -- America Online
- *Superior service* -- FedEx, Ritz-Carlton
- *Spare parts availability* -- Caterpillar
- *More for your money* -- McDonald's, Wal-Mart
- *Engineering design and performance* -- Mercedes
- *Prestige* -- Rolex
- *Quality manufacture* -- Honda , Toyota
- *Technological leadership* -- 3M Corporation, Intel
- *Top-of-the-line image* -- Ralph Lauren, Chanel

Benefits of Differentiation

- A product / service with unique and appealing attributes allows a firm to
 - **Command a premium price** *and/or*
 - **Increase unit sales** *and/or*
 - **Build brand loyalty**
= Competitive Advantage

Characteristics of Successful Differentiators

- Every strategic decision & action is directed at setting the firm apart from competitors
- All functional strategies & capabilities are aimed at isolating & understanding specific market segments & developing product features that are valued by customers
- Has broad and wide product lines -- many different models, features, price ranges, etc.

Characteristics of Successful Differentiators

- Has many market segments & product features
- Controls costs but not as rigorous as the cost leader to preserve source of differentiation
- Strives to establish brand loyalty
- Competitive capabilities tends to be in **marketing** and **research & development**

Competitive Strengths of Differentiation

- **RIVAL COMPETITORS** - Brand loyalty & lower sensitivity to price
- **BUYERS** - lack of alternatives & low sensitivity to price
- **SUPPLIERS** - High margins provide ability to pay increases in input costs
- **POTENTIAL ENTRANTS** - Buyer loyalty & uniqueness of product/service
- **SUBSTITUTES** - lack of comparable features and customer loyalty

When Differentiation Works Better

- There are many ways to differentiate a product that have value and please customers
- Buyer needs and uses are diverse
- Few rivals are following a similar type of differentiation approach
- Technological change is fast-paced and competition is focused on evolving product features

Drawbacks of Differentiation

- Trying to differentiate on a feature buyers do not perceive as lowering their cost or enhancing their well-being
- *Over-differentiating* such that product features exceed customers' needs
- Charging a price premium that customers perceive is too high
- Failing to signal value
- Not understanding what customers want or prefer and differentiating on the “wrong” things
- Low-cost strategy can **defeat** a differentiation strategy when customers are satisfied with a standard product and do not see extra attributes as worth paying for!

Focus Strategy

- Firm pursues either a cost leadership or differentiation strategy but in a narrow customer group or segment
- Concentrates on serving specific market niche
 - Geographical area
 - Type of customer -- specific group of customers
 - Specific & specialized product line

Focus Strategy

- Objective
 - Serve the niche customers **better** than competitors
- Keys to Success
 - Choose a market niche where buyers have ***distinctive preferences, special requirements, or unique needs***
 - Develop unique capabilities to serve needs of target buyer segment

Focus Approaches

- **Approach 1: Cost Advantage**
 - Achieve **lower cost** than rivals in serving the specific or narrow segment
- **Approach 2: Differentiation Advantage**
 - Offer customers in niche market **something unique** in that market
 - Product features
 - Product innovations
 - Product quality
 - Customer responsiveness

Examples of Focus Strategy

- ***Focus Low-cost***
 - **Ikea:** Young furniture buyers who want style at low cost (price sensitive and low service customer groups)
 - **Southwest Airlines:** Short-haul, point-to-point service between midsize cities & secondary airports in large cities (low pricing & low service)
- ***Focus Differentiation***
 - **Rolex:** Serve highest end of wristwatch market (premium pricing & image)
 - **Rolls-Royce:** Serving luxurious end of automobile market (premium pricing & image)

Advantages of the Focus Strategy

- The focuser knows its market niche and knows it well
- The focuser can stay close to customers and respond quickly to their changing needs
- Focuser can develop strong brand loyalty which can be difficult for other competitors to overcome

Drawbacks of Focus Strategy

- Operates in small scale making it difficult to lower costs significantly. Technological advances has minimized this drawback
- Competitors find effective ways to match a focuser's capabilities in serving niche market
- Niche can become part of the overall market
- Segment becomes so attractive it becomes crowded with rivals, causing segment profits to be splintered

Stuck in the Middle

- Happen's when a firm is not successful in pursuing either a low-cost or differentiation strategy
- Occurs when a firm's
 - Costs are too high to compete with the low-cost leader
 - Products & services are not differentiated enough to compete with broad differentiator
- Unprofitable strategic position/direction
- Becoming “unstuck” involves making consistent strategic decisions about what CA to pursue & doing so by aligning resources & capabilities

NEW PERSPECTIVES ON COMPETITIVE STRATEGY

- Integrated Low-Cost Differentiation Strategy
 - Develops CA by simultaneously achieving low-cost and high levels of differentiation
 - Make an upscale product at a lower cost
 - Give customers more value for the money
 - Technological advancements that make this hybrid competitive strategy possible are
 - Flexible manufacturing systems
 - Just-in-time inventory systems
 - Computer-integrated manufacturing systems

NEW PERSPECTIVES ON COMPETITIVE STRATEGY

- Advantages of hybrid strategy
 - Competitive advantage from
 - ***Premium pricing*** and
 - ***Cost efficiency***
 - Success depends on having the capabilities to
 - ***Provide attractive performance and features, &***
 - ***Lower cost than rivals***
 - Can often ***out-compete*** both a low-cost provider and a differentiator

NEW PERSPECTIVES ON COMPETITIVE STRATEGY

- ***Examples of Integrated low-cost differentiation strategy***
 - ***Toyota & Honda***
 - Cost reduction through zero defects and differentiation through quality
 - ***Canon***
 - Cost reduction through EOS and differentiation through design of copiers
 - ***Wal-Mart***
 - Cost reduction through automation and differentiation through quality (more value)

NEW PERSPECTIVES ON COMPETITIVE STRATEGY

- Mintzberg' s generic Competitive Strategies
 - Differentiation by price
 - Differentiation by marketing image
 - Differentiation by product design
 - Differentiation by quality
 - Differentiation by product support
 - Undifferentiated strategy
 - Mirrors the realities of today's dynamic competitive environment

IMPLEMENTING COMPETITIVE STRATEGY

- Without implementation, a strategy is nothing more than a strategic idea or plan
- Role of functional strategies
 - Using resources & capabilities to create & exploit CA takes place through the actual strategies that are being used in the functional areas
 - Have a dual role in determining
 - What competitive strategy is most appropriate?
 - How is the strategy implemented?

Role of Functional Strategies

- What is the Competitive Strategy is most Appropriate?
 - Depends on
 - Current firm resources & capabilities in place
 - Fir resources & capabilities acquired & developed
 - Each of Porter's competitive strategies requires certain skills, resources, & organizational requirements

Role of Functional Strategies

- How is the strategy implemented?
 - Strategies must be aligned with functional expertise
 - Strategy of low-cost
 - Cost efficiencies -- manufacturing & materials mgt.
 - Capital investments in technology to reduce costs
 - Tight overhead cost control
 - Strategy of differentiation
 - Functional strategies **must** reflect choice

Competitive Postures and Actions

- Offensive Moves: Undertaken to
 - ***build new or stronger market positions*** and/or
 - ***create competitive advantage***
- Defensive Moves: Undertaken to
 - ***protect competitive advantage***
 - ***reduce risk of being attacked***
 - ***discourage the offensive strategies of rivals***
 - ***Blunt the impact of any attack***
 - ***Rarely a basis for creating competitive advantage***

Offensive Strategic Moves

- Matching or exceeding rivals' strength (Frontal assault)
- Capitalizing on rivals' weaknesses
- Simultaneous offense on many fronts
- End-run offensives (Komatsu's move to LDC's)
- Guerrilla offenses
- Preemptive Strikes (Microsoft's bundling of Internet Explorer with Windows 95 & 98)
- Acquisition of competitors

Defensive Strategic Moves

- Block avenues rivals can take to mount attack
 - sign exclusive contracts with best suppliers
 - patent alternative technologies
 - broaden product line to match rivals
 - Keep prices low on models that match rivals
 - Challenge rivals' products or practices in regulatory proceedings (Netscape vs. Microsoft), etc.
- Make clear willingness to fight challengers
 - Publicly make commitments to maintain market share
 - Publicly commit firm to policy of matching prices of items offered by rivals
 - Maintain excess cash reserves; etc.
- Lower inducement for attack (e.g., Southwest Airlines)

Evaluating & Changing Competitive Strategy

- Responsibility of managing strategically involves
 - Implementing competitive strategy
 - Monitoring, assessing, and evaluating strategy for performance effectiveness & efficiency
 - Competitive strategies are targeted at increasing sales revenues, market share, or profitability
 - Data on these areas help determine the impact of competitive strategy

Evaluating & Changing Competitive Strategy

- Changing Competitive Strategy
 - Organization's fundamental competitive strategy is not changed frequently and continually
 - Each competitive strategy entails the development of specific resources & capabilities. To change this is difficult
 - Major competitive strategic change should be approached realistically & intelligently
 - Although changing a firm's competitive strategy isn't very likely, modifying the competitive strategy *is*