Production and Efficiency

Economies of scale
- Lower unit costs due to large scale production volumes.

Learning effects
- Cost reductions due to learning by doing.

The experience curve
- Systematic unit-cost reductions that are the result of accumulated output.
Production and Efficiency: Economies of Scale

A typical long-run unit-cost curve:
Production and Efficiency: The Experience Curve

A typical experience curve:

FIGURE 5.3

Accumulated Output

Unit Costs

B

A
Production and Efficiency: Learning Effects

Economies of scale and learning effects:

FIGURE 5.2
Production and Efficiency: The Experience Curve

Unit production costs in an integrated steel mill and a minimill.

FIGURE 5.4
Production and Efficiency: Manufacturing and Mass Customization

Flexible manufacturing technology (lean production)
- Reduced setup times
- Increased machine utilization
- Improved quality control
- Lower inventory levels

Mass customization
- Low cost and product customization

Flexible machine cells
- Increased variety of operations
Production and Efficiency: Flexible Manufacturing

The tradeoff between costs and product variety

FIGURE 5.5
Marketing and Efficiency

Marketing strategy:

- Product design
- Advertising
- Promotion
- Pricing
- Distribution
The Relationship Between Average Unit Costs and Customer Defection Rates

FIGURE 5.6
The Relationship Between Customer Loyalty and Profit per Customer

Profit per Customer

Length of Time Customer Stays with Company

FIGURE 5.7
Materials Management, JIT, and Efficiency

Materials management

- Getting materials into and through the production process and out through the distribution system to the end user.

Just-In-Time (JIT)

- Reduce inventory holding costs by having materials arrive JIT to enter the production process.
- JIT risk: There are no buffer stocks for nondelivery or unanticipated increases in demand.
R&D Strategy and Efficiency

Design easy-to-manufacture products

- Reduce numbers of parts per unit.
- Reduce assembly time.
- Closely coordinate R&D and production activities.

Pioneer process innovations

- Innovations create competitive advantage through gains in process efficiencies.
Achieving Superior Innovation

Causes of the high failure rate of innovation:

- Uncertainty
  - Quantum innovation
  - Incremental innovation
- Poor commercialization
- Poor positioning strategy
- Technological myopia
- Slowness in marketing
Achieving Superior Customer Responsiveness

Developing a customer focus:
- Top leadership commitment to customers.
- Employee attitudes toward customers.
- Bringing customers into the company.

Satisfying customer needs:
- Customization of the features of products and services to meet the unique need of groups and individual customers.
- Reducing customer response times:
  - Marketing that communicates with production.
  - Flexible production and materials management.
  - Information systems that support the process.
Lec 4

Business-Level Strategy

Strategic Management

An Integrated Approach

Charles W. L. Hill

Gareth R. Jones

PowerPoint Presentation
by Charlie Cook

Fifth Edition
What Is Business-Level Strategy?

Business-level strategy

- A plan of action to use the firm’s resources and distinctive competencies to gain competitive advantage.

Abell’s “Business Definition” process

- Customer needs – product differentiation (what)
- Customer groups – market segmentation (who)
- Distinctive competencies – competitive actions (how)
Choosing a Generic Business-Level Strategy

Product/Market/Distinctive-Competency Choices and Generic Competitive Strategies

<table>
<thead>
<tr>
<th></th>
<th>Cost Leadership</th>
<th>Differentiation</th>
<th>Focus</th>
</tr>
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<tbody>
<tr>
<td><strong>Product Differentiation</strong></td>
<td>Low (principally by price)</td>
<td>High (principally by uniqueness)</td>
<td>Low to high (price or uniqueness)</td>
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<td><strong>Market Segmentation</strong></td>
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<td><strong>Distinctive Competency</strong></td>
<td>Manufacturing and materials management</td>
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</table>

**TABLE 6.1**
Types of Business-Level Strategies

- Offers low-priced products to customers
  - Focused Cost-Leadership Strategy
- Offers unique or distinctive products to customers
  - Focused Differentiation Strategy
- Offers products to only one group of customers
  - Cost-Leadership Strategy
- Offers products to many kinds of customers
  - Differentiation Strategy

FIGURE 6.1
Choosing a Business-Level Strategy

Cost-leadership strategy success is affected by:

- Competitors producing at equal or lower costs.
- The bargaining strength of suppliers.
- Powerful buyers demanding lower prices.
- Substitute products moving into the market.
- New entrants overcoming entry barriers.
Choosing a Business-Level Strategy

Differentiation strategy success is achieved through:

- An emphasis on product or service quality.
- Innovation in providing new features for which customers will pay a premium price.
- Responsiveness to customers after the sale.
- Appealing to the psychological desires of customers.
Choosing a Business-Level Strategy

Differentiation strategy success is affected by:

- Competitors imitating features and services.
- Increases in supplier costs exceeding differentiator’s price premium.
- Buyers becoming less brand loyal.
- Substitute products adding similar features.
- New entrants overcoming entry barriers related to differentiator’s competitive advantage.
Choosing a Business-Level Strategy

Focus strategy success is affected by:

- Competitor entry into focuser’s market segment.
- Suppliers capable of increasing costs affecting only the focuser.
- Buyers defecting from market segment.
- Substitute products attracting customers away from focuser’s segment.
- New entrants overcoming entry barriers that are the source of the focuser’s competitive advantage.
Strategic Groups and Business-Level Strategy

Implications for business-level strategy

- Immediate competitors are companies pursuing same strategy within the same strategic group.
- Different strategic groups can have a different standing with respect to the effects of the five competitive forces.

First mover advantage

- Benefits are first choice of customers and suppliers, setting standards, building entry barriers.
Choosing an Investment Strategy at the Business Level

Investment strategy

- The resources (human, functional, and financial) required to gain sustainable competitive advantage.

Competitive position

- Market share is an indicator of competitive strength.
- Distinctive competencies are competitive tools.

Life Cycle Effects

- An industry’s life cycle stage affects its attractiveness to investment prospects.
### Choosing an Investment Strategy at the Business Level

<table>
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<tr>
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**TABLE 6.2**
Chapter 6

Business-Level Strategy
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**TABLE 6.2**
Strategies in Fragmented Industries

Fragmented industry characteristics:

- Localized markets with low entry barriers (e.g., Mom’s Diner).
- Few economies of scale opportunities exist.
- High transportation costs (e.g., sand) for products.
- Focus strategies predominate (e.g., customer group, region).
Strategies in Fragmented Industries

Competing in fragmented industries requires strategic consolidation by:

- Chaining (Wal-Mart)
- Franchising (McDonald’s)
- Horizontal mergers (Dillard’s)
- Using the Internet (eBay)
Strategies in Embryonic and Growth Industries

Three strategies for an innovator competing in a newly emerging market/industry:

- Develop and market the technology itself.
- Develop and market the technology jointly with another company through a strategic alliance.
- License the technology to existing companies and let them develop the market.
How an Innovator’s Profits Can Be Competed Away

FIGURE 7.1

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Strategies in Embryonic and Growth Industries

An innovator’s optimal choice of growth industry strategy depends on:

- Complementary assets the innovator has that can be used to exploit and market the innovation.
- High barriers to imitation by competitors (e.g., patents).
- The capability of competitors to quickly imitate the pioneering company.
## Strategies for Profiting from Innovation

<table>
<thead>
<tr>
<th>Strategy</th>
<th>Does Innovator Have All Required Complementary Assets?</th>
<th>Likely Height of Barriers to Imitation</th>
<th>Number of Capable Competitors</th>
</tr>
</thead>
<tbody>
<tr>
<td>Going it alone</td>
<td>Yes</td>
<td>High</td>
<td>Few</td>
</tr>
<tr>
<td>Entering into alliance</td>
<td>No</td>
<td>High</td>
<td>Limited</td>
</tr>
<tr>
<td>License innovation</td>
<td>No</td>
<td>Low</td>
<td>Many</td>
</tr>
</tbody>
</table>

**TABLE 7.1**
Strategy in Mature Industries

Strategies for Deterring the Entry of Rivals

Figure 7.2

- Product proliferation
- Price cutting
- Maintaining excess capacity
Product Proliferation in the Restaurant Industry

FIGURE 7.3

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Strategies to Manage Rivalry in Mature Industries

Price signaling

- Leading competitors use price changes to convey their intentions to other competitors (i.e., tit-for-tat).

Price leadership

- One company sets the industry price; other competitors reference their prices to that price.

Nonprice competition

- Competition by any means other than price.
Four Nonprice Competitive Strategies

- **Existing**
  - Market penetration
- **New**
  - Product development
  - Market development
  - Product proliferation

**FIGURE 7.4**
Strategies to Manage Rivalry in Mature Industries

Capacity control strategies

- Preempt rival firms by building capacity ahead of anticipated increases in demand.
- Indirect coordination with rival firms to keep industry-wide capacity in line with demand.
FIGURE 7.5

Changes in Industry Capacity and Demand

Units

Time

Capacity

Demand
Supply and Distribution Strategy in Mature Industries

Vertical integration
- Backward towards input suppliers.
- Forward into distribution to consumers.

Choice of integration depends on:
- Need for close relationships with suppliers.
  - *Japanese vs. American styles*
- Need to ensure customer relationships.
  - *Complexity of product*
  - *Amount of product information required*
Strategies in Declining Industries

Leadership strategy
- A firm seeks to become dominant in the industry.

Niche strategy
- Focuses on demand pockets declining more slowly than the industry as a whole.

Harvest strategy
- Limits investment and optimizes cash flow.

Divestment strategy
- Company exits the industry by selling out early to others, avoiding liquidation.
Factors That Determine the Intensity of Competition in Declining Industries

- Speed of decline
- Height of exit barriers
- Level of fixed costs
- Commodity nature of product

Intensity of Competition

FIGURE 7.6
Strategy Selection in a Declining Industry

FIGURE 7.7

Company Strengths Relative to Remaining Pockets of Demand

Few strengths ↔ Many strengths

Divest
Niche or harvest
Harvest or divest
Leadership or niche
A Harvest Strategy

Liquidate

Start to harvest

Cash flow

Cash Flow

Market Share

FIGURE 7.8
Chapter 8
Strategy in the Global Environment

Strategic Management
An Integrated Approach

Charles W. L. Hill
Gareth R. Jones

PowerPoint Presentation
by Charlie Cook

Fifth Edition

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Profiting From Global Expansion

Earning high returns from transferring distinctive competencies to foreign markets.

Realizing location economies
- Using lower-cost locations reduces overall costs and fosters product differentiation for premium pricing.

Moving down the experience curve
- Larger global markets = more accumulated volume.

Global expansion and business-level strategies
- Linked by cost reductions and value creation.
Pressures for Cost Reduction and Local Responsiveness

Pressures for cost reductions

- Global competitors seek to minimize unit costs through location economies and attain low-cost competitor status.
- In commodity-type product industries, intense price competition predominates strategic concerns.

Pressures for local responsiveness arise from:

- Differences in local consumer tastes and preferences.
- Differences in infrastructure and traditional practices.
- Differences in distribution channels among countries.
- Host government economic and political demands.
Pressures for Cost Reduction and Local Responsiveness

FIGURE 8.1

Pressures for Local Responsiveness

Company A

Company C

Company B

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Strategic Choice

International strategy
- Create value by transferring skills and products abroad.

Multidomestic strategy
- Maximize local responsiveness by customizing products and marketing strategy for local markets.

Global strategy
- Pursue low-cost status, offer standardized global products.

Transnational strategy
- Use global learning to achieve low-cost status, differentiation, and local responsiveness simultaneously.
Four Basic Strategies

FIGURE 8.2

Pressures for Local Responsiveness

Pressures for Cost Reductions

Global strategy
Transnational strategy
International strategy
Multidomestic strategy
Cost Pressures and Pressures for Local Responsiveness Facing Caterpillar

FIGURE 8.3

Pressures for Cost Reductions

Low

High

Pressures for Local Responsiveness

Low

High

Caterpillar Inc.
## The Advantages and Disadvantages of Different Strategies for Competing Globally

<table>
<thead>
<tr>
<th>Strategy</th>
<th>Advantages</th>
<th>Disadvantages</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>International</strong></td>
<td>• Transfer of distinctive competencies to foreign markets</td>
<td>• Lack of local responsiveness</td>
</tr>
<tr>
<td></td>
<td>• Lack of local responsiveness</td>
<td>• Inability to realize location economies</td>
</tr>
<tr>
<td></td>
<td>• Inability to realize location economies</td>
<td>• Failure to exploit experience-curve effects</td>
</tr>
<tr>
<td></td>
<td>• Failure to exploit experience-curve effects</td>
<td></td>
</tr>
<tr>
<td><strong>Multidomestic</strong></td>
<td>• Ability to customize product offerings and marketing in accordance with local responsiveness</td>
<td>• Inability to realize location economies</td>
</tr>
<tr>
<td></td>
<td>• Inability to realize location economies</td>
<td>• Failure to exploit experience-curve effects</td>
</tr>
<tr>
<td></td>
<td>• Failure to transfer distinctive competencies to foreign markets</td>
<td>• Failure to exploit experience-curve effects</td>
</tr>
<tr>
<td><strong>Global</strong></td>
<td>• Ability to exploit experience-curve effects</td>
<td>• Lack of local responsiveness</td>
</tr>
<tr>
<td></td>
<td>• Ability to exploit location economies</td>
<td></td>
</tr>
<tr>
<td><strong>Transnational</strong></td>
<td>• Ability to exploit experience-curve effects</td>
<td>• Difficulties in implementation because of organizational problems</td>
</tr>
<tr>
<td></td>
<td>• Ability to exploit location economies</td>
<td></td>
</tr>
<tr>
<td></td>
<td>• Ability to customize product offerings and marketing in accordance with local responsiveness</td>
<td></td>
</tr>
<tr>
<td></td>
<td>• Reaping benefits of global learning</td>
<td></td>
</tr>
</tbody>
</table>

**TABLE 8.1**
Basic Entry Decisions

Which foreign markets?
- Politically and financially stable
- Developed and developing nations
- Free market systems

Timing of entry
- Pioneering costs versus first-mover advantages.

Scale of entry and strategic commitments
- Scale of entry affects the nature of competition in the national market. Implications of risks and benefits must be weighed carefully.
The Choice of Entry Mode

- Exporting
- Licensing
- Franchising
- Joint Ventures
- Wholly Owned Subsidiaries

Distinctive Competencies and Entry Mode

Pressures for Cost Reduction and Entry Mode
# The Advantages and Disadvantages of Different Entry Modes

<table>
<thead>
<tr>
<th>Entry Mode</th>
<th>Advantages</th>
<th>Disadvantages</th>
</tr>
</thead>
<tbody>
<tr>
<td>Exporting</td>
<td>• Ability to realize location and experience-curve economies</td>
<td>• High transport costs</td>
</tr>
<tr>
<td></td>
<td>• Ability to realize location and experience-curve economies</td>
<td>• Trade barriers</td>
</tr>
<tr>
<td></td>
<td>• Ability to realize location and experience-curve economies</td>
<td>• Problems with local marketing agents</td>
</tr>
<tr>
<td>Licensing</td>
<td>• Low development costs and risks</td>
<td>• Inability to realize location and experience-curve economies</td>
</tr>
<tr>
<td></td>
<td>• Low development costs and risks</td>
<td>• Inability to engage in global strategic coordination</td>
</tr>
<tr>
<td></td>
<td>• Low development costs and risks</td>
<td>• Lack of control over technology</td>
</tr>
<tr>
<td>Franchising</td>
<td>• Low development costs and risks</td>
<td>• Inability to engage in global strategic coordination</td>
</tr>
<tr>
<td></td>
<td>• Access to local partner’s knowledge</td>
<td>• Lack of control over quality</td>
</tr>
<tr>
<td></td>
<td>• Shared development costs and risks</td>
<td>• Inability to engage in global strategic coordination</td>
</tr>
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<td>• High costs and risks</td>
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<td>• Protection of technology</td>
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Global Strategic Alliances

Advantages
- Facilitate entry into foreign markets.
- Enable partners to share fixed costs and risks associated with new products and processes.
- Facilitate transfer of complementary skills between companies.
- Help establish technological standards.

Disadvantages
- Risk of giving away technological know-how.
- Risk of opening local market access to foreign alliance partner.
- Risk of not getting anything in return.
Making Strategic Alliances Work

Partner selection when done well:

- Helps the firm achieve its strategic goals.
- Results in a commonly shared vision for the alliance.
- Reduces opportunistic behaviors by the partners.
Structuring Alliances to Reduce Opportunism

Probability of opportunism by alliance partner reduced by

“Walling off” critical technology

Establishing contractual safeguards

Agreeing to swap valuable skills and technologies

Seeking credible commitments

FIGURE 8.4
Managing the Alliance

Maximizing the benefits of an alliance:

- Develop a sensitivity to cultural differences.
- Build interpersonal relationships and networks among managers from different companies.
- Learn from alliance partners and put the knowledge to use in the organization.