Università di Roma

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Business Strategy

Chapter 5

Business-Level Strategy

KNOWLEDGE OBJECTIVES

- Define business-level strategy.
- Discuss the relationship between customers and business-level strategies in terms of who, what, and how.
- Explain the differences among business-level strategies.
- Use the five forces model to explain above average returns
- Risks of using each of the business-level strategies.

Business-Level Strategy

- A **business-level strategy** is an integrated and coordinated set of commitments and actions the firm uses to gain a competitive advantage by exploiting core competencies in specific product markets.
- Every firm forms and uses a business-level strategy.
- Business-level strategy is the core strategy—the strategy that the firm forms to describe how it intends to compete in a product market.

Customers: Their Relationship with Business-Level Strategies

In selecting a business-level strategy the firm determines:

1. *who* it will serve
2. *what* needs those target customers have that it will satisfy
3. *how* those needs will be satisfied

Effectively Managing Relationships with Customers

Customer relationships are strengthened by offering them superior value.

- Delivering superior value often results in increased customer loyalty.
- Customer loyalty has a positive relationship with profitability.

Reach, Richness, and Affiliation

Establish a competitive advantage along these dimensions:

- Reach

  the firm's access and connection to customers
- Richness

  the depth and detail of the two-way flow of information between the firm and customers
- Affiliation

  facilitating useful interactions with customers

Who: Determining the Customers to Serve

Market segmentation is a process used to cluster people with similar needs into individual and identifiable groups.

Consumer Markets
1. Demographic factors
2. Socioeconomic factors
3. Geographic factors
4. Psychological factors
5. Consumption patterns
6. Perceptual factors

Industrial Markets
1. End-use segments
2. Product segments
3. Geographic segments
4. Common buying factor segments
5. Customer size segments

What: Determining Which Customer Needs to Satisfy

- Needs (what) are related to a product's benefits and features.
- A basic need of all customers is to buy products that create value for them.
- The most effective firms continuously strive to anticipate changes in customers' needs.

How: Determining Core Competencies Necessary to Satisfy Customer Needs

- Firms use core competencies (how) to implement value-creating strategies and thereby satisfy customers’ needs.
- Only those firms with the capacity to continuously improve, innovate, and upgrade their competencies can expect to meet and hopefully exceed customers’ expectations across time

Business-Level Strategies

The purpose of a business-level strategy is to create differences between the firm’s position and those of its competitors.

Types of Business-Level Strategies

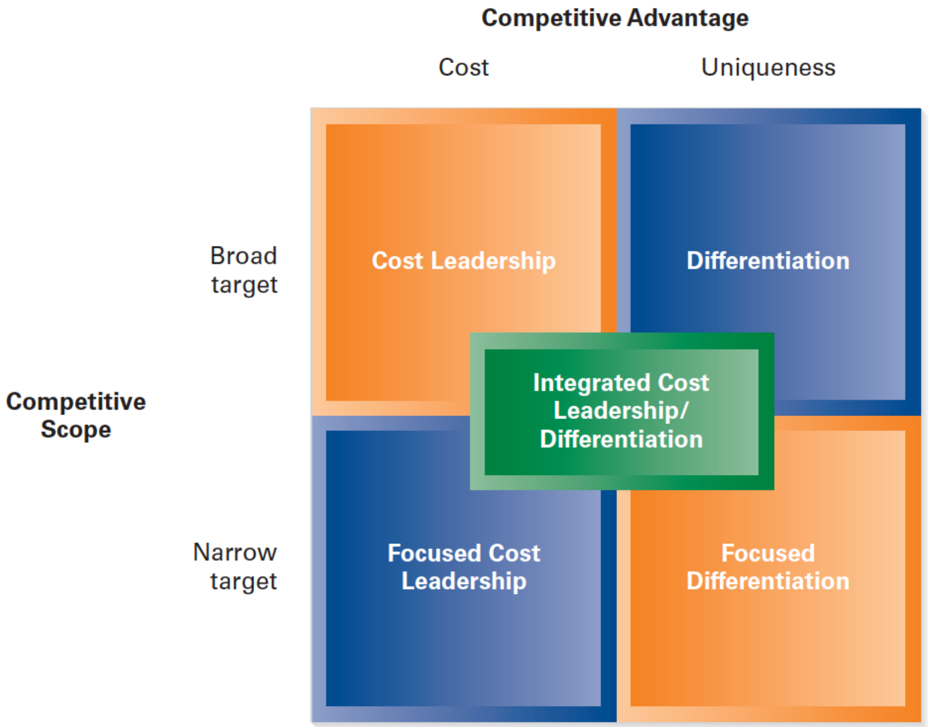


Figure 4.2 Five Business-Level Strategies

Cost Leadership Strategy

- The **cost leadership strategy** is an integrated set of actions taken to produce goods or services with features that are acceptable to customers at the lowest cost, relative to that of competitors.

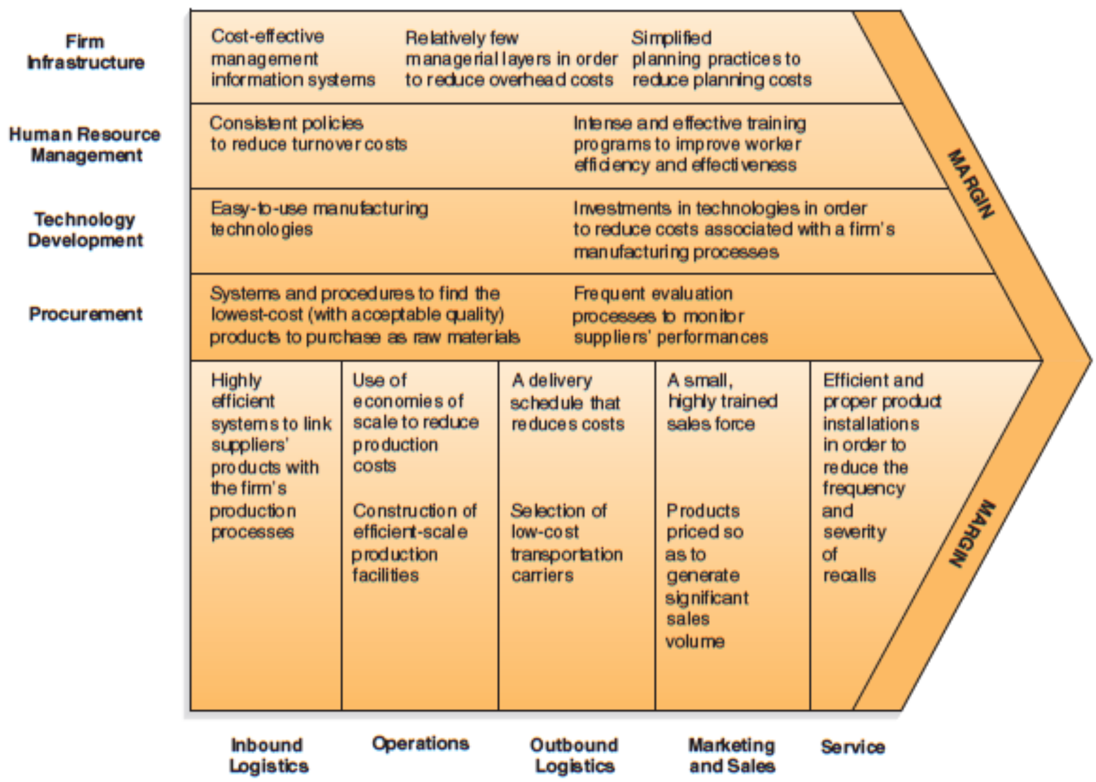
- Firms using the cost leadership strategy commonly sell standardized goods or services (but with competitive levels of differentiation) to the industry's most typical customers.

Cost Leadership Strategy

How to complete
the **primary** and **support activities**
to reduce costs still further while maintaining
competitive levels of differentiation?

- As primary activities: inbound logistics and outbound logistics
- Support activities: for example procurement

Cost Leadership Strategy



Ryanair Cost Leadership Strategy

- Airport-related cost savings
  - Secondary airports
  - Sort of monopoly on many of its routes
  - Short-haul/point-to-point flights
- Aircraft-related cost savings:
  - Single type of aircraft (Boeing 737-800)
  - High aircarft usage (fast turnaround)
- Personnel-related costs savings:
  - Salaries lower than the industry average
  - Salary payments on Ryanair credit cards
  - "Saving" on social security
- Customer service costs:
  - Direct Internet booking
  - Rigid terms towards passengers

30 YEARS OF LOW FARES 1985-2015 RYANAIR

Cost Leadership Strategy and the Five Forces of Competition

- Rivalry Among Competing Firms

Can use cost leadership strategy to advantage since:

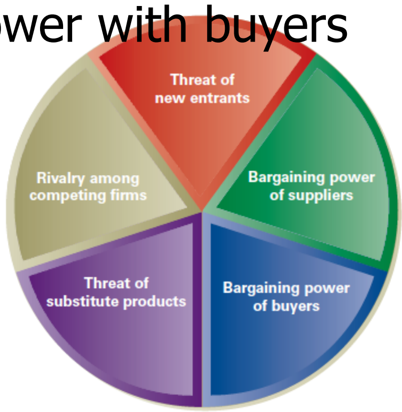
  - competitors avoid price wars with cost leaders, creating higher profits for the entire industry

Cost Leadership Strategy and the Five Forces of Competition

- Bargaining Power of Buyers

Can mitigate buyers' power by:

- driving prices far below competitors, causing them to exit and shifting power with buyers back to the firm



Cost Leadership Strategy and the Five Forces of Competition

- Bargaining Power of Suppliers

Can mitigate suppliers' power by:

- being able to absorb cost increases due to low cost position
- being able to make very large purchases, reducing chance of supplier using power

Cost Leadership Strategy and the Five Forces of Competition

- Threat of New Entrants

Can defend against new entrants because:

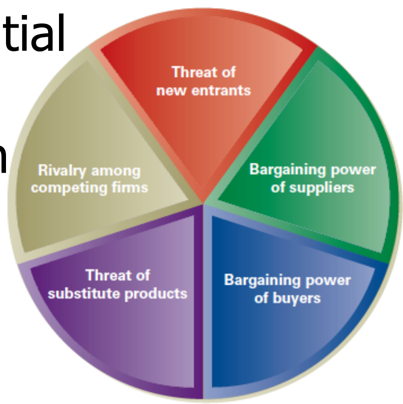
  - their need to enter on a large scale in order to be cost competitive
  - the time it takes to move down the learning curve

Cost Leadership Strategy and the Five Forces of Competition

- Threat of Substitute Products

Well positioned relative to substitutes because:

  - make investments to be first to create substitutes
  - buy patents developed by potential substitutes
  - lower prices in order to maintain value position



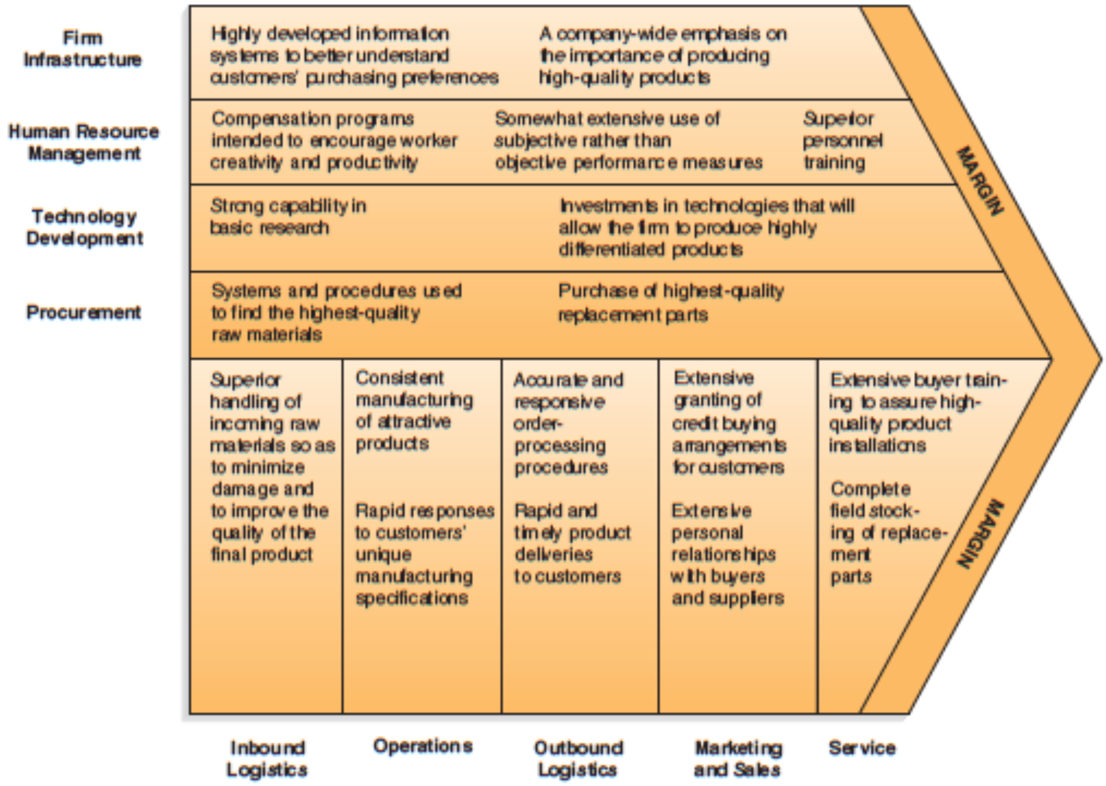
Competitive Risks of the Cost Leadership Strategy

- Dramatic technological change could take away your cost advantage.
- Focus on efficiency could cause cost leader to overlook changes in customer preferences (with a negative impact on pricing).
- Competitors may learn how to imitate value chain.

Differentiation Strategy

- The **differentiation strategy** is an integrated set of actions taken to produce goods or services (at an acceptable cost) that customers perceive as being different in ways that are important to them.
- Through the differentiation strategy, the firm produces nonstandardized (that is, unique) products for customers who value differentiated features more than they value low cost.

Differentiation Strategy



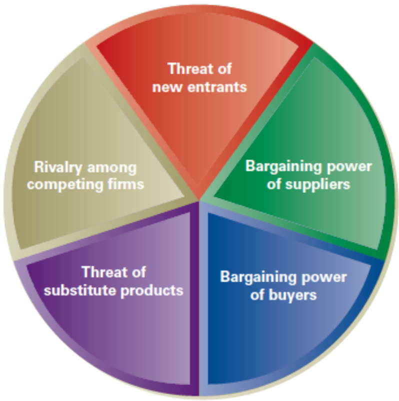
Apple Differentiation Strategy

- Innovation related choices:
  - First mover strategy, creating new markets
  - Apple "eco-system"
  - Closed innovation and "own" standard
- Product features-related choices:
  - Innovative
  - High performance
  - High price
- Distribution related choices:
  - Selected
  - Conveying a special atmosphere
- Branding related choices:
  - Corporate value & Steve Jobs
  - Unique brand experience

Differentiation Strategy and the Five Forces of Competition

- Rivalry Among Competing Firms

Can defend against competition because:
  - brand loyalty to differentiated product offsets price competition



Differentiation Strategy and the Five Forces of Competition

- Bargaining Power of Buyers

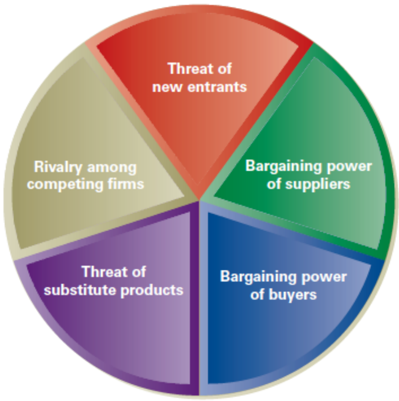
Can mitigate buyer power because:
  - well differentiated products reduce customer sensitivity to price increases

Differentiation Strategy and the Five Forces of Competition

- Bargaining Power of Suppliers

Can mitigate suppliers' power by:

  - absorbing price increases due to higher margins
  - passing along higher supplier prices because buyers are loyal to differentiated brand

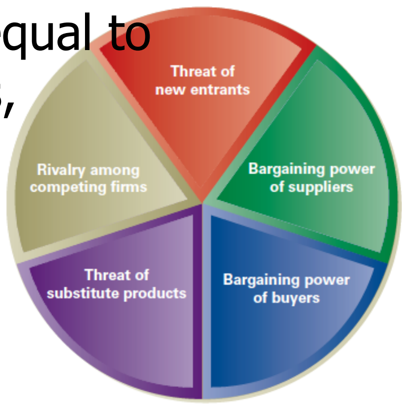


Differentiation Strategy and the Five Forces of Competition

- Threat of New Entrants

Can defend against new entrants because:

  - new products must surpass proven products or,
  - new products must be at least equal to performance of proven products, but offered at lower prices



Differentiation Strategy and the Five Forces of Competition

- Threat of Substitute Products

Well positioned relative to substitutes because:

  - brand loyalty to a differentiated product tends to reduce customers' testing of new products or switching brands

Competitive Risks of the Differentiation Strategy

- Customers might decide that the price differential between the differentiator's product and the cost leader's product is too large.
- Firm's means of differentiation may cease to provide value for which customers are willing to pay.
- Experience may narrow customer's perceptions of the value of differentiated features of the firm's products.
- Makers of counterfeit goods may attempt to replicate differentiated features of the firm's products.

Focus Strategies

- The **focus strategy** is an integrated set of actions taken to produce goods or services that serve the needs of a particular competitive segment.
  - a particular buyer group
  - a different segment of a product line
  - a different geographic market

Focus Strategies

Firms can create value for customers in specific and unique market segments by using the

- the focused cost leadership strategy

or

- the focused differentiation strategy.

Competitive Risks of Focus Strategies

- Firm may be "outfocused" by competitors.
- Large competitor may set its sights on your niche market.
- Preferences of niche market may change to match those of broad market.

Integrated Cost Leadership/Differentiation Strategy

- The integrated cost leadership/ differentiation strategy involves engaging in primary and support activities that allow a fi rm to simultaneously pursue low cost and differentiation.
- The aim is to efficiently produce products (source of maintaining low) with some differentiated features (creating unique value) .

Integrated Cost Leadership/Differentiation Strategy

- **Flexibility** is required for firms to complete primary and support activities in ways that allow them to use the integrated cost leadership/differentiation strategy in order to produce somewhat differentiated products at relatively low costs.

Three source of Flexibility:

- Flexible manufacturing systems,
- Information networks,
- and Total quality management systems

Competitive Risks of the Integrated Cost Leadership/Differentiation Strategy

- An integrated cost/differentiation business level strategy often involves compromises (neither the lowest cost nor the most differentiated firm)

- The firm may become “stuck in the middle” lacking the strong commitment and expertise that accompanies firms following either a cost leadership or a differentiated strategy