Chapter 5
Strategies in Action

Chapter Outline

- Long-Term Objectives
- Types of Strategies
- Integration Strategies

Chapter Outline (cont’d)

- Intensive Strategies
- Diversification Strategies
- Defensive Strategies

Chapter Outline (cont’d)

- Michael Porter’s Generic Strategies
- Means for Achieving Strategies
- First Mover Advantages

Chapter Outline (cont’d)

- Outsourcing
- Strategic Management in Nonprofit & Governmental Organizations
- Strategic Management in Small Firms

Strategies in Action

- Strategies for taking the hill won’t necessarily hold it. – Amar Bhide
- The early bird may get the worm, but the second mouse gets the cheese. – Unknown
Strategies in Action

Companies Embrace Strategic Planning

-- Quest for higher revenues
-- Quest for higher profits

Long-Term Objectives

Objectives --

- Quantifiable
- Measurable
- Realistic
- Understandable
- Challenging

Long-Term Objectives

Objectives --

- Hierarchical
- Obtainable
- Congruent
- Time-line

Long-Term Objectives

Objectives Necessary --

- Corporate Level
- Divisional Level
- Functional Level

Long-Term Objectives

Strategists Should Avoid --

- Managing by Extrapolation
- Managing by Crisis
- Managing by Subjectives
- Managing by Hope
**Long-Term Objectives**

<table>
<thead>
<tr>
<th>Organizational Level</th>
<th>Basis for Annual Bonus/Merit Pay</th>
</tr>
</thead>
<tbody>
<tr>
<td>Corporate</td>
<td>75% on long-term objectives</td>
</tr>
<tr>
<td>Division</td>
<td>50% on long-term objectives</td>
</tr>
<tr>
<td>Function</td>
<td>25% on long-term objectives</td>
</tr>
</tbody>
</table>

**Financial vs. Strategic Objectives**

**Financial Objectives**
- Growth in revenues
- Growth in earnings
- Higher dividends
- Higher profit margins
- Higher Earnings per share
- Improved cash flow

**Strategic Objectives**
- Larger market share
- Quicker on-time delivery than rivals
- Quicker design-to-market times than rivals
- Lower costs than rivals
- Higher product quality than rivals
- Wider geographic coverage than rivals

**Trade-Off**
- Maximize short-term financial objectives – harm long-term strategic objectives
- Pursue increased market share at the expense of short-term profitability
- Tradeoffs related to risk of actions; concern for business ethics; need to preserve natural environment; social responsibility issues

**Types of Strategies**

**A Large Company**
- Corp Level
- Division Level
- Functional Level
- Operational Level

**A Small Company**
- Company Level
- Functional Level
- Operational Level
The Balanced Scorecard

Robert Kaplan & David Norton --

- Strategy evaluation & control technique
- Balance financial measures with non-financial measures
- Balance shareholder objectives with customer & operational objectives

Types of Strategies

- **Vertical Integration Strategies**
- **Forward Integration**
- **Backward Integration**
- **Horizontal Integration**

**Vertical Integration Strategies**

**Gain Control Over --**

- Distributors
- Suppliers
- Competitors

**Forward Integration Strategies**

**Gain Control Over --**

- Distributors
- Retailers

**Forward Integration Strategies**

**Guidelines --**

- Current distributors – expensive or unreliable
- Availability of quality distributors – limited
- Firm competes in industry expected to grow markedly
- Firm has both capital & HR to manage new business of distribution
- Current distributors have high profit margins

**Backward Integration Strategies**

**Ownership or Control --**

- Firm’s suppliers
Backward Integration Strategies
Guidelines --
- Current suppliers – expensive or unreliable
- # of suppliers is small; # competitors is large
- High growth in industry sector
- Firm has both capital & HR to manage new business
- Stable prices are important
- Current suppliers have high profit margins

Horizontal Integration Strategies
Ownership or Control --
- Firm's competitors

Horizontal Integration Strategies
Guidelines --
- Gain monopolistic characteristics w/o federal government challenge
- Competes in growing industry
- Increased economies of scale – major competitive advantages
- Faltering due to lack of managerial expertise or need for particular resource

Types of Strategies
- Intensive Strategies
- Market Penetration
- Market Development
- Product Development

Intensive Strategies
Intensive Efforts --
- Improve competitive position with existing products

Market Penetration Strategies
Increased Market Share --
- Present products/services
- Present markets
- Greater marketing efforts
Market Penetration Strategies

Guidelines --
- Current markets not saturated
- Usage rate of present customers can be increased significantly
- Shares of competitors declining; industry sales increasing
- Increased economies of scale provide major competitive advantage

Market Development Strategies

New Markets --
- Present products/services to new geographic areas

Guidelines --
- New channels of distribution – reliable, inexpensive, good quality
- Firm is successful at what it does
- Untapped/unsaturated markets
- Excess production capacity
- Basic industry rapidly becoming global

Product Development Strategies

Increased Sales --
- Improving present products/services
- Developing new products/services

Guidelines --
- Products in maturity stage of life cycle
- Industry characterized by rapid technological development
- Competitors offer better-quality products @ comparable prices
- Compete in high-growth industry
- Strong R&D capabilities

Types of Strategies

- Concentric Diversification
- Conglomerate Diversification
- Horizontal Diversification
Diversification Strategies

Less Popular --

- More difficult to manage diverse business activities

Concentric Diversification Strategies

Addition --

- New & related products/services

Guidelines --

- Compete in no/slow growth industry
- New & related products increases sales of current products
- New & related products offered at competitive prices
- Current products—decline stage of product life cycle
- Strong management team

Conglomerate Diversification Strategies

Addition --

- New & unrelated products/services

Guidelines --

- Declining annual sales & profits
- Capital & managerial ability to compete in new industry
- Financial synergy between acquired and acquiring firms
- Current markets for present products - saturated

Horizontal Diversification Strategies

Addition --

- New & unrelated products/services for current customers
Horizontal Diversification Strategies

Guidelines --

- Adding new products/services would significantly increase revenues
- Highly competitive and/or no-growth industry; low margins & returns
- Current distribution channels can be used
- New products have counter cyclical sales patterns

Types of Strategies

- Defensive Strategies
  - Retrenchment
  - Divestiture
  - Liquidation

Retrenchment Strategies

Regrouping --

- Cost & asset reduction to reverse declining sales & profit

Guidelines --

- Failed to meet objectives & goals consistency; has distinctive competencies
- Firm is one of weaker competitors
- Inefficiency, low profitability, poor employee morale, pressure for stockholders
- Strategic managers have failed
- Rapid growth in size; major internal reorganization necessary

Divestiture Strategies

- Selling a division or part of an organization.

Guidelines --

- Retrenchment failed to attain improvements
- Division needs more resources than are available
- Division responsible for firm’s overall poor performance
- Division is a mis-fit with organization
- Large amount of cash is needed and cannot be raised through other sources
2003 Examples

<table>
<thead>
<tr>
<th>Integration Type</th>
<th>Example</th>
</tr>
</thead>
<tbody>
<tr>
<td>Forward Integration</td>
<td>Doll maker &amp; mail order firm, Pleasant Co., opened a retail store in Manhattan</td>
</tr>
<tr>
<td>Backward Integration</td>
<td>McDonalds recently acquired a paper cup producer</td>
</tr>
<tr>
<td>Horizontal Integration</td>
<td>Callaway Golf recently acquired Top-Flite Golf Company</td>
</tr>
</tbody>
</table>

2003 Examples

<table>
<thead>
<tr>
<th>Development Type</th>
<th>Example</th>
</tr>
</thead>
<tbody>
<tr>
<td>Market Penetration</td>
<td>SABMiller Plc spent $500 million in 2003 on marketing its Miller brands of beer</td>
</tr>
<tr>
<td>Market Development</td>
<td>JetBlue is adding dozens of new routes</td>
</tr>
<tr>
<td>Product Development</td>
<td>GM developing hydrogen powered automobiles or Pfizer developing a new antismoking pill</td>
</tr>
</tbody>
</table>

2003 Examples

<table>
<thead>
<tr>
<th>Diversification Type</th>
<th>Example</th>
</tr>
</thead>
<tbody>
<tr>
<td>Concentric Diversification</td>
<td>Microsoft launched its first personal computers that double as entertainment centers</td>
</tr>
<tr>
<td>Conglomerate Diversification</td>
<td>The video-rental firm Blockbuster may acquire the DVD and music direct-marketing firm Columbia House</td>
</tr>
<tr>
<td>Horizontal Diversification</td>
<td>Viacom acquired Comedy Central, from AOL</td>
</tr>
</tbody>
</table>

2003 Examples

| Retrenchment              | America West Airlines closing its hub at Columbus, Ohio and laying off 390 employees |
| Divestiture               | ConocoPhillips recently sold its Circle K convenience store chain to Alimentation Couche-Tard, a Canadian firm |
| Liquidation               | Sprint liquidated its Web-hosting division                               |

Liquidation Strategies

Selling

- Company's assets, in parts, for their tangible worth

Liquidation Strategies

Guidelines --

- Retrenchment & divestiture failed
- Only alternative is bankruptcy
- Minimize stockholder loss by selling firm's assets
Michael Porter’s Generic Strategies

Cost Leadership Strategies

Differentiation Strategies

Focus Strategies

Generic Strategies

Cost Leadership

- In conjunction with differentiation
- Economies or diseconomies of scale
- Capacity utilization achieved
- Linkages w/ suppliers & distributors

Low Cost Producer Advantage

- Many price-sensitive buyers
- Few ways of achieving differentiation
- Buyers not sensitive to brand differences
- Large # of buyers w/bargaining power

Differentiation

- Greater product flexibility
- Greater compatibility
- Lower costs
- Improved service
- Greater convenience
- More features

Focus

- Industry segment of sufficient size
- Good growth potential
- Not crucial to success of major competitors

Means for Achieving Strategies

Joint Venture/Partnering -

- Two or more companies form a temporary partnership or consortium for purpose of capitalizing on some opportunity.
Means for Achieving Strategies

Cooperative Arrangements -

- R&D partnerships
- Cross-distribution agreements
- Cross-licensing agreements
- Cross-manufacturing agreements
- Joint-bidding consortia

Why Joint Ventures Fail -

- Managers who must collaborate daily; not involved in developing the venture
- Benefits the company not the customers
- Not supported equally by both partners
- May begin to compete with one of the partners

Joint Ventures

Guidelines --

- Synergies between private and publicly held
- Domestic with foreign firm, local management can reduce risk
- Complementary distinctive competencies
- Resources & risks where project is highly profitable (e.g. Alaska Pipeline)
- Two or more smaller firms competing w/larger firm
- Need to introduce new technology quickly

Means for Achieving Strategies

Mergers & Acquisitions

- Provide improved capacity utilization
- Better use of existing sales force
- Reduce managerial staff
- Gain economies of scale
- Smooth out seasonal trends in sales
- Gain new technology
- Access to new suppliers, distributors, customers, products, creditors

Recent Mergers

<table>
<thead>
<tr>
<th>Acquiring Firm</th>
<th>Acquired Firm</th>
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</thead>
<tbody>
<tr>
<td>IBM</td>
<td>Rational Software Corp</td>
</tr>
<tr>
<td>Yahoo</td>
<td>Inktomi Corp</td>
</tr>
<tr>
<td>U.S. Steel</td>
<td>National Steel Corp</td>
</tr>
<tr>
<td>Pfizer</td>
<td>Pharmacia</td>
</tr>
<tr>
<td>Krispy Kreme Doughnuts</td>
<td>Montana Mills</td>
</tr>
<tr>
<td>Oracle</td>
<td>People Soft</td>
</tr>
<tr>
<td>Palm</td>
<td>Handspring</td>
</tr>
<tr>
<td>Nike</td>
<td>Converse</td>
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First Mover Advantages

- Benefits a firm may achieve by entering a new market or developing a new product or service prior to rival firms.
**First Mover Advantages**

**Potential Advantages**

- Securing access to rare resources
- Gaining new knowledge of key factors & issues
- Carving out market share
- Easy to defend position & costly for rival firms to overtake

**Outsourcing**

**Business-process outsourcing (BPO)**

- Companies taking over the functional operations of other firms

**Outsourcing**

**Benefits**

- Less expensive
- Allows firm to focus on core business
- Enables firm to provide better services

**For Review (Chapter 5)**

**Key Terms & Concepts**

- Acquisition
- Backward Integration
- Bankruptcy
- Combination Strategy
- Concentric Diversification
- Conglomerate Diversification
- Cooperative Arrangements
- Cost Leadership

- Horizontal Diversification
- Intensive Strategies
- Horizontal Integration
- Joint Venture
- Hostile Takeover
- Leveraged Buyout
- Integration Strategies
- Liquidation
<table>
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<th>Key Terms &amp; Concepts</th>
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<td>Long-Term Objectives</td>
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<tr>
<td>Market Development</td>
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<tr>
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<td>Merger</td>
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