DCU BUSINESS SCHOOL

Business Strategy

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Introduction

The strategy has been the keyword in the success of the organisation, but the rational about the strategy in Michael Porter's framework helps explain that how organisations have achieved superior performance when they face competition and generated significant benefits. To understand how the strategy helps in the progression of the firm, it is necessary to start with the understanding of the evolution of the strategy five decades ago. The strategy has evolved over these number of years and still continue to develop, but there have been various perspectives of different people over these years on strategy (Mintzberg & Lampel, 1999). The birth of strategy was in the early 1950's with a goal setting approach to currently being an approach to every thinking being critical and strategic for the wellbeing of the organisation. Managers have been learning new rules of strategy over these time and regarding strategy for companies, they must be flexible to react to market variations, a benchmark to achieve best practice, outsource to increase efficiency and nurture core competencies to stay ahead of competitors (Porter, 1996). But, Strategy is not just a plan or an idea, it is the manner of thinking for the company to approach various things (Montgomery, 2008) because if a company opt for any strategy, they have to live with it because changing a strategy is not spontaneous, it takes time. There was a time when positioning was the core of strategy, but over time due to changing technologies and vibrant market this approach changed as positioning was too passive (Porter, 1996). Sometimes, operational effectiveness is misinterpreted as of being an effective strategy, but both are two different concepts, and it is important to understand differences between them as both lead to higher performance. The strategic approach is vital for the organisation even if they have operational effectiveness because competition which is only based on operational efficiency is vicious leading to wars of attrition that can limit competition (Porter, 1996). The thoughtful approach of the forces that shape competition is also vital as these forces define the profitability of an industry and also plays a significant role in the formulation of the strategy (Porter, 2008). The five competitive forces that are important in shaping the strategy are the threat of entry of the new entrants in the market, the power of supplier, the power of buyers, fear of substitute and conflict amongst existing competitors. By analysing these five forces framework, we can gain a whole scenario of what benefits and hindrances exist in the profitability of the industry, and also the ways restructure the forces in company's favour for superior gain (Porter, 2008). Organisations that have a good business model and technology are growing in the market by harnessing the forces of deregulation and globalisation (Kumar, 2006), but it is also crucial for the organisations to encourage and develop leaders (Zaleznik, 2004) as developing and establishing strategy primarily depends on an organisational leader. This assignment talks about the evaluation of all these areas and critical aspects in strategy, Let us first understand the evolution of the strategy and then move on to detail understanding of strategy, a framework that shapes strategy and a leader's role in strategy.

Evolution of Strategy

Strategy in the past was far more different than it is now and also what it will be in the future (Montgomery, 2008). There are seven phases in which strategy has evolved over the number of years. The initial step consisted of the period wherein the companies were centralised and splendid at goal setting (Horwath, 2006). The phase one was identified as a time where the chief executive officer was considered as the significant person, and his role was to formulate and implement the thinking (Montgomery, 2008). It followed the phase two which was the introduction of the SWOT model within the company to assess the internal strength, weakness, opportunities and threats for the external environment (Montgomery, 2008). The third phase was the period of Corporate Planning wherein decentralisation was considered as the important factor for success (Horwath, 2006), and formal system, standards and strategic analysis was introduced (Montgomery, 2008). The fourth phase was the overview of the Corporate Strategy (Horwath, 2006) wherein the consulting firms like Boston Consulting and McKinsey presented their own framework like Influential growth-share matrix and 7-S Framework respectively within this period to measure the link between the strategy and performance (Montgomery, 2008). The fifth phase was the Internal sourcing of competitive advantage, and in this phase terms like core competencies was introduced. Core competencies were characterised as the source of competitive advantage which was the skills and technologies that enable the company to provide benefit to the customer representing the learning across individual skill set and organisational units (Horwath, 2006). The sixth phase was of Strategic Innovation and Implementation, wherein strategic innovation has been intensified by the application of technology in the business process (Horwath, 2006). The strategy is all about getting the right idea which consists of the formulation of ideas (Montgomery, 2008), but implementation process became necessary as companies realised that strategy is inappropriate if not implemented correctly (Horwath, 2006). The seventh phase which is ongoing is the Strategic Thinking. This is the phase where the strategic thinking is involved in every aspect of business and not an annual, monthly or daily activity (Horwath, 2006). The evolution of Strategic Management follows principles as it is driven by longstanding ideas and practices as described by (Mintzberg & Lampel, 1999),

- Collaboration – Strategies arise from the collaboration of ideas amongst the organisation as firms cannot avoid learning when they work or trade together.
- Opposition and confrontation – Strategy also results while competing with each other as new ideas and practices arise when managers try to beat dominant rivals.

- Modifying the old – New strategies are the inspiration from the old policies as old ideas never vanish.
- Creativity – New Strategies are the creativity of the managers as they find new ways of doing things that are being done or still to be explored.

<u>What is Strategy?</u>

According to (Casadesus-Masanell & Ricart, 2011), every firm has business model, but very few organisation have a Strategy, and it refers to the provisions against the range of contingencies whether they take place or not. He incorporates contingencies like competitors move, environmental changes, government policies and changing market trends. But according to (Magretta, 2002), a competitive business strategy explains that how better or differently do you perform better than your rivals and companies can achieve higher performance when they are unique and do something that cannot be duplicated. For instance, Sam Walton, the founder of Walmart choose to serve a different group of consumers in a diverse set of markets. Even though many retailers at that time were focussing on large metropolitan cities like Newyork but Walton concentrated on the rural market which every retailer ignored and since, Walmart's market was too small, they stopped competitors and dejected them from entering into the Walmart's territory (Magretta, 2002). Walmart sold the national brands at low prices, but the company reduced the cost through innovative practices in the field of logistics, purchasing and information management to compensate the discount provided to customers from the enterprise (Magretta, 2002). In these all aspects, Walmart was unique and came up with ideas that were not thought by its competitors. There are management thinkers like LD Phillips, who have given their perspective on strategy. According to (Phillips, 2011), The strategy is about understanding 'what' do they wish to achieve and 'why' they have existence in the market, and not 'how' shall they do it and by 'when' they will do. Many authors have put in their perspective on what is a strategy, but (Porter, 1996) has three viewpoints on Strategy (Porter, 1996),

1. Firstly, Strategy is creating unique and valuable *positioning* (activities that are different from rivals) which involves a different set of activities (Porter, 1996). If there has been a state where the same set of activities were to produce best results, then *operational effectiveness* (performing similar actions better than competitor accomplish them but it not limited to efficiency)would have been determined performance (Porter, 1996). Positioning emerge from three distinct sources (Porter, 1996),
    - Variety-based positioning – When the positioning is based on the choice of the variety of products or services rather than customer segmentation, it is Variety-based positioning. For example, Jiffy Lube International specialises in automotive lubricants who provides faster

service at a lower cost and customers prefer buying oil changing services from them than the competitor, but they don't offer other repair or maintenance services (Porter, 1996).

- Need-based positioning – When the positioning is based on serving the particular needs of the individual customer or the group of customers at its best, it is Need-based positioning. For example, Ikea, the global furniture retailer based in Sweden understood the need-based positioning at its best, by satisfying all the needs of furniture buyers. They very well catered the needs of customers by providing services like a playroom for children at the entrance, portable furniture for easier transport, a restaurant inside the showroom and opening hours designed to suit customers and working professionals (Huy, et al., 2011).
- Access-based positioning – When the positioning is based on segmenting and serving the customers according to their geographic accessibility, it is Access-based positioning. For example, Carmike Cinemas operates movie theatres in the township with a population under 200000, but they earn money by serving customers through standardised, low-cost theatre complexes and less sophisticated technology than urban areas (Porter, 1996).

2. Secondly, Strategy is not always the activities, the firm will choose to do, but indirectly it is also the activities a firm will not do (Porter, 1996). Without *trade-offs* (the exchange of one thing for another mainly to affect a compromise) there would be no necessity for choice, and thus no requisite for strategy as ideas can be copied, and performance would solely depend on operational effectiveness (Porter, 1996). Trade-off arises for mainly three reasons (Porter, 1996),
   - Inconsistent reputation – Delivering inappropriate things at the same time can happen when a firm known or reputed in one kind of value starts offering another value and in turn can lose reliability and confuse customers.
   - Activities themselves – Trade-offs reflect rigidities in the system, individuals, or frameworks when different position which requires unique arrangements, distinct employee conduct, individual aptitudes, and several administration structures are filled with the same type of situation without understanding the custom-made activities.
   - Limiting internal control – Organisational priorities are made by selection of the way to compete, but it restricts and risks the internal coordination of the company if it alters and contradicts priorities on the everyday decisions.
3. Lastly, Strategy is the creation of the *fit* (a robust link that blocks competitors from imitating) within the activities of the companies, and if there is no fit, there is no unique strategy (Porter, 1996). There are three types of fit (Porter, 1996),
   - First order fit is Simple consistency between each function
   - Second order fit is Reinforcing activities
   - Third order fit is Effort optimisation by strengthening the function

If the three perspectives of Michael Porter's are put together then, the strategy is the combination of differentiated activities tailored to a strategy that a firm decides tactically for the creation of a fit. A sound strategy is the one which is sustainable and works well for the company even in the tougher market conditions.

5 Competitive forces that shape Strategy

The arrangement and importance of the five forces given by Michael Porter in his framework differ from industry to industry, as each one plays a critical role when put in a different scenario, for instance, forces will act differently when applied in airlines manufacturing sector than in the entertainment industry (Porter, 2008). The understanding of these five forces framework can help a strategist to mark an industry with a good future before it is reflected in the price of acquisition candidates (Porter, 2008). The figure (**Figure 1: The 5 Forces That Shape Industry Competition**) shows the forces that are vital for the industry competition which are,

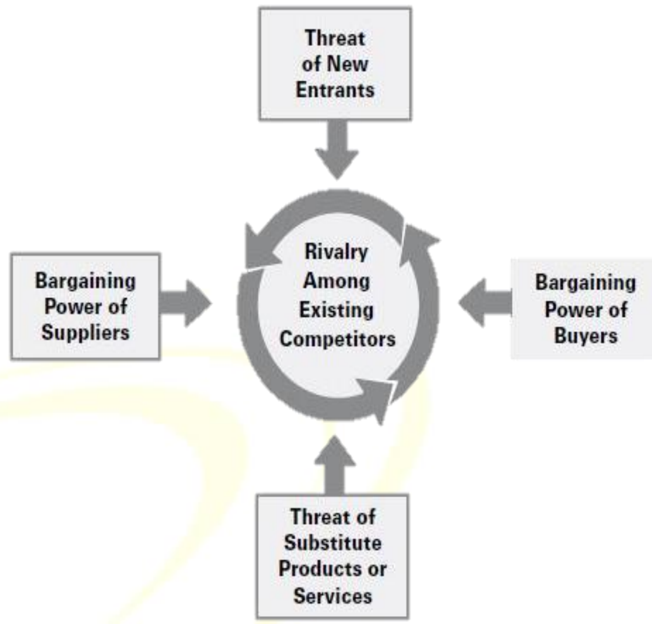

Figure 1: The 5 Forces That Shape Industry Competition

1. Threats of new entrants – Aspiring new entrants are the threat to the existing companies in the market within the same industry due to their desire to gain market share which put pressure on income, expenses and investment. The risk of entrants places a constraint on the potential profit, or either holds down the possible advantage within the industry, but if the risk is high, the existing player must increase the investment to discourage the competitors and in both the case the incumbent loses. The level of threat depends upon the degree of *entry barriers* (advantages that existing player have over new entrants) present within the industry and the incumbent's response (Porter, 2008). According to (Porter, 2008), there are seven primary sources of entry barriers,
   - Economies of scale – Economies of scale is enjoyed by the company that produce in higher volumes as the cost per unit decreases because of spreading of fixed cost over more units by using efficient technology and demanding better terms from suppliers (Porter, 2008). Economies of scale discourage new entrants by forcing them to either enter on a massive scale or to accept the disadvantage of cost.

- Demand-side benefits of scale – This benefit occurs when one buyer influences the other customer to buy the product as network effects and larger companies are more trustable regarding compelling product by customers (Porter, 2008). Demand-side benefits of scale discourage new entrants by forcing the consumer's willingness of not buying from a newcomer in the market.
- Customer switching cost – Switching cost is the cost (for example, altering product specifications, modifying processes or systems) barred by clients when they change suppliers (Porter, 2008). Customer switching cost discourages the new entrant to gain the customer in the market as it will be harder for them to leave the current supplier.
- Capital requirements – Capital requirement is the need of financial resources necessary for the new entrant to fund the startup loss and it discourages new entrant as the incumbents can heavily flow the money to maintain their superiority in the market.
- Incumbency advantage independent of size – Even if the newcomer enters the market with an excellent idea to capture the market but then also the existing player has the cost and quality advantages which are not existing with new entrants, which discourages newcomers regarding efficiency.
- Distribution channels access – If newcomer wants to position itself in the market, they have to secure reliable distribution channels which are already captured by incumbents which discourage the new entrant as the existing competitors have tied up with wholesalers and retailers.
- Government Policies – Government policies can act as a boon if it is in favour of new entrants but can also serve as a disastrous curse if it is against them. Government policies can discourage new entrants by reinforcing the entry barriers (for example, patenting rules, environmental policies and strict business ethics) that raise scale for newcomers (Porter, 2008).

2. The power of suppliers – The Suppliers, play a vital role in business but captures more value by squeezing profits, charging higher prices, restraining quality or services and shifting costs which limit the firm by constraining them to increase the cost of their services.
3. The power of buyers – If there is no customer there is no business, which makes customers king in all aspect and makes them the ultimate decision maker when it comes to buying the product. Due to this aspect, the customer can dictate the terms by forcing the firms to lower their prices and demand better quality at that same price.
4. The threat of substitute – Substitute is the alternative to the existing product in the market which is a threat as it replaces the current industry product, for instance, ticketing agents in airline industry lost their most of the businesses due to the internet as a substitute.
5. Rivalry among existing competitors – It's like a monkey taking advantage between two fighting cats. Similarly, the competition among the existing competitors can work in favour

of the new entrant to the particular industry or business. High rivalry can limit the potential profitability of a business or industry which depends on the intensity of competition and on the basis on which they compete (Porter, 2008).

How 5 forces helps in Business Strategy?

The proper understanding of the forces that shape the competition within the industry is the initial point of developing a strategy. By understanding five forces, a company can incorporate industry conditions into strategy if they know why there is average profitability within the industry and it also helps in understanding the most important features of the competitive environment. The five forces contribute to the understanding of strengths and weaknesses of the company regarding buyers, suppliers, rivals, entrants and substitute which in turn guides managers to take strategic action and decision making (Porter, 2008). According to Michael Porter, the best strategies exploit more than one of these prospects,

- Positioning the company – Strategy can help the industry or the company for positioning where the competitive forces are weak and can also be viewed as resistances against the competitive forces (Porter, 2008).
- Utilising industry change – If the person making the strategy has the proper understanding of five competitive forces and their foundations, he can bring the opportunities and claim to promise strategic positioning in the industry (Porter, 2008).
- Shaping industry structure – The company has the ability to change the structure by altering the five forces aimed at the new ways of competing (Porter, 2008).
- Defining the industry – The five forces has the ability to redefine its own distinct industry depending on the company in which it operates by making correct sector boundaries, clarifying the causes of profitability and suitable units for setting strategy (Porter, 2008).

Is something is missing in Porter's Model?

Michael Porter's five force was introduced in the year 1979 and gives phenomenal foundations and insight expected to understand organisation's future strategy, but there is no variations and alterations were done in the model from the time when it was presented. Many changes occurred in the field of strategic management, but the model remained the same with no effect of the changing market conditions and technological advancement since then. Any learning from utilising Porter's model will rapidly be outdated as it was just intended to give a preview of a particular market without regular updates. There is also criticism of Porter's model that the framework is abstract and highly analytical which make the structure rigid (Grundy, 2006). Also, The five competitive forces which are explained by the porter's framework is in the language of microeconomics theory rather than being practical (Grundy, 2006). While Porter's framework helps to streamline microeconomics, its visual structure is generally hard to integrate and link its rationale to some extent. Any model to be successful, there is a need for every factor involved should interrelate with each other but here in Porter's framework how buyers and suppliers are interrelated, because even if the vendor wants to enter into the mainframe business as a competitor, then he anyhow has the market opportunities open for him. Also, the model doesn't give you relevant data about preventive actions on the contrast it helps you to know problems and threats in the firm by inspection of substitutes. Due to the invention of the social media, it makes a lot of difference of how the porter's model was looked in the past, and also the power social era (**Figure 2: New force (Social Era) that can shape strategy**) has to shift the model (Merchant, 2012). According to (Merchant, 2012), there are four factors involved in the social era which includes,

Figure 2: New force (Social Era) that can shape strategy

- Being big is not enough – In this modern business environment it is crucial for the organisations to be fast, fluid, flexible and technological sound rather than being big as the size of the structure doesn't manner in the current scenario. There was a time when a big organisation has the purchasing power, the power of enabling barriers to entry and keeping rivals out of the competition but now as the capital is not the criteria to enter the market being big is not enough anymore (Merchant, 2012).
- Being distinct or either generic – The current trend in the market is of being distinctive as the things which fall under this category are the different and artistic product which are sold at a premium price, and it is worth of that as it is making life easy and simple. Also, the generic product which is sold in the market is sold because of the brand image and goodwill in the market which is made in years. But if the organisation wants to be in the social era category they should be distinct due to its uniqueness of the idea and its profitability (Merchant, 2012).
- Being social is important – It is vital for the organisation to be social in the modern market as being social gives the company control over its operational adjustments which in turn helps to strengthen weak areas by gathering & understanding them and working on it (Merchant,

2012). Also, It is important to be social inside and outside the organisation as accepting social values can help you in your career and in the future endeavours (Morgan, 2015).

- Understanding the cycle of profitability – Considering the rigid areas and converting them to unique customer-driven approach, the firm can increase their profitability cycle which allows them to develop in the future (Merchant, 2012). The profitability cycle can be established by constantly reinforcing the business models by the help of network effects which consist of the choices and consequences (Casadesus-Masanell & Ricart, 2011).

Leadership and Strategy

It seems that once the strategy is articulated, it is ready for implementation, but it is not the case as even it appears that it is clearly defined, it is not sufficient for the organisation that aims a long and flourishing life (Montgomery, 2008) and there comes a role of a leader. Any leader is not a born leader, he is made by training and developing by exposing his own self to a competitive learning environment. A leader has the authority to select and deselect individual ideas and opportunities that work in favour of the organisation for its growth by serving as the protector and guiding the firm. A report by PwC suggests that only 10% of the leaders have the right skills to lead successful transformational change (PwC, 2015). A person who is able to envisage and articulate a vision for the future of the organisation while making the present efficient is an effective transformational leader, but such leaders are just 8% in the senior positions (PwC, 2015). Managers at lower positions lack the perspective and the confidence to maintain a strategy, but the leader must possess the discipline to respond the industry changes and should have a decision making power while avoiding organisational distractions (Porter, 1996). A strategic leader manages the strength and enthusiasm of the people working under him by radiating the energy towards achieving the goals. Organisations guided by the leader are more efficient in learning, taking initiatives for training and development. It is crucial to understand the depth of the current scenario and has become imperative to encourage leaders in the organisation to grow because, a leader is the one who makes the choices and the decision regarding an intellectual framework of strategy (Porter, 1996). The core strategy of a leader is to define and communicate the company's unique position, making trade-off's and forging fit amongst the events (Porter, 1996) but though improving operational effectiveness is a significant chunk of management, but it is not a strategy. Aspiring managers who want to be future leaders in the organisation have to clearly understand the difference between operational effectiveness and strategy because agendas for both are different. The agenda for operational efficiency is to create continual improvement with no tradeoffs, flexibility, constant change and to work to achieve best practice whereas the agenda of strategy is to create unique positioning and ways to reinforce it, making explicit trade-offs and creating a tightening fit (Porter, 1996). If organisations want to develop a leader out of a manager, then they have to make and develop a one-to-one relationship between junior and senior executives within the group by fostering the culture of individualism and elitism which comes out of a desire to find and nurture a talent that lead the organisation and not just to manage it (Zaleznik, 2004).

Conclusion

It is vital for every company to understand that they must continuously improve its operational effectiveness and also change its strategy which will help to strengthen the fit among its activities as both are important for the firm. Continuous changing of company's old strategy into the modern one will not only assist the business to deal with new entrants quickly but also will help the firm to make new strategic positions in the market as strategic positioning describes where the company currently is and where they wany to reach in the future. Strategic positioning will, in turn, help the company to have an effective and efficient plan which will help the organisation to succeed rather than to fail. Strategic positioning also helps the companies to understand the decisions which they are making is aligning to their mission and vision. The understanding of the five competitive forces reveal the drivers of the industry competition (Porter, 2008) and the person who know this well will identify broader competitive threats and be well equipped to face them. The five competitive forces also tell that whether the particular industry or a firm is attractive or not and helps investors to anticipate positive or negative shifts in the structure of the industry before they become noticeable (Porter, 2008). After understanding the Porter's Model, I think that this model is much helpful for the new entrant who wants to enter the market. If the threat of entry is low, then the attractiveness of the industry is more because the organisation which are going global, the ease of entry to that particular industry and competition within is an element can have a critical effect on profitability. Another significant component while analysing industry attractiveness is a threat of substitutes. The higher the threat of substitute the level of profitability is usually low as customers can switch to other alternative choices. Also, the five forces can distinguish short-term problems from the structural change which allows investors to take benefit of undue pessimism or optimism (Porter, 2008). Lastly, If organisations want to grow in the long run and intend to be in business for years, then it had to deliver something to consumers that are unique and cannot be imitated which can be provided by a transformation leader who has a vision for the organisation. In fact, if corporations want to develop a good and healthy working culture, then they must have a leader as without a leader a culture is just developed, it cannot be reinforced as a way of thinking which comes from within. A true leader has the courage to take tough decisions, has the compassion to listen to others and most importantly the creation and recreation of strategy in the organisation by a leader distinguish him from an ordinary individual.

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