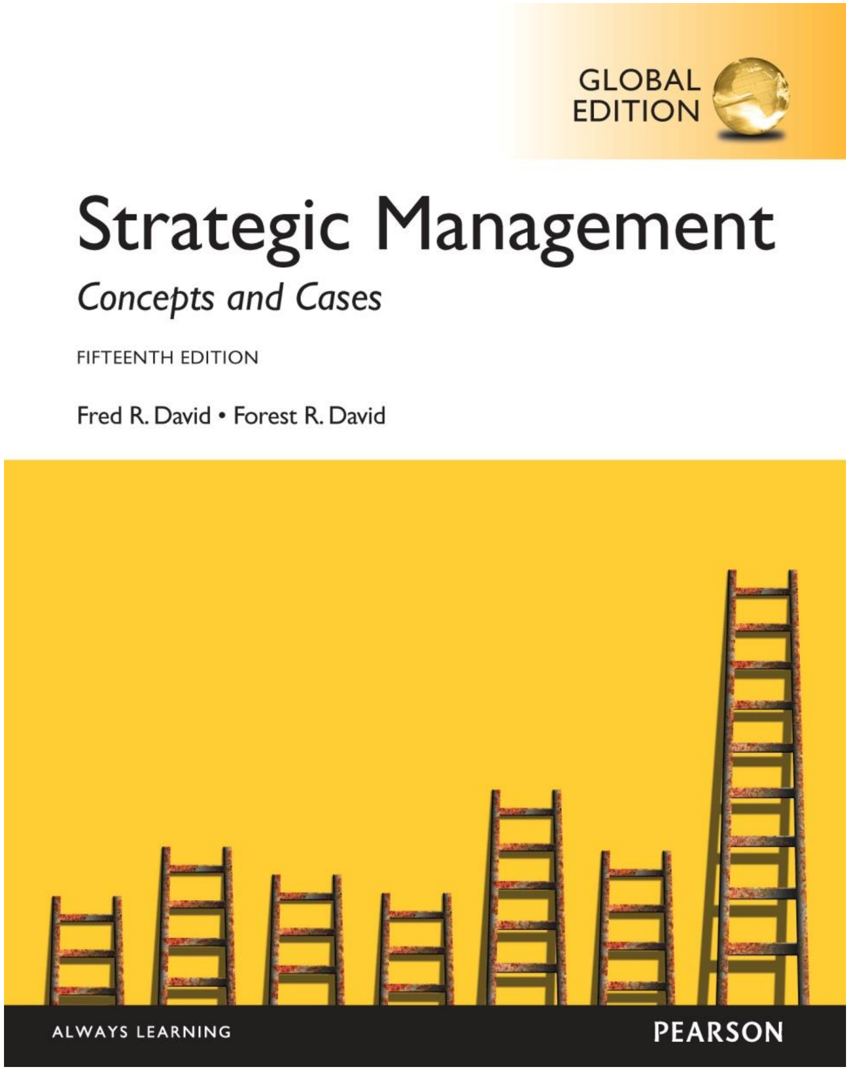

Types of Strategies

Chapter Four

Chapter Objectives

1. Define and discuss secondary buyouts and dividend recapitalizations.
2. Identify the benefits and drawbacks of merging with another firm.
3. Discuss the value of establishing long-term objectives.
4. Identify 16 types of business strategies.
5. Identify numerous examples of organizations pursuing different types of strategies.
6. Discuss guidelines when particular strategies are most appropriate to pursue.

Chapter Objectives (cont.)

7. Discuss Porter's five generic strategies.
8. Describe strategic management in nonprofit, governmental, and small organizations.
9. Discuss the nature and role of joint ventures in strategic planning.
10. Compare and contrast financial with strategic objectives.
11. Discuss the levels of strategies in large versus small firms.
12. Explain the First Mover Advantages concept.
13. Discuss recent trends in outsourcing and reshoring.

The Nature of Long-Term Objectives

- **Objectives** should be:
  - quantitative, measurable, realistic, understandable, challenging, hierarchical, obtainable, and congruent among organizational units

The Nature of Long-Term Objectives

- **Objectives**
  - provide direction
  - allow synergy
  - aid in evaluation
  - establish priorities
  - reduce uncertainty
  - minimize conflicts
  - aid in both the allocation of resources and the design of jobs

Varying Performance Measures by Organizational Level

TABLE 4-1 Varying Performance Measures by Organizational Level

Organizational Level	Basis for Annual Bonus or Merit Pay
Corporate	75% based on long-term objectives 25% based on annual objectives
Division	50% based on long-term objectives 50% based on annual objectives
Function	25% based on long-term objectives 75% based on annual objectives

The Desired Characteristics of Objectives

TABLE 4-2 The Desired Characteristics of Objectives

1. Quantitative
2. Measurable
3. Realistic
4. Understandable
5. Challenging
6. Hierarchical
7. Obtainable
8. Congruent across departments

Not Managing by Objectives

- Managing by Extrapolation
- Managing by Crisis
- Managing by Subjectives
- Managing by Hope

A Comprehensive Strategic-Management Model

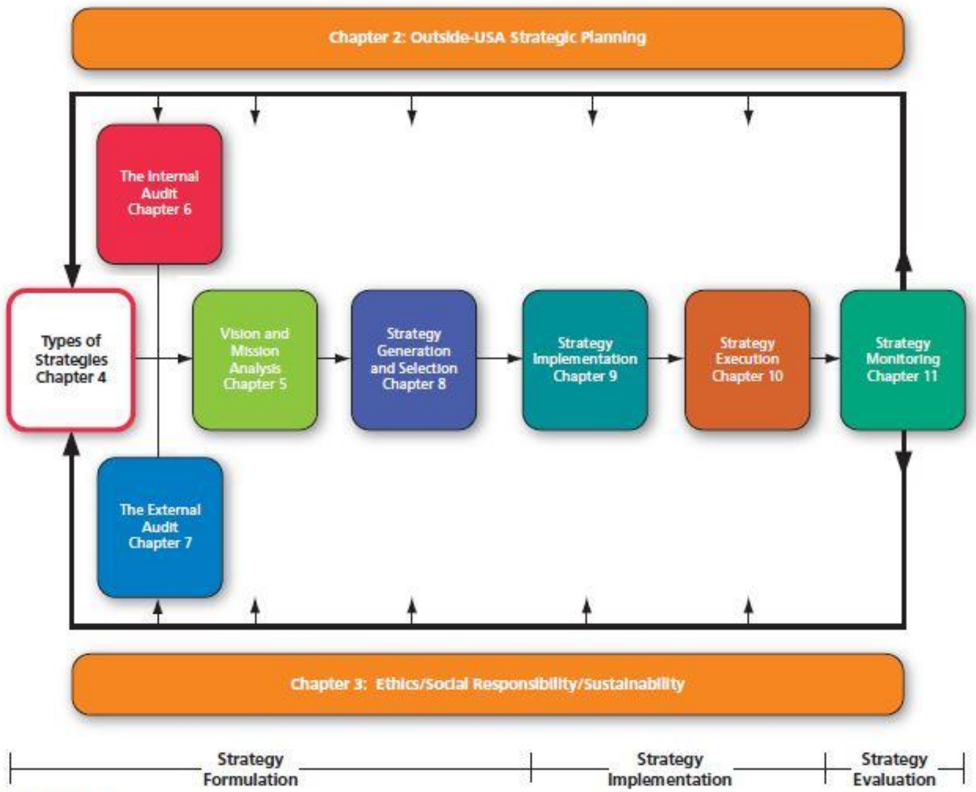

FIGURE 4-1
A Comprehensive Strategic-Management Model

Types of Strategies

- Most organizations simultaneously pursue a combination of two or more strategies, but a *combination strategy* can be exceptionally risky if carried too far.
- No organization can afford to pursue all the strategies that might benefit the firm.
- Difficult decisions must be made and priorities must be established.

Alternative Strategies Defined and Exemplified

TABLE 4-4 Alternative Strategies Defined and Exemplified

Strategy	Definition	Examples
Forward Integration	Gaining ownership or increased control over distributors or retailers	Forward Integration—PayPal is pushing its service off the Web and into stores via an agreement with Discover card.
Backward Integration	Seeking ownership or increased control of a firm's suppliers	Backward Integration—Fancy Motels Inc. acquiring a furniture manufacturer.
Horizontal Integration	Seeking ownership or increased control over competitors	Horizontal Integration—Britain's GlaxoSmithKline PLC acquired Human Genome Sciences Inc. for $3 billion.
Market Penetration	Seeking increased market share for present products or services in present markets through greater marketing efforts	Market Penetration—PepsiCo is heavily advertising its new Diet Pepsi special-edition silver cans featuring the blue-and-red Pepsi logo in a heart shape.
Market Development	Introducing present products or services into new geographic area	Market Development—China Petrochemical purchased three Canadian oil companies, Daylight Energy, Tanganyika Oil, and Syncrude Canada.
Product Development	Seeking increased sales by improving present products or services or developing new ones	Product Development—General Electric is building new composite material jet engines, whereas rival Pratt & Whitney is developing newly designed jet engines.

Alternative Strategies Defined and Exemplified

TABLE 4-4 Alternative Strategies Defined and Exemplified

Strategy	Definition	Examples
Related Diversification	Adding new but related products or services	Related Diversification—The toy retailer, Toys 'R' Us developed a new Wi-Fi tablet computer for children (the Tabeo for $149.99).
Unrelated Diversification	Adding new, unrelated products or services	Unrelated Diversification—Retailer IKEA is opening a chain of motels in Europe.
Retrenchment	Regrouping through cost and asset reduction to reverse declining sales and profit	Retrenchment—Callaway Golf cut 12 percent of its workforce; Deutsche Bank AG cut 1,000 jobs from its investment bank segment.
Divestiture	Selling a division or part of an organization	Divestiture—Dean Foods sold off its WhiteWave-Alpro organic dairy business.
Liquidation	Selling all of a company's assets, in parts, for their tangible worth	Liquidation—Big Sky Farms, one of Canada's biggest hog-producing firms, liquidated.

Levels of Strategies With Persons Most Responsible

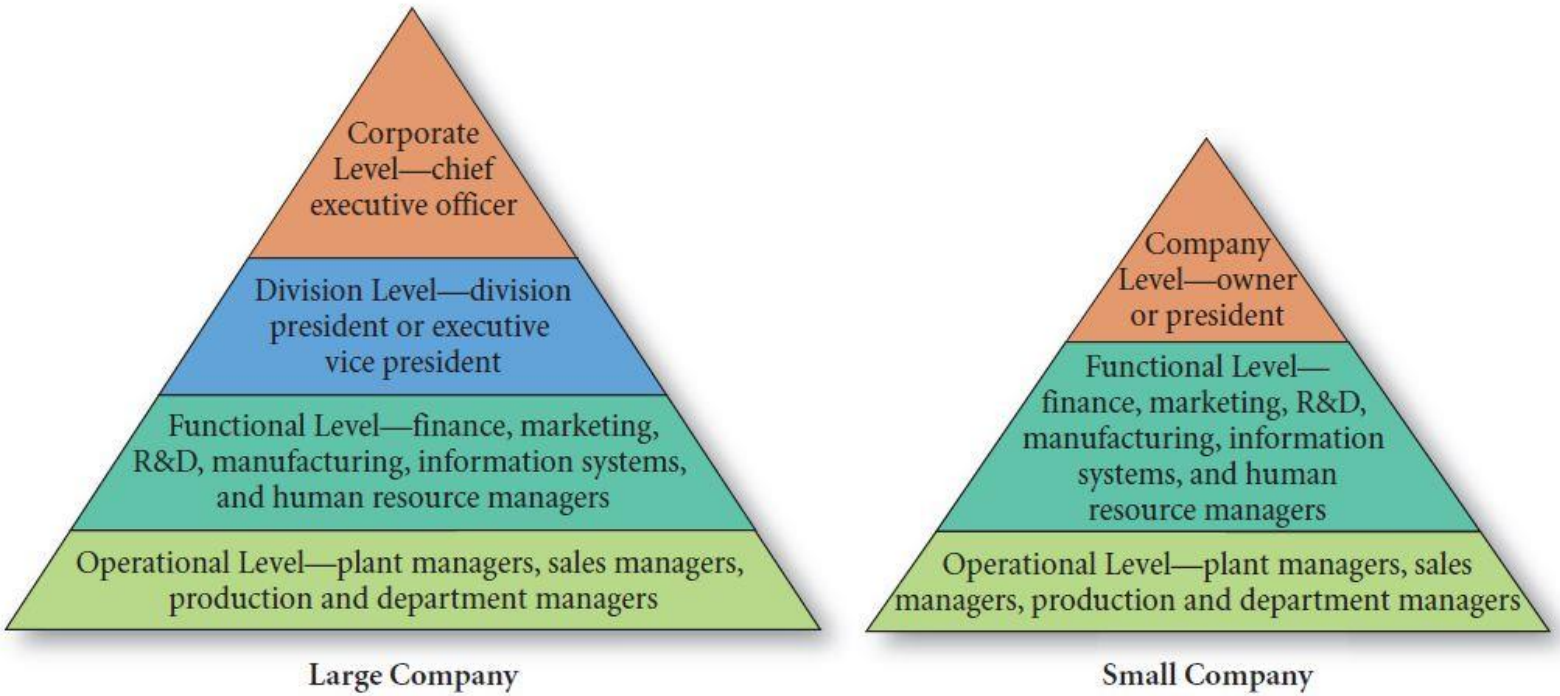

FIGURE 4-2

Levels of Strategies With Persons Most Responsible

Integration Strategies

- **Forward integration**
  - involves gaining ownership or increased control over distributors or retailers
- **Backward integration**
  - strategy of seeking ownership or increased control of a firm’s suppliers
- **Horizontal integration**
  - a strategy of seeking ownership of or increased control over a firm’s competitors

Forward Integration Guidelines

- When an organization’s present distributors are especially expensive
- When the availability of quality distributors is so limited as to offer a competitive advantage
- When an organization competes in an industry that is growing
- When the advantages of stable production are particularly high
- When present distributors or retailers have high profit margins

Backward Integration Guidelines

- When an organization's present suppliers are especially expensive or unreliable
- When the number of suppliers is small and the number of competitors is large
- When an organization has both capital and human resources
- When the advantages of stable prices are particularly important
- When an organization needs to quickly acquire a needed resource

Horizontal Integration Guidelines

- When an organization can gain monopolistic characteristics in a particular area or region without being challenged by the federal government
- When an organization competes in a growing industry
- When increased economies of scale provide major competitive advantages
- When competitors are faltering due to a lack of managerial expertise

Intensive Strategies

- **Market penetration strategy**
  - seeks to increase market share for present products or services in present markets through greater marketing efforts
- **Market development**
  - involves introducing present products or services into new geographic areas
- **Product development strategy**
  - seeks increased sales by improving or modifying present products or services

Market Penetration Guidelines

- When current markets are not saturated with a particular product or service
- When the usage rate of present customers could be increased significantly
- When the market shares of major competitors have been declining while total industry sales have been increasing
- When increased economies of scale provide major competitive advantages

Market Development Guidelines

- When new channels of distribution are available that are reliable, inexpensive, and of good quality
- When an organization is very successful at what it does
- When new untapped or unsaturated markets exist
- When an organization has excess production capacity
- When an organization's basic industry is rapidly becoming global in scope

Product Development Guidelines

- When an organization has successful products that are in the maturity stage of the product life cycle
- When an organization competes in an industry characterized by rapid technological developments
- When major competitors offer better-quality products at comparable prices
- When an organization competes in a high-growth industry
- When an organization has strong research and development capabilities

Diversification Strategies

- **Related diversification**
  - value chains possess competitively valuable cross-business strategic fits
- **Unrelated diversification**
  - value chains are so dissimilar that no competitively valuable cross-business relationships exist

Synergies of Related Diversification

- Transferring competitively valuable expertise, technological know-how, or other capabilities from one business to another
- Combining the related activities of separate businesses into a single operation to achieve lower costs
- Exploiting common use of a known brand name
- Using cross-business collaboration to create strengths

Related Diversification Guidelines

- When an organization competes in a no-growth or a slow-growth industry
- When adding new, but related, products would significantly enhance the sales of current products
- When new, but related, products could be offered at highly competitive prices
- When an organization has a strong management team

Unrelated Diversification Guidelines

- When revenues derived from an organization’s current products would increase significantly by adding the new, unrelated products
- When an organization’s present channels of distribution can be used to market the new products to current customers
- When the new products have countercyclical sales patterns compared to present products
- When an organization’s basic industry is experiencing declining annual sales and profits

Unrelated Diversification Guidelines (cont.)

- When there exists financial synergy
- When an organization has the opportunity to purchase an unrelated business that is an attractive investment opportunity
- When existing markets for an organization's present products are saturated
- When antitrust action could be charged against an organization that historically has concentrated on a single industry

Defensive Strategies

- **Retrenchment**
  - occurs when an organization regroups through cost and asset reduction to reverse declining sales and profits
  - also called a turnaround or reorganizational strategy
  - designed to fortify an organization's basic distinctive competence

Retrenchment Guidelines

- When an organization has a distinctive competence but has failed consistently to meet its goals
- When an organization is one of the weaker competitors in a given industry
- When an organization is plagued by inefficiency, low profitability, and poor employee morale
- When an organization fails to capitalize on external opportunities and minimize external threats
- When an organization has grown so large so quickly that major internal reorganization is needed

Defensive Strategies

- **Divestiture**
  - Selling a division or part of an organization
  - often used to raise capital for further strategic acquisitions or investments

Divestiture Guidelines

- When an organization has pursued a retrenchment strategy and failed to accomplish improvements
- When a division needs more resources to be competitive than the company can provide
- When a division is responsible for an organization’s overall poor performance
- When a division is a misfit with the rest of an organization
- When government antitrust action threatens a firm

Defensive Strategies

- **Liquidation**
  - selling all of a company’s assets, in parts, for their tangible worth
  - can be an emotionally difficult strategy

Liquidation Guidelines

- When an organization has pursued both a retrenchment strategy and a divestiture strategy, and neither has been successful
- When an organization's only alternative is bankruptcy
- When the stockholders of a firm can minimize their losses by selling the organization's assets

Porter's Five Generic Strategies

Type 1: Cost Leadership—Low Cost
Type 2: Cost Leadership—Best Value
Type 3: Differentiation
Type 4: Focus—Low Cost
Type 5: Focus—Best Value

	GENERIC STRATEGIES		
SIZE OF MARKET	Cost Leadership	Differentiation	Focus
Large	Type 1 Type 2	Type 3	—
Small	—	Type 3	Type 4 Type 5

FIGURE 4-3

Porter's Five Generic Strategies

Michael Porter’s Five Generic Strategies

- **Cost leadership**
  - emphasizes producing standardized products at a very low per-unit cost for consumers who are price-sensitive

Michael Porter's Five Generic Strategies

- **Type 1**
  - *low-cost* strategy that offers products or services to a wide range of customers at the lowest price available on the market

- **Type 2**
  - *best-value* strategy that offers products or services to a wide range of customers at the best price-value available on the market

Michael Porter's Five Generic Strategies

- **Differentiation**
  - strategy aimed at producing products and services considered unique industry-wide and directed at consumers who are relatively price-insensitive

Michael Porter's Five Generic Strategies

- **Type 4**
  - *low-cost focus* strategy that offers products or services to a niche group of customers at the lowest price available on the market

- **Type 5**
  - *best-value focus* strategy that offers products or services to a small range of customers at the best price-value available on the market

Cost Leadership Strategies

- To employ a cost leadership strategy successfully, a firm must ensure that its total costs across its overall value chain are lower than competitors' total costs

Cost Leadership Strategies

Two ways:

1. Perform value chain activities more efficiently than rivals and control the factors that drive the costs of value chain activities

2. Revamp the firm’s overall value chain to eliminate or bypass some cost-producing activities

Cost Leadership Guidelines

- When price competition among rival sellers is especially vigorous
- When there are few ways to achieve product differentiation that have value to buyers
- When most buyers use the product in the same ways
- When buyers incur low costs in switching their purchases from one seller to another
- When large buyers can bargain down prices.

Differentiation Strategies

- Differentiation strategy should be pursued only after a careful study of buyers' needs and preferences to determine the feasibility of incorporating one or more differentiating features into a unique product that features the desired attributes

Differentiation

- When there are many ways to differentiate the product
- When buyer needs and uses are diverse
- When few rival firms are following a similar differentiation approach
- When technological change is fast paced

Focus Strategies

- Successful focus strategy depends on an industry segment that is of sufficient size, has good growth potential, and is not crucial to the success of other major competitors
- Most effective when consumers have distinctive preferences

Focus Strategy Guidelines

- When the target market niche is large, profitable, and growing
- When industry leaders do not consider the niche to be crucial to their own success
- When industry leaders consider it too costly or difficult to meet the specialized needs of the niche
- When the industry has many different niches
- When few, if any, other rivals are attempting to specialize in the same target segment

Means for Achieving Strategies

- Cooperation Among Competitors
- Joint Venture/Partnering
- Merger/Acquisition
- Private-Equity Acquisitions
- First Mover Advantages
- Outsourcing/Reshoring

Key Reasons Why Many Mergers and Acquisitions Fail

TABLE 4-5 Key Reasons Why Many Mergers and Acquisitions Fail

- Integration difficulties
- Inadequate evaluation of target
- Large or extraordinary debt
- Inability to achieve synergy
- Too much diversification
- Managers overly focused on acquisitions
- Too large an acquisition
- Difficult to integrate different organizational cultures
- Reduced employee morale due to layoffs and relocations

Potential Benefits of Merging With or Acquiring Another Firm

TABLE 4-6 **Potential Benefits of Merging With or Acquiring Another Firm**

- To provide improved capacity utilization
- To make better use of the existing sales force
- To reduce managerial staff
- To gain economies of scale
- To smooth out seasonal trends in sales
- To gain access to new suppliers, distributors, customers, products, and creditors
- To gain new technology
- To reduce tax obligations

Benefits of a Firm Being the First Mover

TABLE 4-7 Benefits of a Firm Being the First Mover

1. Secure access and commitments to rare resources
2. Gain new knowledge of critical success factors and issues
3. Gain market share and position in the best locations
4. Establish and secure long-term relationships with customers, suppliers, distributors, and investors
5. Gain customer loyalty and commitments