FORMULATION OF COMPETITIVE STRATEGIES

5

After having completed the strategic analysis of a company, managers are now in the possession of a strong pool of information regarding the industry competition, external opportunities and threats, and internal strengths and weaknesses. Based on the information gathered, they would logically proceed towards setting long-term objectives for the organization. Then, they would formulate appropriate strategies in an endeavor to gain competitive advantage in the market

Formulation of strategy is a difficult task. However, in order to ease the formulation of strategy, managers need to have an in-depth look at several issues. They are expected to identify the generic and other competitive strategies as applicable to single-business company, and match the strategies to industry and company situations.

This unit examines the competitive strategies that an organization can employ for achieving competitive advantage. The strategies that an organization may follow can be divided into two groups for convenience of analysis: (1) Generic Strategies and (2) Non-Generic Strategies. Before we go for discussing about these strategies, let us first have an idea about the concept and nature of 'competitive strategy,' competitive advantage and distinctive competency in Lesson-1 of this unit.

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Lesson-1: Competitive Strategy, Competitive Advantage and Distinctive Competency

Learning Objectives:

After studying this lesson, you should be able to:

- Explain the nature of competitive strategy.
- Define competitive advantage.
- Relate competitive advantage with competitive strategy.
- Discuss how an organization can sustain its competitive advantages.
- Clarify the concept of distinctive competency.
- Distinguish between competitive strategy and business strategy.

Introduction

Before we go for analyzing the issues of strategy formulation, we should understand a few concepts that are necessary to comprehend the spirit of formulating strategy in organizations. These concepts would form basis for the formulation of strategy. The concepts that we would discuss in this lesson are competitive strategy, competitive advantage, and distinctive competence.

Competitive Strategy

Competitive strategy consists of the business approaches and initiatives undertaken by a company to attract customers and to deliver superior value to them through fulfilling their expectations as well as to strengthen its market position. This definition of Thompson and Strickland emphasizes on 'approaches and initiatives' of managers in defining strategy. This means that competitive strategy is concerned with actions that managers undertake to improve market position of the company through satisfying the customers. Improving market position implies undertaking actions against competitors in the industry. Thus, the concept of competitive strategy (as opposed to cooperative strategy) has a competitor-orientation. Competitive strategy includes those approaches that prescribe various ways to build sustainable competitive advantage. Management's action plan is the focus of competitive strategy. management adopts action-plan to compete successfully with the competitors in the market. It also aims at providing superior value to customers. The objective of competitive strategy is to win the customers' heart through satisfying their needs and finally to attain competitive advantage as well as out compete the competitors (or rival companies.).

Competitive Advantage:

The Ultimate Goal of Competitive Strategy

Competitive advantage is the special edge over the competitors.

Competitive advantage is the special edge over the competitors. A question is often asked by managers: "What is the duration of competitive advantage?" How long it will be sustained primarily depends on (i) barriers to imitation, (Iii) capability of competitors and (iii) the general dynamism of an industry's environment.[1] 'Barriers to imitation' create obstacles for the competitors to copy a company's distinctive competencies easily. Competitors will always try to imitate a company's resources and capabilities. Evidence indicates that capabilities are more difficult to imitate than resources. Of the resources, tangible resources (e.g., plant and machinery equipment, buildings) are easier to imitate than intangible resources (e.g., patents, goodwill, brand names, technological know-how, marketing techniques). There is, thus, a need to build up distinctive competence based on unique capabilities rather than on tangible resources. This would help the company enjoy the distinctive competence for a longer period of time.

The capability of competitors to imitate a company's distinctive competency need to be given due consideration.

The capability of competitors to imitate a company's distinctive competency need to be given due consideration. If the competitors are strongly committed to doing business in a particular way, they will not suddenly imitate a company's innovation. In such a situation, its distinctive competency will be sustainable for longer. The third factor of sustainability of distinctive competency – that is, industry dynamism – is also an important determinant of competitive advantages. Frequent product innovation makes an industry environment dynamic. For example, software industry, electronics industry and PC industry are highly dynamic because of high rate of innovation. In such industries, competitive advantages are short-lived.

How to sustain competitive advantage?

Since achieving and maintaining competitive advantage is the primary aim of competitive strategies, managers should undertake measures to sustain competitive advantage once they are achieved. Managers can build sustainable competitive advantage by adopting following measures.[2]

Managers can build sustainable competitive advantage by adopting six measures.

- Focusing on building blocks of competitive advantages
- Developing distinctive competencies
- Creating an environment of organizational learning
- Instituting continuous improvement mechanism
- Instituting best practices
- Overcoming barriers to change

A brief discussion of these issues follows:

1. **Focusing on building blocks of competitive advantages:** As stated earlier, a company has a sustained competitive advantage when it can maintain higher-than-industry-average profit rate over a number of years. This becomes possible when the company emphasizes on the four *generic* building blocks of competitive advantage, such as (a) efficiency, (b) quality, (c) innovation, and (d) customer responsiveness. Because of its focus on these building blocks, Apple Computer Company enjoyed sustained competitive advantage over a long period from 1987 to 1993.[3] These are called 'generic' because any organization can adopt them irrespective of its products (or industry in which it operates its business). Superior efficiency enables a company to lower its costs; superior quality allows it both

to lower costs and charge a higher price; superior customer responsiveness allows it to charge a higher price; and superior innovation can lead to higher prices or lower unit costs. Together these four building blocks help a company create more value than the competitors. Thus, company can enjoy a sustained competitive advantage.

2. **Developing distinctive competencies:** Managers have to develop distinctive competencies in order to sustain competitive advantage. When distinctive competencies are developed, they help in improving performance in all the areas of four building blocks. Distinctive competencies should be developed in all required areas – never in some areas at the cost of other important areas. Companies need to be balanced in their pursuit of distinctive competencies.

3. **Creating an environment of organizational learning:** Sustaining competitive advantage requires a congenial environment in the organization that promotes learning within the organization (commonly known as organization learning). Learning organizations can keep themselves at the top of all competitors because they are always in search of knowledge. In the process of seeking and disseminating knowledge, they learn from prior mistakes and improve their work-processes over time.

4. **Instituting continuous improvement mechanism:** Continuous improvement of the quality of both products and services (in fact, of everything that a company does) in sine quo non for sustaining competitive advantage over a longer period of time. Managers need to devise dynamic ways to improve quality on a continuous basis. Some organizations have been successful in their endeavor to improve quality through instituting total quality management (TQM) program and business process reengineering.

5. **Instituting best practices:** Adoption of 'industrial best practices' helps in developing distinctive competencies and thereby in sustaining competitive advantage. Organizations can benchmark (search out) the successful business-practices of other competitors/companies in other industries and then adopt them after necessary fine-tuning. Thus, they can build and maintain resources and capabilities – that are essential to achieve excellence in efficiency, quality, innovation and customer responsiveness.

6. **Overcoming barriers to change:** Companies fail to sustain competitive advantage as because they are unable to adapt to changes in the organization. They need to overcome the resistances to change so that they can maintain competitive advantage. Companies can overcome the barriers to change through providing effective leadership, necessary changes in organization structure, creating appropriate control systems and involving employees in decision making.

Distinctive Competency:
An Essential Requirement for Achieving Competitive Advantage

Distinctive competencies refer to those strengths of the organization that allow it to attain competitive advantage in the market.

A business organization must have distinctive competency in one or more areas of its activities in order to be competitive in the marketplace. Distinctive competencies refer to those strengths of the organization that allow it to attain competitive advantage in the market. These strengths are unique for the organization and they help it achieve superior efficiency, quality, innovation and customer responsiveness. It can be argued that Partex has distinctive competencies in the case of manufacturing bottled drinking water – MUM. Distinctive competencies have helped Partex achieve lower costs and make product differentiation better than its competitors. Thus, distinctive competencies have been helpful in attaining distinctive advantages through achievement of superior efficiency and quality.

Unique organizational resources and capabilities constitute an organization's distinctive competencies. However, the resources of the organization must be unique (i.e., no other companies have these resources) to be regarded as distinctive competencies. The resources comprise physical, human, financial, informational, and technological resources. An organization's capabilities are the skills necessary to exploit the resources for productive use. Capabilities are intangible. It may be noted that an organization may not need unique resources to establish a distinctive competence as long as no other competitors possess such resources. An organization can create distinctive competencies only when it simultaneously has unique resources and has the capabilities to use those resources effectively. Successful strategies often either build on a company's existing competitive competencies or help a company develop new ones.

Competitive Strategy Versus Business Strategy

Business strategy consists of plans of action that strategic managers adopt to use a company's resources and distinctive competencies to gain a competitive advantage over its rivals in a market.

Business strategy has a wider scope than competitive strategy. Business strategy encompasses all the actions and approaches for competing against the competitors and the ways management addresses various strategic issues. As Hill and Jones have remarked, business strategy consists of plans of action that strategic managers adopt to use a company's resources and distinctive competencies to gain a competitive advantage over its rivals in a market. In doing business, companies confront a lot of strategic issues. Management has to address all these issues effectively to survive in the marketplace. Business strategy deals with these issues, in addition to 'how to compete.' The competitive strategy, on the other hand, deals with "management's action plan for competing successfully and providing superior value to customers."

Review Questions

1. What is meant by competitive strategy? What are the actions is it concerned with?
2. What is competitive advantage? Why is it considered as the ultimate goal of competitive strategy?
3. As a manager of an organization, what measures would you undertake to ensure sustenance of competitive advantage?
4. "Distinctive competencies have been helpful in attaining distinctive advantages through achievement of superior efficiency and quality." Explain the statement.
5. Explain what you mean by distinctive competency. How does distinctive competency help in achieving competitive advantages?
6. What are the differences between competitive strategy and business strategy?

Application Discussion Questions

1. What competitive advantage does your university possess? Why do you think that it is a competitive advantage? Ask your friends to verify whether they also agree with your opinion.
2. Visit a neighborhood grocery store and ask the owner or manager if the store has any distinctive competency. Using the definition of distinctive competency presented in this lesson, ask the manager/owner if the definition is consistent with how he/she thinks of distinctive competency.

Lesson-2: Generic Competitive Strategies: Low-Cost Strategy

Learning Objectives:

After studying this lesson, you should be able to:

- Make a list of the four generic strategies as identified by Michael Porter.
- Explain the meaning of low-cost strategy.
- Understand the benefits of low-cost strategy to the business organizations.
- Identify the market situations favorable for low-cost strategy.
- Predict when low-cost strategy may fail.

Introduction

This lesson discusses the first of the four generic strategies that were identified by Michel Porter. These generic strategies are common to all business organizations. Any company may follow these whenever deemed necessary. These are called generic for the commonality in use.

Michael Porter's Four Generic Strategies

Michael Porter has identified four types of competitive strategies that can be applied in any business organization irrespective of size and nature of products. Because of their susceptibility to common use by all business enterprises, they are labeled as generic strategies. These are, in fact, basic types of competitive strategies. In addition to these, there are also other strategies that a company can employ when deemed necessary, such strategic alliance, collaborative partnerships, merger, acquisition, vertical integration, outsourcing strategies, etc. Michael Porter's generic strategies are as follows:

1. Low-cost strategy
2. Differentiation strategy
3. Best-cost strategy
4. Market-niche or focus strategy.

In this lesson we discuss about the low-cost strategy. The subsequent lessons in this unit will be devoted to the discussion of differentiation strategy, best-cost strategy and market-niche strategies respectively.

LOW-COST STRATEGY

Low-cost strategy defined

Low-cost strategy is broadly called 'low-cost provider strategy.'

Low-cost strategy is broadly called 'low-cost provider strategy.' It is so called because the company that follows this strategy intends to become the overall low-cost provider in the industry in which the company operates its business. When a company adopts the strategy of selling its products at a price lower than its competitors, this strategy is known as low-cost strategy. Charging lower price becomes possible when the company can ensure cost reduction by operating business in a highly cost-effective manner. The strategic target of this strategy is a broad section of the market where the company offers economical prices. The company emphasizes on cost reduction without reducing quality.

The key to sustaining the low-cost strategy is to manage costs down in every area of the company's business. The goal of this strategy is to outperform competitors through low-cost leadership. When a company becomes a low-cost leader, it is likely to earn above-average profits.

Creating and then sustaining cost advantages are keys to attaining success in low-cost strategy. A company may achieve cost advantage by (a) doing a better job than competitors in performing internal value chain activities efficiently, (b) taking initiatives to cut down costs of value chain activities, and (c) recognizing the value chain to avoid (bypass) some cost-producing activities. Some widely known companies that employ low-cost strategy include Whirlpool and General Electric Company in home appliances, Black and Decker in power tools, Bashundhara in tissue paper and BIC in ball pen.

Creating and then sustaining cost advantages are keys to attaining success in low-cost strategy.

Low-Cost Strategy: Benefits to the Business Organizations

A business organization may derive the following benefits from pursuing a low-cost strategy:

1. **Overcoming threats from competitors:** Because of its cost advantage, a company can protect itself from the business-attacks of the competitors. If competitors enter into market with low price, the company can even further cut down its prices. This is possible because the company has already developed ways to reduce cost and sustain the cost advantage. Its cost-leadership position helps it dominate the competitors.
2. **Effective dealing with powerful suppliers:** When suppliers are few in number as well as powerful, they may try to increase prices of raw materials/other inputs. The company with a low-cost strategy can endure such price-increase because of its lower costs.
3. **Facing powerful buyers effectively:** Powerful big buyers (such as dealers and wholesalers or retail chains like Agora, Meena Bazaar or Wal-Mart) may dictate prices of a company's products. A company that follows a cost leadership strategy is less affected by such actions of buyers.
4. **Encountering threats from substitute products:** A low-cost leader is able to overcome threats from substitute products. It can reduce the price of its products if substitute products start entering into the market. Low-cost leadership helps the company retain its market share.
5. **Overcoming threats from the entry of potential competitors:** A company with a low-cost strategy can discourage other potential investors to come to the market. Its cost advantage automatically creates barriers to entry. Other companies may find it difficult to match their costs with that of the low-cost leader.

Market Situations Favorable for Low-Cost Strategy/
Situations Where Low-Cost Strategy Will Work Best

A low-cost strategy sounds good but it is not that easy to implement it successfully. It works well in the following situations:

1. When the product produced by all companies in the industry are essentially same. That is, the brand differences from company to company are minor. The products are standardized and are readily available.
2. When a large number of buyers are price-sensitive and they want to buy products at the lowest possible price.
3. When it becomes difficult to differentiate products from those of competitors due to the nature of the product. It means that very few ways are available to the company to differentiate the products and that is why, it is wise for it to follow low-cost strategy. Buyers become sensitive to price differences when product-to-product differences are negligible. In such a situation, they will go for the lowest price.
4. When buyer's costs in switching from one brand to another brand of another company are low or even zero. If buyers purchase another brand and this switching from the previous brand does not involve any additional cost (such as transportation or repair) they are likely to opt for the lower-priced brand.
5. When buyers are large and have significant power to negotiate pricing-related terms and conditions.
6. When price-competition among is very tough. Low-cost strategy helps producers to compete effectively based on the price.
7. When the company is in a position to use the lower-cost edge to attract price-sensitive buyers in great enough numbers to influence total profits.

When Does Low-Cost Strategy Fail?

Managers need to take care of the shortcomings of low-cost strategy.

Low-cost strategy has some shortcomings or pitfalls. Managers need to take care of these pitfalls so that they can undertake appropriate measures to be successful with this strategy. The shortcomings are as follows, which are responsible for the failure of the low-cost strategy:

(i) It may invite overly aggressive price-cutting by competitors. It may lead to price-war that may lead to lower profitability.

(ii) Cost advantages may sustain if it is easy for competitors to copy. When the competitors are able to copy the cost advantages, Low-cost strategy will fail. So, the ways to achieve cost advantage need to be difficult for others to copy.

(iii) If low-cost product does not contain enough attributes to be attractive to prospective buyers, the strategy may fail. Low price is not always appealing to buyers. Attractiveness may be lost if the product is features-poor or quality-deficient.

Review Questions

1. What are the generic strategies as identified by Michael Porter?
2. Explain the meaning of low-cost strategy.
3. Discuss the benefits of low-cost strategy to the business organizations.
4. Discuss the market situations favorable for low-cost strategy.
5. When does the low-cost strategy work best in a business organization dealing with consumer products?
6. Low-cost strategy does not work well in some situations. Do you agree with this view? Give arguments in support of your answers.
7. When does a low-cost strategy may fail.

Application Discussion Questions

1. A company has been using the low-cost strategy for the last 12 years for one of its consumer products. Some managers of the company have become very critical of this strategy a few days ago in a meeting where all senior and mid-level managers attended. They alleged that the strategy is not yielding desired results, although the company achieved distinct competitive advantage in the initial years of launching the strategy. Can you guess why these managers were critical of the strategy? When does actually this type of strategy work well?

Lesson-3: Generic Competitive Strategies: Differentiation Strategy

Learning Objectives:

After studying this lesson, you should be able to:

- Define differentiation strategy
- Determine the ways for achieving product differentiation.
- Make a list of the themes for product differentiation.
- Identify the issues that need to be addressed for achieving sustainability of differentiation strategy.
- Understand how to achieve a differentiation-based competitive advantage.
- Determine the situations where differentiation strategy works best.
- Explore the shortcomings of differentiation strategy.

Differentiation Strategy Defined

Differentiation means making a product different from the similar products of the competitors.

Differentiation strategy refers to making a company's product different from the similar products of the competitors. This strategy is associated with product differentiation (and service differentiation). In this book, we would use the word 'differentiation' mainly to mean differentiation of tangible products, not services. As a marketing terminology, differentiation means making a product different from the similar products of the competitors. According to Philip Kotler, differentiation is the act of designing a set of meaningful differences to distinguish the company's offerings (i.e., products) from competitors' offerings.[4] A differentiated product is unique by itself. A product (or service) can be differentiated on the basis of its form, shape, quality, durability, style, design, or some other features of the product. The goal of differentiation strategy is to achieve a competitive advantage by offering a product to customers that is considered as unique in some important ways. The differences made in the product must be of value to customers. A product with differentiated features can command premium prices (i.e., prices above the industry-average). Customers are usually to pay premium prices because they value the differentiated features of the product. Thus, the company that adopts a differentiation strategy can increase profits by charging higher prices and is able to outperform its competitors.

Hill and Jones suggested ways to achieve differentia-tion in company's products.'

A differentiation strategy is called a "broad differentiation strategy" when the differentiator-company goes for segmenting its market into several small segments (niches) and then offers a product designed for each market-segment. Coca-Cola follows a broad differentiation strategy in that it offers normal bottled cola, can-cola, and diet-cola for different segments.

What are the Ways to Achieve Product Differentiation?

Hill and Jones suggested the following ways to achieve differentiation in a company's products:[5]

1. **Differences in quality:** A company may differentiate its product simply by increasing quality and reliability. P & G Ivory Soap and IBM have sometimes followed differentiation strategy based on quality.

2. **Innovation:** For highly technologically complex products, innovation is an important source for differentiation. Computers, stereos, television sets and refrigerators require differentiation based on new innovated features. When products include innovated/valuable features, customers agree to pay for it.

3. **Responsiveness to customers:** A company may differentiate a product based on responsiveness to customers. When this becomes the basis for differentiation, the company offers comprehensive after-sales services including repair. This sort of differentiation is highly workable in the case of products which require frequent after-sales services, such as microwave ovens, television sets, computers, cars and the like. In Bangladesh, for example, 5M Group of Companies (mainly a software developer and 5M brand computer manufacturer) and Rangs-Sony are famous for their excellence in responsiveness to customers.

4. **Responding to customers' psychological desires:** An important source of product differentiation is a company's response to the psychological desires of customers. Customers may desire to have a special status or unique prestige from using a product. This is especially important in the case of luxury or fashion goods and specialty products. Many customers feel proud of having a BMW car or a Rolex watch.

5. **Wide choice of customers:** differentiation of a product may be done by making available items of any kind in the same product-line instantly to customers as per their demand. Berger Paints Ltd. Has adopted differentiation strategy by making 'color bank' program. By this strategy any shade of color can be provided instantly to any retail paint-customers. It has given a competitive advantage over the competitors.

There are many ways to differentiate a product. Based on the nature and use of the product as well as the nature of the target customers, products can be differentiated along various themes. Below is a description of such themes.

Themes for Product Differentiation

We can summarize the major themes for product differentiation as follows:

No.	Themes	Examples
1	Unique taste	Food products such bread, drink, juice, chocolate, etc.
2	Multiple features	Automobiles such as BMW and Mercedes-Benz, and software such as Microsoft Office 2000

No.	Themes	Examples
3	Wide selection	Retail chain shops such Agora and Meena Bazaar, and online bookstore such as Amazon.com
4	Special features	Transparent ball pen or transparent soap or halal soap.
5	Superior service	Overnight delivery of packets by a courier service company.
6	Prestige and distinctiveness	56-inches television set or Sony Home Theater
7	Product reliability	Revlon Company or Max Factor in cosmetics; Toyota in automobiles.
8	Complete line of products	Bangladesh Thai Aluminium Limited in aluminium products.

Achieving Sustainability of Differentiation Strategy

The differentiation must be sustainable.

Making a company's product different from those of the competitors is not enough to survive competition in the marketplace. The differentiation must be sustainable. In order to sustain product differentiation for a longer period of time, a company needs to address the following issues:

1. The company must try to adopt those differentiation approaches that would be hard or expensive for the competitors to copy (or duplicate). However, strong competitors might be able to clone any feature of a product over a period of time.
2. Differentiation has to be linked to 'core competencies, unique competitive capabilities, and superior management of value chain activities.' The basis for a company's product differentiation would be sustainable if the competitors cannot readily match their competencies with those of the company. Sustainability can also be achieved if competitors cannot manage the value chain activities as uniquely as the company itself.
3. A company may ensure sustainability of differentiation when it can base its differentiation on new product innovation, technological superiority, quality, reliability, unique competitive capabilities and superior as well as comprehensive customer service.
4. The differentiation attributes must be of value to customers.

How to Achieve a Differentiation-Based Competitive Advantage?

The major purpose of differentiation strategy is to gain competitive advantage in the marketplace.

The major purpose of differentiation strategy is to gain competitive advantage in the marketplace. But the question is: how to achieve a differentiation-based competitive advantage? A company must have clear understanding of the basis for competitive advantage. Its basis for competitive advantage may be either –

(i) a product offering in the market whose attributes differ significantly from the offerings of the competitors; or

(ii) company's set of capabilities for delivering customer value unmatched by the competitors.

A company has to create unique attributes for product differentiation so that customers consider them valuable. It can do it if it adopts any of the following approaches:

A company has to create unique attributes for product differentiation so that customers consider them valuable.

1. It may incorporate in its products such attributes or features that will lower the customer's costs of using the product. Product becomes economical to a customer when the company is able to reduce wastage of raw materials, deliver the products just-in-time for reducing customer's stock/inventory, provide regular repair and maintenance service and provide free technical support, etc.
2. The company may incorporate performance-raising features in the product. Several features/attributes can enhance product performance. Michael E. Porter suggested seven such features:
   - Provide buyers greater reliability, durability, convenience, or ease of use.
   - Make the company's product or service cleaner, safer, quieter, or more maintenance-free than rival brands.
   - Exceed environmental or regulatory standards.
   - Meet the buyer's needs and requirements more completely, compared to competitors' offerings.
   - Give buyers the option to add on or to upgrade later as new product versions come on the market.
   - Give buyers more flexibility to tailor their own products to the needs of their customers.
   - Do a better job of meeting the buyer's future growth and expansion requirements.[6]
3. The company may incorporate buyer's satisfaction-raising features in intangible ways. Intangible ways may differ from product-to-product but generally they may include safety, design, superior craftsmanship, upscale fashion, buyer's desire for status, image and prestige, unconditional guarantee, long-time warranty, refund for a purchased product if returned within a specified time, replacing a purchased product, refunding purchasing price for a defective product, and so on.
4. The company may compete on the basis of capabilities that competitors are lacking. A company's all of the capabilities may not have differentiating competitive value. Only those capabilities have such value which the competitors cannot afford to match. Thus, the company must be able to develop capabilities that have differentiating competitive value. As an example, Microsoft Corporation has stronger capabilities than its competitors to develop and sell software products much faster. Microsoft's differentiating competitive capabilities are its unique operating system (Windows), very strong and large project teams consisting of highly qualified programmers, marketing know-how and efficiency, and unparallel financial strength.

Situations Where Differentiation Strategy Works Best

Differentiation strategy may not be suitable for all types of products or in all kinds of market situations. It is likely to be appropriate in the following situations:

1. Existence of several ways for differentiation.
2. Buyers' perception of differentiation as having value.
3. Diversity in buyers' needs.
4. Pursuing different differentiation approaches by various competitors.
5. Rapid technological change and innovation.
6. Competition revolving around rapidly evolving product features.

Let's discuss the issues more elaborately.

1. **Ways for differentiation:** If the ways to differentiate a product are limited, it becomes difficult to profitably differentiate the product. Differentiation strategy works well in situations where there are many ways to differentiate the product.
2. **Buyers' perception:** Differentiation would also be successful if a large number of buyers perceive that the differentiation is valuable. Buyers must be benefited from the differentiation in order to be successful.
3. **Diversity in needs:** Buyers usually have differences in their preferences. One group of buyers may prefer one combination of product-features. But another group may not like the same features. Existence of such differences in buyer preference facilitates a company to pursue different approaches to product differentiation. When buyers needs are diverse, companies can avoid out differentiating (i.e., ousting a competitor through making product different) one another on the same features.
4. **Different approaches of differentiation:** Another situation where companies may be successful with differentiation strategy is a situation of following different approaches of differentiation by different companies. When here are few competitors who follow similar differentiation approach, there is less chance of head-to-head rivalry among them. This is because the companies try to attract customers based on different combination of features.
5. **Technological change:** When there are rapid changes in the technology and product innovation, companies can go for differentiation strategy to maintain buyer interest in the product.
6. **Competition around evolving features:** If market situation is such that competition among the companies centers around rapidly evolving product-features, then this situation provides space for them to pursue separate differentiation approaches. In order to maintain interest of buyers, company may indulge in rapid product innovation and introduction of new versions of the product frequently.

Pitfalls or Shortcomings of Differentiation Strategy

The common pitfalls and mistakes in pursuing differentiation strategy include:

1. **Attribute with little value:** While differentiating a product the company may fail to adequately consider the buyer's perspective in terms of value of he attribute. If buyers consider that the changed attribute is of little value to them, differentiation strategy will fail.
2. **Easy to copy:** Differentiation strategy will fail if the competitors can quickly copy or imitate the differentiated features. In that case, buyers will find no difference among the products of competitors.
3. **Inability to benefit buyers:** Differentiation does not work when buyers perceive that it could not reduce their cost or increase their well-being.
4. **Over differentiation:** Over differentiation occurs when differentiation leads to much higher price than the competitors or differentiation causes product quality exceed buyers' needs.
5. **Failure to understand buyers:** Differentiation will obviously fail if the company cannot understand what buyers consider as value. Every differentiation must be done based on buyers' viewpoint – not the viewpoint of the company.
6. **Buyers' satisfaction with basic product:** When buyers are satisfied with a basic product, differentiation strategy may fail. Because buyers don't like to have any extra attributes in the products that will increase price.

It thus appears that differentiation strategy may not always work. It is difficult to give any guarantee that differentiation of a product would result in competitive advantage in the market. Success depends on careful analysis of buyers' needs and their perceptions. Let the buyers say what kind of new features they want to have in the product.

Success of differentiation depends on careful analysis of buyers' needs and their perceptions.

Review Questions

1. Define differentiation strategy.
2. What are different ways for achieving product differentiation?
3. Make a list of the themes for the differentiation of various products.
4. A product can be differentiated in different ways. Also, the themes are not same for all types of products. Discuss at least five themes for differentiation five different types of products.
5. Discuss the issues that need to be addressed for achieving sustainability of differentiation strategy.
6. How can a company achieve a differentiation-based competitive advantage?
7. State the shortcomings of differentiation strategy.

Application Discussion Questions

1. Discuss the possible themes for product differentiation for food products, machinery products and automobiles.
2. A special brand of Mercedes-Benz car is selling at around Tk.15000000.00 in Dhaka. The dealer of the car has taken strategy of reducing the price of the brand for Tk.500000.00 to increase its sales. Do you think the dealer's strategy would yield the desired results?

Lesson-4: Generic Competitive Strategies: Best-Cost Strategy

Learning Objectives:

After studying this lesson, you should be able to:

- Explain the meaning of best-cost strategy.
- Why is the best-cost strategy called a hybrid strategy? Explain with examples.
- Cite examples of best-cost strategy in the context of Bangladesh.
- Ascertain the preconditions for a company to become a best-cost provider.
- Identify the market situations where the best-cost strategy works best.

Best-Cost Strategy: Meaning and Nature

As a concept, Best-Cost means high quality and low price of a product. This term is used to indicate a situation where the company tries to achieve best (lowest) cost relative to the competitors who offer similar products and simultaneously tries to improve quality. Best-cost strategy is the strategy of increasing quality of products while reducing costs. This strategy is applied to give customers "more value for the money." It is achieved by satisfying customers' expectations on key attributes of products. At the same time, prices are charged lower than the competitors. By following the best-cost strategy, the company attempts to attract the 'value-conscious buyers' (those buyers who want superior product with lower price).

Best-cost strategy is the strategy of increasing quality of products while reducing costs.

This strategy is a hybrid. It balances a strategic emphasis on low-cost against a strategic emphasis on differentiation which is understandable from the following Figure-7.1. It is considered as the most powerful competitive strategy of all. It presupposes 'relentlessly striving to become a lower-and-lower cost provider of a higher-and-higher caliber product.' Toyota Company of Japan followed best-cost strategy for its Lexus cars to beat Mercedes-Benz and BMW cars.

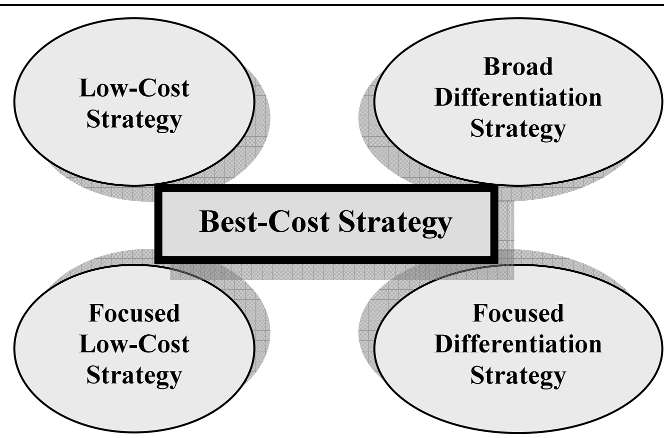

Figure-7.1: Best-cost strategy as a hybrid

Examples of Best-Cost Strategy

Although Toyota Motor Company is known for its low-cost strategy, it applied best-cost strategy when it manufactured its luxury-car Lexus models. To compete against such luxury-car makers as BMW and Mercedes-Benz, Toyota management started making Lexus – a car with premium-quality at costs below those of competitors. Toyota's best-cost strategy was so successful that Lexus model was ranked among the top 10 models – and second best-selling luxury brand in the US market. Another example is Microsoft Corporation. Microsoft is widely recognized as the committed user of best-cost strategy in software. This world-famous IT-giant is continually improving the quality of its software and at the same time reducing the costs of its software products.

Preconditions for a Company to Become a Best-Cost Provider

It is easy to say to be a best-cost provider, but it is really a tough job to become a best-cost provider in the marketplace. In order to successful, the company must have the following resources and capabilities to simultaneously lower down costs and improve quality:

1. It must have the resources and capabilities to achieve high quality at a lower costs than the competitors.
2. It must incorporate appealing (attractive) features at a lower costs than competitors.
3. It must match product preference and a lower cost that competitors.
4. It must provide good-to-excellent customer service at a lower cost than competitors.

Market Situations Where Best-Cost Strategy Works Best

(i) **Buyer diversity:** Best-cost strategy will work very well in a market where product differentiation becomes the norm because of buyer diversity, and also a substantial number of buyers are sensitive to price and quality.

(ii) **Positioning advantage:** A company with Best-cost strategy can position itself near the middle of the market:

   a. With a medium-quality product at a below-average price, or

   b. With a very good product at a medium price.

Many buyers may prefer mid-range products. They avoid cheap, basic products of low-cost producers. They also avoid expensive products of top quality.

(iii) **Resources and capabilities:** it will work best when the company has the resources, know-how and capabilities to incorporate upscale product attributes at a lower cost. This strategy is ill-advised if the resources and capabilities do not permit the company to manage costs down and product caliber up.

Review Questions

1. Clarify the meaning of market-niche strategy or focus strategy.
2. What are the common requirements for successful implementation of niche strategy?
3. When is the niche strategy most useful? Explain.
4. What are the different types of niche strategy**?** Discuss are the risks associated with a niche strategy.
5. If a company wants to follow a combination of low-cost strategy, differentiation strategy and focus strategy for a particular product, what should ideally be the characteristics of the product and also of the market segment?

Application Discussion Questions

1. For decades now, 5M Corporation headquartered at Dhaka has advertised that its 5M Perfume Soap is 99% pure. 5M Corporation has refused to add deodorants, facial creams, or colors to its soap. It also packages its soap in plain paper wrappers – no foil or fancy printing. Is 5M Corporation implementing a product differentiation strategy, low cost strategy, focus strategy (niche strategy), or some combination? Explain your answer.

Lesson-5: Generic Competitive Strategies: Market-Niche Strategy (Focus Strategy)

Learning Objectives:

After studying this lesson, you should be able to:

- Clarify the meaning of market-niche strategy or focus strategy.
- Discuss the common requirements for successful implementation of niche strategy.
- Determine the situations where niche strategy is most suitable.
- Identify the risks associated with niche strategy.
- Classify the niche strategy.

Meaning of Market-Niche Strategy

A market niche is a narrow part of a total market. Niche can be identified on the basis of the following:

(a) particular buyer group (such as women, youths, adolescents or aged 50+); or

(b) geographic uniqueness (such as East of Bangladesh or Rajshahi region or North Bengal); or

(c) special product attributes that appeal only to niche members (such as specially designed neck-tie or fancy Punjabi); or

(d) a particular product line (such as lemon juice, children's ked-shoes or detergent with bleach).

Niche strategy involves concentrating on a narrower buyer segment and offering the niche-customers a product customized to their tastes and requirements.

Niche strategy is often called focus strategy.

After identifying the niche-markets, a company can decide to enter into one or more of the niches with its products. When the company decides to launch its products in the niche markets, its strategy is known as niche strategy. Niche strategy involves concentrating on a narrower buyer segment and offering the niche-customers a product customized to their tastes and requirements. This strategy is often called 'focus strategy.' It focuses on a particular segment or part of a market. It is directed towards serving the needs of a limited customer group. According to Hitt, Ireland and Hoskisson, a niche strategy/focus strategy is an integrated set of actions designed to produce or deliver goods and services that serve the needs of a particular competitive segment.[7] A company usually follows focus strategy when it is able to serve a narrow piece of the market better than competitors. With this strategy

This strategy is successful when the company has the core competencies required to produce value to a narrow competitive segment that exceeds the value available from companies serving customers on an industry-wide basis. A company can achieve a least-cost position or differentiator or both in the particular market segment (niche). Coca-Cola Company has introduced 'diet cola' to serve the niche market consisting of diabetic patients. Tibet Chemical Company for its Tibet Snow initially used niche strategy particularly directed towards rural women. Some real-life examples of niche strategy are given in Table 7.1.

Table 7.1: Niche Strategies of Various Organizations

Organizations	Market Niches
e-Bay	Online auctions
Porsche	Sports cars
Atlantic Southeast Airlines	Low-traffic, short-haul flights
Nissan Motor Company	Mid-sized cars
Toyota Motor Company	Small-sized cars: CAMRY & SOLEIL
Hallmark	Greeting cards with distinctive look and contents
Electronic Data Systems	Outsourcing data processing operations for specific categories of customers
Systems and Computer Technology Company	Software for local governments
Bisys Group	Software for banks
Systematics Company	Software for universities
Motel 6	Travelers who have simple overnight requirements

Classification of Niche/Focus Strategy

A company can pursue a niche strategy either with a low-cost approach or a differentiation approach. There can, thus, be two types of focus or niche strategy:

A company can pursue a niche strategy either with a low-cost approach or a differentiation approach.

1. Focused Low-Cost Strategy: Focused low-cost strategy is the strategy of entering into a niche market with a unique type of product that has a special need among the customers in the niche market. This strategy is targeted to those buyers who desire to have unique products at a low-cost. The company that follows this strategy competes against the cost leader in the niche market where it has cost advantage. With this strategy, a company concentrates on small-volume custom products for which it has a cost advantage. A company may adopt this strategy to serve a buyer-segment whose needs can be satisfied with less cost compared to the rest of the market.

2. Focused Differentiation Strategy: Focused Differentiation Strategy is the strategy of operating business with a differentiated product in a chosen niche market. When a company pursues a focused strategy based on differentiation, it concentrates on a narrow buyer segment and offers customized attributes in products better than competitors' products. Here, the focuser company competes against competitors not based on low-cost, rather based on product differentiation. Since the focuser company has knowledge about the needs of niche customer-groups, it can successfully differentiate its products. For example, Alam Soap Company of Dhaka (producer Ek No. Pacha Saban) competes against other soap producers in the 'laundry bar soap' segment of the soap market, not in perfume soap or liquid soap markets. Its strategy is focused differentiation strategy.

Common Requirements for Successful Implementation of Niche Strategy

The commonly required skills and resources for successful implementation of niche strategy include:

a. Managers' ability to explore a well-defined but narrow market segment.

b. Clear identification of competitors who serve a market broader than the niche market but are unable or disinterested to serve the niche for reasons.

c. Firm's ability to provide adequate capital.

d. Designing and maintaining a low-cost distribution system, with strong cooperation from the channel members.

e. Strong marketing availability and creative flair.

When is Niche Strategy/Focus Strategy Attractive/ When Does Focus Strategy Work Best?

A niche strategy does not work well in all situations. It works well usually in the following situations:

1. **Profitable niche:** The niche strategy is expected to be highly workable when the market niche is big enough to be profitable. Very small niche may not bring enough profit for the marketers.
2. **High growth potential:** Market niche becomes attractive when its growth potential is high. In order to be profitable the niche must be able to offer good growth potential.
3. Availability of different niches in the industry: When an industry has different niches/market segments, the marketer can pick up the attractive niche(s) based on its strengths.
4. **Inability of competitors to serve niche market:** The competitors who sell their products in many segments of the market may find it costly to operate in a small piece of market where there is a need for specialized products. In such a situation, the focus marketer (market-focuser) may do well with his customized products.
5. **Apathy of market leaders to enter into niche market:** Focus strategy also works well when big market leaders do not like to enter into a niche market. This may be because leaders do not consider it important to be a niche marketer for their business success.
6. **No risk of segment overcrowding:** A company may find it useful to follow a focus strategy if rival companies avoid specializing in the same segment. This attitude of rivals reduces the risk of overcrowding by many rivals in the niche market. Few players in the market niche always reduce competitive risk.

7. **Focuser's competitive ability:** Success with a focus strategy to a large extent depends on the ability of the focuser-company to compete effectively in the market. Effective competition is possible when the company has enough resources, capabilities and market image.

8. **Company's farsightedness:** To be successful with focus strategy, the focuser-company must have the farsightedness to pick up those niches that match with its specialized competencies and capabilities as well as attractive by all standards.

Risks Associated with a Focused Strategy/Niche Strategy

Several risks are associated with a niche/focus strategy. These risks originate mainly from more appealing products by rivals, shifting of product-preferences of customers, and high attractiveness of the niche market. Managers should have a clear idea about these risks so that they can consider them before deciding on the adoption of niche strategy.

1. **Risk from more appealing products:** If the competitors come up with such products that are more attractive to the customers, then there is a risk of losing the market. Example includes MUM (bottled drinking water) of Partex Group. Many rivals have gone out of the market because of the appealing attributes of MUM.

2. **Shifting of customers' preferences:** Another risk emanates from the possibilities of shifting customers' preferences and needs for a particular product in the niche market. Over time, their preferences may change or they may need a product with different attributes. Such a situation may allure other producers to enter the niche market. This would intensify competition in the niche market.

3. **High attractiveness of the niche market:** The third risk may come from the niche itself. The niche-market may become so highly attractive that the rivals would jump into the segment and finally it may be flooded with so many competitors. Thus, niche-market profits will slide down.

4. **Universality of customers' needs:** Another risk is that the needs of focused customers in the niche market may become more similar to those of customers in a market as a whole. If this happens, the advantages of focus strategy may be reduced or eliminated.

5. **Price-war:** It may invite overly aggressive price cutting by competitors, which may eventually lead to price-war that may lead to low profitability.

6. **Withering cost advantages:** Cost advantages of the company may not sustain for a long period of time if they can be copied easily by the competitors. So, the ways to achieve cost advantage need to be difficult for others to copy.

7. **Fear of low attractiveness:** If low-cost product does not contain enough attributes to be attractive to prospective buyers the strategy may fail. Low price is not always appealing to buyers. Attractiveness may be lost if the product is feature-poor or quality-deficient.

Review Questions

1. What do you mean by best-cost strategy?
2. Give two examples of best-cost strategy in the context of Bangladesh.
3. What are the preconditions for a company to become a best-cost provider?
4. Discuss the market situations where the best-cost strategy works best.
5. Explain the nature of best-cost strategy. Is it always pragmatic to follow the best-cost strategy? Why?

Application Discussion Questions

1. Visit the web site of Microsoft Corporation – the global giant of computer software. Analyze the information available in the web site and make your comments regarding its strategy. Is it following low-cost strategy or best-cost strategy for the marketing of its software like Windows XP or Windows Professional?

NOTES

1. Hills and Jones, op.cit. p. 127.
2. This section draws on Hill and Jones, op.cit., pp. 134-135.
3. Apple Computer lost its competitive advantage subsequently. Compaq and Dell –two giants in computer business – enjoyed competitive advantage in certain years but both had been at a competitive disadvantage at some other years.
4. Philip Kotler, *Marketing Management* (New Jersey: Prentice-Hall, 1999), p 287.
5. These have been suggested by Hill and Jones, op. cit. pp. 134-135.
6. For details, see Michael E. Porter, *Competitive Advantage* (New York: Free Press, 1985). pp. 135-138.
7. Michel A. Hitt, R. Duane Ireland and Robert E. Hoiskisson, *Strategic Management: Competitiveness and Globalization* (Australia: South-Western, 2001), p. 168.