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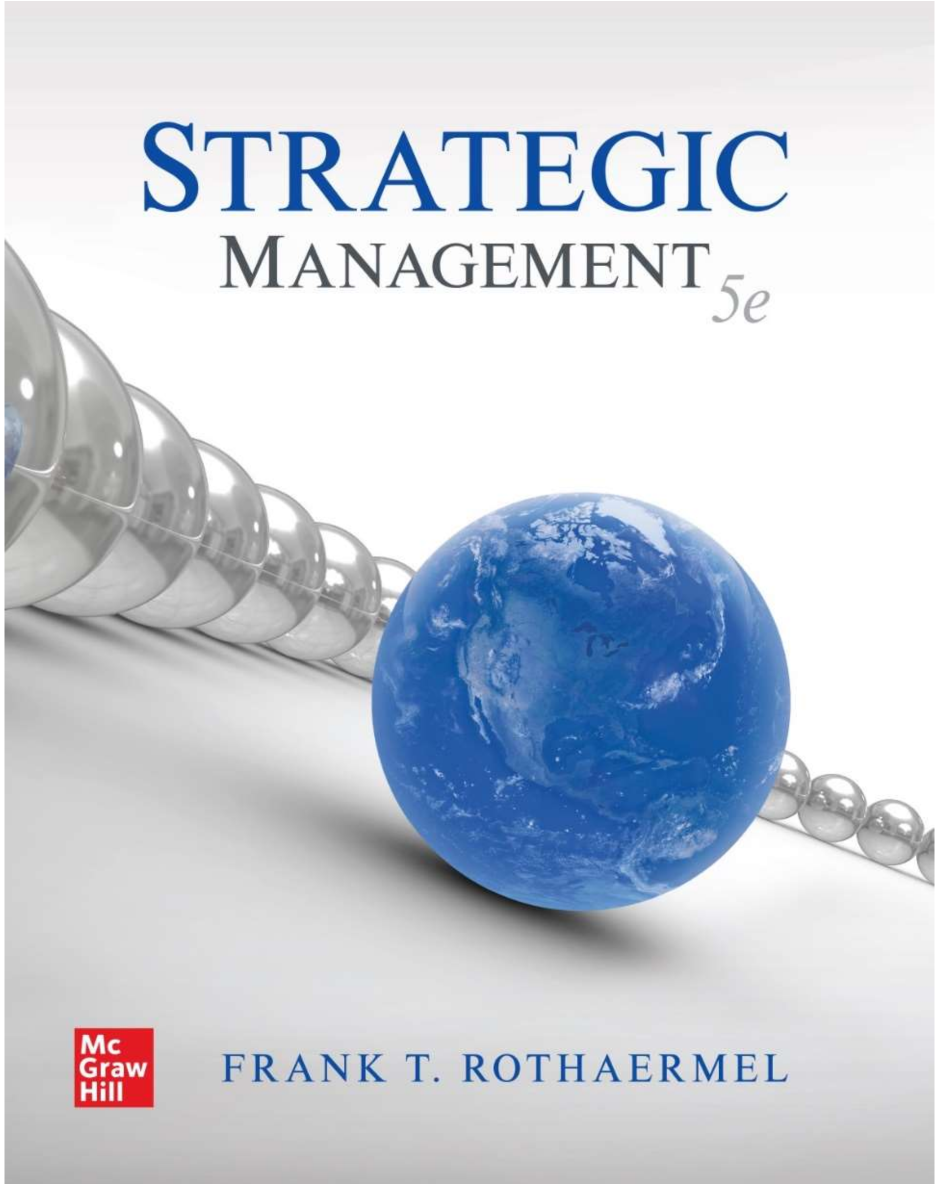
Chapter 1

What Is Strategy?



LEARNING OBJECTIVES

1. Explain the role of strategy in a firm's quest for competitive advantage.
2. Define competitive advantage, sustainable competitive advantage, competitive disadvantage, and competitive parity.
3. Assess the relationship between stakeholder strategy and sustainable competitive advantage.
4. Conduct a stakeholder impact analysis.
5. Explain the Analysis, Formulation, Implementation (AFI) Strategy Framework.

Strategic Management

An integrative management field.

Combines analysis, formulation, and implementation in the quest for competitive advantage.

Mastery of strategic management enables you to:

- View a firm in its entirety.
- Think like a general manager.
- Position your organization for superior performance.

Strategy

A set of goal-directed actions a firm takes to gain and sustain superior performance relative to competitors.

To achieve superior performance, companies compete for resources:

- New ventures: financial and human capital.
- Existing companies: profitable growth.
- Charities: donations.
- Universities: the best students and professors.
- Sports teams: championships.
- Celebrities: media attention.

A Good Strategy Is Based on Three Elements

A diagnosis of the competitive challenge.

- Analysis of the firm's internal and external environments.

A guiding policy to address the competitive challenge.

- Formulation.
- Results in corporate, business and functional strategy.

A set of coherent actions to implement the firm's guiding policy.

- Implementation.

Crafting a Good Strategy at Tesla

The Competitive Challenge:

- Tesla must manufacture attractive and affordable vehicles using its new technology.
- It also needs the required infrastructure for electric vehicles.

A Guiding Policy:

- Tesla is building cost-competitive mass-market vehicles.
- They have made significant investments in lithium-ion battery production.
- They have just broken ground for another factory in Shanghai, China.

Coherent Actions:

- Tesla is attempting to ramp up production volumes to achieve economies of scale.

Competitive Advantage

Superior performance relative to other competitors in the same industry or the industry average.

- Competitive advantage is relative, not absolute.

To assess competitive advantage, benchmark:

- Compare the firm to competitors in the same industry.
- Compare the firm to the industry average.

Sustainable Competitive Advantage

A firm that is able to outperform its competitors or the industry average over a prolonged period.

Example: Apple (smartphone industry):

- Sustainable competitive advantage over Samsung.
- Has lasted over a decade.

Competitive Disadvantage & Competitive Parity

Competitive Disadvantage: a firm that underperforms:

- Its rivals.
- The industry average.

For example, is 15% ROIC superior?

- It depends on the industry.

Competitive Parity: two or more firms that perform at the same level.

How to Gain a Competitive Advantage

Provide goods or services that:

- Consumers value more highly than those of its competitors, or
- Are similar to the competitors' at a lower price.

The rewards of superior value creation:

- Profitability.
- Market share.

Strategic Positioning

A unique position within an industry that allows the firm to provide value to customers, while controlling costs.

Value creation minus costs equal economic contribution.

- The greater, the better.
- Enhances the likelihood of competitive advantage.

Strategic Positioning Requires Trade-Offs

Managers must make conscious trade-offs.

- How to allocate resources?
- Which activities to pursue?

Example: the retail industry:

- Walmart: cost leader – big box outlet, low prices.
- Nordstrom: differentiator – professional salespeople, luxury setting.

A Unique Strategic Position

A successful combination of strategic activities.

Competitive advantage has to come from:

- Performing different activities.
- Performing the same activities differently than rivals.

Example: Walmart:

- Strategic activities strengthen its position as cost leader.
- Big stores, low overhead, low wages.

What Strategy Is Not

1. Grandiose statements:

- "We will be number 1."
- "We will win."

2. A failure to face a competitive challenge:

- Blockbuster didn't address Netflix, Redbox, Amazon Prime, and Hulu.

3. Operational effectiveness, competitive benchmarking, or tactical tools:

- Examples: "pricing strategy," "operations strategy," "brand strategy."
- These are good policies or initiatives, but not a strategy.

Value Creation

Companies with a good strategy are able to provide products or services to consumers:

- At a price point that they can afford.
- That enables the company to make a profit.

Value creation lays the foundation for a successful economy:

- Education.
- Infrastructure.
- Public safety.
- Healthcare.
- Clean water and air.

Stakeholders

Organizations, groups, and individuals:

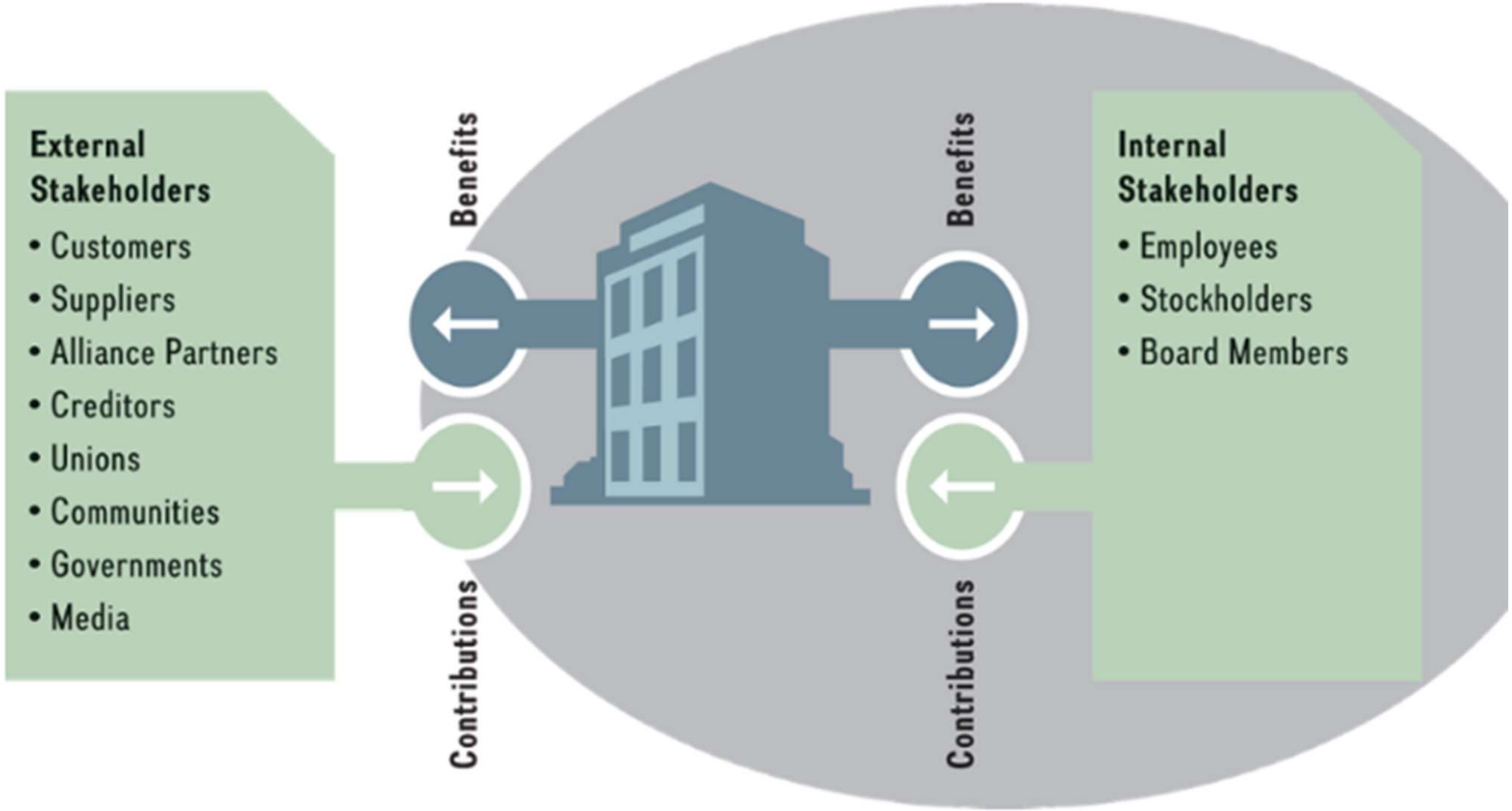
- Can affect or can be affected by a firm’s actions.
- Have an interest in the performance or survival of the firm.

Stockholders, employees (including executives, managers, and workers), and board members.

Customers suppliers, alliance partners, creditors, unions, communities, media, and governments.

Internal and External Stakeholders in an Exchange Relationship with the Firm

Exhibit 1.1



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Stakeholder Strategy

An integrative approach to managing a diverse set of stakeholders to gain and sustain competitive advantage.

Stakeholder management benefits firm performance:

- Cooperative stakeholders reveal important information.
- Increased trust lowers business transaction cost.
- Can lead to greater adaptability and flexibility.
- More predictable and stable returns.
- Stronger reputation.

A Decision Tool for Stakeholder Strategy

Stakeholder Impact Analysis helps to recognize, prioritize and address stakeholder needs.

Three important stakeholder attributes: power, legitimacy, and urgency:

- Power: when the stakeholder can get the company to do something that it would not otherwise do.
- Legitimate claims: perceived to be legally valid or otherwise appropriate.
- Urgent claims: require a company's immediate attention and response.

Stakeholder Impact Analysis

Exhibit 1.2

[Access the text alternative for slide image.]

The Pyramid of Corporate Social Responsibility

Exhibit 1.3

Adapted from Carroll, A. B. (1991, July—August), "The pyramid of corporate social responsibility: Toward the moral management of organizational stakeholders," *Business Horizons*: 42.

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AFI Framework

Effectively managing the strategy process is the result of:

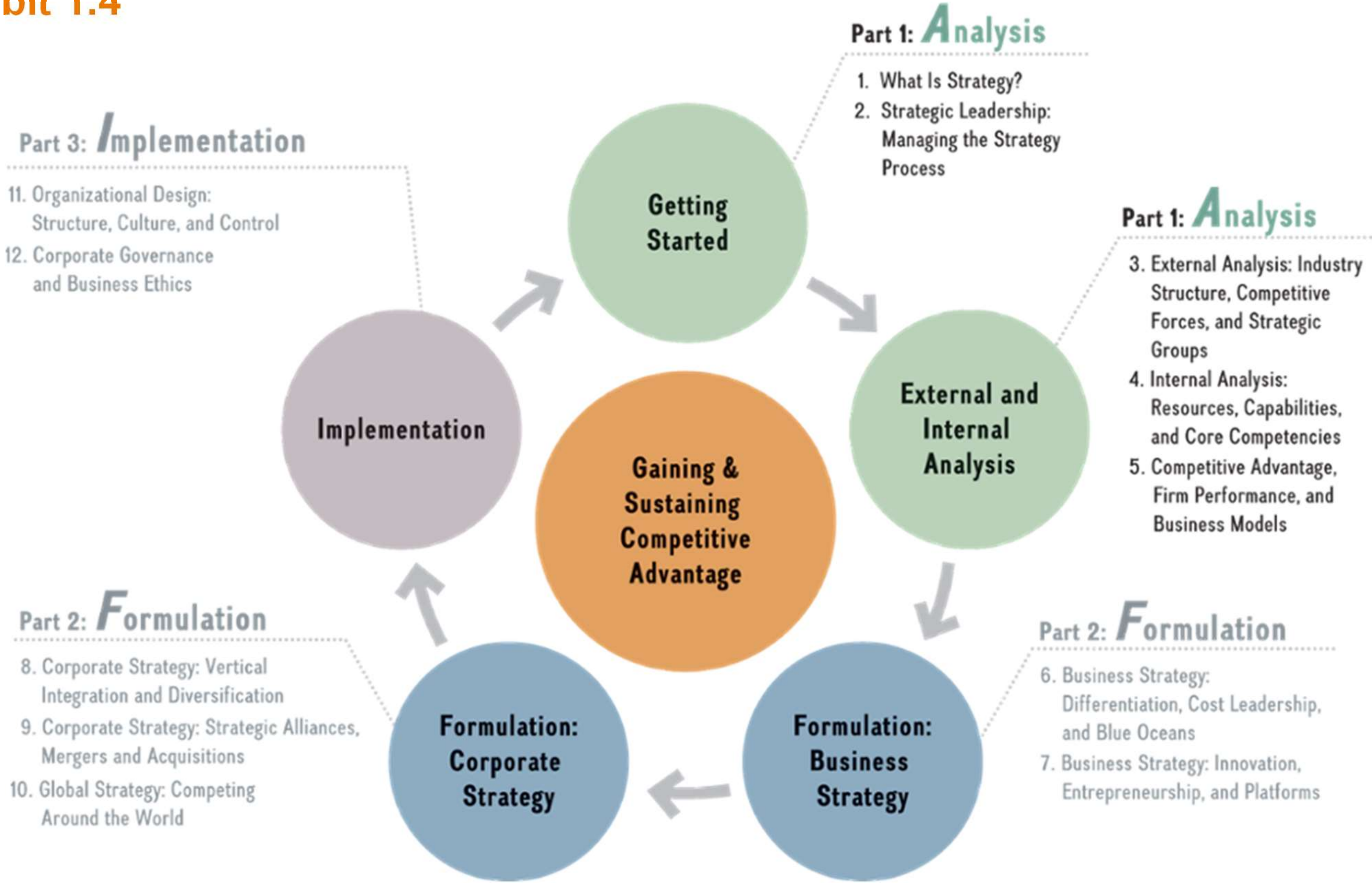
- Analysis (A).
- Formulation (F).
- Implementation (I).

This framework:

- Explains and predicts differences in firm performance.
- Helps leaders formulate and implement a strategy that can result in superior performance.

The AFI Strategy Framework

Exhibit 1.4



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Accessibility Content: Text Alternatives for Images

Internal and External Stakeholders in an Exchange Relationship with the Firm Text Alternative

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The graphic shows the flow of the relationship between stakeholders and the firm.

The external stakeholders are customers, suppliers, alliance partners, creditors, unions, communities, governments, and media.

The internal stakeholders are employees, stockholders, and board members.

Benefits flow from the firm to both of these groups of stakeholders as the firm receives contributions from both.

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Stakeholder Impact Analysis Text Alternative

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The graphic lists the steps of stakeholder impact analysis.

Step 1: Who are our stakeholders?

Step 2: What are our stakeholders' interests and claims?

Step 3: What opportunities and threats do our stakeholders present?

Step 4: What economic, legal, ethical, and philanthropic responsibilities do we have to our stakeholders?

Step 5: What should we do to effectively address the stakeholder concerns?

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The Pyramid of Corporate Social Responsibility Text Alternative

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The pyramid's foundational block represents its economic responsibilities: to gain and sustain competitive advantage.

The second level up is legal responsibilities: laws and regulations are society's codified ethics: define minimum acceptable standard.

The third level up is ethical responsibilities: do what is right, just, and fair.

The top of the pyramid is philanthropic responsibilities: corporate citizenship.

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The AFI Strategy Framework Text Alternative

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The important inside circle is titled "Gaining and Sustaining a Competitive Advantage" that is at the very center of the image, with five different circles on the outside of it. Arrows go back and forth from the center circle to each of the five outer circles. The five outer circles are labeled: (1) Getting Started, (2) External and Internal Analysis, (3) Formulation: Business Strategy, (4) Formulation, Corporate Strategy, and (5) Implementation.

Each of these outer five circles have a brief description beside them to explain what the circle means:

Under the first outer circle titled "Getting Started," it says: Part 1, Strategy Analysis, "What is Strategy (Chapter 1)" and "Strategic Leadership: Managing the Strategy Process (Chapter 2)."

Under the second outer circle titled "External and Internal Analysis," it says: Part 1, Strategy Analysis, "External Analysis: Industry Structure, Competitive Forces and Strategic Groups (Chapter 3)," "Internal Analysis: Resources, Capabilities and Core Competencies (Chapter 4)," and "Competitive Advantage, Firm Performance, and Business Models (Chapter 5)."

Under the third outer circle titled "Formulation: Business Strategy," it says: Part 2, Strategy Formulation, "Business Strategy: Differentiation, Cost Leadership and Integration (Chapter 6)" and "Business Strategy, Innovation and Entrepreneurship (Chapter 7)."

Under the fourth outer circle titled "Formulation: Corporate Strategy," it says: Part 2, Strategy Formulation, "Corporate Strategy: Vertical Integration and Diversification (Chapter 8)," "Corporate Strategy: Strategic Alliances, Mergers and Acquisitions (Chapter 9)," and "Global Strategy: Competing Around the World (Chapter 10)."

Under the fifth outer circle titled "Implementation," it says: Part 3, Strategy Implementation, "Organizational Design: Structure, Culture and Control (Chapter 11)," and "Corporate Governance and Business Ethics (Chapter 12)."

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