



Faculty of Business and Law



GSBS6481 International Business Strategy

Week 2: The Industry-Based View of International Business Strategy

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Reference

- Peng, Mike W (2021), *Global Strategy*, 5th ed. USA: Cengage Learning.
 - Chapter 2 Management industry competition
- Supplementary reading available in the course Blackboard site (in Week 2 Folder)
 - Porter: The Five Competitive Forces That Shape Strategy, available through the UoN library [link](#)

(In this 2008 article in the Harvard Business Review, Porter reaffirms, updates and extends the classic five competitive force framework he first introduced in 1979.)

Some key concepts

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- Industry
 - A **group of firms** producing products or services that are similar to each other
- Structure
 - The structural **attributes** of an industry such as the costs of entry/exit.
- Conduct
 - Firm **actions** (strategies) such as product differentiation.
- Performance
 - The result of firm conduct in response to industry structure, e.g.
 - Average (normal),
 - Below-average, and
 - **Above-average**

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Outline

- Intellectual roots of the industry-based view of international business strategy
- Introduction to the industry-based view of international business strategy
 - The five-force framework
 - Three generic strategies
 - Strategic groups
- Class activity: Five-force analysis of an industry



Industrial economics as the root of the industry-based view of IB strategy

- *Management vs. Economics: What are the differences?*

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- Motivation/purpose: social view vs. private view
- Unit of analysis: industry vs. firm
- Views of the decision maker: single decision making unit vs. collection of individuals
- View of the firm: free-standing entity vs. portfolio of businesses
- Perspective: static vs. dynamic
- Variables of consideration: limited vs. many
- Firm-industry relation: one-way vs. two-way



Fundamental questions in management – especially in strategy

- Why do firms differ?
- How do firms behave?
- What determines the scope of the firm?
- What determines the success and/or failure of firms?

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Frameworks of analysis:

- pre-1980s Economic variables and industry characteristics
- 1980s Porter framework (the Industry-based view)
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- 1990s The Resource-Based View (RBV)
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- 2000s The Institution-based view



The industrial organization (IO) economics

- In searching the explanations for above-average returns, the IO model argues that the firm's performance is primarily determined by a range of industry properties, e.g.
 - Economies of scale, barriers to market entry, diversification, product differentiation and the degree of concentration of firms in the industry



The profitability of industries varies greatly

Median return on equity (%), 1999-2002

Pharmaceuticals	26.8	Gas & Electric Utilities	10.5
Tobacco	22.0	Food and Drug Stores	10.3
Household & Personal Products	20.5	Motor Vehicles & Parts	9.8
Food Consumer Products	20.3	Home Equipment	9.5
Medical Products & Equipment	18.8	Railroads	9.0
Beverages	18.8	Hotels, Casinos, Resorts	8.0
Scientific & Photographic Eqipt.	16.5	Insurance: Life and Health	7.6
Commercial Banks	16.0	Building Materials, Glass	7.0
Publishing, Printing	14.3	Metals	6.0
Petroleum Refining	14.3	Semiconductors &	
Apparel	14.3	Electronic Components	5.8
Computer Software	13.5	Insurance: Property & Casualty	5.3
Electronics, Electrical Equipment	13.3	Food Production	5.3
Furniture	13.3	Telecommunications	3.5
Chemicals	12.8	Forest and Paper Products	3.5
Computers, Office Equipment	11.8	Communications Equipment	(4.0)
Health Care	11.5	Airlines	(34.8)

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The SCP model and the underlying assumption

- SCP model: Industry structure determine the behaviour or conduct of firms, whose joint conduct then determine the collective performance of the firms in the market place



- Underlying assumptions
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- The external environment impose pressures and constraints that determine the strategies that would result in above-average return
- Most firms within an industry or within a certain segment of the industry control similar resources and pursue similar strategies in view of those resources
- Resources are highly mobile across firms
- Organization decision makers are rational

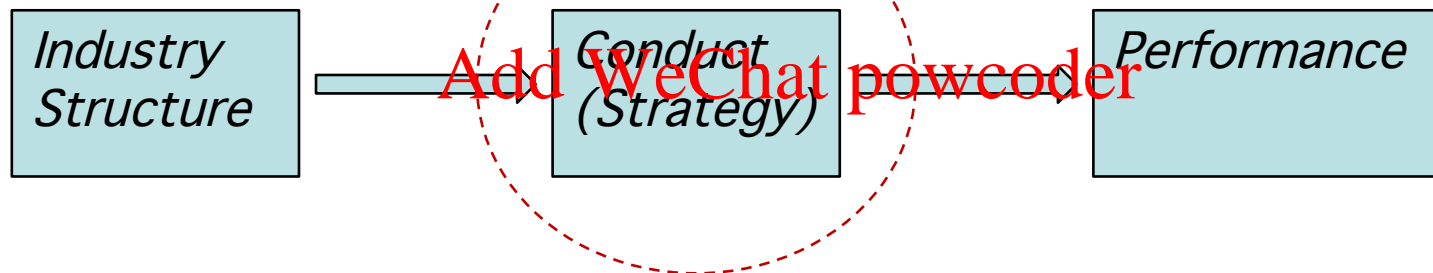


The industry-based view of strategy

- The Five Forces Framework: “Translated” and extended from the SCP model in 1980 by Porter.

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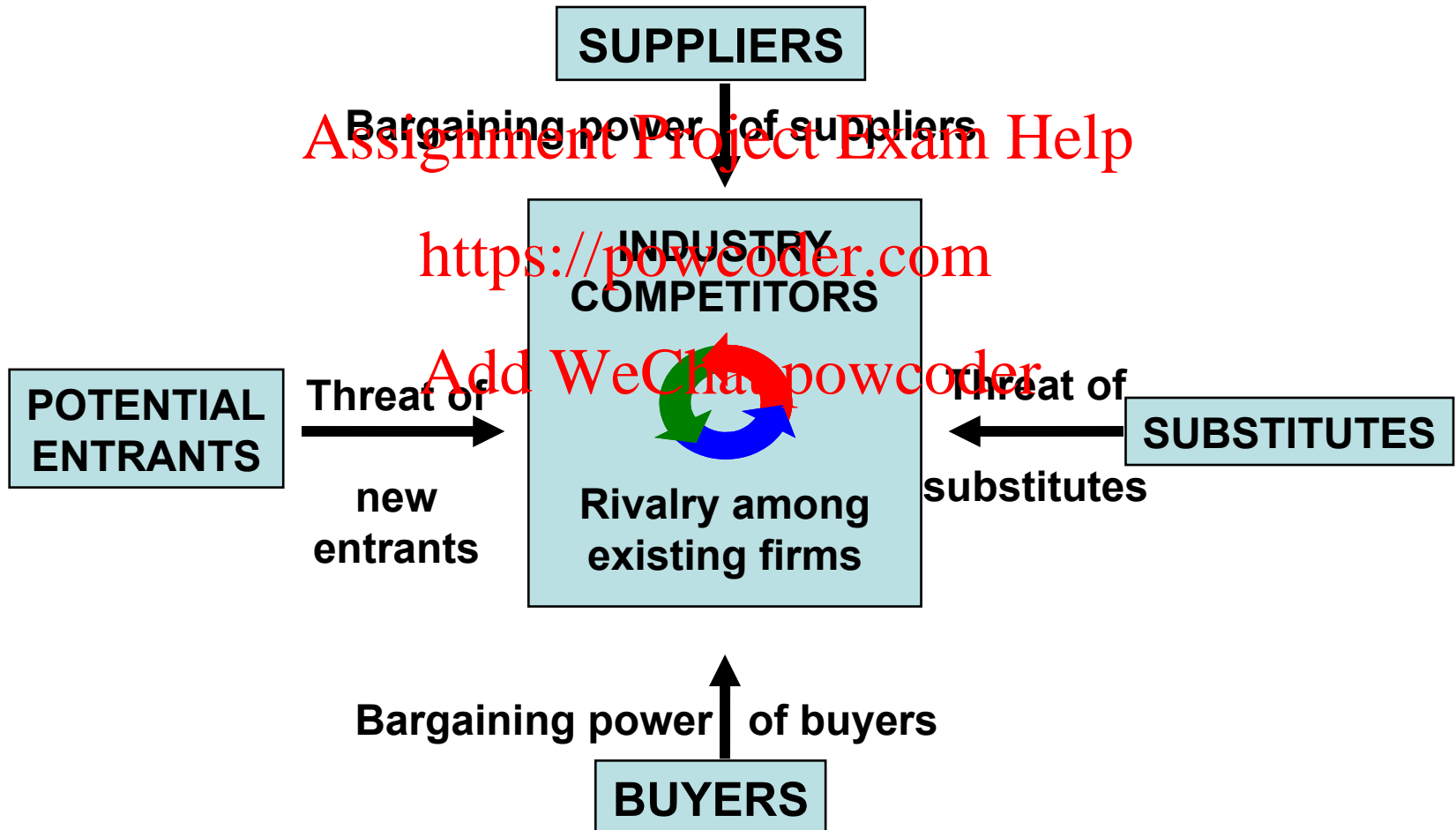
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Firms are not simply passive recipients of those competitive forces in their industry environment



Five Forces Framework





1. Rivalry among competitors

- Conditions that can *depress* industry profitability
 - A large number of competing firms (e.g. luxury vs mass market cars)
 - Rivals are similar in size, influence, and product offerings (e.g. airlines)
 - High-price, low-frequency purchases (e.g. “big tickets” vs “staple goods”)
 - Capacity is added in large increments (e.g. semiconductor)
 - Industry slow growth or decline
 - High exit costs (e.g. airlines)



2. Threat of potential entry

- Conditions that lift up entry barriers
 - Large scale-based advantages (economies of scale) (e.g. telecommunication)
 - large non-scale-based advantages (e.g. drug firms using patent)
 - Adequate product proliferation
 - Sufficient product differentiation
 - Fear of retaliation
 - Government policy banning or discouraging entry



3. Bargaining power of suppliers

Bargaining power - The ability to *raise* prices and/or *reduce* the quality of goods and services.

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- Conditions that **empower** suppliers
 - A small number of suppliers
 - Suppliers provide unique, differentiated products
 - Focal firm is not an important customer of suppliers
 - Suppliers are willing and able to vertically integrate forward

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4. Bargaining power of buyers

- Conditions that empower buyers
 - A small number of buyers
 - Products provide little cost savings or quality-of-life enhancement
 - Buyers purchase standard, undifferentiated products from focal firm
 - Buyers are willing and able to vertically integrate backward



5. Threat of substitutes

Substitute are products or services from *outside* a given industry that perform *similar* functions.

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- Conditions that **increase** the threat of substitutes

- Substitutes are superior to existing products in quality and function
- Switching costs to use substitutes are low

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The sixth competitive force?

- Porter later added the sixth competitive force in the framework
- Complementors – the related and supporting industries

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Additional resources for an industry analysis based on the five forces model

- Porter: The Five Competitive Forces That Shape Strategy, available through the UoN library [link](#) available in the course site
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 - In this 2008 article in the Harvard Business Review, Porter reaffirms, updates and extends the classic five competitive force framework he first introduced in 1979
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- The [website](#) that shows the five forces at work in selected U.S industries (
https://s3.amazonaws.com/he-assets-prod/interactives/074_link_between_econ_profit/Launch.html
)
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- This [website](#) that provides illustrations regarding the forces, their impacts on profitability and the root causes (
https://s3.amazonaws.com/he-assets-prod/interactives/057_porters_forces_framework/Launch.html



Additional resources for an industry analysis based on the five forces model

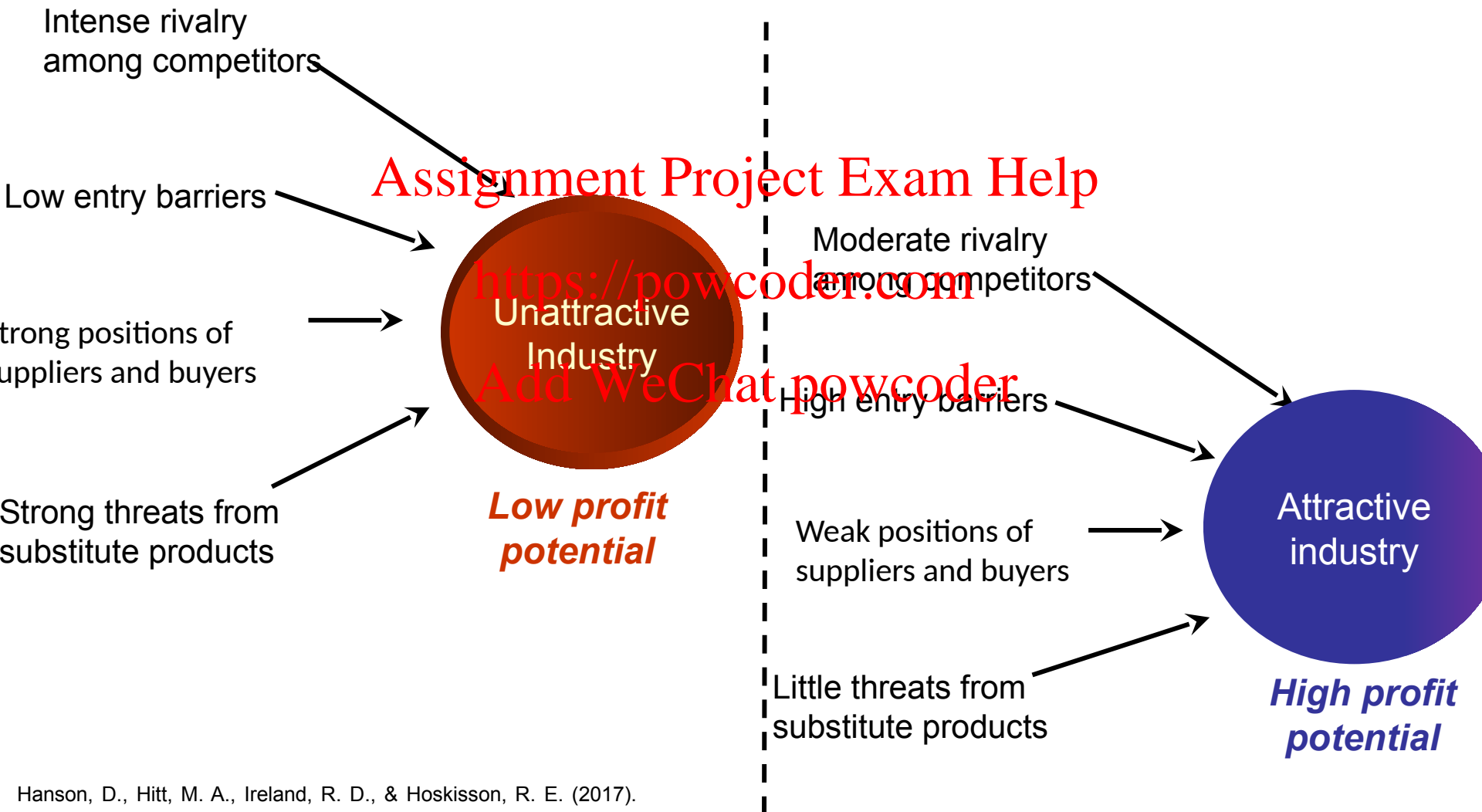
- The [website](https://libguides.bahson.edu/c.php?g=26453&p=161511) that provides a practical guide for Porter's Five Forces Research
<https://libguides.bahson.edu/c.php?g=26453&p=161511>

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- Some criteria or references you can use to define an industry: 1, official industry classification. E.g. [North American Industry Classification System](#); [Australian and New Zealand Standard Industrial Classification](#) which is provided by [Australian Bureau of Statistics](#)
- 2, Defined by industry itself, and reflected by the composition of industry association
- 3, by equity analysts according to companies publically listed in stock markets
- Industry reports/profiles available in database e.g. Marketline Advantage or IBISWorld, both available through UoN Library online



Five forces and attractiveness of an industry



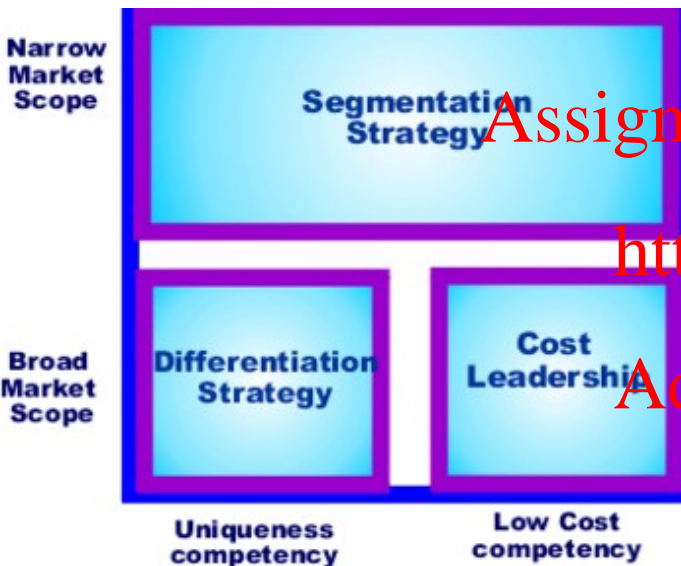
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The three generic strategies identified by Porter



- Cost leadership: centers on low costs and prices.
 - A high volume, low margin approach.
 - Key function areas: manufacturing, materials, logistics management
- Differentiation: Strategically focusing on how to deliver products that perceive to be valuable and different.
 - A low-volume, high-margin approach
 - Research/development and marketing/sales are important functional areas.
- Focus strategy: Serving the needs of a particular niche of an industry such as a geographical market, or product line.
 - Knowledge about a particular segment



Cost leadership Strategy

centers on low costs and prices.

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- A *high-volume, low margin* approach.

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- Key function areas: manufacturing, materials, logistics management

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How to achieve cost leadership?

- **The Sources of Cost Advantages**

- ?
- Input costs
- Economies of scale
- Learning
- Capacity utilization
- Production techniques
- Product design
- Managerial efficiency
- Institutional factors

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How to achieve cost leadership? The case of budget airlines (e.g. Jetstar, Scoot, Southwest Airlines, Ryanair, etc.)

- **The Sources of Cost Advantages**

- Input costs e.g. using secondary airports, no on-board “frills”, small seat size
- Economies of scale e.g. using one type of aircraft
- Learning e.g. using one type of aircraft
- Capacity utilization e.g. short turnarounds
- Production techniques e.g. point-to-point service, mostly short/medium haul flights
- Product design e.g. All baggage charged separately to fares
- Managerial efficiency
- Institutional factors e.g. low tax

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Example – Low Cost Competitive Strategy: Ryanair Europe's oldest Budget-Airline



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- June 2007 the International Air Transport Association ranked Ryanair World No 1 in carrying more International passengers than any other airline and one of the most profitable airlines in the world.
 - low-cost does not mean low –profit!
- New Ryanair aircraft have been delivered with non-reclining synthetic leather seats, no seat-back pockets, safety cards stuck on the back of the seats, and life jackets stowed overhead rather than under the seat. This allows the airline to save on aircraft costs and enables faster cleaning and safety checks during the short turnaround times.
- Other proposed measures to reduce frills further have included
 - eliminating two toilets to add six more seats,
 - redesigning the aircraft to allow standing passengers,
 - suggesting that passengers should pay to use the toilets,
 - charging extra for overweight passengers,
 - asking passengers to carry their checked-in luggage to the plane.



Differentiation strategy

Strategically focusing on how to deliver products that perceive to be valuable and different.

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- A low-volume, high-margin approach
- Research/development and marketing/sales are important functional areas.



How to achieve differentiation?

-- Providing something unique that is valuable to the buyer beyond simply offering a low price. (M. Porter)

THE KEY IS CREATING VALUE FOR THE CUSTOMER

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TANGIBLE DIFFERENTIATION

Observable product characteristics:

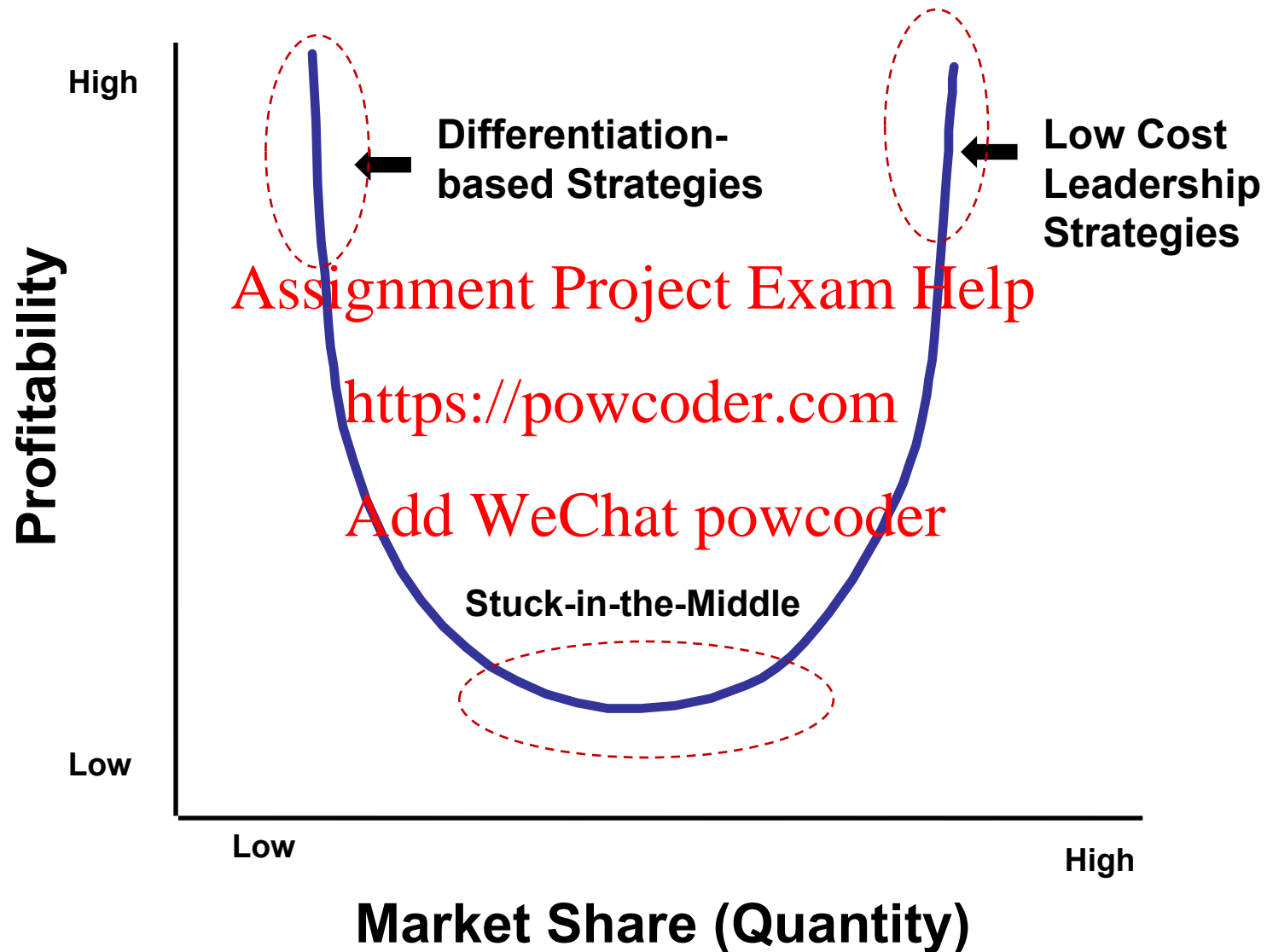
- size, color, materials, etc.
- performance
- packaging
- complementary services

INTANGIBLE DIFFERENTIATION

Unobservable and subjective characteristics relating to image, status, exclusivity, identity

TOTAL CUSTOMER RESPONSIVENESS

Differentiation not just about the *product*, it embraces the whole *relationship* between the supplier and the customer.



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Stuck-in-the-Middle

Market Share (Quantity)

“Porter’s Bucket”



Segmentation (Focus) strategy

Serving the needs of a particular niche of an industry such as a geographical market, or product line, not all the potential marketplace.

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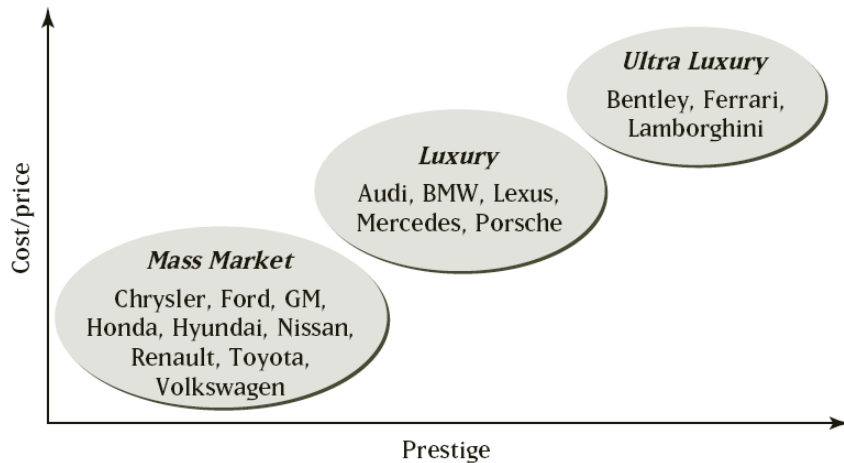
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- Superior Knowledge about a particular segment



Strategic Group

- A group of firms in an industry following the same or similar strategy
- Strategic groups often differ in their product or marketing approaches
- Mobility barriers: barriers to shifting strategic position from one strategic group to another
- Because firms within a group offer similar products to the same customers, the competitive rivalry among them can be intense (inter-strategic group competition)



Sources of competitive advantage

