

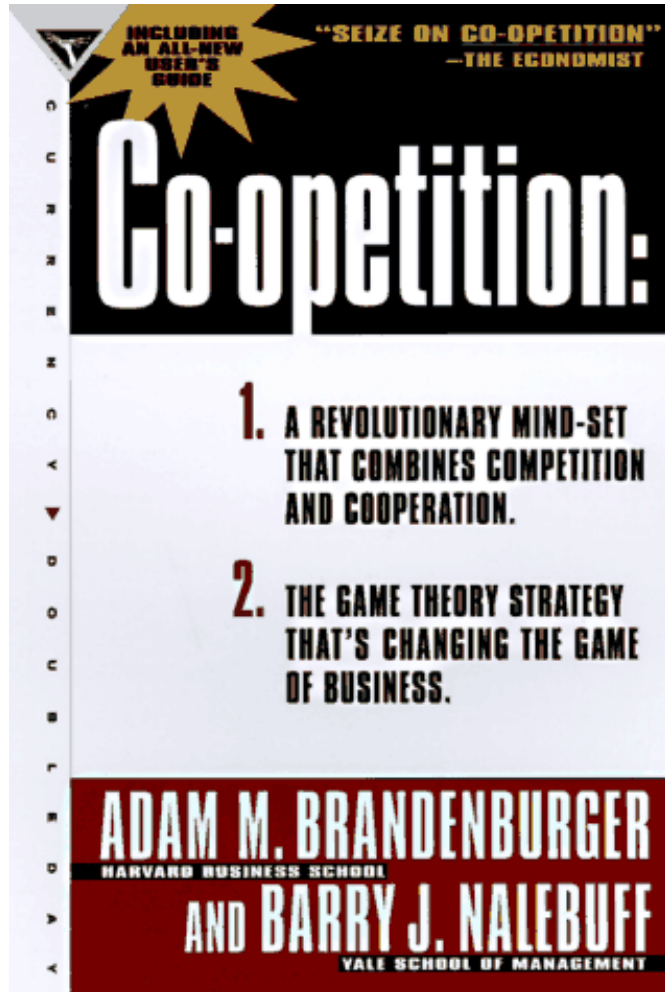


# Competitive strategies in commodity oligopolies

L 13: Coopetition

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# This lecture is about "Co-opetition"



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# The coopetition mindset

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## Thesis: Business as war

- *"Beating the competition – Fighting brands – Price war – Squeezing suppliers – Locking up customers – Making a killing"* (The everyday language of business)
- *"Winners in business play rough and don't apologize for it. [...] In this quicker, tougher world of business, playing hardball is not an option; it is a requirement for winning "* (G. Stalk, R. Lachenauer: The Hardball Manifesto)

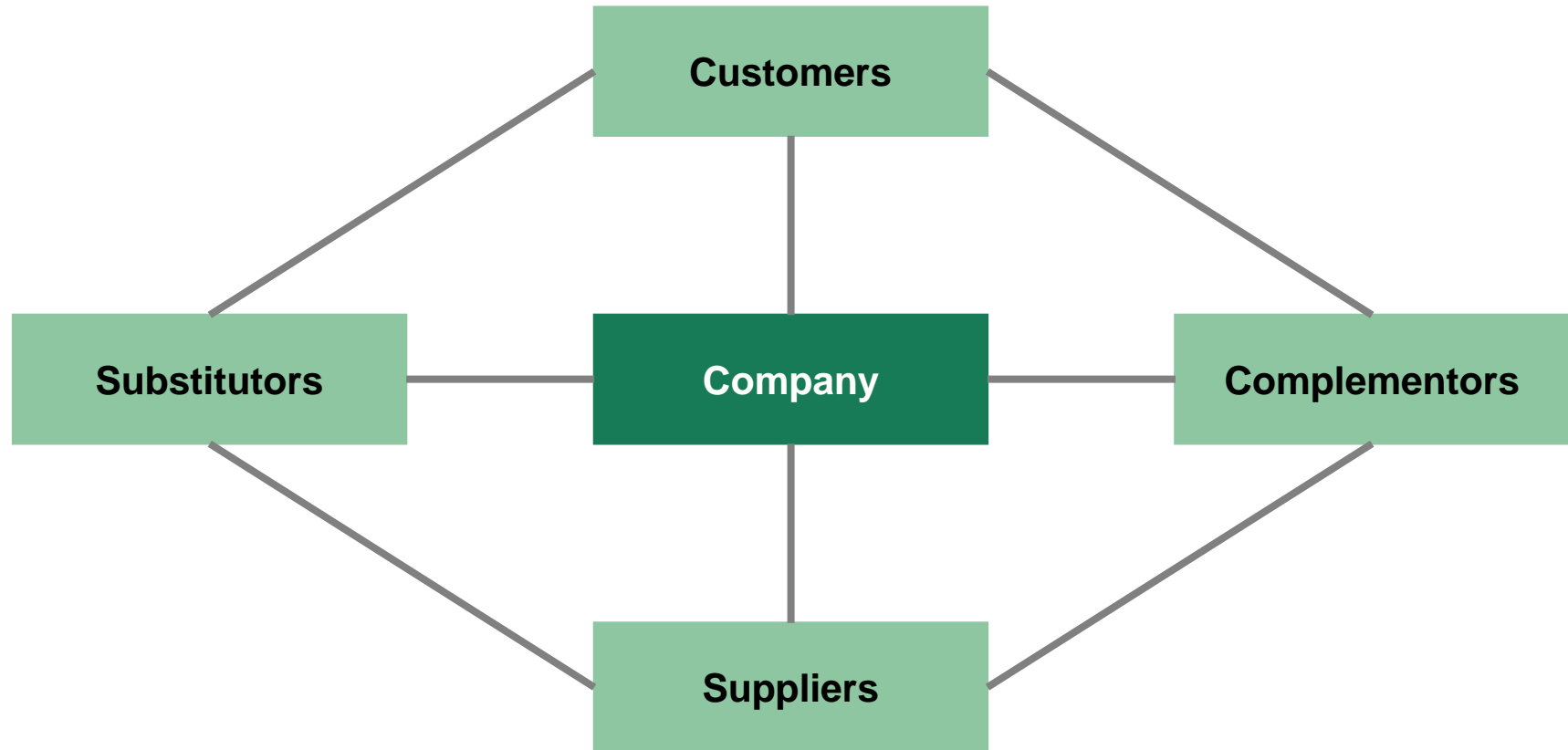
## Antithesis: Business as peace

- *"You don't have to blow out the other fellow's light to let your own shine"* (Bernard Baruch, leading banker and financier)

## Synthesis: Coopetition

- *"Co-opetition: You have to compete and cooperate at the same time"* (R. Noorda, founder of the software firm Novell)
- *"There is a duality in every relationship – the simultaneous elements of win-win and win-lose. Peace and war."* (A. Brandenburger, B. Nalebuff: Co-opetition)

# The Value Net



**Customers and suppliers play symmetric roles.  
Substitutors and complementors play mirror-image roles.**

# Definitions

## Customer perspective

### Substitutor

A player is your substitutor if customers value your product **less** when they have the other player's product than when they have your product alone

### Complementor

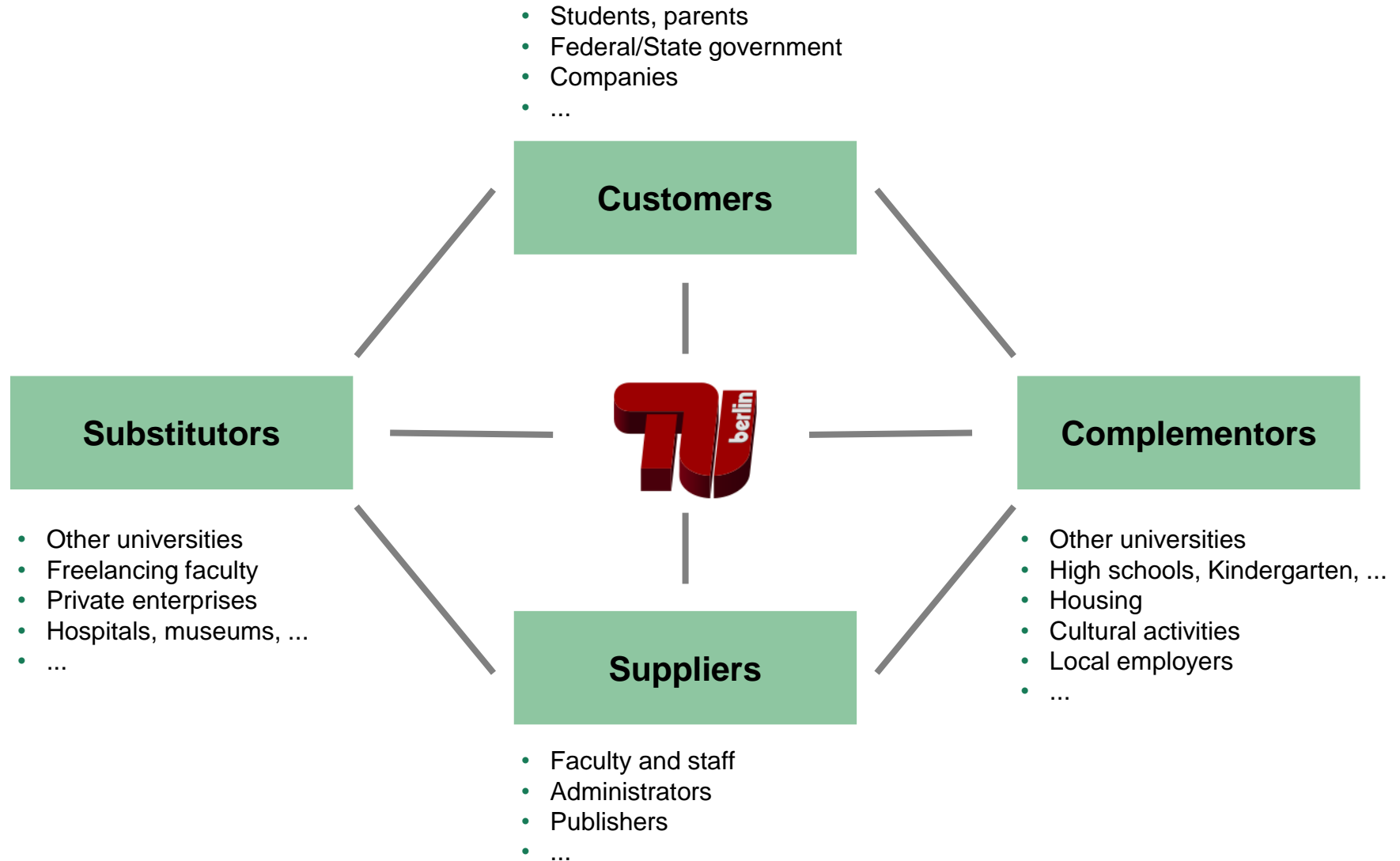
A player is your complementor if customers value your product **more** when they have the other player's product than when they have your product alone

## Supplier perspective

A player is your substitutor if it's **less** attractive for a supplier to provide resources to you when it's also supplying the other player than when it's supplying you alone

A player is your complementor if it's **more** attractive for a supplier to provide resources to you when it's also supplying the other player than when it's supplying you alone

# Example: The Value Net of TU Berlin



# Coopetition: Playing multiple roles

There are both win-win and win-lose elements in relationships with

- Customers
- Suppliers
- Substitutors
- Complementors

Companies are

- **Partners** in making markets
- **Rivals** in dividing up markets



# PARTS: The five elements of the game

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## Players

- The players are customers, suppliers, substitutors and complementors.
- Sometimes it may be smart to change who is playing the game. Including yourself.

## Added Values

- Added values are what each player brings to the game.
- Look for ways to raise your added value – or to lower the added values of other players.

## Rules

- Rules give structure to the game.
- In addition to using existing rules, players may be able to revise them or come up with new ones.

## Tactics (perceptions)

- Tactics are moves used to shape the way players perceive the game and hence how they play.
- Tactics may be designed to reduce misperceptions – or to create or maintain uncertainty.

## Scope

- Scope describes the boundaries of the game.
- Players can expand the scope by creating linkages to other games, or shrink the boundaries of a game



# The Card Game

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Each of you (20 students) will receive one red card.

I will keep 20 black cards.

The dean of the university offers € 100 for every pair of cards that is handed in.

Let's negotiate!



## Added value measures what each player brings to the game

Your added value

=

The size of the pie when you are in the game

*minus*

The size of the pie when you are out of the game

# Allocentrism (rather than egocentrism)

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## Added value

- Put yourself in the shoes of others to assess your added value

## Rules

- Put yourself in the shoes of others to anticipate reactions to your actions

## Tactics (perceptions)

- Put yourself in the shoes of others to see how they see the game

*When I am getting ready to reason with a man I spend one-third of my time thinking about myself and what I am going to say, and two-thirds thinking about him and what he is going to say.*

Abraham Lincoln

# A word on rationality

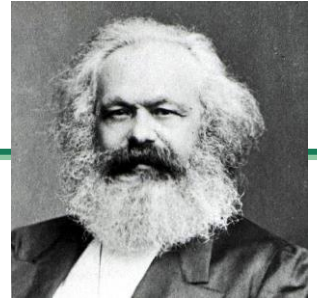
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We need a **broad definition of rationality**:

A person is rational if she does the best she can, given how she perceives the game (including her perceptions of perceptions) and how she evaluates the various possible outcomes of the game.

The fact that other people view the world differently doesn't make them irrational:

- Two people can both be rational and yet perceive the game quite differently (different assumptions, level of information)
- Profits are not the only objective: pride, fairness, jealousy, spite, vengefulness, altruism, charity can matter
- Even if you think others are misguided, don't impose your rationality on them



“Philosophers have only interpreted the world.  
The point, however, is to change it”

# Changing the game by adding players



## Starting situation

- Monsanto holds the monopoly for aspartame sweetener
- US patent expires in 1992
- Coke and Pepsi encourage HSC to build a generic aspartame plant

## Outcome

- Just prior to patent expiration, both Coke and Pepsi sign new long-term contracts with Monsanto
- Coke and Pepsi never wanted to switch suppliers, they just wanted a better price (which they got)

## Analysis

- What was the added value of HSC after entering the game?
- What was the added value of HSC before entering the game?

**Competition is valuable. Don't give it away. Get paid to play.**

## Seven ways to get paid to play

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- 1) Ask for contributions toward bidding expenses / other costs of entering the game
- 2) Ask for a guaranteed sales contract
- 3) Ask for last-look provision
- 4) Ask the customer to quote a price at which she would give you the business
- 5) Ask for better access to information
- 6) Ask to deal with someone who will appreciate what you will bring to the table
- 7) Ask to bid on other pieces of business, in addition to the current contract

# Getting paid to play: The BellSouth Case



## Starting situation in 1989

- Seeing strong synergies, McCaw bids \$120/share for Lin Broadcasting
- Lin's shares jump from \$103.50 to \$129.50
- Lin considers the bid hostile and McCaw lowers its bid to \$110/share
- Lin turns to BellSouth as an alternative acquiror

## Outcome

- As a condition for making a bid, BellSouth gets Lin's promise of \$54m + \$15m for expenses in the event that it is outbid
- BellSouth offers \$112, McCaw responds with \$118
- BellSouth raises to \$120 (in return, Lin raises the expense cap to \$25m)
- McCaw raises its bid to \$130
- In addition, McCaw pays BellSouth \$22.5m to exit the game

## Analysis

- Lin got an extra billion by paying \$79m to BellSouth
- McCaw got Lin and later sold the combined company at a very favorable price to AT&T
- BellSouth turned a weak hand into >\$100m by getting first paid to play and then paid to exit



# Bringing in other players

## Customers

Educate the market  
Pay customers to play  
Subsidize some customers, and other full-paying customers will follow  
Become your own customer to develop the market and achieve scale

## Suppliers

Pay suppliers to play  
Form a buying coalition to become a larger buyer  
Become your own supplier to assure supply and create competition

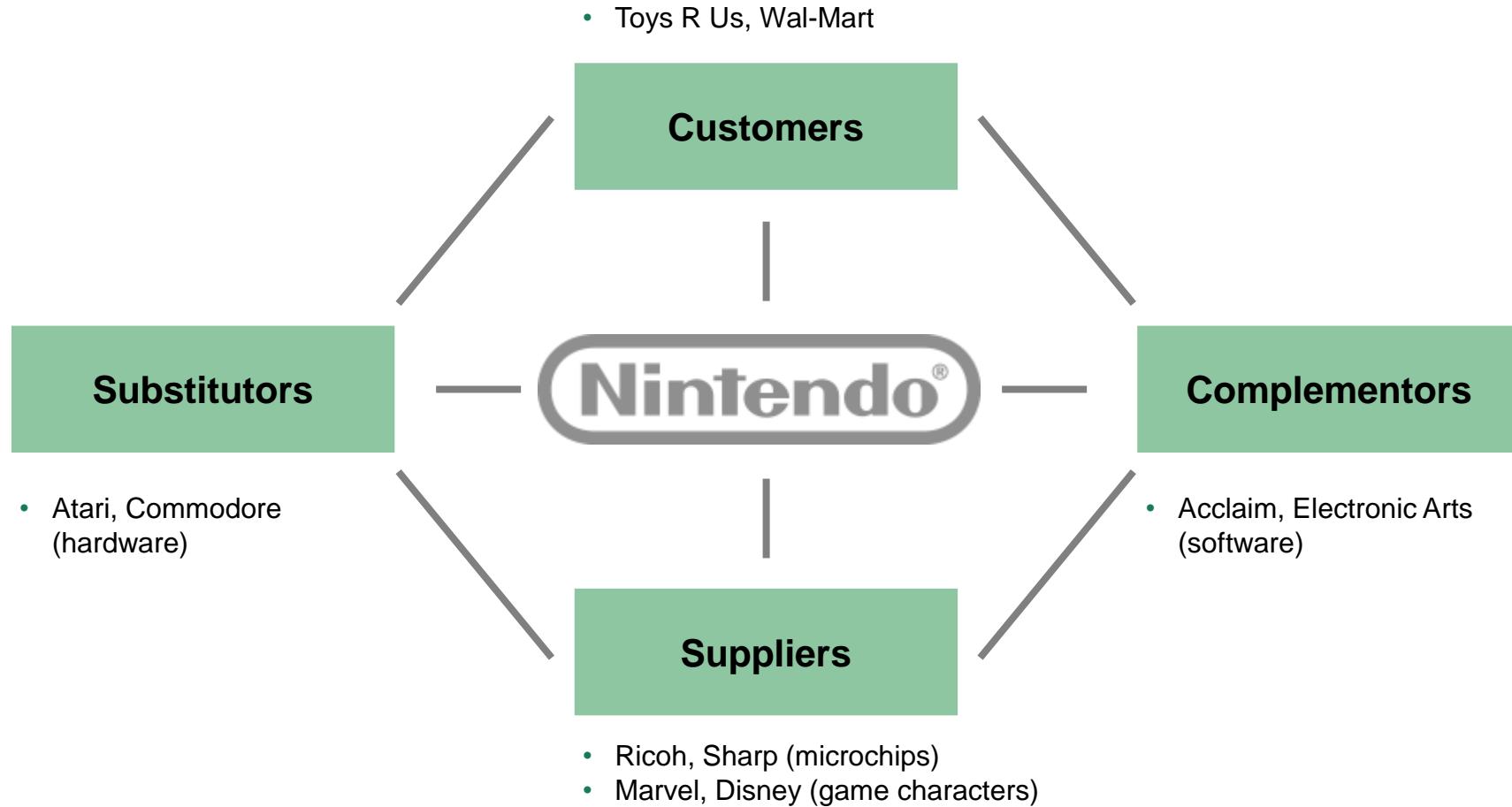
## Complementors

Form a buying coalition on behalf of your customers  
Pay complementors to play  
Become your own complementor

## Competitors

License your technology both to make money and to avoid complacency  
Create second sources to encourage buyers to adopt your technology  
Promote internal competition across teams

# Nintendo trumped every player in its value net



# Pros and cons of limiting supply

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## Pros

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Gets you a bigger slice of the pie

May give you cachet

May provide free publicity

May lead customers to buy your slower moving products while waiting for the shortage to end

## Cons

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Shrinks the pie – costs you sales today

May cost you a relationship and thereby future sales

Creates ill will

Leaves a hole in the market inviting entry

# Contracts with customers

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## Most-favored-customer clause

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Contractual agreement between company and customer that guarantees the customer the best price the company gives to anyone

Pro:

- + Makes you a tougher negotiator
- + Reduces your customers' incentive to bargain

Con:

- Makes it easier for a rival to target one of your customers
- Makes it harder for you to target one of your rival's customers

## Meet-the-competition clause

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Contractual agreement between company and customer that gives the company an option to retain the customer's business by meeting any rival bids

Pro:

- + Reduces the incentive for competitors to bid
- + Takes the guesswork out of bidding – you know what bid you have to beat
- + Lets you decide whether to keep the customer

Con:

- Allows competitors to bid without having to deliver

# Contracts with suppliers and mass-market contracts

## Take-or-pay contract

Contractual agreement between company and supplier that specifies a price for which the company buys a certain volume of the product, and a penalty the company has to pay if it takes less than the pre-defined volume

Pro:

- + Reduces risk to your supplier, in return for which you can ask to pay less
- + Reduces a rival's incentive to come after your customers by making retaliation a near certainty

Con:

- Transforms variable cost into fixed cost
- Increases severity of price war if deterrence fails

## Targeted rebate program

Example GM Card (under MasterCard umbrella): Cardholders would earn credit equal to 5 percent of their charge volume, which could be applied to the purchase or lease of any new GM car or truck

Pro:

- + Allows you to charge your own customers low prices without threatening your rival's customer base
- + Encourages customers – even price shoppers – to become loyal

Con:

- In rewarding loyalty in cash rather than kind, doesn't raise your added value
- Is ineffective on small-ticket items

# Changing perceptions (I): Lifting the fog

## The credibility test

- 1) If you have the goods, put your money where your mouth is
  - Accept a pay-for-performance contract
  - Offer a guarantee
  - Give free trials
  - Advertise
- 2) What you don't do sends a signal, too
- 3) Ask other people to demonstrate their credibility to you
  - Propose a pay-for-performance contract
  - Ask for a guarantee
  - Request a free trial



# Changing perceptions (II): Preserving the fog

## Negotiating in a fog

### Mistakes

- 1) Revealing the minimum you need. You risk getting exactly that, and no more.
- 2) Making threats explicit. Even if a threat is already implicit, making it explicit changes perceptions. There's no going back.
- 3) Trying to resolve differences of opinion between you and the other party. This is hard to do, and possibly counterproductive.

### Solutions

- 1) Establish a settlement escrow to promote good-faith negotiating by both parties.
- 2) Bring in a mediator to help the other party understand the consequences of non-agreement.
- 3) Recognize what you and the other party do – and don't – have to agree on. Use differences of opinion to structure win-win deals.

# Changing perceptions (III): Stirring up the fog

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## Complex pricing schemes

- 1) Hide high prices
- 2) Disguise opportunistic pricing
- 3) Hide low prices, too, preserving an image of quality
- 4) Hamper comparison shopping

## ... but also

- 1) Increase administrative costs
- 2) Confuse and frustrate customers
- 3) Encourage furtive price cutting by competitors



# There is always a larger game

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## Added values can link games

- Judo strategy 1: A challenger prices a superior product sufficiently high to avoid eating into sale of the incumbent's existing product
- Judo strategy 2: A challenger bets on an unproven product – one with some chance of failing

## Rules can link games

- Long-term contracts
- Package discounts

## Perceptions can link games

- Trade negotiations
- NutraSweet in Europe

# Summary: A checklist for changing the game

## Players

What is your Value Net?  
What are the opportunities for cooperation and competition?  
Would you like to change the cast? What new players would you like to bring into the game?  
Who stands to gain if you enter? Who stands to lose?

## Added Value

What is your added value? How can you increase your added value?  
Can you create loyal customers and suppliers?  
What are the added values of the other players?  
Is it in your interest to limit their added values?

## Rules

Which rules are helping you and which are hurting you?  
What rules would you like to have in contracts with your customers and suppliers?  
Do you have power to make rules?  
Does someone have the power to overturn them?

## Tactics

How do other players perceive the game?  
How do these perceptions affect the play?  
Which perceptions would you like to preserve? Which ones would you like to change?  
Do you want the game to be transparent or opaque?

## Scope

What is the current scope of the game?  
Do you want to change it?  
Do you want to link the current game to others?  
Do you want to delink the current game from other games?

## Mental traps to avoid

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Seeing only part of the game

Being egocentric, rather than allocentric

Failing to think methodically about changing the game

Believing that success must come at others' expense

Accepting the game as it is