

Strategy

MIT

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OUTLINE

Approximate timeline

- 10.00 Intro – Setting
- 10.05 – Lectures, exercise, break (85 minutes)
- 11.30 – Lunch (45 min.)
- 12.15 Lectures (45 min.)
- 13.30 – Exercise
- 14.00 – Presentations

My ambition

- Open climate
- Discussions, rather than endless lectures
- Experiential learning through short exercises
- Curiosity, rather than fault-finding

Key outcome: your learning!



Baseline

- customers enjoy music through CDs, i.e. pay for the artefact

- Tying relations to record companies

- iPhone launch June 2007

2006

- Foundation by Daniel Ek and Martin Lorentzon
- Idea: to make customers pay for content
- Experimentation phase

2008

- Launch with streamed access to recorded music via internet-enabled devices
- Subscription-based service
- Available only via invitation

2008

- Open access (but still subscription)
- Downloads possible

2009

- Free access to listen (but not download)
- Advertising
- Albums not played in full
- Forced shuffling

- Apple customers can buy and download music
- Spotify develops an app linked to Apple Store, but Apple and Spotify are still rivals

- Alliance with Facebook

2011

- Raised money to launch in the US

- The worlds leading record companies providing 90% of Spotify's 30 million songs

2017

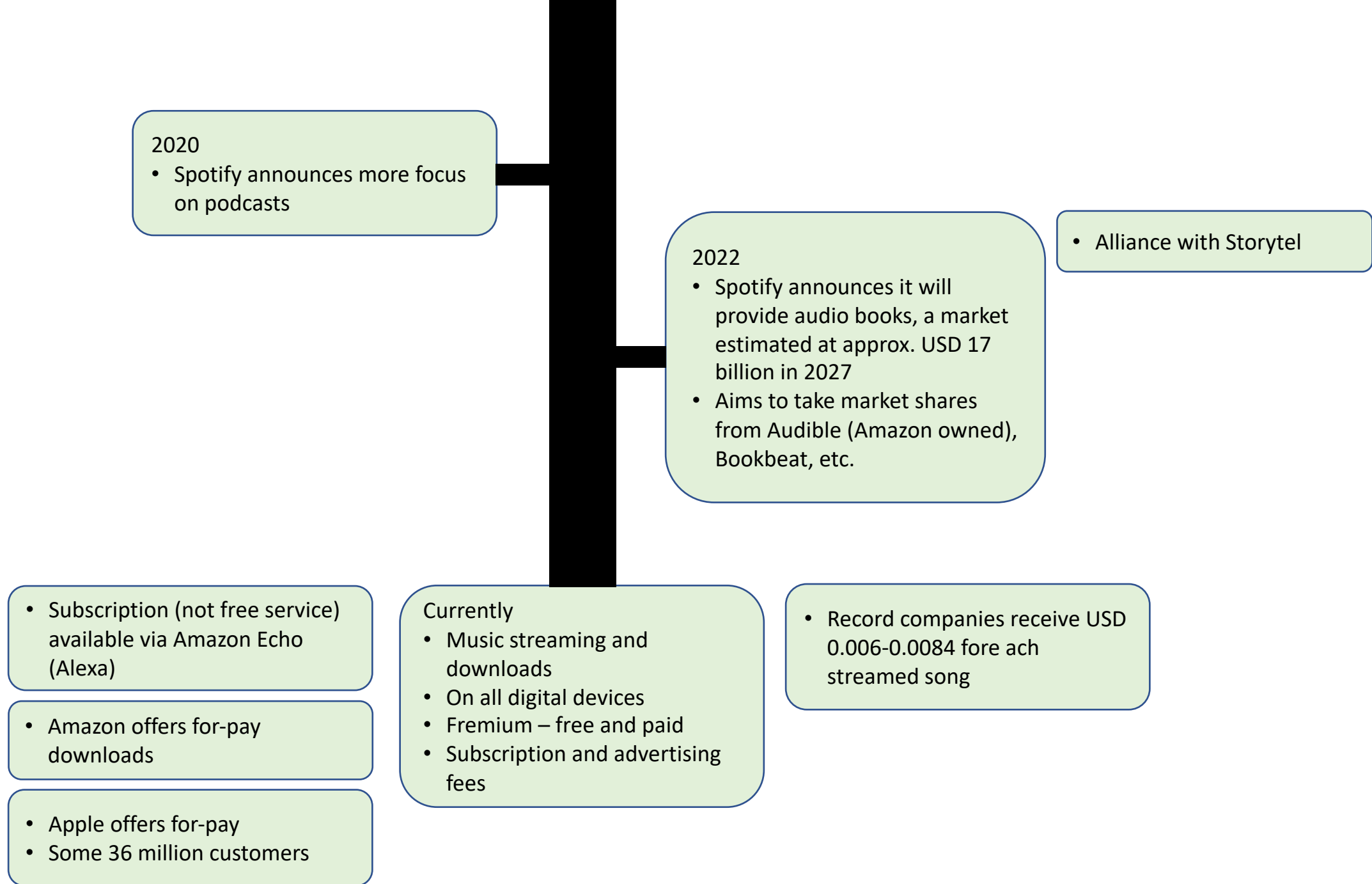
- USD 5 billion in revenues
- But USD 1,5 billion loss
- Valued at USD 25 billion
- 170 million active users of which 70 million paid subscribers (the rest listening with ads)

2015

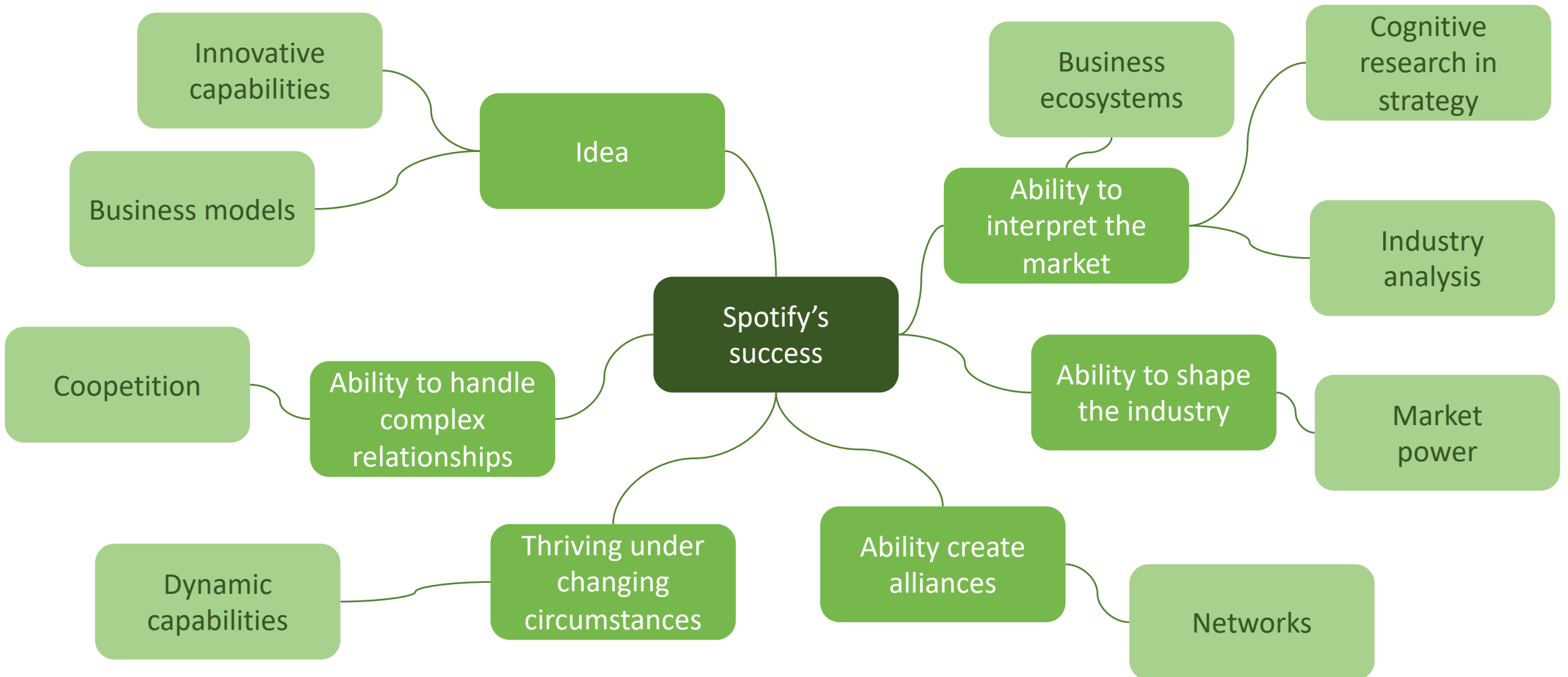
- Music videos added

2018

- Flotation on the NYSE



Strategic takeaways from Spotify – and strategy theories



A strategy is the **overarching idea** of how an **organisation** manages its **resources** to meet the **demands** of a **dynamic** and **competitive environment**

- **Overarching:** the perspective of the entire organisation
- **Idea:** a de facto strategy may be unconscious, but a deliberate strategy can be written down, or only agreed upon
- **Organisation:** firms, large or small, NGOs, government, student groups, etc.
- **Manage:** prioritizing in incommensurable choices, investing, divesting, integrating, initiating, etc., made by people subject to bounded rationality, interests, etc.

- **Resources:** HR, fixed and financial assets, market positions, customer relations, capabilities, etc.
- **Demands:** for products, profits, for employment, for products, legal obligations, etc.
- **Dynamic:** things change and are not fully predictable
- **Competitive Environment:** at least not fully benevolent natural endowments, industry rivalry, demand, legal situation, institutions, environmental requirements, etc.

Levels of strategy

1

Corporate
strategy

What industries should we be in?
What is the boundary of the firm?

2

Competitive
strategy

How can beat our competitors in each industry?
What are the crucial variables to compete on?

1 Corporate strategy

In which industries should the firm compete?

Core questions in corporate strategy

- Product scope - How wide a range of products does the firm supply?
- Vertical scope - What range of vertically linked activities does the firm encompass?
- Geographical scope - What is the geographical spread of the firm's activities? Does it compete locally or globally?

Answers depend e.g. on

- Behavioural abilities – strategic management ability to interpret facts and control the organisation
- Parenting advantage – what units benefit from belonging to the corporation?
- Economics of scope – are the cost economies that arise from increasing the output of multiple products?
- Transaction costs – are the costs of market transactions. When the costs of administering transactions within the firm are lower than the costs of market transactions, the firm grows in size and scope.
- The costs of corporate complexity – impose limits to the firm's growth in size and scope

Motives for diversification

- **Growth** – A powerful motive for managers—but growth without profitability does not create value for shareholders.
- **Risk spreading** – Diversification tends to reduce fluctuations in profits; but this does not necessarily create value for shareholders.
- **Value creation** – For diversification to create shareholder value it must exploit some linkage (“create synergy”) between the different businesses

Porter's three tests for diversification

- **The attractiveness test**

- the industries chosen for diversification must be structurally attractive or capable of being made attractive

- **The cost-of-entry test**

- the cost of entry must not capitalise all the future profits.

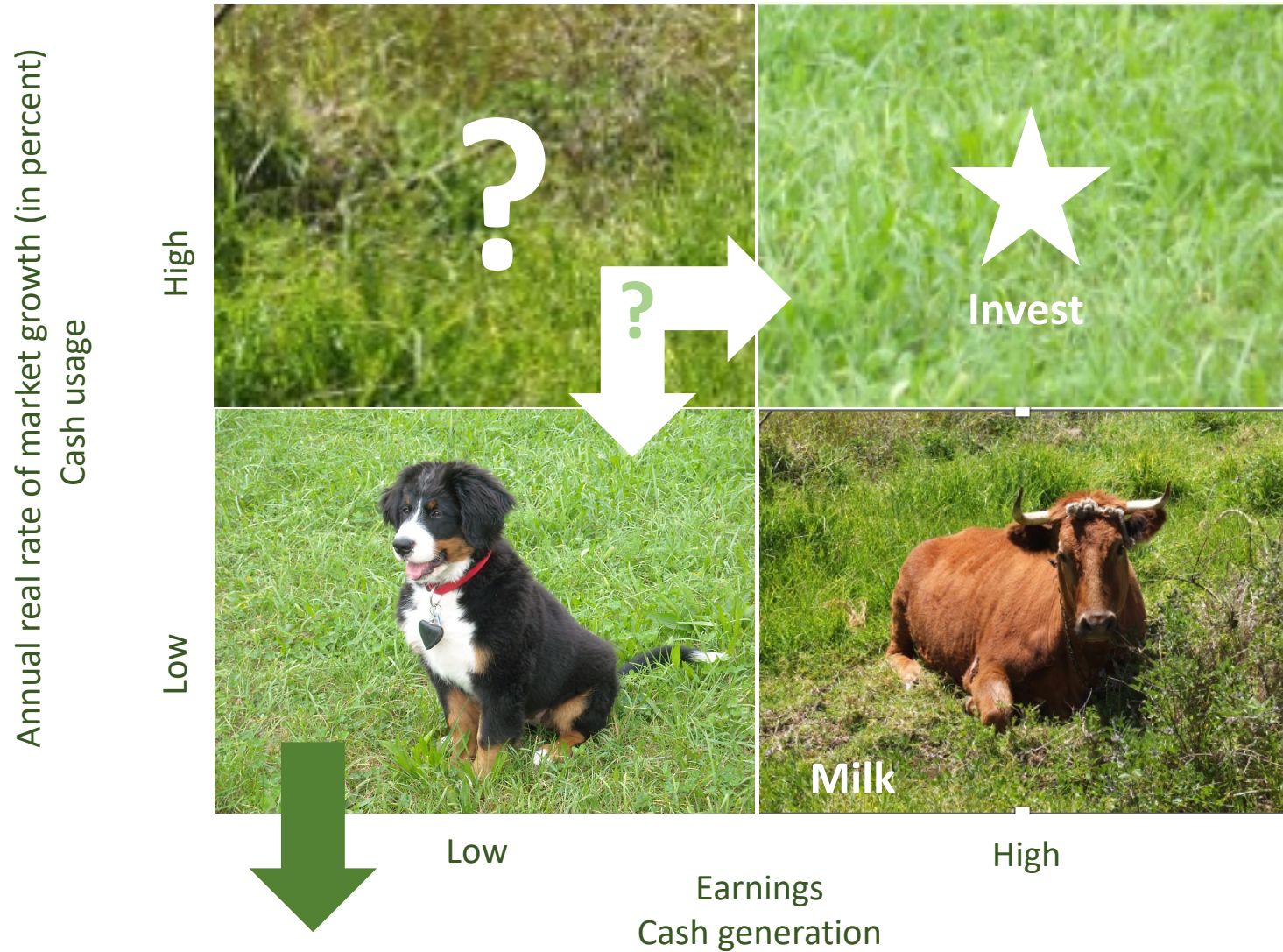
- **The better-off test**

- either the new unit must gain competitive advantage from its link with the corporation, or vice versa.

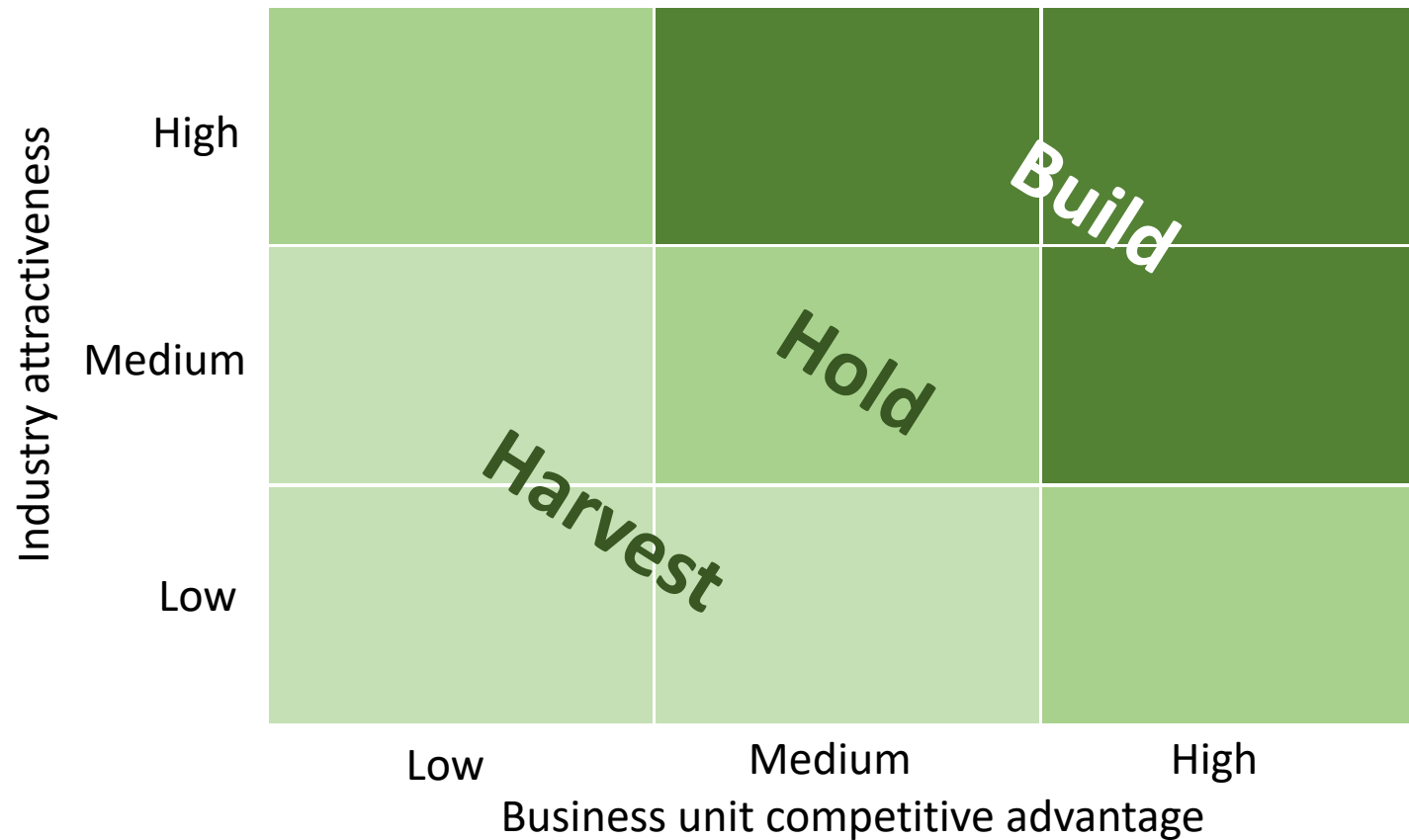
Market entry strategies



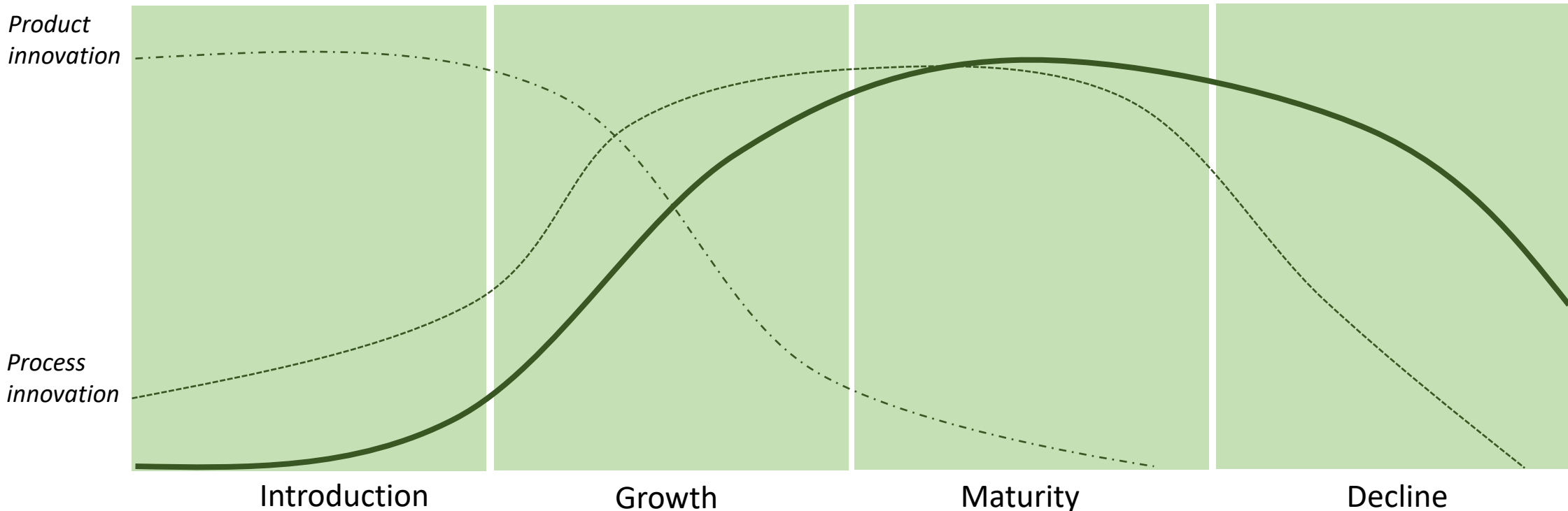
The BCG matrix



The McKinsey/GE portfolio planning matrix



The industry life cycle



- Early adopters
- Few companies
- Variety of designs

- Increasing market penetration
- Market entries
- Design for manufacture

- Replacement buying, commodity and price sensitivity
- Shakeout and consolidation
- Cost efficiency

- Obsolescence
- Price wars and exit
- Rationalisation

2 Competitive strategy

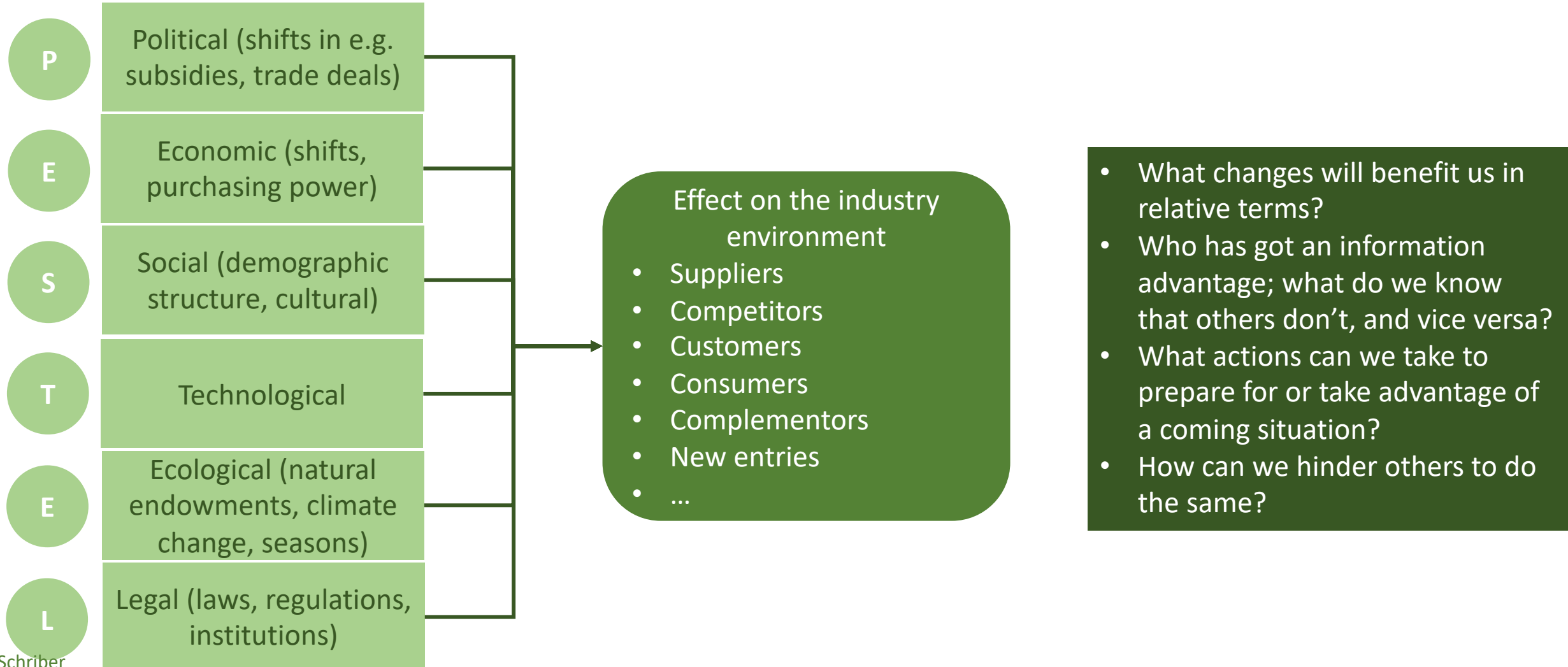
Understanding the strategic context: Industry analysis

PESTEL for analysing contexts

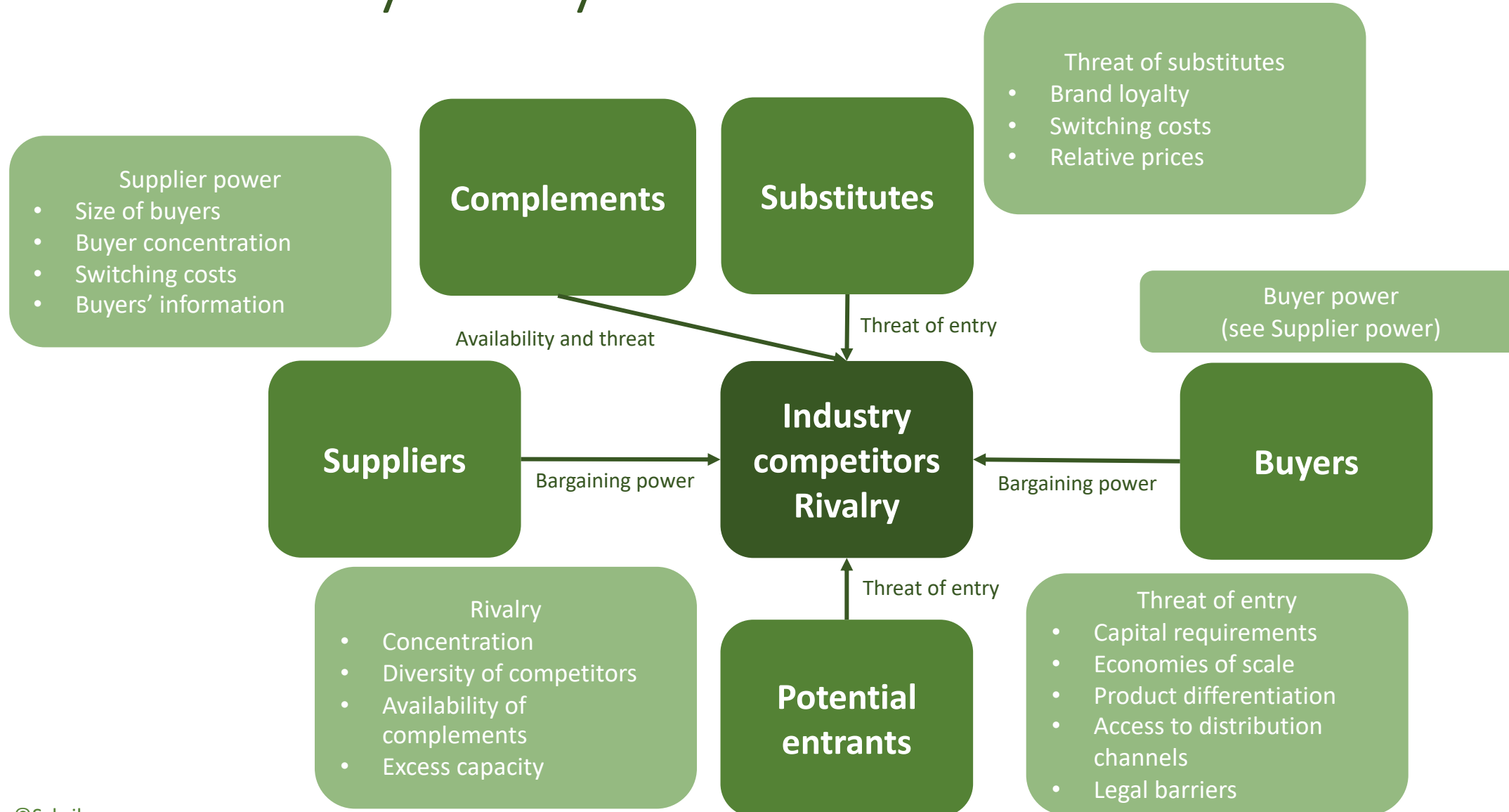
Description

Analysis

Conclusion



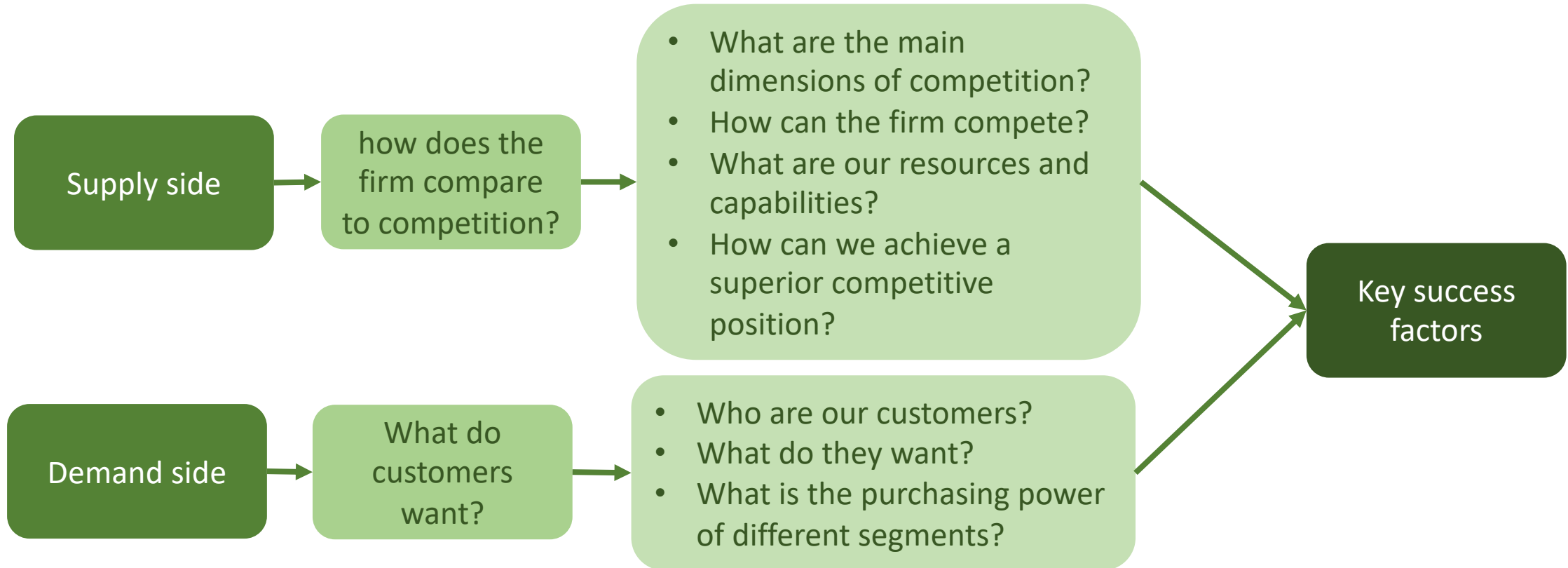
Industry analysis – Porters 5 Forces



Porter's generic strategies



Identifying industry key success factors



In your teams...

- Sketch an analysis of the European airline industry for personal transport (Air Frances, British Airways, and Eurowings etc.)
- Be back in 15 minutes ready to present your analysis including one conclusion (3-4 minutes)
- Use Porters 5 Forces and identify Key Success Factors

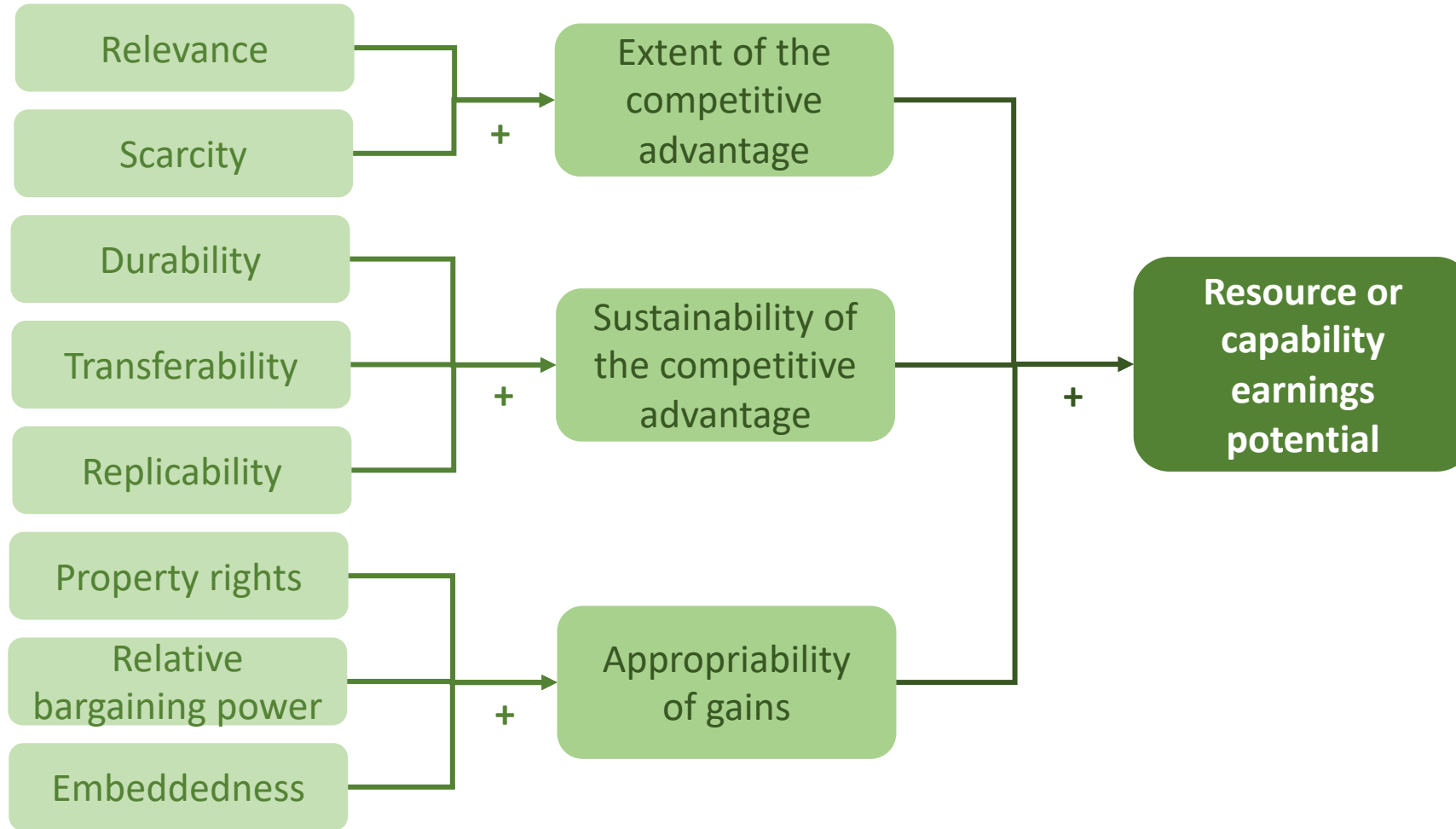
Understanding the impact of firm resources

But why do firms perform differently?

- During the 90s, scholars questioned why firms with similar generic strategies performed differently
- Additionally, assuming only the market defines performance seems simplistic
- Attention therefore was geared towards resources
- In reality, resources are everything the firm needs to function
- However, research has focused on resources explaining performance differences, or competitive advantage

- Valuable, rare, inimitable and non-substitutable resources (typically knowledge and organisational skills) allow firms to extract higher profit margins than competitors
- Core capabilities are the most important capabilities of a firm, that explain what to nurture, and how to expand
- Interest in capabilities in innovation, acquisition target selection, product development, alliance building etc. has grown dramatically

How valuable is your resource?



RESOURCE		CHARACTERISTICS	INDICATORS
Tangible Resources	Financial	Borrowing capacity Internal funds generation	Debt/Equity ratio Credit rating Net cash flow
	Physical	Plant and equipment: Size, location, technology flexibility. Land and buildings Raw materials	Market value of fixed assets. Scale of plants Alternative uses for fixed assets
Intangible Resources	Technology	Patent, copyrights, know-how, R&D facilities Technical and scientific employees	Number of patents owned Royalty income R&D expenditure R&D staff
	Reputation	Brands, customer loyalty, company reputation (with suppliers, customers, government)	Brand equity Customer retention Supplier loyalty
Human Resources		Training, experience, adaptability, commitment and loyalty of employees	Employee qualifications, Pay rates, turnover

The connection between routines and capabilities

Description

Capabilities are socially and technically embedded, complex, collective skills

Routines provide automatized responses to situations, and consist of ostensive (structure) and performative (action) aspects

Organisational function

Combine various resources (and capabilities) to transform input to output

Increase predictability, improvement, and allows economizing with limited cognitive resources

Useful concept in research because

Allow capturing and highlight explanations for performance differences

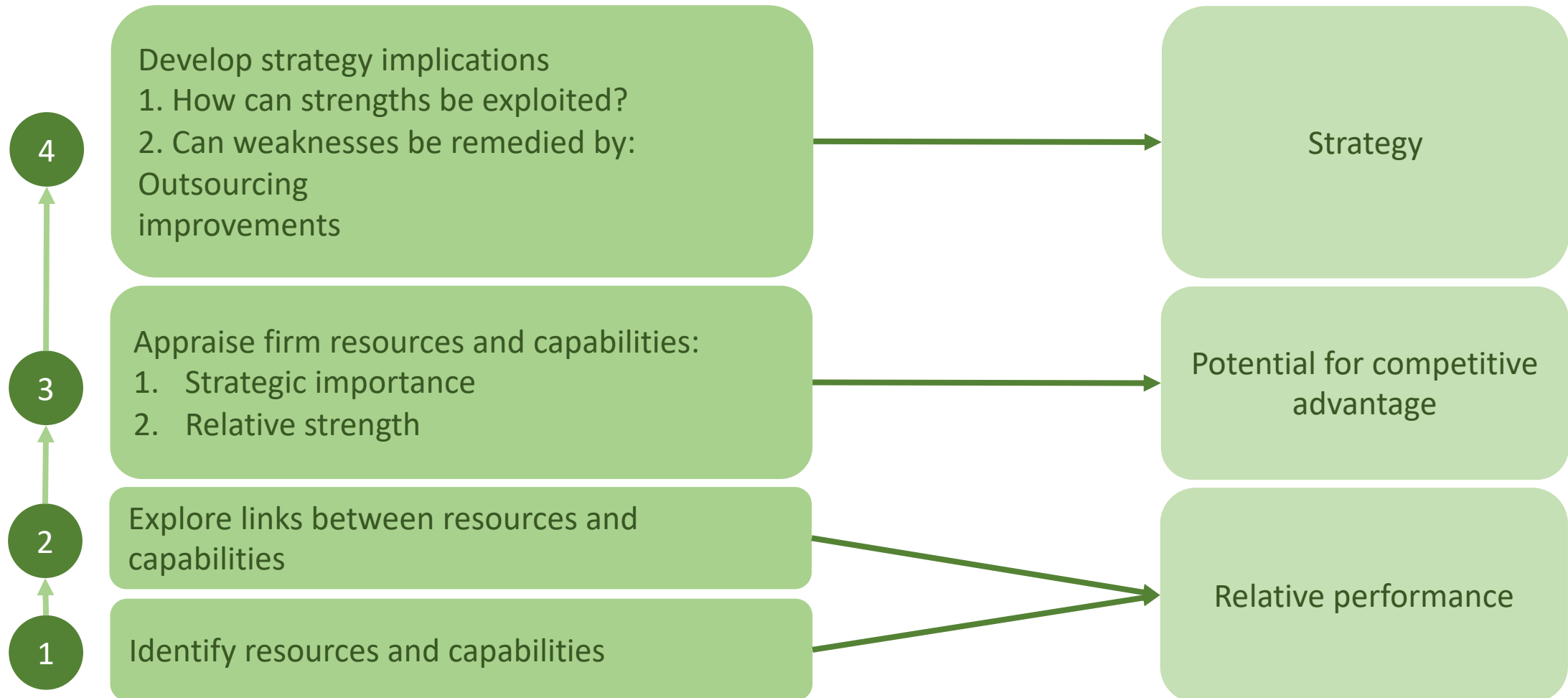
Highlight patterned behaviour as they are stable and evolve over time mainly when 'slipping' or 'mutating', and are separable from luck, chance or haphazard behaviour

FUNCTION	CAPABILITY	EXEMPLARS
CORPORATE FUNCTIONS	Financial control Management development Strategic innovation Multidivisional coordination Acquisition management International management	ExxonMobil, PepsiCo General Electric, Shell Google, Haier Unilever, Shell Cisco Systems, Luxottica Shell, Banco Santander
MANAGEMENT INFORMATION	Comprehensive, integrated MIS network linked to managerial decision making	Wal-Mart, Capital One, Dell
R&D	Research Innovative new product development Fast-cycle new product development	IBM, Merck 3M, Apple Canon, Inditex (Zara)
OPERATIONS	Efficiency in volume manufacturing Continuous improvements in operations Flexibility and speed of response	Briggs & Stratton, YKK Toyota, Harley-Davidson Four Season Hotels
PRODUCT DESIGN	Design capability	Nokia, Apple
MARKETING	Brand management Building reputation for quality Responsiveness to market trends	Procter & Gamble, Altria Johnson & Johnson MTV, L' Oreal
SALES AND DISTRIBUTION	Effective sales promotion and execution Efficiency and speed of order processing Speed of distribution Customer service	PepsiCo, Pfizer L. L. Bean, Dell Amazon.com Singapore Airlines, Caterpillar

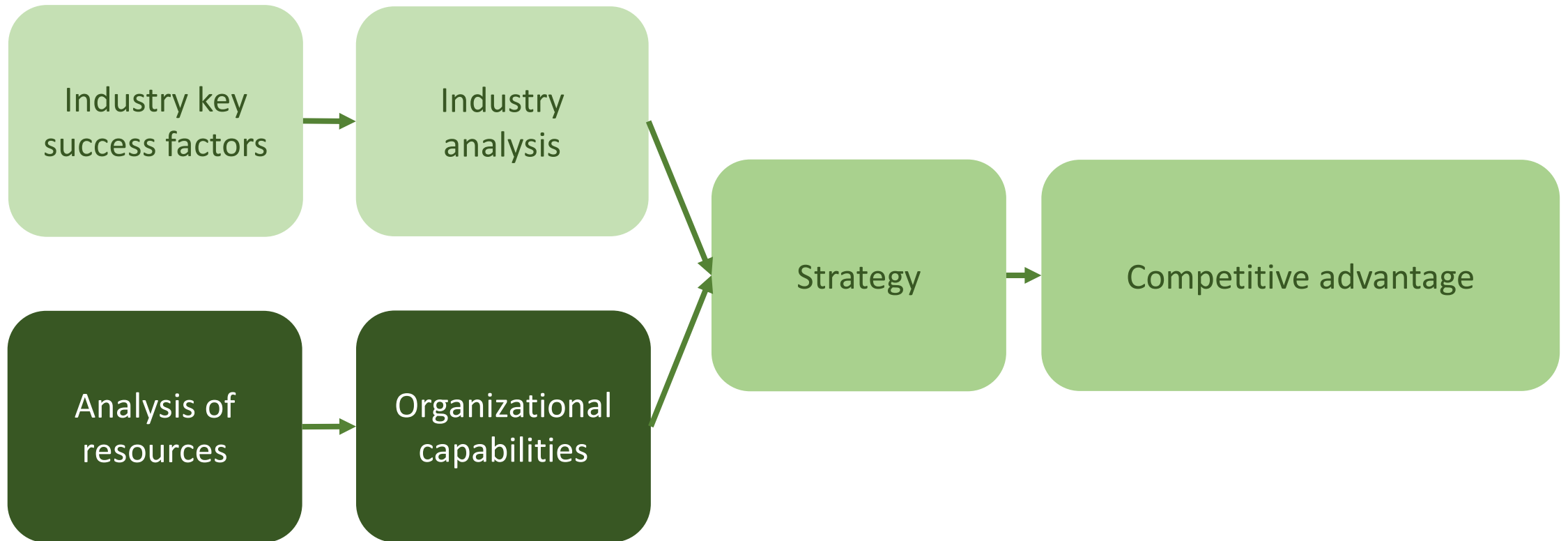
Hierarchy of capabilities

<i>Routine/capability</i>	<i>Organisational effect</i>	<i>Competitive implication</i>
Second level, or dynamic capabilities change lower-order capabilities	Allows adjusting to change	Surviving or thriving in dynamic environments
First level capabilities Improving operating car production	Allows improving existing organisation	Outpace competition
Operating, or zero-level capabilities e.g. producing cars	Allows sufficient change to make a living in the industry	Keep up with competition

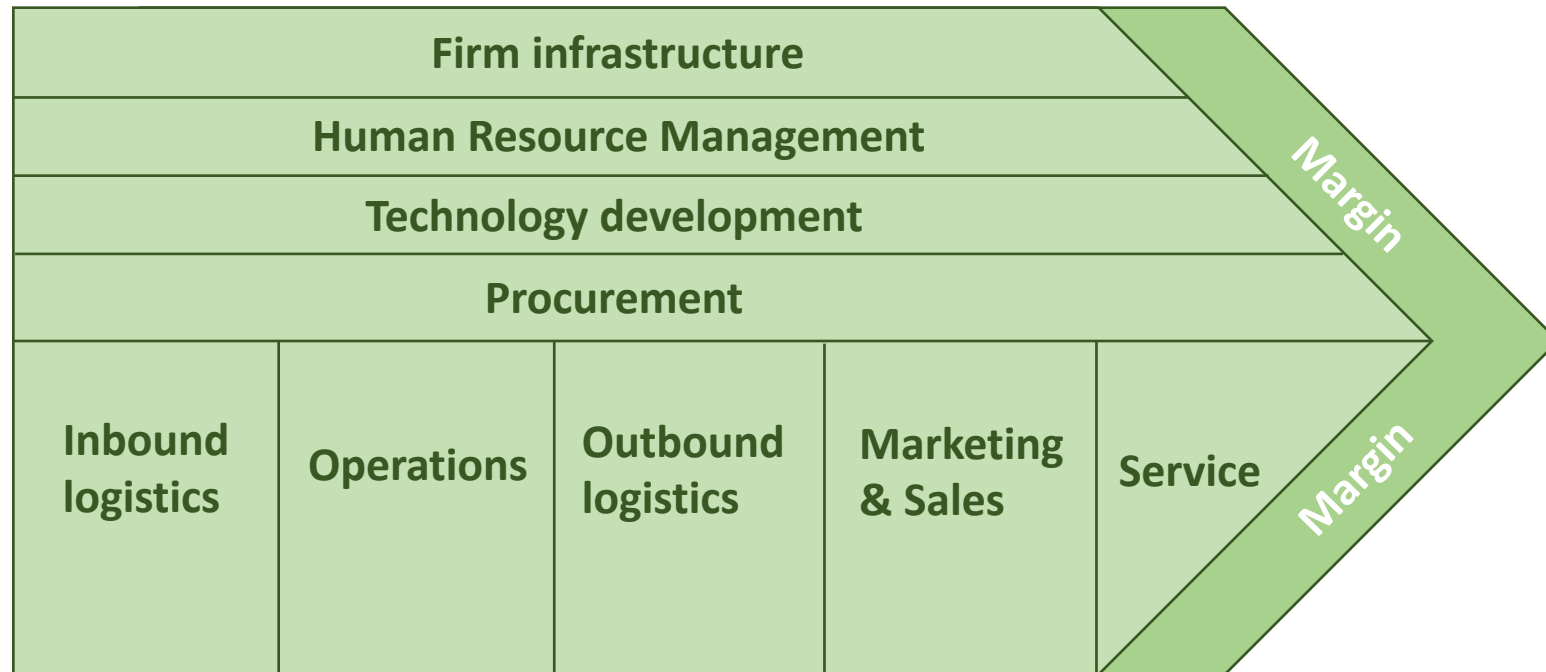
Developing strategies from resources



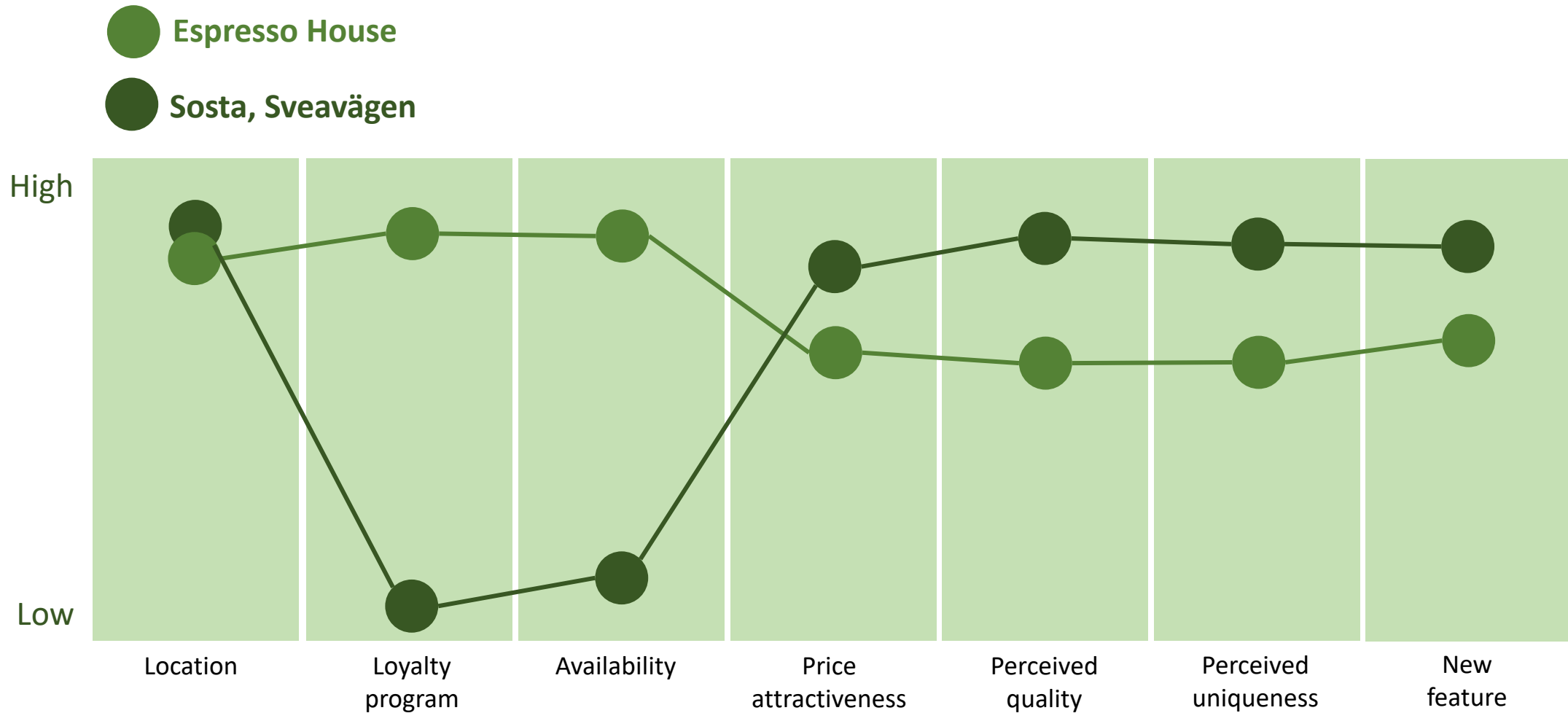
Connecting market and resource analysis



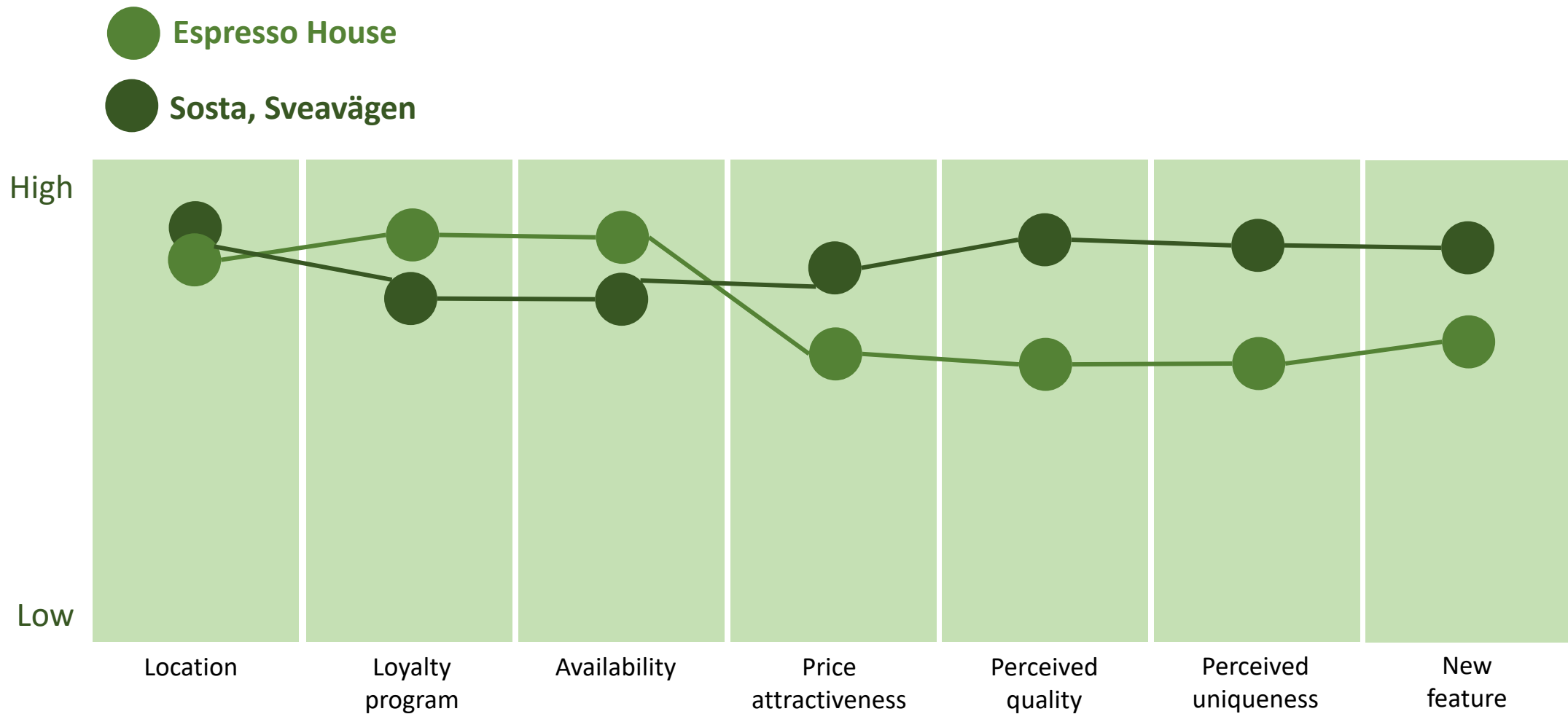
Porter's value chain



Blue Ocean Strategy and the Value Curve



Blue Ocean Strategy and the Value Curve



External dynamism and organizational change

Types of environmental change and impediments to organisational change

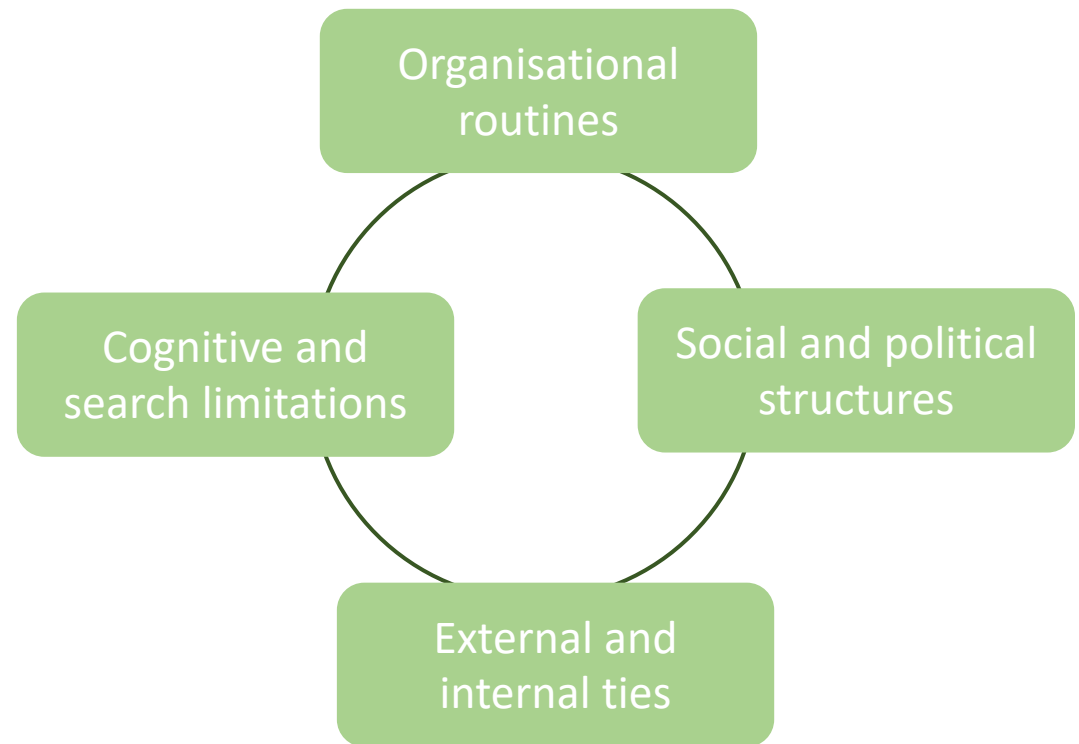
Types of dynamism

Unintentional

- e.g. interest rate changes, economic shifts, epidemics
- Positive or negative
- Affecting entire industry
- Difficult to influence

Intentional

- e.g. competitor price cuts, poaching employees
- Mainly negative
- Affecting focal firm
- Possible to react to



Achieving change

- Identify key drivers for change
- Identify and prioritize key areas of organisational change
- Create sense of urgency
- Involve stakeholders (e.g. middle management, unions)
- Low hanging fruit for momentum
- Follow up and address shortfalls

In sum

Key takeaways

- Strategy takes the overall perspective on organisations
- Anything can be strategic, and strategy research points you to what works
- Strategists work under uncertainty, bounded rationality, and unpredictable dynamism
- Corporate strategy tells you 'in what sport to compete'
- Competitive strategy tells you 'how to beat the other team'
- Competitive strategy requires understanding both the market and the resources
- Implementation is crucial, avoid being just a person with a plan

Exercise

In your teams...

- Analyse how IT can contribute to the competitive advantage of Swedish appliance manufacturer Electrolux
- Use e.g. the Value Curve and Porter's Value chain together with resource/capability analysis
- Consider and briefly address possible impediments to change, and how to overcome these
- Be back at...

• About Electrolux

- Founded 1919
- Some 48,000 employees worldwide
- Produces and markets consumer and professional washing machines, dish washers, vacuum cleaners, food processors, etc.
- www.electrolux.com

Thank you

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