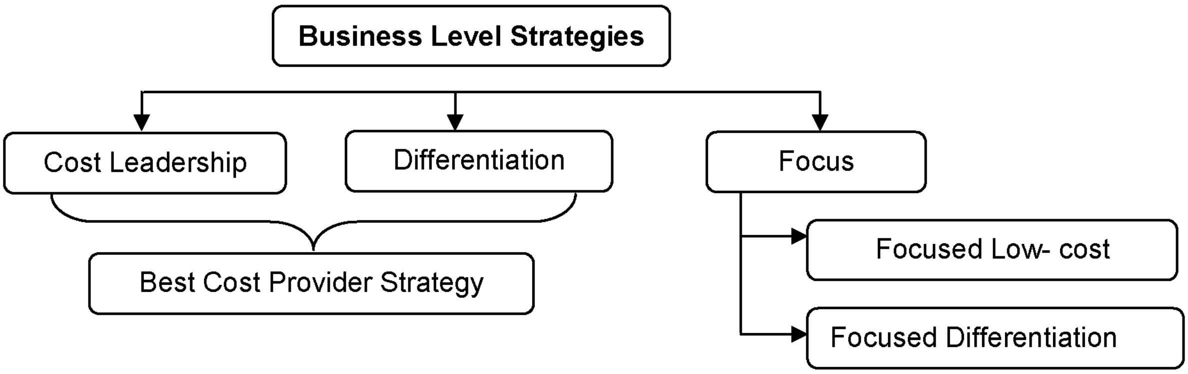
5. BUSINESS LEVEL STRATEGIES



MICHAEL PORTER'S 5 FORCES MODEL OF COMPETITION ANALYSIS

Q.No.1. Explain Michael Porter's Five Forces Model of Competition Analysis. (A)
(OLD PM, RTP- M14, N15, N18, N09 - 10M, N11- 3M, N12 - 3M, MTP M18, N18, M18 - 5M)

MEANING: It is a powerful and widely used tool for systematically diagnosing the principal competitive pressures in a market and assessing their strength and importance. The model states that the state of competition in an industry is the combination of competitive pressures operating in five areas of the overall market. The five forces together determine industry attractiveness/ profitability.

These five forces are:

1. THREAT OF NEW ENTRANTS: A firm's profitability will be higher when new firms are blocked from entering the industry. New entrants can reduce an industry's profitability by adding new production capacity leading to increased supply of the product at a lower price which can reduce the firm's existing market share. To discourage new entrants, existing firms can try to create entry barriers.

2. Common entry barriers include:

   a) Capital Requirements: *When a large amount of capital is required, new firms lacking funds can't enter, thus enhancing the profitability of existing firms in the industry.*

   b) Economies of Scale: *Economies of scale refer to the decline in the per-unit cost of production (or other activity) as volume grows. A large firm with economies of scale can discourage new entrants.*

   c) Product Differentiation: *It refers to the physical or perceptual differences, or enhancements, that make a product special or unique in the eyes of customers.* The cost of creating genuine product differences may be too high for the new entrants.

   d) Switching Costs: *To succeed in an industry, new entrant must be able to persuade existing customers of other companies to switch to its products. Buyers often incur substantial financial (and psychological) costs in switching between firms. When such switching costs are high, buyers are often reluctant to change.*

   e) Brand Identity: *The brand identity of products or services offered by existing firms can serve as another entry barrier.*

   f) Access to Distribution Channels: *The unavailability of distribution channels for new entrants poses another significant entry barrier.*

   g) Possibility of Aggressive Retaliation: *Sometimes the mere threat of aggressive retaliation by existing players can prevent entry of new firms into an industry.*

3. BARGAINING POWER OF CUSTOMERS:

   a) This force will become heavier depending on the possibilities of the buyers forming groups or cartels. Mostly, this is a phenomenon seen in industrial products.

b) Buyers of an industry's products or services can sometimes exercise considerable pressure on existing firms to secure lower prices or better services. This can be seen when

i) Buyers have full knowledge of the sources of products and their substitutes.

ii) They spend a lot of money on the industry's products i.e. they are big buyers.

iii) The industry's product is not perceived as critical to the buyer's needs and

iv) Buyers are more concentrated than firms supplying the product.

4. **BARGAINING POWER OF SUPPLIERS:** Suppliers can influence the profitability of an industry in a number of ways. Suppliers can command bargaining power over a firm when:

a) Suppliers' products are crucial to the buyer and substitutes are not available.

b) Suppliers can create high switching costs.

c) Suppliers' market is more concentrated than their buyers market.

Intel & AMD are the two major players in the micro processors market globally. Though they are in the 1st & 2nd places, the gap between the two is enormous with Intel clearly in the lead in the global market.

5. **RIVALRY AMONG EXISTING FIRMS:** The intensity of rivalry in an industry is a significant determinant of industry attractiveness and profitability. Rivalry among competitors tends to be cutthroat and industry profitability low when:

a) An industry has no clear leader.

b) Competitors in the industry are numerous.

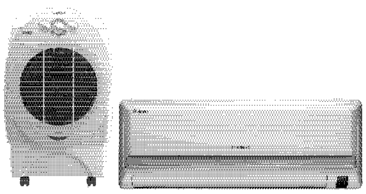
c) Competitors operate with high fixed costs.

d) Competitors face high exit barriers.

e) Competitors have little opportunity to differentiate their offerings.

f) The industry faces slow or diminished growth.

6. **THREAT OF SUBSTITUTES:** A final force that can influence industry profitability is the availability of substitutes for an industry's product. *For example, introduction of digital filmless cameras virtually replace the film cameras and threatened the existence of Eastman Kodak and Fuji Film. Further, the introduction of smart phones has replaced cameras to a great extent.*



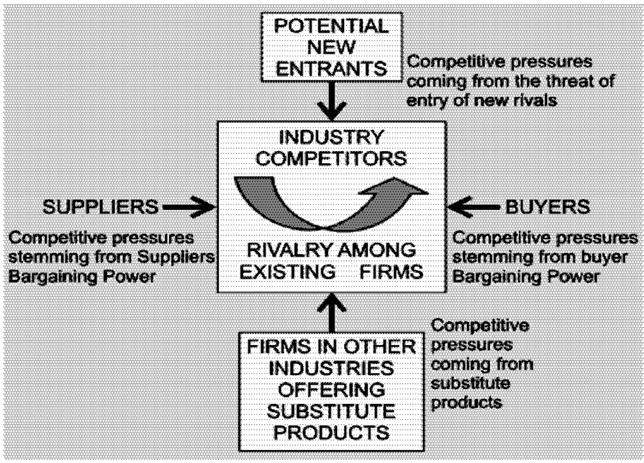
Air Cooler is a better Substitute for Air Conditioner.

STEPS: *The steps to determine competition in a given industry are:*

Step 1: *Identify the specific competitive pressures associated with each of the five forces.*

Step 2: *Evaluate how strong the pressures from each of the five forces are: (a) Fierce, (b) Strong, (c) Moderate to Normal or (d) Weak.*

Step 3: *Determine whether the collective strength of the five competitive forces is conducive to earning attractive profits or not.*



SIMILAR QUESTIONS:

1. **Industry is a composite of competitive pressures in five areas of the overall market. Briefly explain the competitive pressures. (N11 - 3M)**

A. Same as above.

2. **How the new entrant affects the competition? (OLD PM)**

A. Refer 1st point in the above answer.

3. **Explain the factors that affect the strength of competitive pressures from substitute products. (OLD PM, N12 - 3M)**

A. Refer 5th point in the above answer.

4. **Discuss the Porter's model for systematically diagnosing the significant competitive pressures in a market. (RTP M14)**

A. Same as above.

5. **Define Five Forces Model (RTP M12)**

A. Refer meaning in the above answer

6. **Porter's five forces model considers new entrants as a significant source of competition.**

A. Porter's five forces model considers new entrants as major source of competition. + write 1st point as given in the above answer (no need to write entry barriers). **(OLD PM)**

7. **What are the common barriers that are faced by new entrants when an existing firm earns higher profits? (RTP M18)**

A. Refer 1st point in thw above answer.

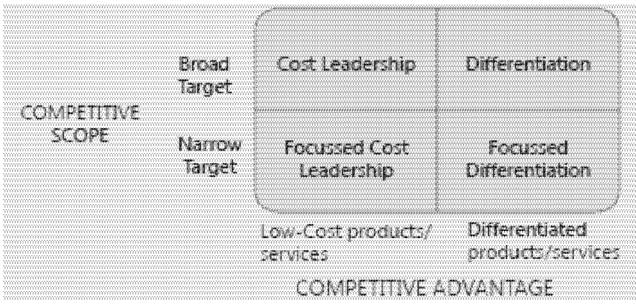
8. **Explain Porter's five forces model as to how businesses can deal with the competition.**

(SM, RTP N18, MTP N18)

A. To gain a deep understanding of a company's industry and competitive environment, managers do not need to gather all the information they can find and waste a lot of time digesting it. Rather, the task is much more focused. + write the meaning above + write the following:

1. Competitive pressures associated with the market manoeuvring and jockeying for buyer patronage that goes on among rival sellers in the industry.
2. Competitive pressures associated with the threat of new entrants into the market.
3. Competitive pressures coming from the attempts of companies in other industries to win buyers over to their own substitute products.
4. Competitive pressures stemming from supplier bargaining power and supplier - seller collaboration.

5. Competitive pressures stemming from buyer bargaining power and seller - buyer Collaboration.



MICHAEL PORTER'S GENERIC STRATEGIES

Q.No.2. Write short notes on Michael Porter's Generic Strategies. (A)

(OLD PM, M10 - 10M, RTP M12, M15, N16)

According to Michael Porter, Generic or basic strategies allow organisations to gain competitive advantage from three different bases as stated below. These strategies have been termed generic because they can be pursued by any type or size of business firm and even by not-for-profit organisations.

COST LEADERSHIP: Emphasizes producing standardized products at a very low per-unit cost for consumers who are price-sensitive. *It allows a firm to earn higher profits than its competitors.*

DIFFERENTIATION: It is a strategy aimed at producing unique products and services and directed at consumers who are relatively price-insensitive.

FOCUS: It means producing products and services that fulfil the needs of small groups of consumers. It involves selecting or focussing a market or customer segment in which to operate.

FACTORS INFLUENCING A FIRM TO CHOOSE A PARTICULAR GENERIC STRATEGY: *Depending upon factors such as type of industry, size of firm and nature of competition, a company can select an appropriate option among the above generic strategic alternatives.*

SIMILAR QUESTION:

1. **Competitive advantage can be achieved by an organisation at business level by following generic strategies proposed by Porter covering three different bases .What are they?**

A. Refer the above answer.

COST LEADERSHIP STRATEGY

Q.No.3. Write short notes on Cost Leadership Strategy? (A)

1. It is a low cost competitive strategy that aims at broad mass market.
2. It requires vigorous (=dynamic/forceful) pursuit of cost reduction in the areas of procurement, production, storage and distribution of product or service and also economies in overhead costs.
3. Due to its lower costs, the cost leader is able to charge a lower price for its products than its competitors and still make satisfactory profits.
4. *For example, McDonald's fast food restaurants have successfully followed low cost leadership strategy.*
5. This strategy is effective when the market is composed of many price-sensitive buyers, when there are few ways to achieve product differentiation, when buyers do not care much about differences from brand to brand, or when there are a large number of buyers with significant bargaining power.

In 2004, Nirma's detergent approached 800,000 tonnes – one of the largest volumes sold in the world – under a single brand 'Nirma'.

6. The basic objective of this strategy is to underprice competitors and thereby gain market share and sales, driving some competitors out of the market entirely.

7. In a 'Low Cost Leader' company there will be high efficiency, low overheads, limited perks, intolerance of waste, intensive screening of budget requests, wide spans of control, rewards linked to cost containment, and broad employee participation in cost control efforts

8. Some risks of cost leadership strategy are

a) Competitors may imitate the strategy, thus reducing the overall industry profits;

b) The technological breakthroughs in the industry may make the strategy ineffective;

c) Buyer interest may shift to other differentiating features in addition to price.

SIMILAR QUESTION:

1. A primary reason for pursuing forward, backward, and horizontal integration strategies is to gain cost leadership benefits. In this context write a short note on cost leadership strategy.

A. Refer answer above.

Q.No.4. How to achieve Cost Leadership Strategy? (B)

To achieve cost leadership, the following actions have to be taken by a firm:

a) Forecast the demand of a product or service promptly.

b) Optimum utilization of the resources to achieve cost advantage.

c) Achieving economies of scale leads to lower per unit cost of product/service.

d) Standardization of products for mass production to yield low cost per unit.

e) Invest in cost saving technologies and try using advance technology for smart working.

f) Resistance to differentiation till it becomes necessary.

SIMILAR QUESTION:

1. Achieving cost leadership strategy requires certain cost saving and other measures to be followed by the organisations, List out the ways to achieve the cost leadership strategy.

A. Refer above answer.

Q.No.5. What are the Advantages and Disadvantages of Cost Leadership Strategy? (A) (RTP M18)

Advantages of Cost Leadership Strategy:

Cost leadership strategy may help the firm remain profitable even in the presence of: existing rivalry, new entrants, supplier's bargaining power, substitute products, and buyers' bargaining power.

a) Existing Rivalry: Competitors are likely to avoid a price war, since the low cost firm will continue to earn profits.

b) Buyers: Powerful buyers/customers can't exercise their bargaining power over the cost leader firm and will continue to buy its product.

c) Suppliers: Cost leader firms can absorb greater price increases of raw materials.

d) New Entrants: Low cost leader firms can create entry barriers to new entrants through their continuous focus on efficiency and reduction of costs.

e) Substitutes: Low cost leaders can successfully persuade customers to stay with their product.

Disadvantages of Cost Leadership Strategy

a) Cost advantage may not remain for long as competitors can copy or follow cost reduction techniques.

b) A firm can succeed with this strategy only if it can achieve higher sales volume.

c) Cost leaders tend to keep their costs low by minimizing advertising, market research, and research and development, but this approach is not suggested in the long run.

d) Technology changes are a great threat to the cost leader firm.

SIMILAR QUESTIONS:

1. **Write short notes on the advantages of Cost Leadership Strategy. (RTP M18, MTP1 N18)**

A. Refer advantages in the above answer.

2. **Cost leadership strategy offers advantages to handle competition based on Porter's five forces of competition framework. Elucidate.**

A. Refer advantages in the above answer.

3. **No strategy is an all-time right strategy. Hence cost leadership strategy has its own fair share of disadvantages. Elucidate.**

A. Refer disadvantages in above answer.

DIFFERENTIATION STRATEGY

Q.No.6. Write short notes on Differentiation Strategy? (A)

1. This strategy involves producing unique products and services and charging a premium price, targeting consumers who are relatively price-insensitive.
2. Successful differentiation can mean greater product flexibility, greater compatibility, lower costs, improved service, less maintenance, greater convenience, or more features.
3. *Differentiation strategy should be pursued only after a careful study of buyers' needs and preferences to make a unique product.*
4. A successful differentiation strategy allows a firm to charge a higher price for its product and to gain customer loyalty because consumers may become strongly attached to the differentiation features.
5. Special features that differentiate one's product can include superior service, spare parts availability, engineering design, product performance, useful life, mileage, or ease of use.
6. A risk of pursuing a differentiation strategy is that the unique product may not be valued high enough by customers to justify the higher price. When this happens, a cost leadership strategy easily will defeat a differentiation strategy. Another risk of pursuing a differentiation strategy is that competitors may develop ways to copy the differentiating features quickly.

Basis of Differentiation: There are several basis of differentiation: product, pricing and organization.

- **Product:** Innovative products that meet customer needs can be an area where a company has an advantage over competitors.
- **Pricing:** Companies that differentiate based on product price can either determine to offer the lowest price, or can attempt to establish superiority through higher prices.
- **Organisation:** Organisational differentiation is yet another form of differentiation. Maximizing the power of a brand, or using the specific advantages that an organization possesses can be instrumental to a company's success.

Surf Excel is the premium quality detergent brand of HUL with its communication theme 'Dirt is Good'.

SIMILAR QUESTION:

1. **Differentiation strategy should be pursued only after a careful study of buyers' needs and preferences to determine the feasibility of incorporating one or more differentiating features into a unique product that features the desired attributes. In this context write about differentiation strategy.**

A. Refer above answer.

Q.No.7. How to achieve Differentiation Strategy? (B)

To achieve differentiation, the following measures should be adopted by an organization.

a) Offer utility for the customers and match the products with their tastes and preferences.

b) Elevate the performance of the product (Superior Performance).

c) Offer the promise of high quality product/service for buyer satisfaction.

d) Rapid product innovation.

e) Taking steps for enhancing image and brand value.

f) Fixing product prices based on the unique features of the product and buying capacity of the customer.

Mercedes Benz is the world's most prestigious brand and its positioning strategy is based on differentiation.

SIMILAR QUESTION:

1. Discuss differentiation strategy? How is it achieved? (MTP M18)

A. Refer 1, 2 & 3 points in the answer of Q.no.6 + refer Q.no.7.

Q.No.8. What are the Advantages and Disadvantages of Differentiation Strategy? (B)

Advantages of Differentiation Strategy: Differentiation strategy may help a firm remain profitable even in the presence of: existing rivalry, new entrants, suppliers' bargaining power, substitute products, and buyers' bargaining power.

1. **Existing Rivalry:** Brand loyalty acts as a safeguard against competitors. It means that customers will be less sensitive to price increases, as long as the firm can satisfy the needs of its customers.
2. **Buyers:** They do not negotiate for price as they get special features and also they have fewer options in the market.
3. **Suppliers:** Because differentiators charge a premium price, they can afford to absorb higher costs of supplies and customers are willing to pay extra too.
4. **New Entrants:** Innovative features are an expensive offer. So, new entrants generally avoid these features because it is tough for them to provide the same product with special features at a comparable price.
5. **Substitutes:** Substitute products can't replace differentiated products which have high brand value and enjoy customer loyalty.

Disadvantages of Differentiation Strategy:

1. In long term, uniqueness is difficult to sustain.
2. Charging too high a price for differentiated features may cause the customer to switch to another alternative.
3. Differentiation fails to work if its basis is something that is not valued by the customers.

SIMILAR QUESTIONS:

1. Differentiation strategy offers advantages in view of Porter's framework of Competition Analysis. Comment.

A. Refer the advantages in the above answer.

FOCUS STRATEGY

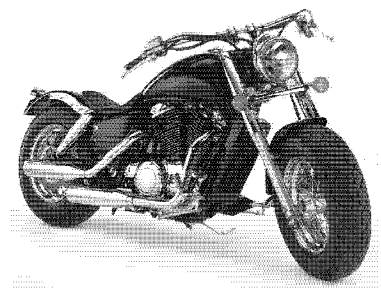
Q.No.9. Write short note on Focus Strategy. (A)

1. Focus strategy involves producing products and services that fulfill the needs of a narrow market that consists of consumers whose needs and preferences are distinctively different from the rest of the market.
2. An organization using a focus strategy may concentrate on a particular group of customers, geographic markets, or on particular product - line segments in order to serve a well - defined but narrow market better than competitors who serve a broader market.
3. A successful focus strategy depends on an industry segment that is of
   - sufficient size,
   - has good growth potential, and
   - is not crucial to the success of other major competitors.
4. Midsize and large firms can effectively pursue focus-based strategies only in conjunction with differentiation or cost leadership-based strategies.
5. Focus strategy is most effective when consumers have distinctive preferences or requirements and when rival firms are not attempting to specialize in the same target segment.
6. Risks of pursuing a focus strategy include the possibility that numerous competitors will recognize the successful focus strategy and copy it, or that consumer preferences will drift toward the product attributes desired by the market as a whole.
7. **Types of Focus Strategy:** There are two variants of Focus Strategy, namely Focused Cost Leadership and Focused Differentiation strategies.
   a) **Focused Cost Leadership Strategy:** It involves competing based on low price and targeting a narrow market. Firms that compete based on price and target a narrow market are following this strategy. A firm that follows this strategy does not necessarily charge the lowest prices in the industry. Instead, it charges low prices relative to other firms that compete within the target market.
   b) **Focused Differentiation Strategy:** It involves offering unique features that fulfill the demands of a narrow market. Firms that compete based on uniqueness and target a narrow market are following a focused differentiation strategy. *For example, Rolls-Royce sells limited number of high-end, custom-built cars.*

Q.No.10. How to achieve Focus Strategy? (B)

To achieve focus strategy the following are the following measures have to be adopted by an organization:

1. Selecting specific niches which are not covered by cost leaders and differentiators.
2. Creating superior skills for catering to such niche markets.
3. Generating high efficiencies for serving such niche markets.
4. Developing innovative ways in managing the value chain.



Harley – Davidson concentrates only on the super – heavy weight motors cycles market. It does not produce small street bikes or off-road bikes.

Q.No.11. what are the Advantages and Disadvantages of Focus Strategy? (B)

Advantages of Focused Strategy:

1. Premium prices can be charged by the organisations for their focused product/ services.
2. Due to the tremendous expertise about the goods and services that organisations following focus

strategy offer, rivals and new entrants will find it difficult to compete.

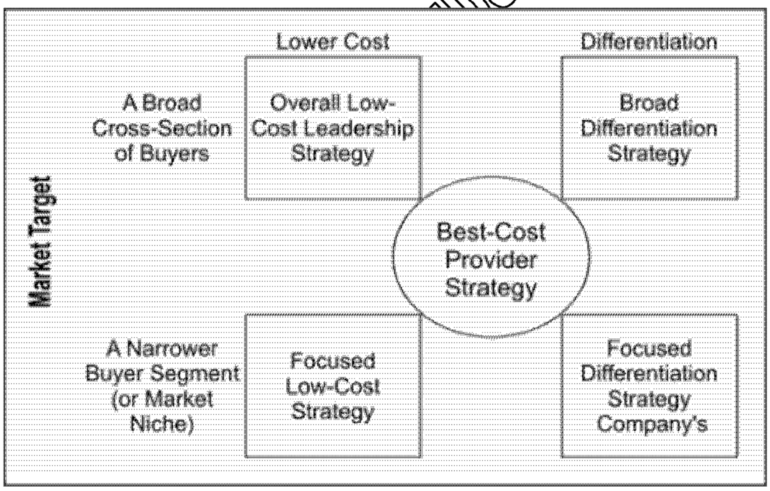
Disadvantages of Focused Strategy:

1. The firms lacking in distinctive competencies may not be able to pursue focus strategy.
2. Due to the limited demand of product/services, costs are high which can cause problems.
3. In long run, the niche could disappear or be taken over by larger competitors by acquiring the same distinctive competencies.

BEST- COST PROVIDER STRATEGY

Q.No.12. Write short notes on Best- Cost Provider Strategy (A) (OLD PM, N12 - 1M)

1. Best Cost provider strategy is a further development of 3 generic strategies i.e. Cost Leadership, Differentiation and Focus Strategies.
2. Best - cost provider strategy involves providing more value for money to the Customers by emphasizing low cost and better quality difference. It can be done in any of the following 2 ways:
   a) By offering products at lower price than what is being offered by rivals for products with comparable quality and features.
   b) Charging similar price as that of rivals for products with much higher quality and better features.
3. The objective is to keep costs and prices lower than those of other sellers of comparable products.



SIMILAR QUESTIONS:

1. **Explain the meaning of 'Best cost provider strategy'. (N12 - 1M)**

A. Refer 2nd point in above answer.

2. **Consumers always prefer best products at cheaper prices. What is the strategy to be followed by organisations to suit the consumer aspirations?**

A. Refer the above answer.

Q. No.13. What are the situations under which the three generic strategies can be used? (C) (For Students Self - Study)

SITUATIONS UNDER WHICH THESE GENERIC STRATEGIES CAN BE USED ARE:

a) **COST LEADERSHIP:** When the market is price-sensitive and much room is not left for differentiation. Cost leadership is a better option when buyers do not care much about differences between the brands.

b) **DIFFERENTIATION:** This strategy is suitable when the customers are attracted to specific attribute(s) of the products. It is directed towards creating separate market with a product with different attribute(s). The strategy is useful in a perfectly competitive market where all the products look similar.

c) **FOCUS:** Smaller firms may compete on a focus basis. When the customers have distinctive preferences or requirements and the rival firms are not attempting to specialise in the same target segment.

SIMILAR QUESTIONS:

1. **Michael E. Porter has suggested three generic strategies. Briefly Explain them. What is the basic objective to follow a generic Strategy? In what situations can the three strategies be used? (RTP M16)**

A. Refer 2nd question + above question

2. **According to Michael Porter, strategies allow organizations to gain competitive advantages from different bases. Explain these bases as mentioned by Porter. (M13 - 3M)**

A. Refer 2nd question + write above answer.

APPLICATION ORIENTED QUESTIONS

Q.No.14. Identify the type of generic strategy used in the following examples.

i) Dell Computer has decided to rely exclusively on direct marketing.

ii) "Our basic strategy was to charge a price so low that microcomputer makers couldn't do the software internally for that cheaply".

iii) 'NDTV', a TV channel has identified a profitable audience niche in the electronic media and exploited that niche through the addition of new channels like NDTV 'Profit' and 'Image'. (C)

(OLD PM, M10)

i) **DIFFERENTIATION:** Dell Computers is differentiating on product delivery. Computer market is highly competitive and the products are very similar.

ii) **COST LEADERSHIP:** Keeping the prices low so that microcomputer makers acquire the software rather than developing themselves is a case of cost leadership.

iii) **FOCUS:** NDTV has identified a profitable area (audience niche) and is focusing on it.

Q.No.15. Airlines industry in India is highly competitive with several players. Businesses face severe competition and aggressively market themselves with each other. Luxury Jet is a private Delhi based company with a fleet size of 9 small aircrafts with seating capacity ranging Between 6 seats to 9 seats. There aircrafts are chartered by big business houses and high net worth individuals for their personalized use. With customized tourism packages their aircrafts are also often hired by foreigners. Identify and explain the Michael Porter's Generic Strategy followed by Luxury Jet. (B) (RTP M18)

1. The Airlines industry faces stiff competition. However, Luxury Jet has attempted to create a niche market by adopting focused differentiation strategy. A focused differentiation strategy requires offering unique features that fulfill the demands of a narrow market.

2. Luxury Jet compete in the market based on uniqueness and target a narrow market which provides business houses, high net worth individuals to maintain strict schedules. The option of charter flights provided several advantages including, flexibility, privacy, luxury and many a times cost saving. Apart from conveniences, the facility will provide time flexibility. Travelling by private jet is the most comfortable, safe and secures way of flying your company's senior business personnel.

3. Chartered services in airlines can have both business and private use. Personalized tourism packages can be provided to those who can afford it.

Q.No.16. Analyse the following cases in the context of Michael Porter's Five Forces Model:
i) A supplier has a large base of customers.
ii) A manufacturer of sports goods has the advantage of economies of large scale production.
iii) Products offered by competitors are almost similar. (B) (NEW SM)

i) Large base of customers of an organization (supplier) may increase its bargaining power in comparison to the bargaining power of the customer.

ii) The manufacturer of sports goods would be in better position amongst existing competitors since it has advantage of economies of scale. Even the threat of new entrants gets reduced.

iii) Similar products will reduce the bargaining power of the rivals, i.e., competitors. In other words the bargaining power of the customer will be more.

Q.No.17. Gennex is a company that designs, manufactures and sells computer hardware and Software. Gennex is well known for their innovative product that has helped the company to have advantage over its competitors. It also spends on research and development and concerned with innovative softwares. Often the unique features of their product, that are not available with their competitors helps them to gain competitive advantage. Gennex using the strategy is consistently gaining its position in the industry over its competitors. Identify and explain the Porter's generic strategy which Gennex has opted to gain the competitive advantage. (B) (RTP N18)

1. According to Porter, strategies allow organizations to gain competitive advantage from three different bases: cost leadership, differentiation, and focus. Porter called these basic or generic strategies.

2. Gennex has opted differentiation strategy. Its products are designed and produced to give the customer value and quality. They are unique and serve specific customer needs that are not met by other companies in the industry. Highly differentiated and unique hardware and software enables Gennex to charge premium prices for its products hence making higher profits and maintain its competitive position in the market.

3. Differentiation strategy is aimed at broad mass market and involves the creation of a product or service that is perceived by the customers as unique. The uniqueness can be associated with product design, brand image, features, technology, and dealer network or customer service.

TEST YOUR KNOWLEDGE

1. Explain why is cost-leadership strategy very effective in a country like India?

2. Can a low- cost leader firm make its customers loyal to its products/services? Substantiate your answer with proper reasoning

3. List out the various national and global companies which are successfully pursuing differentiation strategy?

4. Is differentiation strategy apt for an educational institution? Explain with some examples if your answer is 'yes'.

5. What are 'No-frills' airlines? List out the various no-frills airline companies operating in India.

6. Will it be ok for Rolex, if it introduces watches in the economy range of Rs.700 - Rs.2000 under the same brand name?

THE END