Crafting & Executing STRATEGY

THE QUEST FOR COMPETITIVE ADVANTAGE

Concepts and Readings

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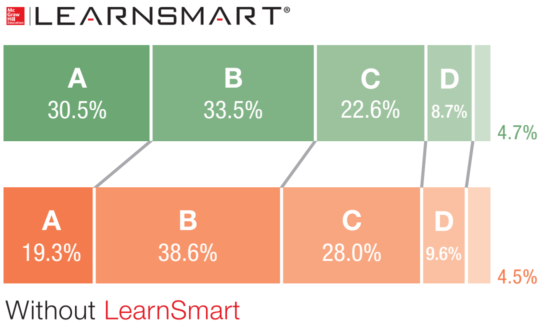

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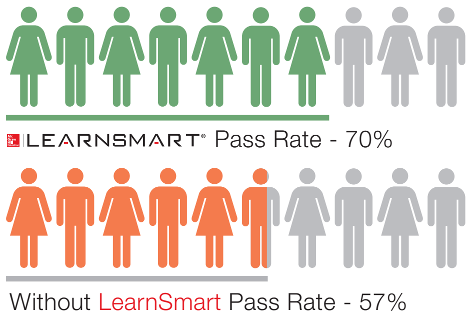

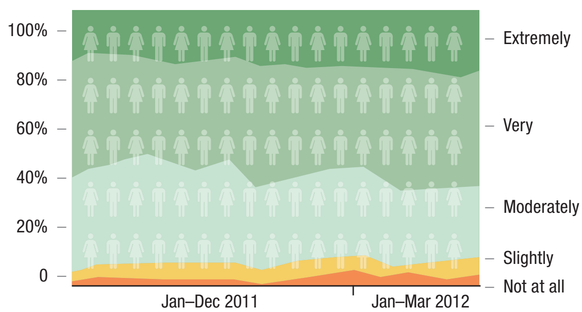

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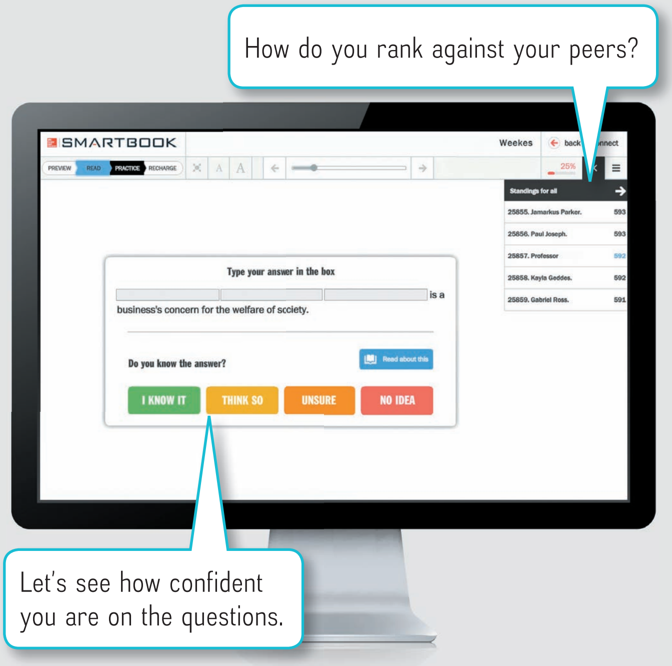

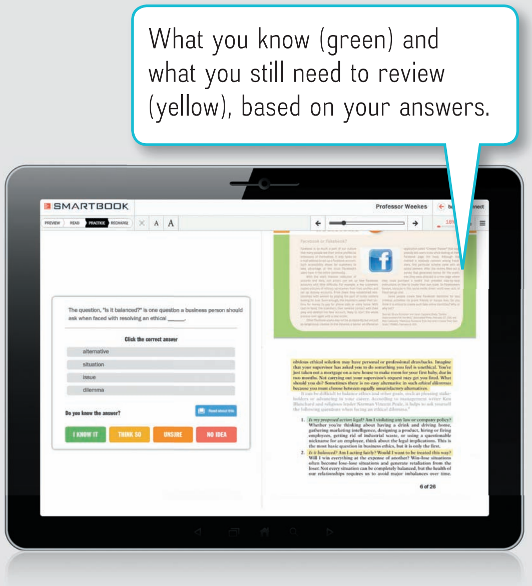

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Crafting and Executing Strategy

Concepts and Readings

Crafting and Executing Strategy

Concepts and Readings | TWENTIETH EDITION

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Mc Graw Hill Education

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To our families and especially our spouses:
Hasseline, Paul, and Kitty.

ABOUT THE AUTHORS

Arthur A. Thompson, Jr., earned his B.S. and Ph.D. degrees in economics from The University of Tennessee, spent three years on the economics faculty at Virginia Tech, and served on the faculty of The University of Alabama's College of Commerce and Business Administration for 24 years. In 1974 and again in 1982, Dr. Thompson spent semester-long sabbaticals as a visiting scholar at the Harvard Business School.

His areas of specialization are business strategy, competition and market analysis, and the economics of business enterprises. In addition to publishing over 30 articles in some 25 different professional and trade publications, he has authored or co-authored five textbooks and six computer-based simulation exercises. His textbooks and strategy simulations have been used at well over 1,000 college and university campuses worldwide.

Dr. Thompson spends much of his off-campus time giving presentations, putting on management development programs, working with companies, and helping operate a business simulation enterprise in which he is a major partner.

Dr. Thompson and his wife of 53 years have two daughters, two grandchildren, and a Yorkshire Terrier.

Margaret A. Peteraf is the Leon E. Williams Professor of Management at the Tuck School of Business at Dartmouth College. She is an internationally recognized scholar of strategic management, with a long list of publications in top management journals. She has earned myriad honors and prizes for her contributions, including the 1999 Strategic Management Society Best Paper Award recognizing the deep influence of her work on the field of Strategic Management. Professor Peteraf is a fellow of the Strategic Management Society and the Academy of Management. She served previously as a member of the Board of Governors of both the Society and the Academy of Management and as Chair of the Business Policy and Strategy Division of the Academy. She has also served in various editorial roles and on numerous editorial boards, including the *Strategic Management Journal*, the *Academy of Management Review*, and *Organization Science*. She has taught in Executive Education programs in various programs around the world and has won teaching awards at the MBA and Executive level.

Professor Peteraf earned her Ph.D., M.A., and M.Phil. at Yale University and held previous faculty appointments at Northwestern University's Kellogg Graduate School of Management and at the University of Minnesota's Carlson School of Management.

John E. Gamble is a Professor of Management and Dean of the College of Business at Texas A&M University–Corpus Christi. His teaching and research for nearly 20 years has focused on strategic management at the undergraduate and graduate levels. He has conducted courses in strategic management in Germany since 2001, which have been sponsored by the University of Applied Sciences in Worms.

Dr. Gamble's research has been published in various scholarly journals and he is the author or co-author of more than 75 case studies published in an assortment of strategic management and strategic marketing texts. He has done consulting on industry and market analysis for clients in a diverse mix of industries.

Professor Gamble received his Ph.D., Master of Arts, and Bachelor of Science degrees from The University of Alabama and was a faculty member in the Mitchell College of Business at the University of South Alabama before his appointment to the faculty at Texas A&M University–Corpus Christi.

Dr. A. J. (Lonnie) Strickland is the Thomas R. Miller Professor of Strategic Management at the Culverhouse School of Business at The University of Alabama. He is a native of north Georgia, and attended the University of Georgia, where he received a Bachelor of Science degree in math and physics; Georgia Institute of Technology, where he received a Master of Science in industrial management; and Georgia State University, where he received his Ph.D. in business administration.

Lonnie's experience in consulting and executive development is in the strategic management arena, with a concentration in industry and competitive analysis. He has developed strategic planning systems for numerous firms all over the world. He served as Director of Marketing and Strategy at BellSouth, has taken two companies to the New York Stock Exchange, is one of the founders and directors of American Equity Investment Life Holding (AEL), and serves on numerous boards of directors. He is a very popular speaker in the area of strategic management.

Lonnie and his wife, Kitty, have been married for 48 years. They have two children and two grandchildren. Each summer, Lonnie and his wife live on their private game reserve in South Africa where they enjoy taking their friends on safaris.

PREFACE

By offering the most engaging, clearly articulated, and conceptually sound text on strategic management, *Crafting and Executing Strategy* has been able to maintain its position as the leading textbook in strategic management for 30 years. With this latest edition, we build on this strong foundation, maintaining the attributes of the book that have long made it the most teachable text on the market, while updating the content, sharpening its presentation, and providing enlightening new illustrations and examples.

The distinguishing mark of the 20th edition is its enriched and enlivened presentation of the material in each of the 12 chapters, providing an as up-to-date and engrossing discussion of the core concepts and analytical tools as you will find anywhere. As with each of our new editions, there is an accompanying collection of new, contemporary readings that amplify important topics in managing a company's strategy-making, strategy-executing process and help drive the chapter lessons home.

While this 20th edition retains the 12-chapter structure of the prior edition, every chapter—indeed every paragraph and every line—has been reexamined, refined, and refreshed. New content has been added to keep the material in line with the latest developments in the theory and practice of strategic management. In other areas, coverage has been trimmed to keep the book at a more manageable size. Scores of new examples have been added, along with 15 new Illustration Capsules, to enrich understanding of the content and to provide students with a ringside view of strategy in action. The result is a text that cuts straight to the chase in terms of what students really need to know and gives instructors a leg up on teaching that material effectively. It remains, as always, solidly mainstream and balanced, mirroring *both* the penetrating insight of academic thought and the pragmatism of real-world strategic management.

A standout feature of this text is the tight linkage between the content of the chapters and the selected readings—two or three new readings for each chapter. The lineup of readings that accompany the 20th edition is outstanding in this respect—a truly appealing mix of strategically relevant and practically oriented readings, certain to engage students and sharpen their thinking on how to apply the concepts and tools of strategic analysis. We are confident you will be impressed with how well the readings work as discussion vehicles and the amount of student interest they will spark.

For some years now, growing numbers of strategy instructors at business schools worldwide have been transitioning from a purely text-readings course structure to a more robust and energizing text-readings-simulation course structure. Incorporating a competition-based strategy simulation has the strong appeal of providing class members with *an immediate and engaging opportunity to apply the concepts and analytical tools covered in the chapters and to become personally involved in crafting and executing a strategy for a virtual company that they have been assigned to manage and that competes head-to-head with companies run by other class members.* Two widely used and pedagogically effective online strategy simulations, *The Business Strategy Game* and *GLO-BUS,* are optional companions for this text. Both simulations were created by Arthur Thompson, one of the text authors, and, like the readings, are closely linked to the content of each chapter in the text. The Exercises for Simulation Participants, found at the end of each chapter, provide clear guidance to class members in applying the concepts and analytical tools covered in the chapters to the issues and decisions that they have to wrestle with in managing their simulation company.

To assist instructors in assessing student achievement of program learning objectives, in line with the latest AACSB requirements, the 20th edition includes a set of Assurance of Learning Exercises at the end of each chapter that link to the specific learning objectives appearing at the beginning of each chapter and highlighted throughout the text. An important instructional feature of the 20th edition is its more closely *integrated* linkage of selected chapter-end Assurance of Learning Exercises to the publisher's web-based assignment and assessment platform called Connect™. Your students will be able to use the online Connect™ supplement to (1) complete two of the Assurance of Learning Exercises appearing at the end of each of the 12 chapters, and (2) complete chapter-end quizzes. Many of the Connect™ exercises are automatically graded, thereby enabling you to easily assess the learning that has occurred.

In addition, both of the companion strategy simulations have a built-in Learning Assurance Report that quantifies how well each member of your class performed on nine skills/learning measures *versus tens of thousands of other students worldwide* who completed the simulation in the past 12 months. We believe the chapter-end Assurance of Learning Exercises, the all-new online and automatically graded Connect exercises, and the Learning Assurance Report generated at the conclusion of *The Business Strategy Game* and *GLO-BUS* simulations provide you with easy-to-use, empirical measures of student learning in your course. All can be used in conjunction with other instructor-developed or school-developed scoring rubrics and assessment tools to comprehensively evaluate course or program learning outcomes and measure compliance with AACSB accreditation standards.

Taken together, the various components of the 20th-edition package and the supporting set of instructor resources provide you with enormous course design flexibility and a powerful kit of teaching/learning tools. We've done our very best to ensure that the elements constituting the 20th edition will work well for you in the classroom, help you economize on the time needed to be well prepared for each class, and cause students to conclude that your course is one of the very best they have ever taken—from the standpoint of both enjoyment and learning.

DIFFERENTIATING FEATURES OF THE 20TH EDITION

Six standout features strongly differentiate this text and the accompanying instructional package from others in the field:

1. *Our integrated coverage of the two most popular perspectives on strategic management—positioning theory and resource-based theory—is unsurpassed by any other leading strategy text.* Principles and concepts from both the positioning perspective and the resource-based perspective are prominently and comprehensively integrated into our coverage of crafting both single-business and multibusiness strategies. By highlighting the relationship between a firm's resources and capabilities to the activities it conducts along its value chain, we show explicitly how these two perspectives relate to one another. Moreover, in Chapters 3 through 8 it is emphasized repeatedly that a company's strategy must be matched *not only*

to its external market circumstances *but also* to its internal resources and competitive capabilities.

2. *Our coverage of cooperative strategies and the role that interorganizational activity can play in the pursuit of competitive advantage, is similarly distinguished.* The topics of the value net (newly added), strategic alliances, licensing, joint ventures, and other types of collaborative relationships are featured prominently in a number of chapters and are integrated into other material throughout the text. We show how strategies of this nature can contribute to the success of single-business companies as well as multibusiness enterprises, whether with respect to firms operating in domestic markets or those operating in the international realm.
3. *With a stand-alone chapter devoted to this topic, our coverage of business ethics, corporate social responsibility, and environmental sustainability goes well beyond that offered by any other leading strategy text.* Chapter 9, "Ethics, Corporate Social Responsibility, Environmental Sustainability, and Strategy," fulfills the important functions of (1) alerting students to the role and importance of ethical and socially responsible decision making and (2) addressing the accreditation requirement of the AACSB International that business ethics be visibly and thoroughly embedded in the core curriculum. Moreover, discussions of the roles of values and ethics are integrated into portions of other chapters to further reinforce why and how considerations relating to ethics, values, social responsibility, and sustainability should figure prominently into the managerial task of crafting and executing company strategies.
4. *Long known as a valuable accompaniment to this text, the readings collection in the 20th edition is truly unrivaled* from the standpoints of student appeal, teachability, and suitability for sparking discussions of the application of the concepts in Chapters 1 through 12. The 25 readings included in this edition are the very latest, the best, and the most on target that we could find.
5. *The text is now more tightly linked to the publisher's trailblazing web-based assignment and assessment platform called Connect™.* This will enable professors to gauge class members' prowess in accurately completing (a) selected chapter-end exercises and (b) chapter-end quizzes.
6. *Two cutting-edge and widely used strategy simulations—*The Business Strategy Game *and* GLO-BUS*—are optional companions to the 20th edition.* These give you an unmatched capability to employ a text-readings-simulation model of course delivery.

ORGANIZATION, CONTENT, AND FEATURES OF THE 20TH-EDITION TEXT CHAPTERS

- Chapter 1 serves as a brief, general introduction to the topic of strategy, focusing on the central questions of *"What is strategy?"* and "Why *is it important?"* As such, it serves as the perfect accompaniment for your opening-day lecture on what the course is all about and why it matters. Using the newly added example of Starbucks to drive home the concepts in this chapter, we introduce students to what we mean by "competitive advantage" and the key features of business-level strategy. Describing strategy making as a process, we explain why a company's strategy is partly planned and partly reactive and why a strategy tends to co-evolve with its environment over time. We show that a viable business model must provide both an attractive value proposition for the company's customers and a formula for making profits for the company. New to this chapter is a depiction of how the Value-Price-Cost Framework can be used to frame this discussion. We show how the mark of a winning strategy is its ability to pass three tests: (1) the *fit test* (for internal and external fit), (2) the *competitive advantage test,* and (3) the *performance test.* And we explain why good company performance depends not only upon a sound strategy but upon solid strategy execution as well.

- Chapter 2 presents a more complete overview of the strategic management process, covering topics ranging from the role of vision, mission, and values to what constitutes good corporate governance. It makes a great assignment for the second day of class and provides a smooth transition into the heart of the course. It introduces students to such core concepts as strategic versus financial objectives, the balanced scorecard, strategic intent, and business-level versus corporate-level strategies. It explains why *all managers are on a company's strategy-making, strategy-executing team* and why a company's strategic plan is a collection of strategies devised by different managers at different levels in the organizational hierarchy. The chapter concludes with a section on the role of the board of directors in the strategy-making, strategy-executing process and examines the conditions that led to recent high-profile corporate governance failures.
- The next two chapters introduce students to the two most fundamental perspectives on strategy making: the positioning view, exemplified by Michael Porter's "five forces model of competition"; and the resource-based view. Chapter 3 provides *what has long been the clearest, most straightforward discussion of the five forces framework to be found in any text on strategic management.* It also offers a set of complementary analytical tools for conducting competitive analysis and demonstrates the importance of tailoring strategy to fit the circumstances of a company's industry and competitive environment. What's new in this edition is the inclusion of the value net framework for conducting analysis of how cooperative as well as competitive moves by various parties contribute to the creation and capture of value in an industry.
- Chapter 4 presents the resource-based view of the firm, showing why resource and capability analysis is such a powerful tool for sizing up a company's competitive assets. It offers a simple framework for identifying a company's resources and capabilities and explains how the VRIN framework can be used to determine whether they can provide the company with a sustainable competitive advantage over its competitors. Other topics covered in this chapter include dynamic capabilities, SWOT analysis, value chain analysis, benchmarking, and competitive strength assessments, thus enabling a solid appraisal of a company's relative cost position and customer value proposition vis-à-vis its rivals. *An important feature of this chapter is a table showing how key financial and operating ratios are calculated and how to interpret them.* Students will find this table handy in doing the number crunching needed to evaluate whether a company's strategy is delivering good financial performance.
- Chapter 5 sets forth the basic approaches available for competing and winning in the marketplace in terms of the five generic competitive strategies—low-cost leadership, differentiation, best-cost provider, focused differentiation, and focused low cost. It describes when each of these approaches works best and what pitfalls to avoid. It explains the role of *cost drivers* and *uniqueness drivers* in reducing a company's costs and enhancing its differentiation, respectively.

- Chapter 6 focuses on *other strategic actions* a company can take to complement its competitive approach and maximize the power of its overall strategy. These include a variety of offensive or defensive competitive moves, and their timing, such as blue-ocean strategies and first-mover advantages and disadvantages. It also includes choices concerning the breadth of a company's activities (or its *scope* of operations along an industry's entire value chain), ranging from horizontal mergers and acquisitions, to vertical integration, outsourcing, and strategic alliances. This material serves to segue into the scope issues covered in the next two chapters on international and diversification strategies.
- Chapter 7 takes up the topic of how to compete in international markets. It begins with a discussion of why differing market conditions across countries must necessarily influence a company's strategic choices about how to enter and compete in foreign markets. It presents five major strategic options for expanding a company's geographic scope and competing in foreign markets: export strategies, licensing, franchising, establishing a wholly owned subsidiary via acquisition or "greenfield" venture, and alliance strategies. It includes coverage of topics such as Porter's Diamond of National Competitive Advantage, profit sanctuaries, and the choice between multidomestic, global, and transnational strategies. This chapter explains the impetus for sharing, transferring, or accessing valuable resources and capabilities across national borders in the quest for competitive advantage, connecting the material to that on the resource-based view from Chapter 4. The chapter concludes with a discussion of the unique characteristics of competing in developing-country markets.
- Chapter 8 concerns strategy making in the multibusiness company, introducing the topic of corporate-level strategy with its special focus on diversification. The first portion of this chapter describes when and why diversification makes good strategic sense, the different means of diversifying a company's business lineup, and the pros and cons of related versus unrelated diversification strategies. The second part of the chapter looks at how to evaluate the attractiveness of a diversified company's business lineup, how to decide whether it has a good diversification strategy, and what the strategic options are for improving a diversified company's future performance. The evaluative technique integrates material concerning both industry analysis and the resource-based view, in that it considers the relative attractiveness of the various industries the company has diversified into, the company's competitive strength in each of its lines of business, and the extent to which its different businesses exhibit both *strategic fit* and *resource fit.*
- Although the topic of ethics and values comes up at various points in this textbook, Chapter 9 brings more direct attention to such issues and may be used as a stand-alone assignment in either the early, middle, or late part of a course. It concerns the themes of ethical standards in business, approaches to ensuring consistent ethical standards for companies with international operations, corporate social responsibility, and environmental sustainability. The contents of this chapter are sure to give students some things to ponder, rouse lively discussion, and help to make students more *ethically aware* and conscious of *why all companies should conduct their business in a socially responsible and sustainable manner.*
- The next three chapters (Chapters 10, 11, and 12) comprise a module on strategy execution that is presented in terms of a 10-step framework. Chapter 10 provides an overview of this framework and then explores the first three of these

tasks: (1) staffing the organization with people capable of executing the strategy well, (2) building the organizational capabilities needed for successful strategy execution, and (3) creating an organizational structure supportive of the strategy execution process.

- Chapter 11 discusses five additional managerial actions that advance the cause of good strategy execution: (1) *allocating resources* to enable the strategy execution process, (2) ensuring that *policies and procedures* facilitate rather than impede strategy execution, (3) using *process management tools* and *best practices* to drive continuous improvement in the performance of value chain activities, (4) installing *information and operating systems* that help company personnel carry out their strategic roles, and (5) using *rewards and incentives* to encourage good strategy execution and the achievement of performance targets.
- Chapter 12 completes the framework with a consideration of the roles of corporate culture and leadership in promoting good strategy execution. The recurring theme throughout the final three chapters is that executing strategy involves deciding on the specific actions, behaviors, and conditions needed for a smooth strategy-supportive operation and then following through to get things done and deliver results. The goal here is to ensure that students understand that the strategy-executing phase is a *make-things-happen and make-them-happen-right* kind of managerial exercise—one that is critical for achieving operating excellence and reaching the goal of strong company performance.

In this latest edition, we have put our utmost effort into ensuring that the 12 chapters are consistent with the latest and best thinking of academics and practitioners in the field of strategic management and provide the topical coverage required for both undergraduate and MBA-level strategy courses. The ultimate test of the text, of course, is the positive pedagogical impact it has in the classroom. If this edition sets a more effective stage for your lectures and does a better job of helping you persuade students that the discipline of strategy merits their rapt attention, then it will have fulfilled its purpose.

THE COLLECTION OF READINGS

The 25 readings in this edition are flush with practical examples and valuable lessons for students of the art and science of crafting and executing strategy. There are two or three readings for each chapter—all chosen with three criteria in mind: relevance, readability, and recency of publication. The *relevance* criterion led us to seek out articles that connected clearly to the material in the text chapters and either extended the chapter coverage or expanded on a topic of strategic importance. The *readability* criterion helped us identify articles that were clearly written, engaging, practically oriented, and relatively short. The *recency* criterion limited our selections to those that appeared in the 2012–2014 period, with the exception of one important article from 2011. We endeavored to be highly selective in our choices, deciding that a manageable number of on-target readings was a better fit with the teaching/learning objectives of most senior and MBA courses in strategy than a more sweeping collection of readings. The readings we chose came from recent issues of *Harvard Business Review, MIT Sloan Management Review, McKinsey Quarterly, Business Strategy Review, Business Horizons, Journal of Business Strategy, Ivey Business Journal,* and *Long Range Planning,* among others.

The first reading, by Richard Rumelt, "The Perils of Bad Strategy," makes an excellent accompaniment to the introductory chapter with its focus on the question of "What distinguishes good strategy from bad strategy?" It reminds readers that strategy is as much about what NOT to do as it is about what TO do and explains why having a compelling vision, mission, and set of core values is not enough. The second reading, "The Role of the Chief Strategy Officer," provides an outstanding discussion of the different ways in which an empowered strategist can contribute to the strategy formulation and strategy execution capabilities of a company.

The third reading, "Managing the Strategy Journey," focuses on the process of developing strategies and making strategic decisions, arguing that there are ten big things that top management teams always need to do. The fourth reading, "The Balanced Scorecard in China: Does it Work?" addresses another key topic from Chapter 2. It suggests that there are limitations to the balanced scorecard approach but provides recommendations for how to overcome these and successfully implement this management tool in China.

The next article, "Competing in Network Markets: Can the Winner Take All?" provides a wonderful complement to the value net and five forces frameworks in Chapter 3. It describes the factors that influence success and failure in network markets and concludes with a set of recommendations for increasing the likelihood of success for both entrepreneurs and incumbent firms. "BlackBerry Forgot to Manage the Ecosystem," by Michael Jacobides, draws attention to the importance of viewing the competitive landscape through an ecosystem lens. This short piece derives from a framework that can be seen as a valuable extension of, and complement to, the familiar five-forces framework and the value net.

Reading 7, by David Teece, continues the theme of the need for shaping the ecosytem, but focuses instead on the role of dynamic capabilities, as its title, "Dynamic Capabilities: Routines versus Entrepreneurial Action," suggests. Reading 8, "Meta-SWOT: Introducing a New Strategic Planning Tool," offers an enhancement to another of Chapter 4's most widely employed frameworks. The short piece, titled "Are You Ready for the Digital Value Chain?" completes the readings for Chapter 4, showing how the increasing digitization of the value chain is likely to transform all industry sectors.

The next two readings provide valuable supplements to the material on generic strategies covered in Chapter 5. The first, "Limits to Growing Customer Value: Being Squeezed between the Past and the Future," discusses the importance of value engineering in managing trade-offs and driving growth. The second, "Organizational Ambidexterity," argues that the key to surviving in extreme competitive conditions is striking a balance between competing effectively today and innovating for the future.

The article by Constantinos Markides and Lourdes Sosa makes a perfect accompaniment to Chapter 6. In "Pioneering and First Mover Advantages: The Importance of Business Models," they argue that pioneering has both advantages and disadvantages; which predominates will depend on the business model chosen for both attacking and defending one's position. The next reading, "Adding Value through Offshoring," by Joan Enric Ricart and Pablo Agnese, adds the topic of offshoring to the discussion about outsourcing covered in Chapter 6. They offer insight on modern offshoring practices, showing how companies can not only lower costs through such practices but create value as well.

Reading 14, by Vijay Govindarajan and Chris Trimble, focuses on a topic of concern in the area of international strategies. The authors suggest that traditional approaches for entering emerging markets may not be appropriate for poor countries like India and China, where market needs are so different from those of rich countries that companies are advised to pursue "Reverse Innovation: A Global Growth Strategy That Could Pre-empt Disruption at Home." The next article, "How Emerging Giants Can Take on the World," focuses on the strategies of successful and ambitious companies headquartered in developing countries. The authors argue that the key to their continuing growth and success depends upon their ability to acquire needed capabilities and they propose a four-stage approach.

The next two readings complement and extend the material on corporate strategy presented in Chapter 8. Reading 16, "Why Conglomerates Thrive (Outside the U.S.)," describes the path to success taken by many widely diversified foreign companies. The next reading, "Diversification: Best Practices of the Leading Companies," describes the contrasting case of how successful diversifiers such as GE and McDonald's manage this aspect of their businesses.

Readings 18 and 19 deal with the core material found in Chapter 9. "Pragmatic Business Ethics," as its title suggests, takes on the topic of business ethics. It offers an approach for assessing and resolving ethical dilemmas in the gray areas of business ethics. Gary Hamel's piece, "Leaders as Stewards," urges managers to embrace the responsibility of stewardship and argues that what matters is the bedrock values of companies and their leaders.

The next six readings comprise a set of readings that cover various aspects concerning strategy execution. The first of these, also by Hamel and titled "Attract Top Talent: Become a Passion Multiplier," argues that to attract creative young workers and magnify their passions you need to reinvent your management practices to align with their expectations. The second, titled "Building Superior Capabilities for Strategic Sourcing," describes how firms can create more value by investing in capability-building in the purchasing domain.

Readings 22 and 23 link to the topical material found in Chapter 11. The point of the first of these is well captured by its title: "How Collaboration Technologies Are Improving Process, Workforce, and Business Performance." The second, "The ROI of Employee Recognition," complements the material of the first, showing how well-designed reward and recognition programs can also enhance company performance.

The last two readings were chosen to expand upon and complement the central themes of Chapter 12. As its title suggests, "The Critical Few: Components of a Truly Effective Culture" contends that a few key practices can make all the difference in building a performance-enhancing culture. In "How Strategists Lead," the closing article, corporate strategy expert Cynthia Montgomery reflects upon the unique value that strategic leaders can bring to their companies, thus providing a strong and thoughtful conclusion for a course on strategic management.

THE TWO STRATEGY SIMULATION SUPPLEMENTS: *THE BUSINESS STRATEGY GAME* AND *GLO-BUS*

The Business Strategy Game and *GLO-BUS: Developing Winning Competitive Strategies*—two competition-based strategy simulations that are delivered online and that feature automated processing and grading of performance—are being marketed by the publisher as companion supplements for use with the 20th edition (and other texts in the field).

- *The Business Strategy Game* is the world's most popular strategy simulation, having been used by over 2,500 instructors in courses involving approximately 750,000 students on 1,050+ university campuses in 60 countries.
- *GLO-BUS,* a somewhat simpler strategy simulation introduced in 2004, has been used by more than 1,450+ instructors in courses involving over 180,000 students at 640+ university campuses in 48+ countries.

How the Strategy Simulations Work

In both *The Business Strategy Game (BSG)* and *GLO-BUS,* class members are divided into teams of one to five persons and assigned to run a company that competes head-to-head against companies run by other class members.

- In *BSG,* team members run an athletic footwear company, producing and marketing both branded and private-label footwear.
- In *GLO-BUS,* team members operate a digital camera company that designs, assembles, and markets entry-level digital cameras and upscale, multifeatured cameras.

In both simulations, companies compete in a global market arena, selling their products in four geographic regions—Europe-Africa, North America, Asia-Pacific, and Latin America. Each management team is called upon to craft a strategy for their company and make decisions relating to plant operations, workforce compensation, pricing and marketing, social responsibility/citizenship, and finance.

Company co-managers are held accountable for their decision making. Each company's performance is scored on the basis of earnings per share, return-on-equity investment, stock price, credit rating, and image rating. Rankings of company performance, along with a wealth of industry and company statistics, are available to company co-managers after each decision round to use in making strategy adjustments and operating decisions for the next competitive round. You can be certain that the market environment, strategic issues, and operating challenges that company co-managers must contend with are *very tightly linked* to what your class members will be reading about in the text chapters. The circumstances that co-managers face in running their simulation company embrace the very concepts, analytical tools, and strategy options they encounter in the text chapters (this is something you can quickly confirm by skimming through some of the Exercises for Simulation Participants that appear at the end of each chapter).

We suggest that you schedule 1 or 2 practice rounds and anywhere from 4 to 10 regular (scored) decision rounds (more rounds are better than fewer rounds). Each decision round represents a year of company operations and will entail roughly two hours of time for company co-managers to complete. In traditional 13-week, semester-long courses, there is merit in scheduling one decision round per week. In courses that run 5 to 10 weeks, it is wise to schedule two decision rounds per week for the last several weeks of the term (sample course schedules are provided for courses of varying length and varying numbers of class meetings).

When the instructor-specified deadline for a decision round arrives, the simulation server automatically accesses the saved decision entries of each company, determines the competitiveness and buyer appeal of each company's product offering relative to the other companies being run by students in your class, and then awards sales and market shares to the competing companies, geographic region by geographic region. The unit sales volumes awarded to each company *are totally governed by:*

- How its prices compare against the prices of rival brands.
- How its product quality compares against the quality of rival brands.
- How its product line breadth and selection compare.
- How its advertising effort compares.
- And so on, for a total of 11 competitive factors that determine unit sales and market shares.

The competitiveness and overall buyer appeal of each company's product offering *in comparison to the product offerings of rival companies* is all-decisive—this algorithmic feature is what makes *BSG* and *GLO-BUS* "competition-based" strategy simulations. Once each company's sales and market shares are awarded based on the competitiveness of its respective overall product offering, the various company and industry reports detailing the outcomes of the decision round are then generated. Company co-managers can access the results of the decision round 15 to 20 minutes after the decision deadline.

The Compelling Case for Incorporating Use of a Strategy Simulation

There are *three exceptionally important benefits* associated with using a competition-based simulation in strategy courses taken by seniors and MBA students:

- *A three-pronged text-readings-simulation course model delivers significantly more teaching-learning power than the traditional text-readings model.* Using *both* readings and a strategy simulation to drill students in thinking strategically and applying what they read in the text chapters is a stronger, more effective means of helping them connect theory with practice and develop better business judgment. But what a competition-based strategy simulation does far better is thrust class members squarely into *an active, hands-on managerial role* where they are totally responsible for assessing market conditions, determining how to respond to the actions of competitors, forging a long-term direction and strategy for their company, and making all kinds of operating decisions. Because they are held fully accountable for their decisions and their company's performance, *co-managers are strongly motivated* to dig deeply into company operations, probe for ways to be more cost-efficient and competitive, and ferret out strategic moves and decisions calculated to boost company performance. *Consequently, incorporating both readings assignments and a strategy simulation to develop the skills of class members in thinking strategically and applying the concepts and tools of strategic analysis turns out to be more pedagogically powerful than relying solely on readings assignments—there's stronger retention of the lessons learned and better achievement of course learning objectives.*

  To provide you with quantitative evidence of the learning that occurs with using *The Business Strategy Game* or *GLO-BUS,* there is a built-in Learning Assurance Report showing how well each class member performs on nine skills/learning measures versus tens of thousands of students worldwide who have completed the simulation in the past 12 months.
- *The competitive nature of a strategy simulation arouses positive energy and steps up the whole tempo of the course by a notch or two.* Nothing sparks class excitement quicker or better than the concerted efforts on the part of class members at each decision round to achieve a high industry ranking and avoid the perilous

consequences of being outcompeted by other class members. Students really enjoy taking on the role of a manager, running their own company, crafting strategies, making all kinds of operating decisions, trying to outcompete rival companies, and getting immediate feedback on the resulting company performance. Lots of back-and-forth chatter occurs when the results of the latest simulation round become available and co-managers renew their quest for strategic moves and actions that will strengthen company performance. Co-managers become *emotionally invested* in running their company and figuring out what strategic moves to make to boost their company's performance. Interest levels climb. All this stimulates learning and causes students to see the practical relevance of the subject matter and the benefits of taking your course.

As soon as your students start to say "Wow! Not only is this fun but I am learning a lot," *which they will,* you have won the battle of engaging students in the subject matter and moved the value of taking your course to a much higher plateau in the business school curriculum. This translates into *a livelier, richer learning experience from a student perspective and better instructor-course evaluations.*

- *Use of a fully automated online simulation reduces the time instructors spend on course preparation, course administration, and grading.* Since the simulation exercise involves a 20- to 30-hour workload for student teams (roughly 2 hours per decision round times 10 to 12 rounds, plus optional assignments), simulation adopters often compensate by trimming the number of assigned readings from, say, 10 to 12 to perhaps 4 to 6. Not only does use of a simulation permit assigning fewer readings, but it also permits you to eliminate at least one assignment that entails considerable grading on your part. Grading one less essay exam or other written assignment saves enormous time. With *BSG* and *GLOBUS,* grading is effortless and takes only minutes; once you enter percentage weights for each assignment in your online grade book, a suggested overall grade is calculated for you. You'll be pleasantly surprised—and quite pleased—at how little time it takes to gear up for and administer *The Business Strategy Game* or *GLO-BUS.*

In sum, incorporating use of a strategy simulation turns out to be *a win–win proposition for both students and instructors.* Moreover, a very convincing argument can be made that a competition-based strategy simulation is *the single most effective teaching/learning tool that instructors can employ to teach the discipline of business and competitive strategy, to make learning more enjoyable, and to promote better achievement of course learning objectives.*

A Bird's-Eye View of *The Business Strategy Game*

The setting for *The Business Strategy Game (BSG)* is the global athletic footwear industry (there can be little doubt in today's world that a globally competitive strategy simulation is *vastly superior* to a simulation with a domestic-only setting). Global market demand for footwear grows at the rate of 7 to 9 percent annually for the first five years and 5 to 7 percent annually for the second five years. However, market growth rates vary by geographic region—North America, Latin America, Europe-Africa, and Asia-Pacific.

Companies begin the simulation producing branded and private-label footwear in two plants, one in North America and one in Asia. They have the option to establish production facilities in Latin America and Europe-Africa, either by constructing new plants or by buying previously constructed plants that have been sold by competing companies. Company co-managers exercise control over production costs on the basis of the styling and quality they opt to manufacture, plant location (wages and incentive compensation vary from region to region), the use of best practices and Six Sigma programs to reduce the production of defective footwear and to boost worker productivity, and compensation practices.

All newly produced footwear is shipped in bulk containers to one of four geographic distribution centers. All sales in a geographic region are made from footwear inventories in that region's distribution center. Costs at the four regional distribution centers are a function of inventory storage costs, packing and shipping fees, import tariffs paid on incoming pairs shipped from foreign plants, and exchange rate impacts. At the start of the simulation, import tariffs average $4 per pair in Europe-Africa, $6 per pair in Latin America, and $8 in the Asia-Pacific region. However, the Free Trade Treaty of the Americas allows tariff-free movement of footwear between North America and Latin America. Instructors have the option to alter tariffs as the game progresses.

Companies market their brand of athletic footwear to footwear retailers worldwide and to individuals buying online at the company's website. Each company's sales and market share in the branded footwear segments hinge on its competitiveness on 11 factors: attractive pricing, footwear styling and quality, product line breadth, advertising, use of mail-in rebates, appeal of celebrities endorsing a company's brand, success in convincing footwear retailers to carry its brand, number of weeks it takes to fill retailer orders, effectiveness of a company's online sales effort at its website, and customer loyalty. Sales of private-label footwear hinge solely on being the low-price bidder.

All told, company co-managers make as many as 53 types of decisions each period that cut across production operations (up to 10 decisions per plant, with a maximum of four plants), plant capacity additions/sales/upgrades (up to 6 decisions per plant), worker compensation and training (3 decisions per plant), shipping (up to 8 decisions per plant), pricing and marketing (up to 10 decisions in four geographic regions), bids to sign celebrities (2 decision entries per bid), financing of company operations (up to 8 decisions), and corporate social responsibility and environmental sustainability (up to 6 decisions).

Each time company co-managers make a decision entry, an assortment of on-screen calculations instantly shows the projected effects on unit sales, revenues, market shares, unit costs, profit, earnings per share, ROE, and other operating statistics. The on-screen calculations help team members evaluate the relative merits of one decision entry versus another and put together a promising strategy.

Companies can employ any of the five generic competitive strategy options in selling branded footwear—low-cost leadership, differentiation, best-cost provider, focused low cost, and focused differentiation. They can pursue essentially the same strategy worldwide or craft slightly or very different strategies for the Europe-Africa, Asia-Pacific, Latin America, and North America markets. They can strive for competitive advantage based on more advertising, a wider selection of models, more appealing styling/quality, bigger rebates, and so on.

Any well-conceived, well-executed competitive approach is capable of succeeding, provided it is not overpowered by the strategies of competitors or defeated by the presence of too many copycat strategies that dilute its effectiveness. The challenge for each company's management team is to craft and execute a competitive strategy that produces good performance on five measures: earnings per share, return on equity investment, stock price appreciation, credit rating, and brand image.

All activity for *The Business Strategy Game* takes place at **www.bsg-online.com**.

A Bird's-Eye View of *GLO-BUS*

The industry setting for *GLO-BUS* is the digital camera industry. Global market demand grows at the rate of 8 to 10 percent annually for the first five years and 4 to 6 percent annually for the second five years. Retail sales of digital cameras are seasonal, with about 20 percent of consumer demand coming in each of the first three quarters of each calendar year and 40 percent coming during the big fourth-quarter retailing season.

Companies produce entry-level and upscale, multifeatured cameras of varying designs and quality in a Taiwan assembly facility and ship assembled cameras directly to retailers in North America, Asia-Pacific, Europe-Africa, and Latin America. All cameras are assembled as retail orders come in and are shipped immediately upon completion of the assembly process—companies maintain no finished-goods inventories, and all parts and components are delivered on a just-in-time basis (which eliminates the need to track inventories and simplifies the accounting for plant operations and costs). Company co-managers exercise control over production costs on the basis of the designs and components they specify for their cameras, workforce compensation and training, the length of warranties offered (which affects warranty costs), the amount spent for technical support provided to buyers of the company's cameras, and their management of the assembly process.

Competition in each of the two product market segments (entry-level and multifeatured digital cameras) is based on 10 factors: price, camera performance and quality, number of quarterly sales promotions, length of promotions in weeks, size of the promotional discounts offered, advertising, number of camera models, size of the retail dealer network, warranty period, and amount/caliber of technical support provided to camera buyers. Low-cost leadership, differentiation strategies, best-cost provider strategies, and focus strategies are all viable competitive options. Rival companies can strive to be the clear market leader in either entry-level cameras or upscale multifeatured cameras or both. They can focus on one or two geographic regions or strive for geographic balance. They can pursue essentially the same strategy worldwide or craft slightly or very different strategies for the Europe-Africa, Asia-Pacific, Latin America, and North America markets. Just as with *The Business Strategy Game,* almost any well-conceived, well-executed competitive approach is capable of succeeding, *provided it is not overpowered by the strategies of competitors or defeated by the presence of too many copycat strategies that dilute its effectiveness.*

Company co-managers make 49 types of decisions each period, ranging from R&D, camera components, and camera performance (10 decisions) to production operations and worker compensation (15 decisions) to pricing and marketing (15 decisions) to the financing of company operations (4 decisions) to corporate social responsibility (5 decisions). *Each time participants make a decision entry, an assortment of on-screen calculations instantly shows the projected effects on unit sales, revenues, market shares, unit costs, profit, earnings per share, ROE, and other operating statistics. These on-screen calculations help team members evaluate the relative merits of one decision entry versus another and stitch the separate decisions into a cohesive and promising strategy.* Company performance is judged on five criteria: earnings per share, return on equity investment, stock price, credit rating, and brand image.

All activity for *GLO-BUS* occurs at **www.glo-bus.com**.

Administration and Operating Features of the Two Simulations

The Internet delivery and user-friendly designs of both *BSG* and *GLO-BUS* make them incredibly easy to administer, even for first-time users. And the menus and controls are so similar that you can readily switch between the two simulations or use one in your undergraduate class and the other in a graduate class. If you have not yet used either of the two simulations, you may find the following of particular interest:

- Setting up the simulation for your course is done online and takes about 10 to 15 minutes. Once setup is completed, no other administrative actions are required beyond those of moving participants to a different team (should the need arise) and monitoring the progress of the simulation (to whatever extent desired).
- Participant's Guides are delivered electronically to class members at the website—students can read the guide on their monitors or print out a copy, as they prefer.
- There are 2- to 4-minute Video Tutorials scattered throughout the software (including each decision screen and each page of each report) that provide on-demand guidance to class members who may be uncertain about how to proceed.
- Complementing the Video Tutorials are detailed and clearly written Help sections explaining "all there is to know" about (a) each decision entry and the relevant cause-effect relationships, (b) the information on each page of the Industry Reports, and (c) the numbers presented in the Company Reports. *The Video Tutorials and the Help screens allow company co-managers to figure things out for themselves, thereby curbing the need for students to ask the instructor "how things work."*
- Team members running the same company who are logged in simultaneously on different computers at different locations can click a button to enter Collaboration Mode, enabling them to work collaboratively from the same screen in viewing reports and making decision entries, and click a second button to enter Audio Mode, letting them talk to one another.
    - When in "Collaboration Mode," each team member sees the same screen at the same time as all other team members who are logged in and have joined Collaboration Mode. If one team member chooses to view a particular decision screen, that same screen appears on the monitors for all team members in Collaboration Mode.
    - Each team member controls their own color-coded mouse pointer (with their first-name appearing in a color-coded box linked to their mouse pointer) and can make a decision entry or move the mouse to point to particular on-screen items.
    - A decision entry change made by one team member is seen by all, in real time, and all team members can immediately view the on-screen calculations that result from the new decision entry.
    - If one team member wishes to view a report page and clicks on the menu link to the desired report, that same report page will immediately appear for the other team members engaged in collaboration.
    - Use of Audio Mode capability requires that each team member work from a computer with a built-in microphone (if they want to be heard by their team members) and speakers (so they may hear their teammates) or else have a headset with a microphone that they can plug into their desktop or laptop. A headset is recommended for best results, but most laptops now are equipped

with a built-in microphone and speakers that will support use of our new voice chat feature.

- ◦ Real-time VoIP audio chat capability among team members who have entered both the Audio Mode and the Collaboration Mode is a tremendous boost in functionality that enables team members to go online simultaneously on computers at different locations and conveniently and effectively collaborate in running their simulation company.
- ◦ In addition, instructors have the capability to join the online session of any company and speak with team members, thus circumventing the need for team members to arrange for and attend a meeting in the instructor's office. Using the standard menu for administering a particular industry, instructors can connect with the company desirous of assistance. Instructors who wish not only to talk but also to enter Collaboration (highly recommended because all attendees are then viewing the same screen) have a red-colored mouse pointer linked to a red box labeled Instructor.

Without a doubt, the Collaboration and Voice-Chat capabilities are hugely valuable for students enrolled in online and distance-learning courses where meeting face-to-face is impractical or time-consuming. Likewise, the instructors of online and distance-learning courses will appreciate having the capability to join the online meetings of particular company teams when their advice or assistance is requested.

- Both simulations are quite suitable for use in distance-learning or online courses (and are currently being used in such courses on numerous campuses).
- Participants and instructors are notified via e-mail when the results are ready (usually about 15 to 20 minutes after the decision round deadline specified by the instructor/game administrator).
- Following each decision round, participants are provided with a complete set of reports—a six-page Industry Report, a one-page Competitive Intelligence report for each geographic region that includes strategic group maps and bulleted lists of competitive strengths and weaknesses, and a set of Company Reports (income statement, balance sheet, cash flow statement, and assorted production, marketing, and cost statistics).
- Two "open-book" multiple-choice tests of 20 questions are built into each simulation. The quizzes, which you can require or not as you see fit, are taken online and automatically graded, with scores reported instantaneously to participants and automatically recorded in the instructor's electronic grade book. Students are automatically provided with three sample questions for each test.
- Both simulations contain a three-year strategic plan option that you can assign. Scores on the plan are automatically recorded in the instructor's online grade book.
- At the end of the simulation, you can have students complete online peer evaluations (again, the scores are automatically recorded in your online grade book).
- Both simulations have a Company Presentation feature that enables each team of company co-managers to easily prepare PowerPoint slides for use in describing their strategy and summarizing their company's performance in a presentation to either the class, the instructor, or an "outside" board of directors.
- *A Learning Assurance Report provides you with hard data concerning how well your students performed vis-à-vis students playing the simulation worldwide over the past 12 months.* The report is based on nine measures of student proficiency,

business know-how, and decision-making skill and can also be used in evaluating the extent to which your school's academic curriculum produces the desired degree of student learning insofar as accreditation standards are concerned.

For more details on either simulation, please consult Section 2 of the Instructor's Manual accompanying this text or register as an instructor at the simulation websites (**www.bsg-online.com** and **www.glo-bus.com**) to access even more comprehensive information. You should also consider signing up for one of the webinars that the simulation authors conduct several times each month (sometimes several times weekly) to demonstrate how the software works, walk you through the various features and menu options, and answer any questions. You have an open invitation to call the senior author of this text at (205) 722-9145 to arrange a personal demonstration or talk about how one of the simulations might work in one of your courses. We think you'll be quite impressed with the cutting-edge capabilities that have been programmed into *The Business Strategy Game* and *GLO-BUS,* the simplicity with which both simulations can be administered, and their exceptionally tight connection to the text chapters, core concepts, and standard analytical tools.

RESOURCES AND SUPPORT MATERIALS FOR THE 20TH EDITION

For Students

Key Points Summaries At the end of each chapter is a synopsis of the core concepts, analytical tools, and other key points discussed in the chapter. These chapter-end synopses, along with the core concept definitions and margin notes scattered throughout each chapter, help students focus on basic strategy principles, digest the messages of each chapter, and prepare for tests.

Two Sets of Chapter-End Exercises Each chapter concludes with two sets of exercises. The *Assurance of Learning Exercises* can be used as the basis for class discussion, oral presentation assignments, and short written reports. The *Exercises for Simulation Participants* are designed expressly for use by adopters who have incorporated use of a simulation and want to go a step further in tightly and explicitly connecting the chapter content to the simulation company their students are running. The questions in both sets of exercises (along with those Illustration Capsules that qualify as "mini-cases") can be used to round out the rest of a 75-minute class period should your lecture on a chapter last for only 50 minutes.

The Connect™ Management Web-Based Assignment and Assessment Platform Beginning with the 18th edition, we began taking advantage of the publisher's innovative Connect™ assignment and assessment platform and created several features that simplify the task of assigning and grading three types of exercises for students:

- There are self-scoring chapter tests consisting of 20 to 25 multiple-choice questions that students can take to measure their grasp of the material presented in each of the 12 chapters.

- There are two author-developed Interactive Application exercises for each of the 12 chapters that drill students in the use and application of the concepts and tools of strategic analysis.

All of the Connect™ exercises are automatically graded (with the exception of those exercise components that entail student entry of short-answer and/or essay answers), thereby simplifying the task of evaluating each class member's performance and monitoring the learning outcomes. The progress-tracking function built into the Connect™ Management system enables you to:

- View scored work immediately and track individual or group performance with assignment and grade reports.
- Access an instant view of student or class performance relative to learning objectives.
- Collect data and generate reports required by many accreditation organizations, such as AACSB.

LearnSmart and SmartBook TM LearnSmart is an adaptive study tool proven to strengthen memory recall, increase class retention, and boost grades. Students are able to study more efficiently because they are made aware of what they know and don't know. Real-time reports quickly identify the concepts that require more attention from individual students—or the entire class. SmartBook is the first and only adaptive reading experience designed to change the way students read and learn. It creates a personalized reading experience by highlighting the most impactful concepts a student needs to learn at that moment in time. As a student engages with SmartBook, the reading experience continuously adapts by highlighting content based on what the student knows and doesn't know. This ensures that the focus is on the content he or she needs to learn, while simultaneously promoting long-term retention of material. Use SmartBook's real-time reports to quickly identify the concepts that require more attention from individual students—or the entire class. The end result? Students are more engaged with course content, can better prioritize their time, and come to class ready to participate.

For Instructors

Instructor Library The Connect Management Instructor Library is your repository for additional resources to improve student engagement in and out of class. You can select and use any asset that enhances your lecture.

Instructor's Manual The accompanying IM contains:

- A section on suggestions for organizing and structuring your course.
- Sample syllabi and course outlines.
- A set of lecture notes on each chapter.
- Answers to the chapter-end Assurance of Learning Exercises.
- A copy of the test bank.
- Discussion questions and suggested answers for the readings.

Test Bank and EZ Test Online There is a test bank containing over 900 multiple-choice questions and short-answer/essay questions. It has been tagged with

AACSB and Bloom's Taxonomy criteria. All of the test bank questions are also accessible within a computerized test bank powered by McGraw-Hill's flexible electronic testing program, EZ Test Online (www.eztestonline.com). Using EZ Test Online allows you to create paper and online tests or quizzes. With EZ Test Online, instructors can select questions from multiple McGraw-Hill test banks or author their own and then either print the test for paper distribution or give it online.

PowerPoint Slides To facilitate delivery preparation of your lectures and to serve as chapter outlines, you'll have access to approximately 500 colorful and professional-looking slides displaying core concepts, analytical procedures, key points, and all the figures in the text chapters.

***The Business Strategy Game* and *GLO-BUS* Online Simulations** Using one of the two companion simulations is a powerful and constructive way of emotionally connecting students to the subject matter of the course. We know of no more effective way to arouse the competitive energy of students and prepare them for the challenges of real-world business decision making than to have them match strategic wits with classmates in running a company in head-to-head competition for global market leadership.

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As always, we value your recommendations and thoughts about the book. Your comments regarding coverage and contents will be taken to heart, and we always are grateful for the time you take to call our attention to printing errors, deficiencies, and other shortcomings. Please e-mail us at **athompso@cba.ua.edu**, **margaret.a.peteraf@tuck.dartmouth.edu**, **john.gamble@tamucc.edu**, or **astrickl@cba.ua.edu**.

Arthur A. Thompson

Margaret A. Peteraf

John E. Gamble

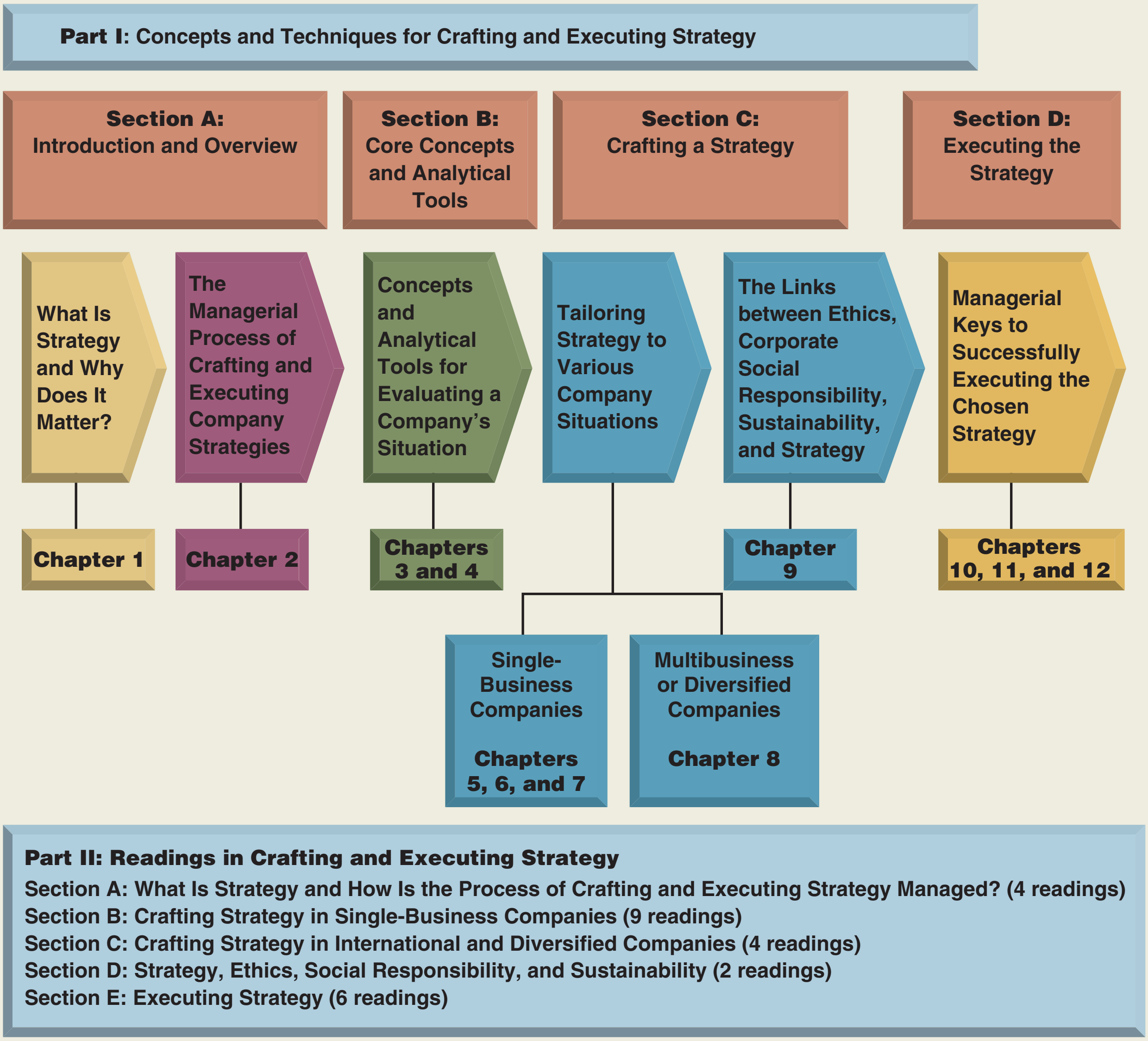
A. J. Strickland

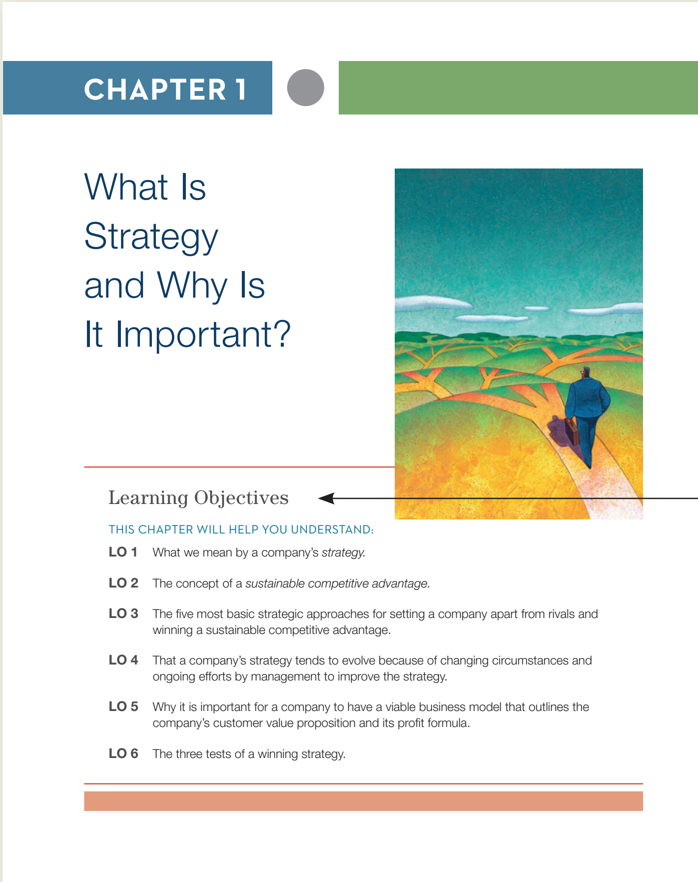
Crafting and Executing Strategy

Concepts and Readings

GUIDED TOUR

Chapter Structure and Organization





CHAPTER 1

What Is Strategy and Why Is It Important?

Learning Objectives

THIS CHAPTER WILL HELP YOU UNDERSTAND:

LO 1 What we mean by a company's *strategy.*

LO 2 The concept of a *sustainable competitive advantage.*

LO 3 The five most basic strategic approaches for setting a company apart from rivals and winning a sustainable competitive advantage.

LO 4 That a company's strategy tends to evolve because of changing circumstances and ongoing efforts by management to improve the strategy.

LO 5 Why it is important for a company to have a viable business model that outlines the company's customer value proposition and its profit formula.

LO 6 The three tests of a winning strategy.

Learning Objectives are listed at the beginning of each chapter; corresponding numbered indicators in the margins show where learning objectives are covered in the text.

Illustration Capsules appear in boxes throughout each chapter to provide in-depth examples, connect the text presentation to real-world companies, and convincingly demonstrate "strategy in action." Some are appropriate for use as mini-cases.

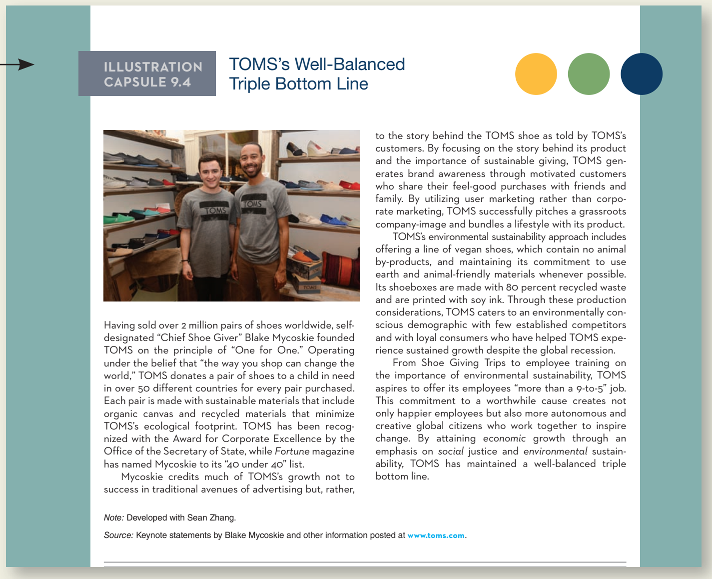


ILLUSTRATION CAPSULE 9.4

TOMS's Well-Balanced Triple Bottom Line

Having sold over 2 million pairs of shoes worldwide, self-designated "Chief Shoe Giver" Blake Mycoskie founded TOMS on the principle of "One for One." Operating under the belief that "the way you shop can change the world," TOMS donates a pair of shoes to a child in need in over 50 different countries for every pair purchased. Each pair is made with sustainable materials that include organic canvas and recycled materials that minimize TOMS's ecological footprint. TOMS has been recognized with the Award for Corporate Excellence by the Office of the Secretary of State, while *Fortune* magazine has named Mycoskie to its "40 under 40" list.

Mycoskie credits much of TOMS's growth not to success in traditional avenues of advertising but, rather, to the story behind the TOMS shoe as told by TOMS's customers. By focusing on the story behind its product and the importance of sustainable giving, TOMS generates brand awareness through motivated customers who share their feel-good purchases with friends and family. By utilizing user marketing rather than corporate marketing, TOMS successfully pitches a grassroots company-image and bundles a lifestyle with its product.

TOMS's environmental sustainability approach includes offering a line of vegan shoes, which contain no animal by-products, and maintaining its commitment to use earth and animal-friendly materials whenever possible. Its shoeboxes are made with 80 percent recycled waste and are printed with soy ink. Through these production considerations, TOMS caters to an environmentally conscious demographic with few established competitors and with loyal consumers who have helped TOMS experience sustained growth despite the global recession.

From Shoe Giving Trips to employee training on the importance of environmental sustainability, TOMS aspires to offer its employees "more than a 9-to-5" job. This commitment to a worthwhile cause creates not only happier employees but also more autonomous and creative global citizens who work together to inspire change. By attaining *economic* growth through an emphasis on *social* justice and *environmental* sustainability, TOMS has maintained a well-balanced triple bottom line.

Note: Developed with Sean Zhang.

Source: Keynote statements by Blake Mycoskie and other information posted at www.toms.com.

LO 4

The concepts of corporate social responsibility and environmental sustainability and how companies balance these duties with economic responsibilities to shareholders.

The idea that businesses have an obligation to foster social betterment, a much-debated topic over the past 50 years, took root in the 19th century when progressive companies in the aftermath of the industrial revolution began to provide workers with housing and other amenities. The notion that corporate executives should balance the interests of all stakeholders—shareholders, employees, customers, suppliers, the communities in which they operate, and society at large—began to blossom in the 1960s. Some years later, a group of chief executives of America's 200 largest corporations, calling themselves the Business Roundtable, came out in strong support of the concept of **corporate social responsibility (CSR):**

> Balancing the shareholder's expectations of maximum return against other priorities is one of the fundamental problems confronting corporate management. The shareholder must receive a good return but the legitimate concerns of other constituencies (customers, employees, communities, suppliers and society at large) also must have the appropriate attention. . . . [Leading managers] believe that by giving enlightened consideration to balancing the legitimate claims of all its constituents, a corporation will best serve the interest of its shareholders.

Today, corporate social responsibility is a concept that resonates in western Europe, the United States, Canada, and such developing nations as Brazil and India.

CORE CONCEPT

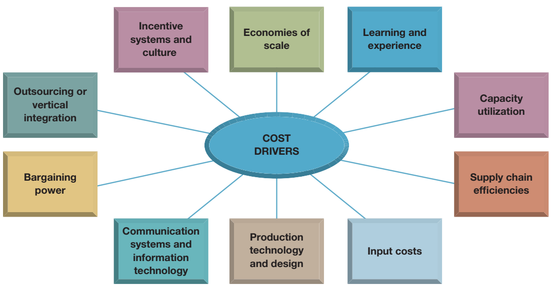
Corporate social responsibility (CSR) refers to a company's *duty* to operate in an honorable manner, provide good working conditions for employees, encourage workforce diversity, be a good steward of the environment, and actively work to better the quality of life in the local communities where it operates and in society at large.

Margin Notes define core concepts and call attention to important ideas and principles.

The Concepts of Corporate Social Responsibility and Good Corporate Citizenship

The essence of socially responsible business behavior is that a company should balance strategic actions to benefit shareholders against the *duty* to be a good corporate citizen. The underlying thesis is that company managers should display a *social conscience* in operating the business and specifically take into account how management decisions and company actions affect the well-being of employees, local communities, the environment, and society at large.[20] Acting in a socially responsible manner thus encompasses more than just participating in community service projects and donating money to charities and other worthy causes. Demonstrating

FIGURE 5.2 Cost Drivers: The Keys to Driving Down Company Costs



Source: Adapted from M. Porter, *Competitive Advantage: Creating and Sustaining Competitive Advantage* (New York: Free Press, 1985).

Figures scattered throughout the chapters provide conceptual and analytical frameworks.

2. *Taking full advantage of experience- and learning-curve effects.* The cost of performing an activity can decline over time as the learning and experience of company personnel build. Learning and experience economies can stem from debugging and mastering newly introduced technologies, using workers' experiences and suggestions to install more efficient plant layouts and assembly procedures, and repeatedly picking sites for and building new plants, retail outlets, or distribution centers—gaining speed and greater effectiveness in the process.

KEY POINTS

1. Deciding which of the five generic competitive strategies to employ—overall low cost, broad differentiation, focused low cost, focused differentiation, or best cost—is perhaps the most important strategic commitment a company makes. It tends to drive the remaining strategic actions a company undertakes and sets the whole tone for pursuing a competitive advantage over rivals.
2. In employing a low-cost provider strategy and trying to achieve a low-cost advantage over rivals, a company must do a better job than rivals of cost-effectively managing value chain activities and/or it must find innovative ways to eliminate cost-producing activities. An effective use of cost drivers is key. Low-cost provider strategies work particularly well when price competition is strong and the products of rival sellers are virtually identical, when there are not many ways to differentiate, when buyers are price-sensitive or have the power to bargain down prices, when buyer switching costs are low, and when industry newcomers are likely to use a low introductory price to build market share.
3. Broad differentiation strategies seek to produce a competitive edge by incorporating attributes that set a company's product or service offering apart from rivals in ways that buyers consider valuable and worth paying for. This depends on the appropriate use of value drivers. Successful differentiation allows a firm to (1) command a premium price for its product, (2) increase unit sales (if additional buyers are won over by the differentiating features), and/or (3) gain buyer loyalty to its brand (because some buyers are strongly attracted to the differentiating

Key Points at the end of each chapter provide a handy summary of essential ideas and things to remember.

EXERCISE FOR SIMULATION PARTICIPANTS

1. Is your company's strategy ethical? Why or why not? Is there anything that your company has done or is now doing that could legitimately be considered "shady" by your competitors? **LO 1**
2. In what ways, if any, is your company exercising corporate social responsibility? What are the elements of your company's CSR strategy? Are there any changes to this strategy that you would suggest? **LO 4**
3. If some shareholders complained that you and your co-managers have been spending too little or too much on corporate social responsibility, what would you tell them? **LO 3, LO 4**
4. Is your company striving to conduct its business in an environmentally sustainable manner? What specific *additional* actions could your company take that would make an even greater contribution to environmental sustainability? **LO 4**
5. In what ways is your company's environmental sustainability strategy in the best long-term interest of shareholders? Does it contribute to your company's competitive advantage or profitability? **LO 4**

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Exercises at the end of each chapter, linked to learning objectives, provide a basis for class discussion, oral presentations, and written assignments. Several chapters have exercises that qualify as mini-cases.

The 25 readings in this edition are flush with practical examples and valuable lessons for students of the art and science of crafting and executing strategy. There are two or three readings for each chapter—all chosen with three criteria in mind: relevance, readability, and recency of publication.

READING 09

Are You Ready for the Digital Value Chain?

Rüdiger Stern
Accenture

Matthias Ziegler
Accenture

Music, books, art, maps, the ways we communicate—these and countless other things that used to be primarily physical or analog are now digital as well, and that has changed the ways we live, work, learn and play. But that is just the tip of the iceberg. Today, technology is enabling the digitization of almost everything—even manufacturing. Want your own special protective case for your mobile phone? One device manufacturer has made available digital files that will let consumers design a custom case for their phone, then have the case made on a 3D printer.

In fact, innovative examples of digitization are arising across the entire corporate value chain—not just manufacturing but also new-product development, sourcing, marketing, distribution and service (see chart). Sooner or later, every company will have to deal with the impact of digitization on its business model. Innovative digital solutions can reduce costs and add value at every stage of a product's lifecycle, both within each stage of the value chain and across its entirety. Digitization enables businesses and governments to operate with greater transparency and efficiency, and it boosts consumers' access to everything from innovative products to public services.

Although the focus of media reports is often on specific examples of digitization, it is essential for businesses to see the bigger picture—the truly revolutionary possibilities available by harnessing the synergies of a fully integrated digital value chain. Companies also now need to see data management as a core competence. In the digital age, data is a strategic asset. A company's data must be able to yield the relevant information for improved or new products and services across intelligent, digital networks.

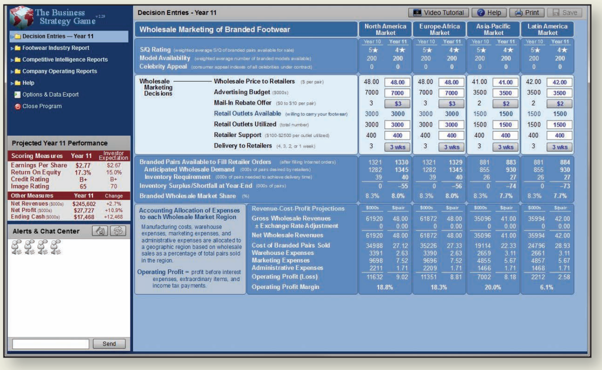
INNOVATIVE APPLICATIONS ACROSS THE DIGITAL VALUE CHAIN

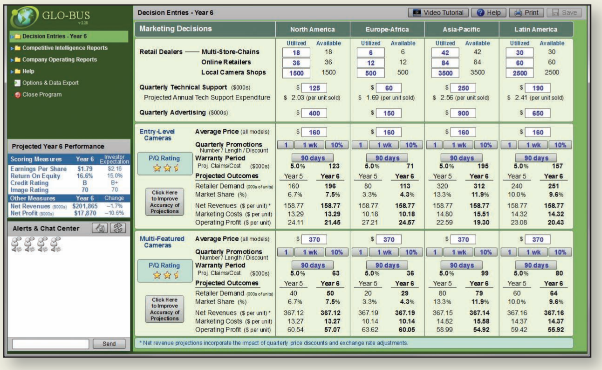
How is digitization altering specific steps in the value chain, and even optimizing the makeup of the chain itself? The marketplace is seeing vibrant innovation in many specific areas; the next step will be to integrate these one-off innovations to help create an end-to-end digital value chain that creates unparalleled business opportunities.

Sourcing and Procurement: eKanban

Kanban is a scheduling system for lean and just-in-time production. For decades, Kanban has been helping companies keep inventories low by ensuring that goods and equipment arrive just before a production run begins. Today, electronic Kanban (eKanban) uses the Internet to route messages to external suppliers, providing real-time visibility into the entire supply chain. These methods can lead to a host of benefits, including lower inventory stock levels, less physical transportation, a reduction in working capital and increased liquidity.

Auto manufacturer BMW implemented an eKanban system together with Lear Corp., a supplier of car seats. Based on BMW's daily demand and supported by an enterprise resource planning





***The Business Strategy Game* or *GLO-BUS* Simulation Exercises** Either one of these text supplements involves teams of students managing companies in a head-to-head contest for global market leadership. Company co-managers have to make decisions relating to product quality, production, workforce compensation and training, pricing and marketing, and financing of company operations. The challenge is to craft and execute a strategy that is powerful enough to deliver good financial performance despite the competitive efforts of rival companies. Each company competes in America, Latin America, Europe-Africa, and Asia-Pacific.

Crafting and Executing Strategy

Concepts and Readings

BRIEF CONTENTS

PART 1 Concepts and Techniques for Crafting and Executing Strategy

PART 2 Readings in Crafting and Executing Strategy

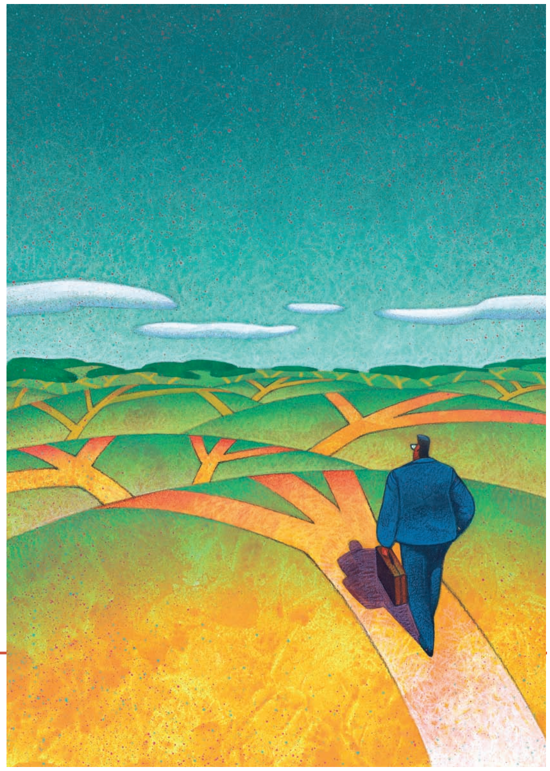
CONTENTS

PART 1

Concepts and Techniques for Crafting and Executing Strategy

CHAPTER 1

What Is Strategy and Why Is It Important?



Learning Objectives

THIS CHAPTER WILL HELP YOU UNDERSTAND:

LO 1 What we mean by a company's *strategy.*

LO 2 The concept of a *sustainable competitive advantage.*

LO 3 The five most basic strategic approaches for setting a company apart from rivals and winning a sustainable competitive advantage.

LO 4 That a company's strategy tends to evolve because of changing circumstances and ongoing efforts by management to improve the strategy.

LO 5 Why it is important for a company to have a viable business model that outlines the company's customer value proposition and its profit formula.

LO 6 The three tests of a winning strategy.

Strategy is about making choices, trade-offs; it's about deliberately choosing to be different.

Michael Porter – *Professor and Consultant*

If your firm's strategy can be applied to any other firm, you don't have a very good one.

David J. Collis and Michael G. Rukstad
– *Consultants and Professors*

If you don't have a competitive advantage, don't compete.

Jack Welch – *Former CEO of General Electric*

According to *The Economist,* a leading publication on business, economics, and international affairs, "In business, strategy is king. Leadership and hard work are all very well and luck is mighty useful, but it is strategy that makes or breaks a firm."[1] Luck and circumstance can explain why some companies are blessed with initial, short-lived success. But only a well-crafted, well-executed, constantly evolving strategy can explain why an elite set of companies somehow manages to rise to the top and stay there, year after year, pleasing their customers, shareholders, and other stakeholders alike in the process. Companies such as ExxonMobil, IBM, Southwest Airlines, FedEx, Google, Apple, Coca-Cola, Procter & Gamble, McDonald's, and Berkshire Hathaway come to mind—but long-lived success is not just the province of U.S. companies. Diverse kinds of companies, both large and small, from many different countries have been able to sustain strong performance records, including Russia's Gazprom (in energy), Korea's Samsung (in electronics), Singapore Airlines, Sweden's IKEA (in home furnishings), Mexico's America Movil (in telecommunications), and Japan's Toyota Motor.

In this opening chapter, we define the concept of strategy and describe its many facets. We explain what is meant by a competitive advantage, discuss the relationship between a company's strategy and its business model, and introduce you to the kinds of competitive strategies that can give a company an advantage over rivals in attracting customers and earning above-average profits. We look at what sets a winning strategy apart from others and why the caliber of a company's strategy determines whether the company will enjoy a competitive advantage over other firms. By the end of this chapter, you will have a clear idea of why the tasks of crafting and executing strategy are core management functions and why excellent execution of an excellent strategy is the most reliable recipe for turning a company into a standout performer over the long term.

WHAT DO WE MEAN BY *STRATEGY*?

A company's **strategy** is the set of actions that its managers take to outperform the company's competitors and achieve superior profitability. The objective of a well-crafted strategy is not merely temporary competitive success and profits in the short run, but rather the sort of lasting success that can support growth and secure the

CORE CONCEPT

A company's **strategy** is the set of actions that its managers take to outperform the company's competitors and achieve superior profitability.

company's future over the long term. Achieving this entails making a managerial commitment to a coherent array of well-considered choices about how to compete.[2] These include choices about:

- *How* to attract and please customers.
- *How* to compete against rivals.
- *How* to position the company in the marketplace and capitalize on attractive opportunities to grow the business.
- *How* to respond to changing economic and market conditions.
- *How* to manage each functional piece of the business (R&D, supply chain activities, production, sales and marketing, distribution, finance, and human resources).
- *How* to achieve the company's performance targets.

LO 1

What we mean by a company's *strategy.*

In most industries, companies have considerable freedom in choosing the *hows* of strategy.[3] Thus some companies strive to achieve lower costs than rivals, while others aim for product superiority or more personalized customer service or enhanced quality dimensions that rivals cannot match. Some companies opt for wide product lines, while others concentrate their energies on a narrow product lineup. Some competitors deliberately confine their operations to local or regional markets; others opt to compete nationally, internationally (several countries), or globally (all or most of the major country markets worldwide).

Strategy Is about Competing Differently

Mimicking the strategies of successful industry rivals—with either copycat product offerings or maneuvers to stake out the same market position—rarely works. Rather, every company's strategy needs to have some distinctive element that draws in customers and produces a competitive edge. Strategy, at its essence, is about competing differently—doing what rival firms *don't* do or what rival firms *can't* do.[4] This does not mean that the key elements of a company's strategy have to be 100 percent different, but rather that they must differ in at least *some important respects.* A strategy stands a better chance of succeeding when it is predicated on actions, business approaches, and competitive moves aimed at (1) appealing to buyers in ways that *set a company apart from its rivals* and (2) staking out a market position that is not crowded with strong competitors.

Strategy is about competing differently from rivals—doing what competitors *don't* do or, even better, doing what they *can't* do!

A company's strategy provides direction and guidance, in terms of not only what the company *should* do but also what it *should not* do. Knowing what not to do can be as important as knowing what to do, strategically. At best, making the wrong strategic moves will prove a distraction and a waste of company resources. At worst, it can bring about unintended long-term consequences that put the company's very survival at risk.

Figure 1.1 illustrates the broad types of actions and approaches that often characterize a company's strategy in a particular business or industry. For a more concrete example of the specific actions constituting a firm's strategy, see Illustration Capsule 1.1, describing Starbucks's strategy in the specialty coffee market.

LO 2

The concept of a *sustainable competitive advantage.*

Strategy and the Quest for Competitive Advantage

The heart and soul of any strategy are the actions and moves in the marketplace that managers are taking to gain a competitive advantage over rivals. A company achieves a competitive advantage whenever it has some type of edge over rivals in attracting buyers and coping with competitive forces. There are many routes to competitive advantage, but they all involve either giving buyers what they perceive as superior value

FIGURE 1.1 Identifying a Company's Strategy—What to Look For

compared to the offerings of rival sellers or giving buyers the same value as others at a lower cost to the firm. Superior value can mean a good product at a lower price, a superior product that is worth paying more for, or a best-value offering that represents an attractive combination of price, features, quality, service, and other attributes. Delivering superior value or delivering value more efficiently—whatever form it takes—nearly always requires performing value chain activities differently than rivals do and building competencies and resource capabilities that are not readily matched. In Illustration Capsule 1.1, it's evident that Starbucks has gained a competitive advantage over its rivals in the coffee shop industry through its efforts to create an upscale experience for coffee drinkers by catering to individualized tastes, enhancing the atmosphere and comfort of the shops, and delivering a premium product produced under environmentally sound, Fair Trade practices. By differentiating itself in this manner from other coffee purveyors, Starbucks has been able to charge prices for its coffee that are well above those of its rivals and far exceed the low cost of its inputs. Its expansion policies have allowed the company to make it easy for customers to find a Starbucks shop almost anywhere, further enhancing the brand and cementing customer loyalty. A creative *distinctive* strategy such as that used by Starbucks is a company's most reliable ticket for developing a competitive advantage over its rivals. If a strategy is not distinctive, then there can be no competitive advantage, since no firm would be meeting customer needs better or operating more efficiently than any other.

ILLUSTRATION CAPSULE 1.1

Starbucks's Strategy in the Coffeehouse Market

Since its founding in 1985 as a modest nine-store operation in Seattle, Washington, Starbucks had become the premier roaster and retailer of specialty coffees in the world, with over 18,800 store locations as of April 2013. In fiscal 2013, its annual sales were expected to exceed $15 billion—an all-time high for revenues and net earnings. The key elements of Starbucks's strategy in the coffeehouse industry included:

- *Train "baristas" to serve a wide variety of specialty coffee drinks that allow customers to satisfy their individual preferences in a customized way.* Starbucks essentially brought specialty coffees, such as cappuccinos, lattes, and macchiatos, to the mass market in the United States, encouraging customers to personalize their coffee-drinking habits. Requests for such items as an "Iced Grande Hazelnut Macchiato with Soy Milk, and *no* Hazelnut Drizzle" could be served up quickly with consistent quality.
- *Emphasize store ambience and elevation of the customer experience at Starbucks stores.* Starbucks's management viewed each store as a billboard for the company and as a contributor to building the company's brand and image. The company went to great lengths to make sure the store fixtures, the merchandise displays, the artwork, the music, and the aromas all blended to create an inviting environment that evoked the romance of coffee and signaled the company's passion for coffee. Free Wi-Fi drew those who needed a comfortable place to work while they had their coffee.
- *Purchase and roast only top-quality coffee beans.* The company purchased only the highest-quality arabica beans and carefully roasted coffee to exacting standards of quality and flavor. Starbucks did not use chemicals or artificial flavors when preparing its roasted coffees.
- *Foster commitment to corporate responsibility.* Starbucks was protective of the environment and contributed positively to the communities where Starbucks stores were located. In addition, Starbucks promoted Fair Trade practices and paid above-market prices for coffee beans to provide its growers and suppliers with sufficient funding to sustain their operations and provide for their families.
- *Expand the number of Starbucks stores domestically and internationally.* Starbucks operated stores in high-traffic, high-visibility locations in the United States and abroad. The company's ability to vary store size and format made it possible to locate stores in settings such as downtown and suburban shopping areas, office buildings, and university campuses. The company also focused on making Starbucks a global brand, expanding its reach to more than 60 countries in 2013.

- *Broaden and periodically refresh in-store product offerings.* Noncoffee products by Starbucks included teas, fresh pastries and other food items, candy, juice drinks, music CDs, and coffee mugs and coffee accessories.
- *Fully exploit the growing power of the Starbucks name and brand image with out-of-store sales.* Starbucks's Consumer Packaged Goods division included domestic and international sales of Frappuccino, coffee ice creams, and Starbucks coffees.

Source: Company documents, 10-Ks, and information posted on Starbucks's website.

If a company's competitive edge holds promise for being *sustainable* (as opposed to just temporary), then so much the better for both the strategy and the company's future profitability. What makes a competitive advantage **sustainable** (or durable), as opposed to temporary, are elements of the strategy that give buyers lasting reasons to prefer a company's products or services over those of competitors—*reasons that competitors are unable to nullify or overcome despite their best efforts*. In the case of Starbucks, the company's unparalleled name recognition, its reputation for high-quality specialty coffees served in a comfortable, inviting atmosphere, and the accessibility of the shops make it difficult for competitors to weaken or overcome Starbucks's competitive advantage. Not only has Starbucks's strategy provided the company with a sustainable competitive advantage, but it has made Starbucks one of the most admired companies on the planet.

CORE CONCEPT

A company achieves a **competitive advantage** when it provides buyers with superior value compared to rival sellers or offers the same value at a lower cost to the firm. The advantage is **sustainable** if it persists despite the best efforts of competitors to match or surpass this advantage.

Five of the most frequently used and dependable strategic approaches to setting a company apart from rivals, building strong customer loyalty, and winning a competitive advantage are:

LO 3

The five most basic strategic approaches for setting a company apart from rivals and winning a sustainable competitive advantage.

1. *A low-cost provider strategy*—achieving a cost-based advantage over rivals. Walmart and Southwest Airlines have earned strong market positions because of the low-cost advantages they have achieved over their rivals. Low-cost provider strategies can produce a durable competitive edge when rivals find it hard to match the low-cost leader's approach to driving costs out of the business.
2. *A broad differentiation strategy*—seeking to differentiate the company's product or service from that of rivals in ways that will appeal to a broad spectrum of buyers. Successful adopters of differentiation strategies include Apple (innovative products), Johnson & Johnson in baby products (product reliability), LVMH (luxury and prestige), and BMW (engineering design and performance). One way to sustain this type of competitive advantage is to be sufficiently innovative to thwart the efforts of clever rivals to copy or closely imitate the product offering.
3. *A focused low-cost strategy*—concentrating on a narrow buyer segment (or market niche) and outcompeting rivals by having lower costs and thus being able to serve niche members at a lower price. Private-label manufacturers of food, health and beauty products, and nutritional supplements use their low-cost advantage to offer supermarket buyers lower prices than those demanded by producers of branded products.
4. *A focused differentiation strategy*—concentrating on a narrow buyer segment and outcompeting rivals by offering buyers customized attributes that meet their specialized needs and tastes better than rivals' products. Lululemon, for example, specializes in high-quality yoga clothing and the like, attracting a devoted set of buyers in the process. Jiffy Lube International in quick oil changes, McAfee in virus protection software, and The Weather Channel in cable TV provide some other examples of this strategy.
5. *A best-cost provider strategy*—giving customers more value for the money by satisfying their expectations on key quality features, performance, and/or service attributes while beating their price expectations. This approach is a hybrid strategy that blends elements of low-cost provider and differentiation strategies; the aim is to have lower costs than rivals while simultaneously offering better differentiating attributes. Target is an example of a company that is known for its hip product design (a reputation it built by featuring cheap-chic designers such as Isaac Mizrahi), as well as a more appealing shopping ambience for discount store shoppers. Its dual focus on low costs as well as differentiation shows how a best-cost provider strategy can offer customers great value for the money.

Winning a *sustainable* competitive edge over rivals with any of the preceding five strategies generally hinges as much on building competitively valuable expertise and capabilities that rivals cannot readily match as it does on having a distinctive product offering. Clever rivals can nearly always copy the attributes of a popular product or service, but for rivals to match the experience, know-how, and specialized capabilities that a company has developed and perfected over a long period of time is substantially harder to do and takes much longer. FedEx, for example, has superior capabilities in next-day delivery of small packages, while Google is known for its Internet search capabilities. Apple has demonstrated impressive product innovation capabilities in digital music players, smartphones, and e-readers. Hyundai has become the world's fastest-growing automaker as a result of its advanced manufacturing processes and unparalleled quality control system. Each of these capabilities has proved hard for competitors to imitate or best.

LO 4

A company's strategy tends to evolve because of changing circumstances and ongoing efforts by management to improve the strategy.

Why a Company's Strategy Evolves over Time

The appeal of a strategy that yields a sustainable competitive advantage is that it offers the potential for an enduring edge over rivals. However, managers of every company must be willing and ready to modify the strategy in response to changing market conditions, advancing technology, unexpected moves by competitors, shifting buyer needs, emerging market opportunities, and new ideas for improving the strategy. Most of the time, a company's strategy evolves incrementally as management fine-tunes various pieces of the strategy and adjusts the strategy in response to unfolding events.[5] However, on occasion, major strategy shifts are called for, such as when the strategy is clearly failing or when industry conditions change in dramatic ways. Industry environments characterized by high-velocity change require companies to repeatedly adapt their strategies.[6] For example, companies in industries with rapid-fire advances in technology like medical equipment, electronics, and wireless devices often find it essential to adjust key elements of their strategies several times a year, sometimes even finding it necessary to "reinvent" their approach to providing value to their customers.

Changing circumstances and ongoing management efforts to improve the strategy cause a company's strategy to evolve over time—a condition that makes the task of crafting strategy a *work in progress,* not a one-time event.

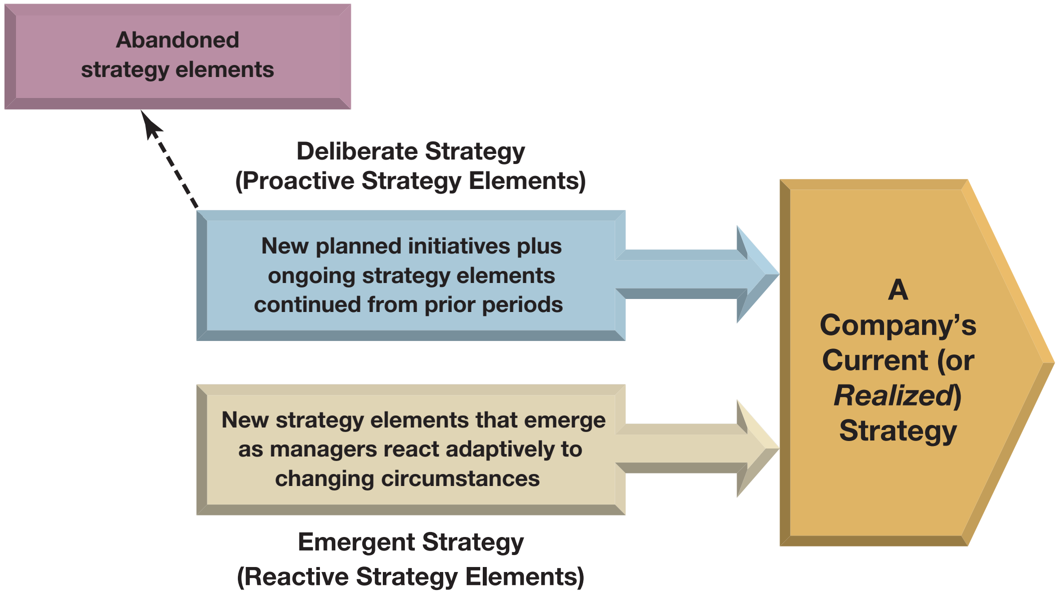
Regardless of whether a company's strategy changes gradually or swiftly, the important point is that the task of crafting strategy is not a one-time event but always a work in progress. Adapting to new conditions and constantly evaluating what is working well enough to continue and what needs to be improved are normal parts of the strategy-making process, resulting in an *evolving strategy.*[7]

A Company's Strategy Is Partly Proactive and Partly Reactive

A company's strategy is shaped partly by management analysis and choice and partly by the necessity of adapting and learning by doing.

The evolving nature of a company's strategy means that the typical company strategy is a blend of (1) *proactive,* planned initiatives to improve the company's financial performance and secure a competitive edge and (2) *reactive* responses to unanticipated developments and fresh market conditions. The biggest portion of a company's current strategy flows from previously initiated actions that have proven themselves in the marketplace and newly launched initiatives aimed at edging out rivals and boosting financial performance. This part of management's action plan for running the company is its **deliberate strategy,** consisting of proactive strategy

FIGURE 1.2 A Company's Strategy Is a Blend of Proactive Initiatives and Reactive Adjustments



elements that are both planned and realized as planned (while other planned strategy elements may not work out and are abandoned in consequence)—see Figure 1.2.[8]

But managers must always be willing to supplement or modify the proactive strategy elements with as-needed reactions to unanticipated conditions. Inevitably, there will be occasions when market and competitive conditions take an unexpected turn that calls for some kind of strategic reaction. Hence, *a portion of a company's strategy is always developed on the fly,* coming as a response to fresh strategic maneuvers on the part of rival firms, unexpected shifts in customer requirements, fast-changing technological developments, newly appearing market opportunities, a changing political or economic climate, or other unanticipated happenings in the surrounding environment. These adaptive strategy adjustments make up the firm's **emergent strategy.** A company's strategy *in toto* (its **realized strategy**) thus tends to be a *combination* of proactive and reactive elements, with certain strategy elements being *abandoned* because they have become obsolete or ineffective. A company's realized strategy can be observed in the pattern of its actions over time, which is a far better indicator than any of its strategic plans on paper or any public pronouncements about its strategy.

CORE CONCEPT

A company's **deliberate strategy** consists of *proactive* strategy elements that are planned; its **emergent strategy** consists of *reactive* strategy elements that emerge as changing conditions warrant.

A COMPANY'S STRATEGY AND ITS BUSINESS MODEL

At the core of every sound strategy is the company's **business model.** A business model is management's blueprint for delivering a valuable product or service to customers in a manner that will generate revenues sufficient to cover costs and yield an