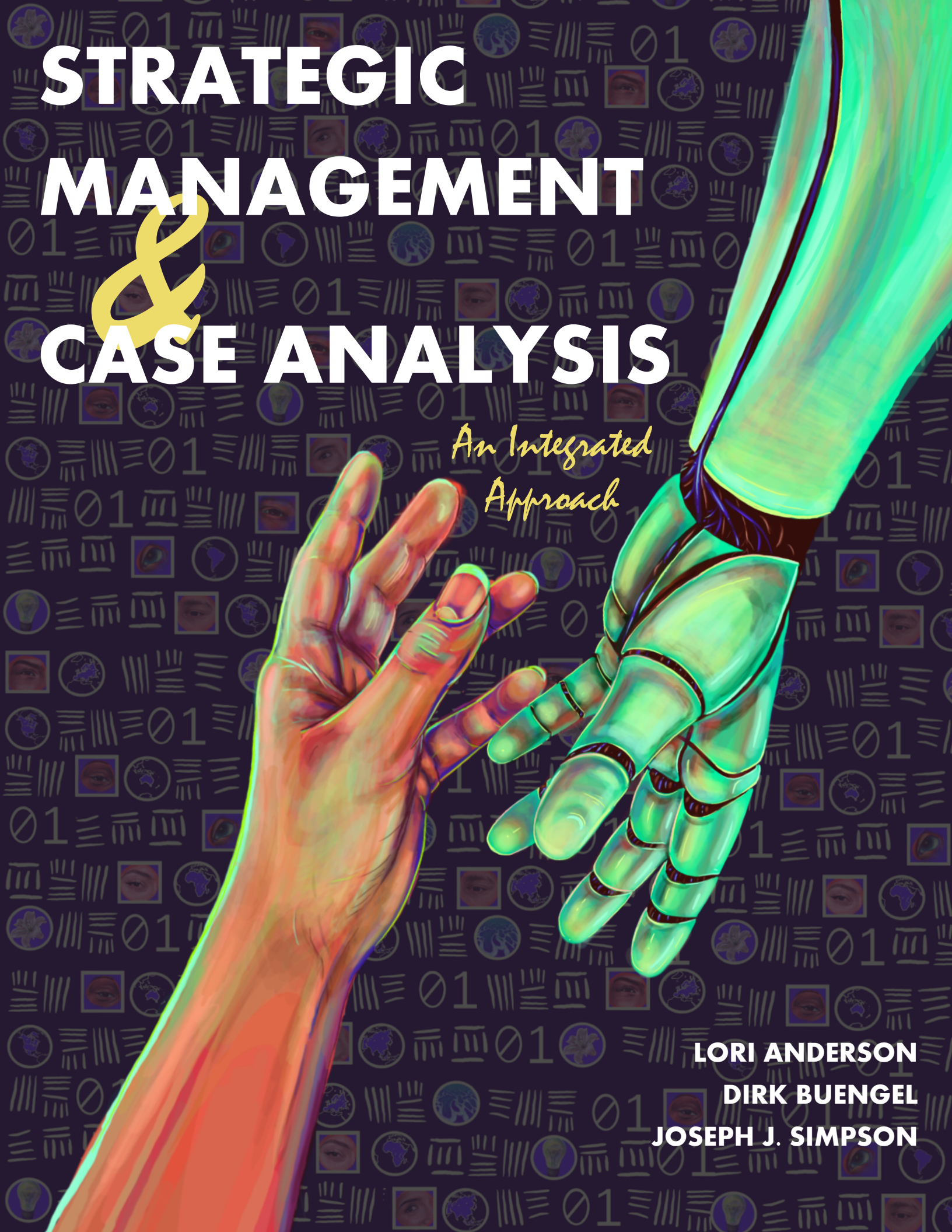


STRATEGIC MANAGEMENT & CASE ANALYSIS

*An Integrated
Approach*



LORI ANDERSON
DIRK BUENGEL
JOSEPH J. SIMPSON

Strategic Management and Case Analysis: An Integrated Approach provides a fresh take on a familiar subject. Readers learn how strategic leaders analyze, formulate, and implement strategy. In addition to considering corporate- and business-level strategy, the text also reviews current megatrends and their impact on innovation, sustainability and ethics, technology, and multinational strategy. Throughout the book, students are invited to practice strategic management by conducting case analyses that apply the theories, concepts, and analytical frameworks and tools of the field. The text introduces analysis instruments that guide students through analyzing, interpreting, and evaluating data in cases, which supports critical thinking and evidenced-based decision making. The book integrates strategic management as a research-led field of study with an experiential learning approach to conducting a case analysis. Instructors are supported with a platform of supplemental materials. Available in multiple formats that are free of cost, the text provides a quality suite of resources to support both students and instructors.

STRATEGIC MANAGEMENT AND CASE ANALYSIS

AN INTEGRATED APPROACH

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Lori Anderson

Dirk Buengel

Joseph J. Simpson

PDF and EPUB free online at <https://doi.org/10.21061/strategicmanagementandcaseanalysis>


VIRGINIA TECH.
PUBLISHING


VIRGINIA TECH PUBLISHING

BLACKSBURG, VA

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Suggested citation: Lori Anderson, Dirk Buengel, and Joseph J. Simpson, *Strategic Management and Case Analysis: An Integrated Approach* (Virginia Tech Publishing, 2025). CC BY-NC-SA 4.0. <https://doi.org/10.21061/strategicmanagementandcaseanalysis>.

Publisher: This work is published by Virginia Tech Publishing.

Virginia Tech Publishing
University Libraries at Virginia Tech
560 Drillfield Drive Blacksburg, VA 24061
<https://publishing.vt.edu> | publishing@vt.edu

Peer review: This book has undergone single-anonymous peer review by three reviewers.

Accessibility statement: Virginia Tech is committed to making its publications accessible in accordance with the Americans with Disabilities Act of 1990. The text, images, and links in the PDF versions of this text are tagged structurally and include alternative text, which allows for machine readability. Virginia Tech Publishing is continuously working to improve accessibility and welcomes any feedback from readers.

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Use of AI: This publication was developed without the use of generative artificial intelligence.

Funding: This project was made possible in part through financial support from the University Libraries' Center for Digital Research and Scholarship, the University Libraries' Open Education Initiative, and the Pamplin College of Business Department of Management.

Cataloging-in-Publication Data

Anderson, Lori, Buengel, Dirk, & Simpson, Joseph J.
Strategic Management and Case Analysis: An Integrated Approach / Lori Anderson, Dirk Buengel, and Joseph J. Simpson
Pages cm
ISBN 978-1-962841-39-9 (PDF)
ISBN 978-1-962841-38-2 (EPUB)
ISBN 978-1-962841-40-5 (Pressbooks; <https://pressbooks.lib.vt.edu/strategicmanagementandcaseanalysis>)
ISBN 978-1-962841-37-5 (Print)
URI: <https://hdl.handle.net/10919/136127>
DOI: <https://doi.org/10.21061/strategicmanagementandcaseanalysis>

Strategic planning--Textbooks.
Business planning--Textbooks.
HD30.28 .A528 2025

Cover art: Claire Lympus

Cover design: Kindred Grey

This book is dedicated to students. We enjoy learning with you and value your insights.

You teach us how to teach. Thank you!

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INTRODUCTION

Target Audience

This textbook is intended for students in undergraduate business programs who are taking courses in strategic management. Since strategic management synthesizes many business topics to develop a holistic view of business, strategic management courses are often senior-level capstone courses. Most undergraduate business school students begin their business educations with broad introductory business courses before concentrating on courses in their majors; then they return to a broader view of business to cap off their business educations at a higher-level of learning. This textbook supports this level of comprehensive learning. If used with a senior-level capstone course, this textbook supports seniors in synthesizing business education through the lens of strategic management and helps them understand how businesses become successful by leveraging their competitive advantages. This textbook integrates strategic management and case analysis, with cases linked from an open access collection of business strategy cases, [RMIT Strategic Management Case Studies](#). This textbook is most beneficial if it is used alongside cases that students analyze.

About This Book

Strategic Management and Case Analysis: An Integrated Approach integrates strategic management as a research-led field of study and practice-informed area of business, taking on an experiential learning approach to conducting a case analysis. The book explains how strategic leaders and managers analyze their firm's organizational performance and its external and internal environments; how they formulate corporate-level and business-level strategy (which includes strategies related to innovation, sustainability and ethics, technology, and multinational business); and how they implement strategy across an organization. Students maintain an active and engaged role with the subject and practice of strategic management as they apply the theories, concepts, and analytical frameworks and tools of the field. The text teaches students how to conduct a case analysis and introduces analysis instruments that facilitate robust case analyses that are based on analysis, interpretation, and evaluation of data in a case. A platform of supplemental materials are provided to lend support to instructors. The book illustrates how strategic management is relevant to multiple majors, at multiple stages in their careers, and in multiple work environments. This ensures that undergraduate students clearly understand how strategic management is relevant to them.

The book is an original work available free of cost in electronic formats. We hope it reflects Virginia Tech's motto, *Ut Prosim* ("That I May Serve"). We also hope it embodies Virginia Tech's Principles of Community:

Virginia Tech is a public land-grant university committed to teaching and learning, research, and outreach to the Commonwealth of Virginia, the nation, and the world community. Learning from the experiences that shape Virginia Tech as an institution, we acknowledge those aspects of our legacy that reflected bias and exclusion. Therefore, we adopt and practice the following principles as fundamental to our ongoing efforts to increase access and inclusion and to create a community that nurtures learning and growth for all of its members:

- We affirm the inherent dignity and value of every person and strive to maintain a climate for work and learning based on mutual respect and understanding.
- We affirm the right of each person to express thoughts and opinions freely. We encourage open expression within a climate of civility, sensitivity, and mutual respect.
- We affirm the value of human diversity because it enriches our lives and the university. We acknowledge and respect our differences while affirming our common humanity.
- We reject all forms of prejudice and discrimination, including those based on age, color, disability, gender, gender identity, gender expression, national origin, political affiliation, race, religion, sexual orientation, and veteran status. We take individual and collective responsibility for helping to eliminate bias and discrimination and for increasing our own understanding of these issues.

through education, training, and interaction with others.

- We pledge our collective commitment to these principles in the spirit of the Virginia Tech motto, *Ut Prosim* ("That I May Serve").

Features of the Book

1. Analysis instruments that teach students how to conduct case analyses by applying analysis, interpretation, and evaluation to strategic management frameworks
 - a. These seven analysis instruments can be found in the Appendix. Readers can also download them by visiting <https://doi.org/10.21061/strategicmanagementandcaseanalysis>.
2. Use of active voice and directive language activate students to engage in conducting robust case analysis (e.g., "analyze the external environment," rather than "external analysis.")
3. Direct addresses to students encourage active engagement with the text and concepts
4. Links to externally vetted, open-access cases
5. Descriptions of how strategic management is relevant to multiple majors, at multiple stages in their careers, and in multiple work environments
6. An example-rich narrative and multimedia approach, including graphic elements that illustrate and reinforce concepts
7. Key takeaways and applications
8. Embedded navigation, such as glossary terms that are linked in the online version (and appear at the end of the book in PDF and print versions) and image alt-text for screen readers
9. Alignment with AACSB principles and standards
10. The book is free online and in PDF, and it is available in print at vendor cost of production.
11. Open license, Creative Commons BY-NC-SA 4.0, permitting customization and sharing
12. Support for an instructor community through a portal that enables sharing of ancillary resources, a Register Your Use form that allows instructors to opt to receive book updates, errata, and forms for reporting errors and sharing suggestions to promote currency

Use of Color

Students experiencing the complexity and interrelated nature of strategic management concepts and theories may find the analytical frameworks and tools demanding. Students can also find it challenging to shift between focusing on strategy for strategic leaders and managers to the perspective necessary for conducting case analyses. Color is used in the book to facilitate learning complex and interrelated ideas by successfully shifting between vantage points. Because of the interrelated nature of the material, choices were sometimes necessary when assigning an item in the book a color. When this was the case, a practical perspective guided the decision: the color assigned is the one most supportive of clarity and learning. Elements that use color are clearly identified using text so that readers with sight disabilities have full access to the intended meaning.

The analysis, formulation, implementation (AFI) framework frames the book. Strategic management concepts and theories as well as analytical frameworks and tools that relate primarily to strategic analysis are **blue**. Those that deal mostly with strategy formulation are **green**. An **orange-brown** is used when strategy implementation is the predominant focus.¹



Figure I.1

Yellow is reserved for items that teach students how to conduct case analyses.²

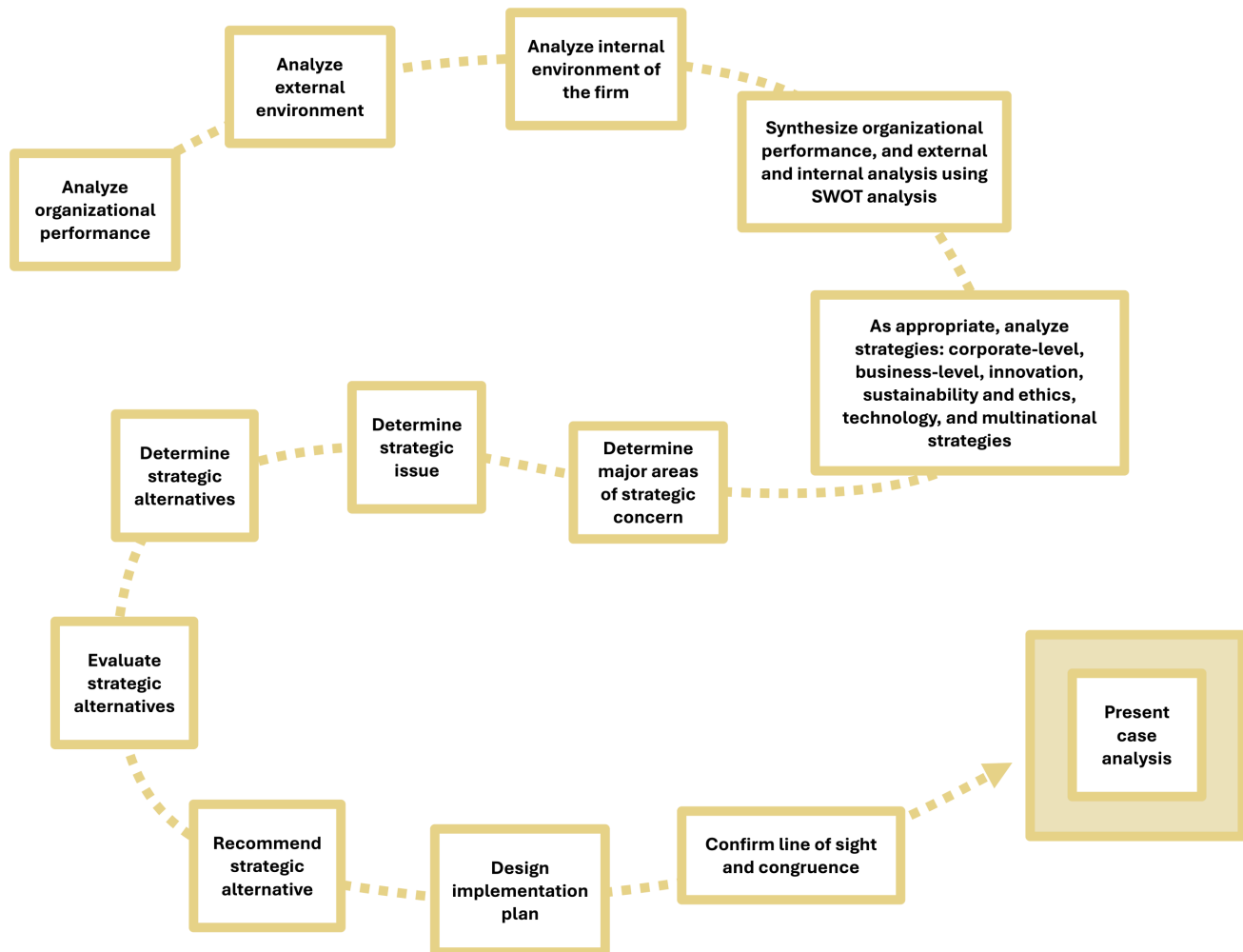


Figure I.2

Purple is used for all other items not as directly related to the AFI framework or case analysis, including learning objectives and key takeaways.

Learning Objectives

Learning objectives and key takeaways appear in these purple boxes.

Book Organization

Part I: Introduction to Strategic Management and Case Analysis

- Chapter 1: Introduction to Strategic Management
- Chapter 2: Introduction to Case Analysis

Part II: Analyze Organizational Performance and a Firm's External and Internal Environments

- Chapter 3: Analyze Organizational Performance
- Chapter 4: Analyze the External Environment
- Chapter 5: Analyze the Internal Environment

Part III: Synthesize Analysis and Determine a Firm's Strategic Issue

- Chapter 6: Synthesize Analysis and Determine a Firm's Strategic Issue

Part IV: Formulate Corporate- and Business-Level Strategy

- Chapter 7: Formulate Corporate-Level Strategy
- Chapter 8: Formulate Business-Level Strategy

Part V: Formulate Strategies that are Embedded in Business-Level Strategy: Innovation, Sustainability and Ethics, Technology, and Multinational Strategy

- Chapter 9: Formulate Innovation Strategy
- Chapter 10: Formulate Sustainability and Ethics Strategy
- Chapter 11: Formulate Technology Strategy
- Chapter 12: Formulate Multinational Strategy

Part VI: Implement Strategy

- Chapter 13: Implement Strategy

Levels of Cognitive Gain

There are multiple taxonomies of learning among several different dimensions, such as cognitive, affective, and psychomotor. These taxonomies have evolved over time, and there is debate about their specifics. We offer one based on Bloom's taxonomy as a heuristic that guides the book. When students engage with the complex subject of strategic management and conduct robust cases analyses, they have multiple opportunities to engage with levels of learning in Bloom's taxonomy. The following table illustrates a few of the ways students demonstrate each level of cognitive gain in Bloom's taxonomy when using the book.³

Level	Characteristic	Verbs for assignments	Ways students demonstrate this level of cognitive gain when using the book
Create	Generate new ideas and products; compile information in a new way.	Assemble Compile Compose Construct Create Design Develop Draft Formulate Invent Model Plan Produce Propose Publish Repurpose Write	Students write a case analysis using strategic management concepts and theories in addition to analytical frameworks and tools. They synthesize the analysis, interpretation, and evaluation of strategic management concepts and theories and of analytical frameworks and tools using a SWOT. Students use a SWOT to develop major areas of strategic concern, a strategic issue, and strategic alternatives. They develop and utilize criteria to assess strategic alternatives. Students develop an implementation plan.
Evaluate	Defend opinions and decisions; justify a course of action by making judgments about information.	Argue Assess Collaborate Criticize Critique Debate Decide Defend Estimate Evaluate Hypothesize Judge Justify Measure Moderate Predict Recommend Reflect Test Verify	As used in the book, interpretation is the process and result of examining the analysis to identify and explain relationships in the analysis and underlying root causes of the situation. Evaluation is the examination of the analysis and interpretation to identify and explain the meaning of the information to the company by considering its impact, relevance, and importance to the company and by identifying the company's current, potential, or needed assets, organizational capacity, and managerial ability that may support or mitigate the areas of highest impact, relevance, and importance for the firm. Using strategic management instruments that are introduced in the book, students interpret the analysis they have conducted so far and evaluate the analysis and interpretation they have conducted.
Analyze	Examine and break information into parts to explore relationships.	Analyze Categorize Classify Compare Conclude Contrast Correlate Deconstruct Deduce Differentiate Distinguish Edit Investigate Reverse engineer Select Separate Solve	As used in the book, data is the information in the case being reviewed, the company being researched, or the company receiving consulting services. Analysis is the process and result of examining all the data available for the firm and correctly identifying and classifying all the data for each category in a strategic management tool. Using strategic management instruments that are introduced in the book, students analyze data in cases.

Level	Characteristic	Verbs for assignments	Ways students demonstrate this level of cognitive gain when using the book
Apply	Use existing knowledge to solve new problems; apply acquired knowledge in new situations.	Apply Articulate Calculate Change Choose Complete Dramatize Execute Illustrate Interpret Operate Practice Relate Share Show Teach Use	Through the strategic management instruments that are introduced in the book, students use analytical frameworks and tools to apply strategic management concepts and theories. Students demonstrate their understanding of strategic management and analytical frameworks and tools by completing application exercises throughout the book.
Understand	Demonstrate an understanding of the facts by explaining ideas or concepts.	Annotate Convert Demonstrate Describe Discuss Explain Extend Identify Interpret Outline Paraphrase Predict Research Review Summarize	Students demonstrate their understanding of theories and concepts by answering questions that appear in boxes at the end of each chapter titled “Demonstrate Your Knowledge, Skills, and Competence.”
Remember	Exhibit memory of previously learned material by recalling facts, concepts, and answers.	Cite Define Find Highlight Label List Locate Name Recall Recognize Reproduce Retrieve Search	Students demonstrate their recall of key theories and concepts by engaging with sections throughout the text titled “Key Takeaways.”

Figure 1.3: Ways students demonstrate levels of cognitive gain when using *Strategic Management and Case Analysis: An Integrated Approach* (from most complex to most foundational)

Development

Strategic Management and Case Analysis: An Integrated Approach is a new collaborative work by three colleagues in the Pamplin College of Business at Virginia Tech. Lori Anderson, who also serves as the course coordinator, was lead author and project manager for the project.

Anita Walz, Assistant Director of Open Education in the University Libraries at Virginia Tech, guided the book through ideation and development. Kindred Grey, Graphic Design and Production Specialist, managed review, design, and production of the book, leading up to its publication by Virginia Tech Publishing. Multiple staff formatted the text in Pressbooks, offered feedback to the editorial team, and provided copyediting and proofreading. The resulting book has been published in online formats (Pressbooks, EPUB, and PDF) and in a print-on-demand version.

Impact

Our hope is that this textbook enlightens and prepares students to enter the business world. After engaging with the material in the book, students can understand and apply strategic management theories, concepts, and analytical frameworks and tools, instilled with a much better grasp of the ways organizations achieve success at the strategic level. Throughout the book, students practice analyzing, interpreting, and evaluating complex data by conducting robust case analyses. This integrated approach serves to make students better specialists in their fields and better prepares them as employees, especially as they rise in responsibility and take on more strategic roles in their organizations. Ultimately, we hope to support students in becoming better critical thinkers, prepared to analyze the full range of situations they will face in their professional lives.

Finally, this book is meant to provide instructors in other colleges and universities with a no-cost textbook solution with high-quality content and structure.

Notes

1. Figure 1: Kindred Grey. 2025. CC BY.
2. Figure 2: Kindred Grey. 2025. CC BY.
3. Bloom, B. S. (1956). Taxonomy of educational objectives, handbook I: The cognitive domain. David McKay Co., Inc.

LETTER TO STUDENTS

Dear students,

Welcome to *Strategic Management and Case Analysis: An Integrated Approach*! We are delighted you are using this book to support your mastery of strategic management as a subject and build your competence in conducting robust strategic case analyses. Competence in strategy is important to you immediately upon graduation and throughout your business career, in all the work environments you may choose, and no matter your business major—whether you are focused on accounting and information systems, business information technology and cybersecurity, finance, insurance and business law, hospitality and tourism management, human resource management, business management, management consulting and analytics, entrepreneurship, innovation and technology management, marketing, real estate, or another business area. As you make your way through the book, you will learn just how relevant strategic confidence is to you and your career.

Over these pages, you will work with analysis instruments that teach you how to conduct case analyses by applying analysis, interpretation, and evaluation to strategic management frameworks. This expands your critical thinking and evidenced-based decision-making skills.

You are why we wrote this book! We wish you an enriching learning experience.

Sincerely,

Dr. Lori Anderson, Dirk Buengel, and Dr. Joseph J. Simpson

INSTRUCTOR RESOURCES

Available formats and helpful links

Navigate to [the book's main landing page](#) to access:

- Links to multiple electronic versions of the textbook (PDF, EPUB, HTML)
- Analysis instruments
- Slide decks to accompany the text
- A link to Amazon for ordering a print copy
- A link to the [errata document](#)
- A link to [report errors](#)

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Instructors reviewing, adopting, or adapting this textbook are encouraged to [register their interest](#) and check out the [public-facing instructor sharing portal](#). This assists the Open Education Initiative at Virginia Tech in assessing the impact of the book and allows us to more easily alert instructors of additional resources, features, and opportunities.

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About this book



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Additional resources: Strategic management cases

At the time of publication, a number of freely available cases on strategic management were available at:

- O'Shannassy, T., et al. (2023). RMIT strategic management case studies. RMIT University. CC BY-NC-ND. <https://rmit.press-books.pub/strategycases>
- 27 MIT strategy case studies: <https://mitsloan.mit.edu/teaching-resources-library/strategy-case-studies>
- One strategy case study from Ivey Business School: <https://www.ivey.uwo.ca/hba/classroom-cases/whitewater-specialties-limited>
- 19 Rutgers strategy case studies (Select: "Strategy" from the list of disciplines, and select "Cases" from the list of Formats): <https://cleo.rutgers.edu/search>

URLs

License: <https://creativecommons.org/licenses/by-nc-sa/4.0/deed.en>

Instructor interest form: https://bit.ly/interest_strategicmanagementandcaseanalysis

Public-facing instructor sharing portal: <https://oercommons.org/groups/strategic-management-and-case-analysis/15446>

Book's main landing page: <https://doi.org/10.21061/strategicmanagementandcaseanalysis>

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PART I: INTRODUCTION TO STRATEGIC MANAGEMENT AND CASE ANALYSIS

In this book, you learn strategic management concepts and theories, in addition to analytical frameworks and tools. You also learn how to conduct a case analysis using these ideas. Part I introduces strategic management and case analysis.

In Chapter 1, you learn what strategic management is and why it is important. You also are introduced to the analysis, formulation, implementation (AFI) framework, which serves as a guiding framework for the book. You learn about intended, deliberate, emergent, realized, and unrealized strategies. Additionally, you explore the history of strategic management and contemporary critiques of the field. Finally, you learn why strategic management is valuable to you in all career settings and at all career stages.

Chapter 2 introduces you to case analysis, including the relationships and differences between the terms *case*, *case analysis*, *data*, *analysis*, *interpretation*, *evaluation*, *line of sight*, and *congruence*. You then learn what the case analysis process entails.

1. INTRODUCTION TO STRATEGIC MANAGEMENT

Learning Objectives

Chapter 1 ensures that you understand and are able to apply the following key strategic management concepts:

1. How the terms *organization*, *business*, *company*, *firm*, and *industry* are used in the textbook
2. How the terms *strategic management concepts and theories* and *analytical frameworks* and tools are used in the textbook
3. What strategic management is
4. The analysis, formulation, implementation (AFI) framework
5. Intended, deliberate, emergent, realized, and unrealized strategies
6. Why strategic management is important
7. The history of strategic management
8. Contemporary critique of strategic management
9. Why strategic management is valuable to you in all career settings and at all career stages

Tesla's Market Share Growth

Perhaps best known to many consumers as a producer of electric vehicles (EVs), Tesla has beaten well-known legacy automotive companies like Ford and GM in the U.S. market to become the most profitable automaker in U.S. history despite the intense competition in the U.S. automotive sector. With a valuation of over \$81 billion, Tesla is more than an automaker. Founded as Tesla Motors in 2003 in San Carlos, California, by Martin Eberhard and Marc Tarpenning, today Tesla is a successful multinational company headquartered in Austin, Texas, that also specializes in renewable energy solutions, such as energy storage devices and solar panels, in addition to EVs. An early investor, Elon Musk became CEO in 2008. Tesla continuously innovates in many areas, especially in sustainable technology. This is evident not only in its products but also throughout its production, which includes the advanced use of robotics.

Despite its outstanding accomplishments, Tesla has encountered a number of external and internal challenges. Infrastructure has been slow to support long-distance EV travel, making traveling beyond a vehicle's range a challenge due to a lack of readily available charging stations, especially in remote and rural areas. Some consumers express concerns over the capacity of the power grid to support the increase in EVs.

An industry characteristic of automakers is that they can face long-term reliability challenges—to greater and lesser degrees, of course. While automakers new to the industry may have a brief honeymoon period before long term reliability issues are evident, Tesla vehicles have now been on the market long enough for these issues to become evident.

Elon Musk is known for being outspoken about his views, especially through his social media posts mostly on X. The successor to Twitter, Inc., X is a wholly owned subsidiary of X Holdings Corp., which is mostly owned by Musk. In a display of his influence, on May 1, 2020, when he posted that Tesla's stock price was too high, the company's stock price immediately dropped.

Within the organization, persistent challenges have included employee dissatisfaction, loyalty issues, and retention problems. These internal problems, which frequently result from highly demanding work environments, high standards, and leadership concerns, have made it difficult to attract and retain a steady and loyal employee base and have impacted the company's work culture.



Figure 1.1: Elon Musk follows through on Tesla's Master Plan

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1.1 Introduction

The problems mentioned in the example above about Tesla raise significant questions:

- Will relating and supporting industries, such as charging stations and power grid capacity, grow to meet the demand of EVs?
- To what degree will Tesla integrate with these industries to control them or partner with them to influence their growth?
- How will Tesla address the emergence of reliability issues in its vehicles?
- How will Elon Musk's leadership style influence company success?
- How will Tesla address its talent attraction and loyalty concerns?
- Will Tesla be able to maintain its position as the leading electric vehicle manufacturer with the biggest market share in the United States?
- What emphasis will Tesla place on its EVs and other product lines, such as energy storage devices and solar panels, in the future?
- How will the company sustain its competitive advantage in the automotive industry and its success in renewable energy industries as the business expands?

As the market evolves and competition increases, the answers to these questions will depend on how well Tesla navigates its challenges, applies the right strategies, adapts to changing consumer preferences, and continues to innovate. These concerns, which are not unique to Tesla, are a few of the questions and issues addressed by strategic management.

1.2 Organization, Business, Company, Firm, Industry

Before we introduce strategic management, it is important to understand how the terms *organization*, *business*, *company*, *firm*, and *industry* are used in the book. **Organization** is the broadest term used to describe a specific entity and applies to entities in all sectors: private (for-profit), governmental (public), and not-for-profit (including nonprofit, nongovernmental organizations [NGOs], and voluntary organizations). Strategic management is important to all sectors. As a business textbook, the book focuses primarily on organizations in the private sector. A few examples of organizations in other sectors are given throughout the book, as you may work in the governmental and not-for-profit sectors at some stage in your career.

Organizations in the private sector are also referred to as **businesses**, **companies**, and **firms**. Therefore, all four terms can be correctly applied to entities in the private sector that engage in commerce and aim to make a profit. The terms *organization*, *business*, *company*, and *firm* are used interchangeably in the book.

Industry is a group of organizations, businesses, companies, or firms that offer similar products and services while competing in the marketplace for profit. The term *industry* is used to indicate this group of competing organizations, businesses, companies, or firms.

In the example of Tesla above, Tesla may be referred to as an organization, business, company, or firm. Tesla competes in at least two industries: the automotive industry and the renewable energy industry. Large multinational firms often compete in more than one industry.

Unlike businesses like Tesla, units in the governmental or public sector, such as departments in the federal government like the Environmental Protection Agency (EPA), are referred to as *organizations*. This also is true for not-for-profit organizations, like the Red Cross.

Key Takeaways

Organization is the broadest term used to describe a specific entity and applies to entities in all sectors: private (for-profit), governmental (public), and not-for-profit (including nonprofit, NGOs, and voluntary organizations). Organizations in the private sector are also referred to as *businesses*, *companies*, and *firms*. Therefore, all four terms can be correctly applied to entities in the private sector that engage in commerce and aim to make a profit. Industry is a group of organizations, businesses, companies, or firms that compete in the marketplace for profit.

1.3 Strategic Management Concepts and Theories & Analytical Frameworks and Tools

As a multidisciplinary field of study, strategic management incorporates concepts and theories from many disciplines. **Concepts** are ideas. **Theories** are collections of concepts that explain something. Common examples include the concept of gravity, which is an idea that is part of the theory of relativity; likewise, the concept of genetic mutation is a part of the theory of evolution. In business, theories are collections of concepts that explain something that occurs in the business world. For example, the concept of power is a part of leadership theories, such as shared leadership theory.

An **analytical framework** provides a structured format for analyzing data. Continuing with the example of the concept of power as an essential building block of leadership theories, there are multiple analytical frameworks that support analyzing power dynamics, such as French and Raven's five bases of power—legitimate, reward, expert, referent, coercive power—that can be used to evaluate how leaders influence others.

Strategic management frameworks provide a structured format to analyze company data as it relates to a major area of strategic management. Strategic management analytical frameworks may also be referred to as strategic management tools.

Strategic management concepts and theories inform the analytical frameworks and tools used in strategic management. The terms *frameworks* and *tools* are used interchangeably in the textbook.

You learn many strategic management concepts and theories throughout the book, with frequent opportunities to apply multiple strategic management frameworks to analyze companies.

Application

- Think of additional examples of concepts, theories, and analytical frameworks. How many more examples can you identify?

Key Takeaways

Concepts are ideas. Theories are collections of concepts that explain something. An analytical framework provides a structured format for analyzing data. Strategic management frameworks provide a structured format to analyze company data as it relates to a major area of strategic management. Analytical frameworks for strategic management may also be referred to as strategic management tools.

1.4 What is Strategic Management?

Just as it is important to understand what strategic management is and how to apply its concepts and theories, analytical frameworks and tools are central to successful strategic management. The process of applying the concepts and theories through analytical frameworks and tools is known as case analysis. This chapter introduces you to the subject of strategic management; the next chapter teaches you how to apply the concepts, theories, and tools of strategic management through the process of conducting case analysis.

Strategic management is an area of business that is grounded in research. Like most areas of business, strategic management is both a focused area of business practice and a field of study supported by robust research. In this introductory chapter to strategic management, you first learn about strategic management in the context of business practice, and then you learn about strategic management as a field of study. The remainder of the book approaches strategic management as a research-grounded field of business practice.

Strategic management is a multidisciplinary subject, relying on and synthesizing all areas of business expertise, such as accounting and information systems, business information technology and cybersecurity, finance, insurance and business law, hospitality and tourism management, human resource management, business management, management consulting and analytics, entrepreneurship, innovation and technology management, marketing, and real estate. The primary aim of strategic management is to continuously apply evidenced-based analysis to formulating and implementing strategies that allow a firm to differentiate itself in the market. Strategic management uses many frameworks and tools that are based on many interrelated concepts and theories. To support you in learning these interrelated complex ideas and effectively applying them, we introduce you to the broad landscape of strategic management so that you can see the big picture of how the ideas fit together and then break them down in more detail so that you can apply them.

To understand the broad field of strategic management from both business practice and field of study perspectives, you need to understand the terms *strategic leadership*, *strategic management*, *strategy*, *strategic analysis*, *strategy formulation*, and *strategy implementation*. We introduce each of these below as a way for you to see the big picture of strategic management before addressing them in greater detail.

Strategic Leadership

Think about leadership and management. How are they similar? How are they different? One way to consider these different roles is that leaders define the direction the organization is going, while managers identify the roadmap for getting there. In practice, many employees both lead and manage, depending upon the size of a company and whether the management style of the firm is centralized or decentralized. When it comes to strategic management, both strategic leadership and strategic management are important.

Strategic leadership includes the responsibility, talent, capacity, power, and actions necessary to steer an organization strategically through a dynamic market to create and sustain a competitive advantage and to become and remain an industry leader. Strategic leaders direct the strategic management process.

Strategic leadership is an essential focus for top leaders in a company, such as those in the C-suite and the board of directors. Elon Musk, his colleagues in the C-suite, and Tesla's board of directors provide strategic leadership for Tesla. However, strategic leadership is not always the exclusive focus of those at the very top of an organization, depending on whether a firm relies on a centralized or decentralized leadership style. In companies with a decentralized leadership style, leadership may be shared among more company leaders.

Strategic Management

Strategic management is the dynamic and ongoing process of managing a firm's approach to strategy. Strategic management follows a structured process to methodically and thoroughly analyze the environment, industry, and firm as well as to formulate and implement strategy.

Large companies often have departments or teams focused exclusively on leading strategic management. Managers in a firm also participate in strategic management. To support their data driven decisions, managers solicit data from areas of business expertise such as accounting and information systems, business information technology and cybersecurity, finance, insurance and business law, human resource management, and marketing.

You will likely be asked for data that supports strategic management early in your career. Demonstrating that you understand how this data can support broader strategic management efforts can accelerate your career. Below, we explore exactly how competency in strategic management is a vital skill to all business majors in all career settings and at all career stages, an assertion that will be explained in greater detail later in the book.

Strategy

Think about the strategies you use to be successful in your coursework. They may include studying, time management, and remaining up to date on assignments.

Strategic management focuses on **strategy**. Strategy is a collection of organizational plans and processes that focus on creating and sustaining superior firm performance relative to a company's competitors, which creates a sustainable competitive advantage. Strategies are broad and long range, with few specifics. They do not typically address actions.

The strategies this book covers in detail include corporate-level strategy, business-level strategy, innovation strategy, sustainability and ethics strategy, technology strategy, and multinational strategy. We introduce those in [section 1.5](#) and cover them in detail in their own dedicated chapters.

Strategic Analysis

In firms, **strategic analysis** is the process of applying strategic management concepts and theories with analytical frameworks and tools to conduct a thorough 360-degree analysis of a firm. This enables strategy managers to make evidenced-based decisions about strategy formulation and strategy implementation in all areas of the company's operations.

You conduct strategic analysis of a company by conducting a case analysis, which the next chapter describes in detail so that you may apply the knowledge throughout the remainder of the book.

When you graduate, you likely will be involved in strategic analysis either immediately or very early in your career, depending on the size company you join and its management style, whether you serve as an internal or external consultant or you begin an entrepreneurial venture of your own. Competency in strategic analysis is essential to both navigating a career and to starting your own business.

Strategy Formulation

Strategy formulation is the process of designing strategies throughout all levels and areas of an organization. Successful strategy formulation relies on evidenced-based decisions that are grounded in strategic analysis.

Strategic leaders and managers in firms formulate strategy. You analyze the company strategies when you conduct a case analysis. As with strategic analysis, you learn exactly how understanding strategy formulation is important for your career as you progress through the book.

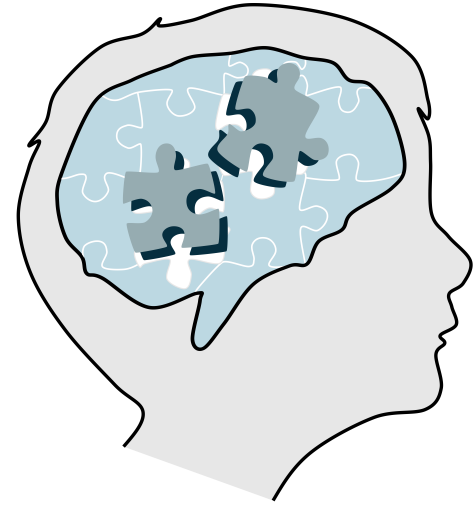


Figure 1.2: Strategic leaders align strategic analysis, strategy formulation, and strategy implementation, much like fitting puzzle pieces together correctly

Strategy Implementation

Strategy implementation is the process of executing the strategies that a company has formulated.

Employees at all levels of a firm are responsible for implementing the company's strategies. You will be involved in strategy implementation immediately in your career. Knowing how strategy is analyzed and formulated gives you an advantage in implementing strategy.

Application

- Think of the jobs you have had.
 - Were there people that engaged exclusively in leadership and people that engaged exclusively in management, or did the same person both lead and manage?
 - Describe the responsibilities leaders had.
 - Discuss the tasks managers did.
 - What do you see as the primary differences in leadership and management from your experience?
 - Can you identify a specific strategy that the company was implementing? Why do you think it was or was not visible to you?

Key Takeaways

Strategic management is both a focused area of business practice and a field of study supported by robust research. Strategic leadership includes the responsibility, talent, capacity, power, and actions necessary to steer an organization strategically through a dynamic market to create and sustain a competitive advantage and to become and remain an industry leader. As a focused area of business practice, strategic management is the dynamic and ongoing process of managing a firm's approach to strategy. Strategic management follows a structured process to methodically and thoroughly analyze the environment, industry, and firm as well as to formulate and implement strategy. Strategy is a collection of organizational plans and processes that focus on creating and sustaining superior firm performance relative to a company's competitors, which creates a sustainable competitive advantage. Strategy formulation is the process of relying on evidence-based decisions that are grounded in strategic analysis to design strategies throughout all levels and areas of an organization. Strategy implementation is the process of executing the strategies that a company has formulated.

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1.5 The Analysis, Formulation, Implementation (AFI) Framework

The practice and research of strategic management includes the three pillars of strategic analysis, strategy formulation, and strategy implementation. These are represented in the analysis, formulation, implementation (AFI) framework that guides the focus and structure of this book.

Figure 1.3 shows the AFI framework. We cover each element below.



Figure 1.3: The analysis, formulation, implementation (AFI) framework

At the center of the AFI framework are **strategic management** and **strategic leadership**, with which you are now familiar.

Below you learn more about the three stages of the strategic management process—strategic analysis, strategy formulation, and strategy implementation—and the three essential questions that guide each stage. Next you learn what you’re specifically analyzing in the strategic analysis stage and in what order. Then the chapter focuses on strategy formulation, which is addressed at three organizational levels of strategy (corporate-level strategy, business-level strategy, and functional-level strategy) and by the more focused strategies that are embedded into business-level strategy (innovation strategy, sustainability and ethics strategy, technology strategy, and multinational strategy). Finally, you consider strategy implementation.

Strategic management’s foundations rest in three essential questions that align with the three stages of strategic management:

1. Where are we?
2. Where are we going?
3. How are we going to get there?

Strategic analysis addresses “Where are we?” Strategy formulation begins to answer, “Where are we going?” And strategy implementation addresses “How are we going to get there?”

Strategic Analysis

Strategic analysis addresses the broad question “Where are we?” and includes multiple steps. In this section, we review the steps to strategic analysis so that you can see the overall approach to strategic analysis. Later chapters discuss what is involved in each step of strategic analysis. You learn how to conduct a strategic analysis when you conduct a case analysis using strategic management tools.

The order of the steps is important. First, analyze organizational performance, which assesses the robustness and congruence of a firm's mission, purpose, vision, values, and goals as well as its financial position, its market position, and other relevant quantitative data. This step also includes a review of the firm's balanced scorecard. Next, review the external environment of the firm, which considers the company's general, industry, and competitive environments. Then analyze the internal environment of the firm, which assesses a firm's resources, capabilities, core competencies, and value chain. Once you have analyzed an organization's organizational performance and its external and internal environments, synthesize the analysis using a strengths, weaknesses, opportunities, and threats (SWOT) analysis. Finally, identify a strategic issue and strategic alternatives.

Each of these steps in strategic analysis is the subject of a chapter, ensuring that you learn them in much greater detail as you make your way through the book.

Consider figure 1.4. The order of the steps in strategic analysis is important, as each step progressively narrows the focus until you can define a strategic issue and how to address it.

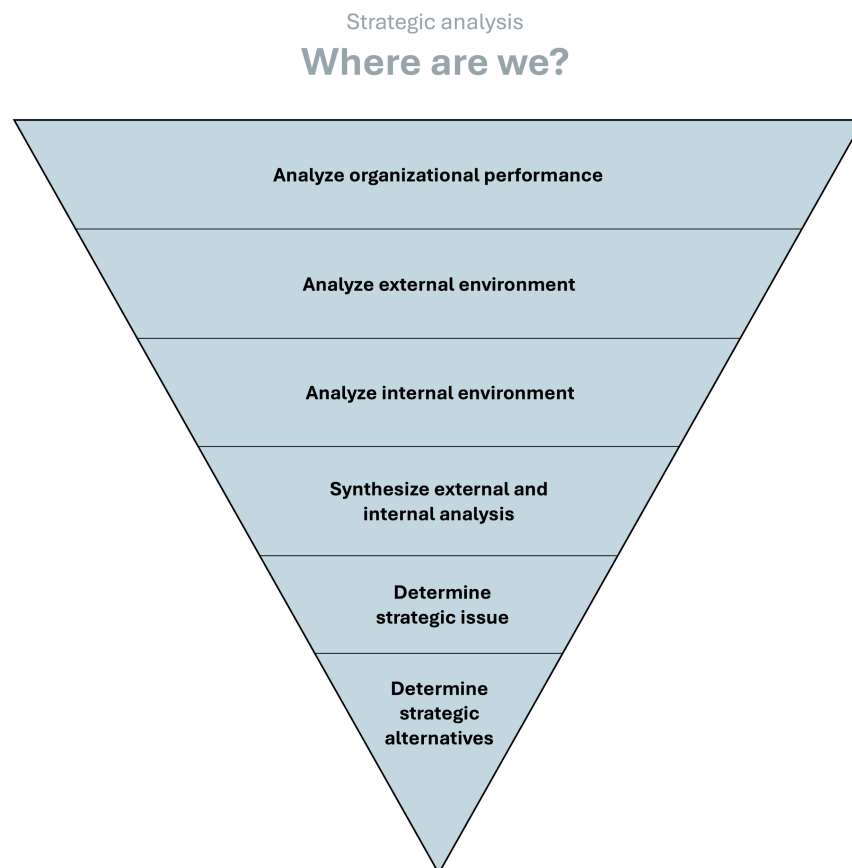


Figure 1.4: Strategic analysis

A firm's strategic issue and strategic alternatives are central to strategic management. They are introduced here and elaborated upon in detail in subsequent chapters.

A firm's **strategic issue** is the most important, urgent, broad, long-term matter that the company is facing. Strategic issues are the result of multiple causes in multiples areas of a business and require significant organizational talent and resources to resolve. Addressing a strategic issue moves a firm toward its mission, purpose, and vision, and it should therefore be congruent with the firm's values and goals. A strategic issue focuses on the present and specific organizational context, addressing what is happening with this firm at this time, in this place, and under these circumstances. What a strategic issue is and how to determine it is elaborated on in subsequent chapters.

A **strategic alternative** is an action that addresses and has the potential to resolve every aspect of a strategic issue. Strategic alternatives are also explained in greater detail in later chapters.

Strategy Formulation

Once strategic analysis is complete, **strategy formulation** begins. This process addresses the broad question “Where are we going?” Strategy formulation is presented in order from broadest to narrowest (in relation to the level of the organization where it is addressed).

Figure 1.5 illustrates strategy formulation, and the text below explains each element in the figure.



Figure 1.5: Strategy formulation

There are three levels of strategy in an organization: corporate-level strategy, business-level strategy, and functional-level strategy. Strategy is formulated at all levels of a company.

Corporate-Level Strategy

The corporate level of a company consists of senior executives in the C-suite, and if the company is large enough, it includes the board of directors. **Corporate-level strategy** is a companywide strategy that focuses on creating and maintaining a firm's competitive advantage by creating synergy within and between multiple **industries, markets, market segments, and businesses**, across

multiple industry value chains, and in different geographical locations. Corporate-level strategy is the responsibility of senior executives and the board of directors.

When you conduct a case analysis, you may analyze a company's corporate-level strategy.

Business-Level Strategy

Business-level strategy focuses on how to compete within an organization's chosen market and market segments to create and sustain competitive advantage. Business-level strategy addresses a firm's strategic market position (cost leadership and differentiation) and strategic market size (whether it competes in a focused market segment or a broad market).

Business-level strategy is the strategy of a **strategic business unit**. A strategic business unit is a fully functional unit of a business that has its own vision and direction and may be part of a larger organizational unit like a division. The unit's focus and structure may be based on factors such as markets served, products offered, or regions served. Smaller firms may have only one strategic business unit, and large corporations may have more than one strategic business unit.

Strategic business units focus on one business-level strategy. Smaller firms that have only one strategic business unit have only one business-level strategy. In large companies with more than one strategic business unit, different strategic business units may have different business-level strategies. Therefore, large corporations that have more than one strategic business unit potentially have multiple business-level strategies.

All strategy should be specific and differentiating. Though business-level strategies include a finite number of strategies that are common to all companies, companies implement them in ways that reflect their specific company conditions.

In addition to each strategic business unit's business-level strategy, there are additional strategies that are embedded into business-level strategies at the strategic business unit level. The four embedded strategies that are covered in this text are innovation, sustainability and ethics, technology, and multinational strategy.

When you conduct a case analysis, you may analyze a company's business-level strategy and its innovation, sustainability and ethics, technology, and multinational strategies.

Innovation Strategy

All companies of all sizes and stages of development and growth must address innovation and formulate innovation strategies. **Innovation strategies** are strategies that are embedded into business-level strategies at the strategic business unit level that focus on a firm's approach to innovation so that it can create and sustain a competitive advantage.

Sustainability and Ethics Strategy

Sustainability strategies are strategies that are embedded into business-level strategies at the strategic business unit level that focus on a company's approach to reducing its adverse environmental and social impacts while establishing competitive differentiation through the firm's positive environment and social performance (usually measured against environmental, social, and governance [ESG] metrics).

Business ethics strategies are strategies that are embedded into business-level strategies at the strategic business unit level that focus on a company's approach to increasing ethical behavior and remaining legally compliant.

Technology Strategy

Technology strategies are strategies that are embedded into business-level strategies at the strategic business unit level that focus on a company's approach to using technology as a source of competitive differentiation and that align the firm's use of new and emerging technologies with the firm's roadmap to reach its vision and overall business objectives.

Multinational Strategy

Multinational corporations (MNCs) are firms that have operations in more than one country.

Though all successful companies formulate innovation, sustainability and ethics, and technology strategies, not all businesses are MNCs and therefore not all companies formulate multinational strategies. Multinational corporations formulate **multinational strategies**, which are embedded into business-level strategies at the strategic business unit level, and are strategies that address different ways to position the company in multinational markets. They include international, multidomestic, global, and transnational strategies.

Three Critical Strategic Questions

Strategy can be described as a firm's answer to three strategic questions that are critical for every organization:

1. Where to play?
2. How to win?
3. Right to win?

The first two questions ("Where to play?" and "How to win?") are addressed at the two broad levels of strategy. "Where to play?" is answered at the corporate level with corporate-level strategy. "How to win?" is addressed through business-level strategy at the strategic business unit level. The third question ("Right to win?") is addressed by the specific strategies that are embedded into business-level strategies at the strategic business unit level: innovation strategy, sustainability and ethics strategy, technology strategy, and multinational strategy. All three questions drive the firm's formulation of a roadmap and action plan toward sustained superior performance.

Where to play?

This first question is addressed at the corporate level of a company and considers which industries, markets, market segments, businesses, and regions in which the firm wants to operate (play). The answers to the question are largely determined by the firm's assessment of the attractiveness and profit potential of alternative markets, market segments, businesses, and synergies between them. The answers also provide important solutions to the allocation of limited company resources to different businesses. In this sense, it is also important for every organization to decide where *not* to play. Overall, the strategy that focuses on where to "play" can be described as the firm's search for markets and market segments that are attractive today and in the future.

How to win?

After the first question has been addressed, the firm needs to decide how it will win in its chosen markets, and this is approached through business-level strategy at the strategic business unit level of a company. Answers to this question are largely determined by the firm's ability to develop a winning strategy around its resources, capabilities, and core competencies that are superior to those of its competitors and that will create value for the firm's customers. There are various drivers of how a firm can win in its chosen markets, like differentiation and cost leadership or whether the firm chooses to operate in a focused or broad market. Overall, the "How to win?" question addresses the firm's search for a sustainable competitive advantage.

Right to win?

Once the question of where to play has been resolved at the strategic business unit level through business-level strategy, the question “Right to win?” can be considered. All companies have the ambition to win in their chosen markets. They want to gain market share, increase revenue and profit, and enter new markets and regions. However, strategy is more than a wish list of what a company would ideally want to do and achieve. Strategy is a company-specific roadmap for navigating its industry, directing how a firm moves from its current state toward the firm's vision.

With this conception of strategy in mind, the company's right to win is addressed by the specific strategies that are embedded into business-level strategies at the strategic business unit level: innovation strategy, sustainability and ethics strategy, technology strategy, and multinational strategy. An organization needs a clear right to win in its chosen markets. This right is supported by truly differentiating and valuable resources, capabilities, and core competencies that are unique for the specific organization.

Let's take the example of your university's volleyball team. The team surely has the ambition to do well, win as many games as possible, and maybe even win the conference title. Going beyond just the hope to win requires a clear right to win. This right (or reason or justification) to win could be that the team has the best coach, the best training conditions, the best infrastructure, the best team captain, or outstanding individual players. Maybe it is not the superior quality of individual players but the superior chemistry and teamwork that makes the team win. Whatever it may be, without a true right to win, strategy just becomes wishful thinking—an exercise written on paper.

On a business level, the right to win needs to be clearly anchored in business-level strategy because it is in strategic business units where a firm decides how it wants to win in its chosen markets.

Functional-Level Strategy

The third level of strategy formulation is **functional-level strategy**. Functional-level strategy, or just functional strategy, focuses on implementing strategy in business support units. **Business support units** focus on single **business functions**, such as accounting, business information technology, business law, finance, human resource management, marketing and sales, supply chain management, operations, and procurement.

Many of you will join firms in business support units in your first professional positions after graduation. All types of strategy cascade down to business support units, influencing strategy implementation at each level. Because functional-level strategy is the focus of most courses in your major, it is not addressed in detail in this book.

Strategy Implementation

Once strategy formulation is complete, each type of strategy must be implemented. Strategy implementation addresses the question “How are we going to get there?” Unless it is concerning a new strategy area for a company, then strategy implementation often begins with analyzing the gap between the previous strategy and the newly formulated strategy. Strategy implementation involves setting goals, allocating resources to operationalize the strategy, communicating and cascading the strategy, ensuring the organizational design and control systems support the strategy, hardwiring the strategy throughout the organization, aligning culture to support the strategy, and managing the changes required to implement the strategy. Strategy implementation is the subject of [Chapter 13](#).

Application

- Think about your career aspirations. Maybe you would like to join a large firm as a subject expert in an area such as accounting or marketing. Perhaps you plan to start an entrepreneurial venture (or already have) or maybe you want to work as a consultant. Now think about your career from the point of view of the AFI framework and the roles of strategic analysis, strategy formulation, and strategy implementation.
 - What analysis are you conducting to support your strategy? Are you analyzing your strengths and preferences? Perhaps you are considering the job market and projected income growth over five years. What else is important to you?
 - Based on your analyses, what strategy have you formulated to ensure you are successful? State your strategy in one concise sentence.
 - Have you begun implementing your strategy? What else do you need to do before implementing your strategy?

Key Takeaways

The analysis, formulation, implementation (AFI) framework represents the stages of the strategic management process: strategic analysis, strategy formulation, and strategy implementation. Strategic analysis addresses the question “Where are we?” Strategy formulation begins to answer “Where are we going?” Strategy implementation addresses the question “How are we going to get there?” Strategy formulation includes three levels of strategy in an organization: corporate-level strategy, business-level strategy, and functional-level strategy. This text discusses four specific strategies that are embedded into business-level strategies at the strategic business unit level: innovation, sustainability and ethics, technology, and multinational strategy. Strategy addresses three critical strategic questions that every organization has to answer. “Where to play?” is addressed through corporate-level strategy. “How to win?” is addressed through business-level strategy in a strategic business unit. “Right to win?” is addressed through the four specific strategies that are embedded into business-level strategies at the strategic business unit level. Strategy implementation is executing strategy at all levels across a firm.

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1.6 Intended, Deliberate, Emergent, Realized, and Unrealized Strategies

The AFI framework is a popular and useful model of strategic management. It is a top-down, rational model that is driven by managers focused on managing the strategic management process and by strategic leaders steering a firm strategically. It is planned and methodical.

There are other approaches to strategy, such as Mintzberg and Waters's (1985) model that considers intended, deliberate, emergent, realized, and unrealized strategies. This view considers how strategies evolve over time.

The AFI framework and Mintzberg and Waters's approach are two schools of strategic thought that business leaders often find complementary.

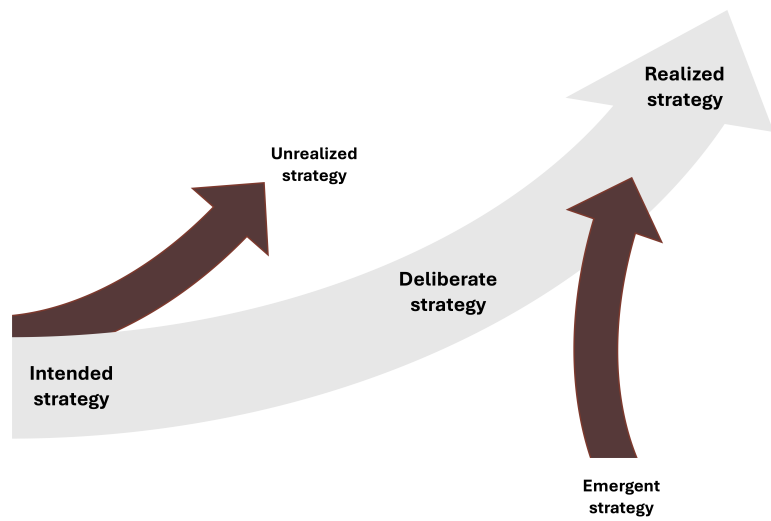


Figure 1.6: Intended, deliberate, emergent, realized, and unrealized strategies

Intended Strategy

An **intended strategy** is the strategy that an organization plans to implement. The structured strategic management process described above produces intended strategies.

Deliberate Strategy

Many things can happen between planning a strategy and implementing it, potentially requiring changes to the intended strategy. A **deliberate strategy** is the strategy that a firm implements in such a situation. It is a planned response to alter, but not completely change, an intended strategy in the face of dynamic conditions. Sometimes the factors that lead to the difference between an intended and deliberate strategy are internal to the organization, such as talent and managerial capacity. Often these differences can come from sources external to the organization, like the COVID-19 global pandemic, climate change, and changing competition.

Emergent Strategy

An **emergent strategy** is a completely new and unplanned strategy that is formulated in response to an unexpected circumstance, which most often originates from a firm's external environment (such as the emergence of a new technology). Emergent strategies are as important to a firm's success as intended and deliberate strategies. Firms that are skilled at horizon scanning for new opportunities and are nimble in response to changing conditions are better positioned to take advantage of these dynamic conditions and formulate effective and profitable emergent strategies.

Companies formulate emergent strategies and deliberate strategies in response to changing circumstances. The distinction is that deliberate strategies alter, but do not completely change, the intended strategy. They tend to be dynamic tweaks to the intended strategy. Emergent strategies, on the other hand, are completely new strategies that are formulated in response to surprising and unforeseen conditions. An emergent strategy is completely different than the intended strategy and requires a change of strategic direction.

Realized Strategy

A **realized strategy** is the strategy that an organization follows over time. Realized strategies include a firm's intended strategy and deliberate strategy if the company has altered but not completely changed the intended strategy in the face of dynamic conditions. Realized strategies may also include an emergent strategy if an unanticipated and completely new opportunity has arisen and the firm has been nimble and quick enough to capitalize on it by formulating an emergent strategy.

One way to think about intended, deliberate, and realized strategies is as an evolution of strategy over time. The company initially plans an intended strategy. A deliberate strategy is the part of the intended strategy a firm implements after taking into account dynamic conditions either in the company's external environment, such as a new competitor, or in the firm's internal environment, like a change in CEO. The deliberate strategy alters, but does not completely change, the intended strategy. A firm's realized strategy is the strategy that an organization follows over time that includes the intended and deliberate strategies and also incorporates any emergent strategies that have been formulated in response to conditions that were unforeseen when the intended and deliberate strategies were formulated. A firm's realized strategy can be different than the intended and deliberate strategy if the company has formulated an emergent strategy.

The Southern Bloomer manufacturing company is an example that illustrates intended, deliberate, emergent, and realized strategy. Managers of prison facilities believed that the underwear brands currently on the market were not suitable for harsh prison activities and constant laundry processes. Southern Bloomer saw this need and responded. They planned well and made an intended strategy to meet this market demand. This involved a structured approach to analyzing factors external to the company, such as a market assessment and competition analysis, as well as an evaluation of factors in their internal firm environment, such as talent and managerial capacity.

Southern Bloomer started selling underwear made from mostly cotton fabric to cope with prison activities and the institutional environment. They responded to customer feedback and market conditions and grew their business to a solid customer base within that market, eventually supplying institutional underwear to 125 prisons. This was Southern Bloomer's deliberate strategy because it was closely aligned to their intended strategy and amended to respond to external and internal factors.

An emergent strategy arose from an unexpected challenge related to the excess scrap fabric produced during production. The company had been discarding the leftover fabric. One day, cofounder Don Sonner visited a gun shop with his son, where he spotted a potential use for his scrap fabric. The patches that the gun shop sold to clean the inside of gun barrels were of poor quality. According to Sonner, when he saw those flimsy woven patches that unraveled when touched, he thought, "That's what I can do with the scrap fabric!" Unlike other gun-cleaning patches, the patches made by Southern Bloomer didn't shed threads or lint, which can hurt a gun's accuracy and reliability. Patches produced by Southern Bloomer quickly became popular with the military, police departments, and gun enthusiasts. Soon, Southern Bloomer was selling thousands of pounds of patches each month. A simple trip to a gun store unexpectedly led to a profitable new strategy (Wells, 2002).

In summary, the intended strategy of Southern Bloomer was to produce durable underwear for institutional settings like prisons. The company pursued this strategy closely and executed a deliberate strategy based on this intended strategy, amended to respond to dynamic conditions both in its external and internal environments. This strategy was successful and profitable, and the company continued to pursue this strategy. An emergent strategy arose that allowed Southern Bloomer to use the scrap fabric it had been sending to landfills. Southern Bloomer was quick to spot this new opportunity and nimble enough to capitalize on it. They seized the opportunity to produce gun-cleaning patches from their scrap material left over from their manufacturing of prison underwear, turning that into a second profitable line of business. Rather than sending this scrap fabric to landfills, the company found a new alternative way to make use of the material. They turned a challenge into an opportunity. Southern Bloomer's realized strategy was formed from a combination of its intended strategy, deliberate strategy, and emergent strategy. They continued to manufacture and sell underwear to prisons and opened a new successful business line in a new market to sell patches to clean guns to a variety of customers.

Unrealized Strategy

An **unrealized strategy** is an abandoned part of the intended strategy. There are many reasons why parts of strategies are abandoned, creating a gap between strategy formulation and implementation. These are elaborated on in detail in [Chapter 13](#).

Let's now consider all the strategies with another example. David McConnell was an aspiring author who faced difficulty selling his books. He tried several strategies and conventional marketing methods before he discovered the idea of giving out free perfume to those who bought his books. This innovative approach not only attracted attention but also helped him find success, leading him to lay the foundation of what would become the California Perfume Company, which was formed to market perfumes. This company developed into the massive personal care goods company that is now known as Avon. Though McConnell's dream of becoming a successful writer remained an unfulfilled plan, he created a successful strategy through Avon that was mostly driven by his capacity to seize the moment by adjusting to changing circumstances and making use of newly emerging tactics. Ultimately, his journey transformed a setback into a remarkable opportunity.

Let's look at Avon's story through the lens of intended, deliberate, emergent, realized, and unrealized strategies. David McConnell had an intended strategy to sell books he had written. He executed this intended strategy with little initial success. His books were not selling well, and his business was not profitable. In the face of this market information, McConnell decided to offer perfume as an incentive to buy his books. This was his deliberate strategy because he amended his original intended strategy of selling books to take into account lagging sales by adding the gift of perfume. His deliberate strategy altered but did not completely change his intended strategy. His focus was primarily on selling books and adding the gift of perfume was an innovation that tweaked his intended strategy. When the perfume sales proved to be a hit with customers, this provided a market opportunity that McConnell had not anticipated. The emergence of a market for the perfume independent of the books was new and unanticipated. McConnell acted quickly and decisively to take advantage of this new and unforeseen market opportunity and formulated a new emergent strategy of selling only perfume. The emergent strategy of selling only perfume was completely different than his original planned intended strategy of selling books and significantly different than his deliberate strategy of adding perfume as a gift to incentivize customers to buy his books. He capitalized on this emergent strategy that came from his own innovation. The strategy he followed over time, his realized strategy, is selling perfume. He discarded his original intended strategy of selling books and this became an unrealized strategy in the end because he abandoned that all together.

Application

- In [section 1.5](#), you considered your career aspirations from the point of view of strategic analysis, strategy formulation, and strategy implementation. Now think about your career through the lens of Mintzberg and Waters's model.
 - What is your intended career strategy?
 - Have you yet responded to any emergent strategies in your career plans?
 - How will horizon scanning help you prepare for emergent opportunities?

Key Takeaways

An intended strategy is the strategy that an organization plans to implement. The structured strategic management process described above produces intended strategies. A deliberate strategy is a planned response to alter, but not completely change, an intended strategy in the face of dynamic conditions. An emergent strategy is a completely new and unplanned strategy that is formulated in response to an unexpected circumstance. A realized strategy is the strategy that an organization follows over time. Realized strategies include a firm's intended strategy and deliberate strategy if the company has altered but not completely changed the intended strategy in the face of dynamic conditions. Realized strategies may also include an emergent strategy if an unanticipated and completely new opportunity has arisen and the firm has been nimble and quick enough to capitalize on it by formulating an emergent strategy. An unrealized strategy is an abandoned part of the intended strategy.

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1.7 Why Strategic Management Is Important

As you have learned, strategic management is a dynamic and ongoing process consisting of strategic analysis, strategy formulation, and strategy implementation. Strategic management is a critical business activity.

Strategy addresses the fundamental business question of how to create and sustain a competitive advantage by positioning a firm for superior performance relative to its competitors. This is a question all firms must ask throughout each step of the strategic management process.

Strategic leaders are responsible for ensuring their company has the human talent and organizational capacity to carry out robust and dynamic strategic management. They have the power to direct actions to ensure a sound, evidence-based strategy is formulated and implemented throughout all levels of the firm and in all areas of strategy. Strategic leadership is essential to successful strategic management.

Strategic management and strategic leadership are central to whether a company survives, grows, is successful, adapts to changing conditions, and becomes a market leader. Business success rests on strategy and its successful management and leadership.

Key Takeaways

Strategic management and strategic leadership are central to whether a company survives, grows, is successful, adapts to changing conditions, and becomes a market leader. Business success rests on strategy and its successful management and leadership.

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1.8 The History of Strategic Management

When studying any field of study, it is important to understand its history and the pivotal events that shaped it. Strategy is a part of human history. Prior to written histories, indigenous nations employed strategy to form complex alliances. For example, before European contact in the Americas, many indigenous nations formed elaborate federations and complex trade agreements (Blackhawk, 2023).

Strategy appears in historical, religious, and literary texts:

- Published in the late spring and autumn period, which corresponds to approximately the fifth century BC, Sun Tzu's *The Art of War* is an ancient Chinese treatise on military strategy that has influenced both Eastern and Western military strategy. Among its advice, is “to win without fighting is the best.”
- In the Latin poem the *Aeneid* (written between 29 and 19 BC), Virgil recounts the story of the Trojan Horse. After an unsuccessful ten-year siege of Troy, the Greeks build a large wooden horse that hides a military force; they station it outside Troy and then pretend to sail away. Intrigued, the Trojans roll the wooden horse into their city and unknowingly roll their enemy inside along with it.
- *The Prince* is a political treatise written by Florentine Niccolò di Bernardo dei Machiavelli (1469–1527). It contains the famous maxim “the ends justify the means.”

Military strategy is also studied across all nations. A few examples include Napoleon's military defeat at Waterloo in 1851, which illustrates how spreading resources too thinly can lead to defeat. In the American Civil War (1861–1865), although the Confederacy is credited with having better generals, the Union won. This is assessed to be due in part because the Union possessed better resources and employed them more successfully. Many battles of World War II (1939–1945) are still studied today. Among them is the D-Day invasion that aimed to liberate Europe from Nazi control. This is credited as bringing together many important factors for strategic success, including excellent intelligence, superior planning, and detailed preparation.

Strategic management as a field of study emerged over the last century, with several pivotal events focusing its formation.

- In 1911, Frederick W. Taylor published *The Principles of Scientific Management*, which advocated “one best way” of performing important tasks. Although the merits of “one best way,” are largely disputed today, Taylor’s emphasis on maximizing organizational performance became the core focus of strategic management as the field developed.
- Building on ideas about efficiency from Taylor and others, Henry Ford pioneered assembly lines for creating automobiles. Lowering costs dramatically allowed a once luxury item to become much more affordable.
- In 1959, the Ford Foundation widely circulated a report that recommended all business schools offer a capstone course to integrate knowledge across different business fields. The aim was to teach students to address complex business problems by emphasizing critical thinking skills. This propelled strategic management to the foreground of business education.
- In 1962, Sam Walton opened the first Walmart in Rogers, Arkansas. A decade later, Walmart was the largest company in the world. Strategic management needed to adapt to address companies like Walmart.
- In 1980, the [Strategic Management Journal](#) was created, which facilitates research and focuses a community of scholars.
- Also in 1980, Harvard professor Michael Porter published [Competitive Strategy: Techniques for Analyzing Industries and Competitors](#). Porter is a significant thought leader in strategic management.
- In 1995, Jeff Bezos launched Amazon, changing the landscape of shopping to online. Strategic management needed to adapt to address the rise of companies like Amazon.
- In the early 2000s, a series of companies such as the Enron Corporation, WorldCom, Tyco, Qwest, and Global Crossing brought ethics to the foreground of business as executives were imprisoned, investors lost money, and jobs were lost.
- In 2005 Thomas L. Friedman published *The World Is Flat: A Brief History of the Twenty-First Century*, which argues that firms in developed countries are losing the advantage they had taken for granted. One implication is that these firms will need to improve their strategies if they are to remain successful. This brought the implications of multinational competition to the foreground for strategic management.
- Although the causes of climate change have been present since nineteenth century, it was not until 1938 that amateur scientist Guy Callendar collected records from 147 weather stations across the world, and doing all his calculations by hand, discovered that global temperatures had risen 0.3°C over the previous fifty years. He argued that carbon dioxide (CO₂) emissions from industry were responsible for global warming. In 1967, researchers Syukuro Manabe and Richard Wetherald produced the first accurate computer model of Earth’s climate. However, it was not until 2006, when former U.S. Vice President Al Gore published *An inconvenient Truth*, that climate change became a household phrase in the U.S. Climate change is a major force behind the rise of sustainability as an essential business focus. Strategic management needed to adjust to this change.
- In 2018, Apple became the first company to be worth \$1 trillion.
- Leading technology company NVIDIA is well-known for its graphics processing units (GPUs). Today, NVIDIA continues to innovate through technology, integrating deep learning, artificial intelligence (AI), and gaming. Through its advancements in AI and gaming, the corporation has been important in bringing technology to the center of social media. As one of the biggest firms by market capitalization, NVIDIA has sometimes out-performed Apple throughout the years, showing its growing significance in the technology sector, particularly with the rise of AI-driven technologies. Strategic management needed to adapt to address companies like Apple and NVIDIA. It also needed to integrate the megatrend of technology as a primary focus.

Key Takeaways

When studying any field of study, it is important to understand its history and the pivotal events that shaped it. Strategy is a part of human history. Prior to written histories, indigenous nations employed strategy to form complex alliances. Strategy appears in historical, religious, and literary texts. Strategic management as a field of study has evolved and matured over the last century.

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1.9 Contemporary Critique of Strategic Management

In addition to understanding a field of study's history, it is also valuable to understand its criticisms. Strategic management is a dynamic and evolving field of practice. Along with the pivotal events presented in [section 1.8](#), criticism of strategic management influences the direction in which the field continues to grow.

Criticism about strategic management as a field of study captures the ways in which scholars and business leaders think critically about the subject and process of managing strategy. Since strategic management is a field that requires critical thinking, scholars and business leaders embrace criticism as an opportunity to thoughtfully consider it and respond so that the field continuously improves.

Strategic management is a resource-intensive process. Some strategic leaders are concerned about the time and cost to focus on a thorough strategic management process. Firm executives can be skeptical whether strategic management achieves its intended outcome of formulating and implementing evidence-based strategies that are grounded in analysis. A few critics of strategic management suggest that it constrains firms from adapting rapidly to changing circumstances.

To be open to criticism is not to suggest that the value of strategic management is under question. The value of strategic management is well established. To be open to criticism reflects a confidence in the value of strategic management and a commitment to continuously improving it. Continuous assessment and improvement is not only central to strategic management; it is a primary focus of all areas of business practice and functional expertise, including accounting and information systems, business information technology and cybersecurity, finance, insurance and business law, hospitality and tourism management, human resource management, business management, management consulting and analytics, entrepreneurship, innovation and technology management, marketing, and real estate.

Key Takeaways

Strategic management is a dynamic and evolving field of practice. Criticism of strategic management influences the direction in which the field continues to grow.

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1.10 Why Strategic Management Is Valuable in All Career Settings and at All Career Stages

In [section 1.9](#), you learned the importance of strategic management to business. It is also important to consider the ways in which strategic management is valuable to you. In doing so, we consider different career paths as well as varying career stages.

Students studying business usually obtain a broad business overview and then focus on a particular area of business. This means most business graduates are experts in a specific functional area such as accounting and information systems, business information technology and cybersecurity, finance, insurance and business law, hospitality and tourism

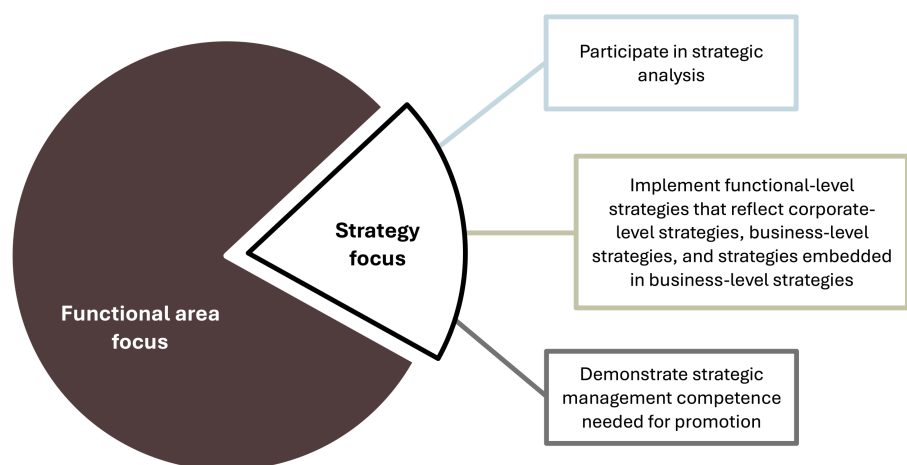


Figure 1.7: Amount of time spent on strategy in your first position as a functional area expert for a large company

management, human resource management, business management, management consulting and analytics, entrepreneurship, innovation and technology management, marketing, or real estate.

Many business graduates join large companies with formalized structures for strategic management. Although new business graduates in large companies usually focus on their functional areas of expertise early in their careers, there are multiple reasons that functional area experts need to understand strategic management when entering their first professional positions. In these roles, you immediately implement functional-level strategies, which address all areas of strategy, including corporate-level strategies and business-level strategies. You may also implement innovation strategies, sustainability and ethics strategies, technology strategies, and possibly multinational strategies. A thorough knowledge of each is essential to being successful as a functional expert in a functional business unit. Analysis in strategic management considers data at all levels of a company, so a functional expert such as yourself may be asked to participate in strategic management analysis as it relates to your functional area of expertise. When this opportunity arises, it is wise to demonstrate competence in strategic management, as this knowledge is needed even more in future positions.

As your career progresses, the amount of time spent focusing on strategic analysis, strategy formulation, and strategy implementation increases. Therefore, it is important to demonstrate competence with strategic management early, placing you on the company's radar for future promotions. To secure future positions, it is essential to demonstrate in your current position the strategic management ability needed for the next.

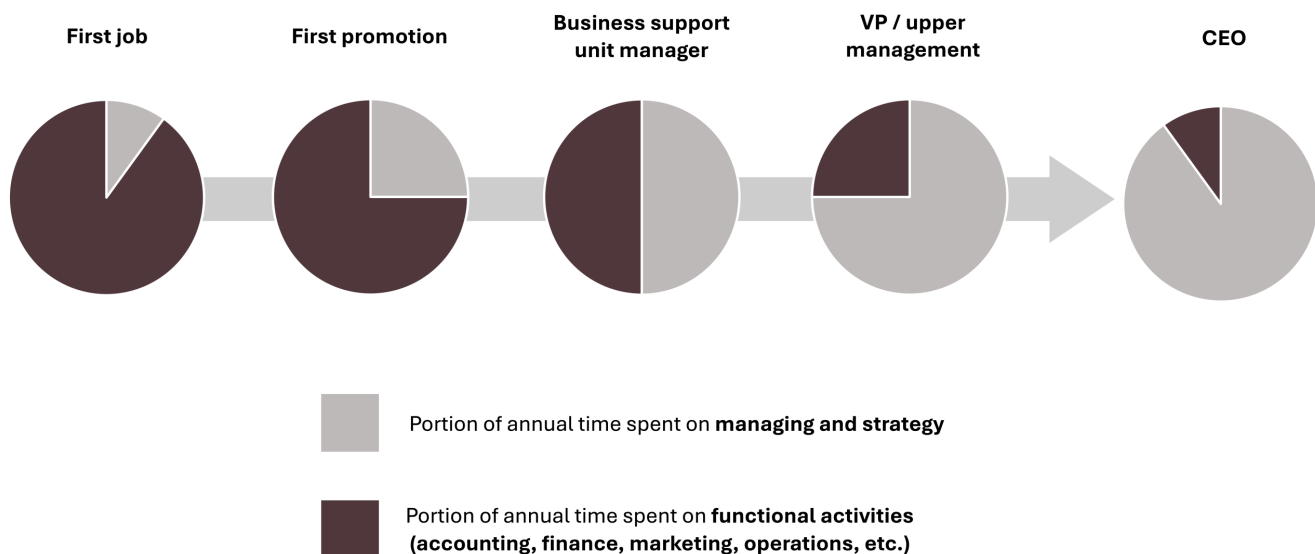


Figure 1.8: Amount of time spent on strategy as your career progresses in a large company

Some business graduates join smaller companies. In smaller firms, strategic management may be managed through more informal structures. In a smaller organization, there is an even greater chance that skills in strategic management are needed earlier in your career.

Other business graduates enter internal or external consulting roles that require competence with strategic management as a primary focus. Even if the consultation is not directly related to strategic management, consultants make presentations to business managers responsible for strategic management and organizational executives responsible for strategic leadership. It is essential to be fluent in strategic management to be competent in consulting roles.

Some business graduates already are or will become entrepreneurs. As an entrepreneur, you must understand strategic management because you may need to lead every stage of strategic management to ensure your startup is successful. It is necessary to create a competitive advantage immediately and keep that in focus as your entrepreneurial enterprise grows.

Of course, your career path may include several or all of these options. You may begin your career with a large company, then become a consultant, and then start your own business. Understanding how strategic management applies to you and your career is important to your success in any area of business throughout your career. Strategic management is not something someone else does. It will be your immediate focus in any business career.

Application

- You have now considered your career plans from the point of view of the AFI framework and through the lens of Mintzberg and Waters's model. Now that you understand why strategic management is valuable to you in any career setting and at all stages of your career, consider:
 - How specifically will you use your strategic management knowledge and skills in your first professional position after graduation?

Key Takeaways

As a new business graduate entering your first professional position at a large company, you need to understand strategic management because you will immediately implement functional-level strategies that reflect corporate-level strategy, business-level strategy, and strategies that are embedded into business-level strategy, such as innovation, sustainability and ethics, technology, and possibly multi-national strategies; you may be asked to participate in strategic management analysis as it relates to your functional area of expertise; and it is wise to demonstrate competence in strategic management because this knowledge is needed in future positions. As your career progresses in a large company, the focus on strategic management increases. If you graduate and join a smaller company where strategic management is managed through more informal structure, you are likely to participate in more of the strategic management process immediately. Internal or external consultants require strategic management competence as the primary focus of your role. Entrepreneurial business graduates need to understand strategic management to ensure your startup is successful.

1.11 Conclusion

In this introduction to strategic management, you learned how a few essential terms are used in the book, including *organization*, *business*, *company*, *firm*, *industry*, *strategic management concepts and theories*, and *analytical frameworks and tools*. You considered what strategic management is and reviewed the analysis, formulation, implementation (AFI) framework, which guides the book. You learned an alternative and complementary approach to the AFI framework's planned and methodical approach, involving intended, deliberate, emergent, realized, and unrealized strategies. You considered why strategic management is important to businesses. You reviewed the history of strategic management and the contemporary critique of the field. Finally, you learned how strategic management is valuable to you in all career settings and at all career stages. Now that you have learned what strategic management is, the next chapter introduces you to conducting a case analysis.

Demonstrate Your Knowledge, Skills, and Competence

1. Describe organization, business, company, firm, and industry and their relationships to each other. Give examples, and explain how your examples illustrate each.
2. Explain concepts, theories, and analytical frameworks and tools and their relationships to each other. Give examples, and explain how your examples illustrate each.
3. Define strategic management. How does this compare to what you expected strategic management to be before you began this course?
4. Describe strategic leadership, strategic management, and strategy and their relationships to each other.
5. Explain strategic analysis, strategy formulation, and strategy implementation and their relationships to each other.
6. Describe the analysis, formulation, implementation (AFI) framework. How much of the framework can you recall without referring to the diagram? Now return to figure 1.3 and be sure you understand each element in the figure and their relationships.
7. Explain the concepts of strategic issue and strategic alternative, giving an example of each. These are essential throughout the course, so understanding them now is important.
8. Describe the three levels of strategy. Which level of strategy are you most likely to directly analyze, formulate, and implement in your first position after graduation?
9. Explain Mintzberg and Waters's (1985) model of strategy. How does this compare and contrast with the strategy in the AFI framework?
10. Discuss why strategic management is important to businesses. What are the risks when firms do not manage strategy well?
11. Describe several key events in the history of strategic management. Which events were familiar to you? Were there any that surprised you? Discuss why knowing the history of a subject is important.
12. Discuss a few of the critiques of strategic management. Why is critiquing a field important?
13. Describe how strategic management is relevant to you and your career.

By answering these questions robustly, you have demonstrated your thorough knowledge of this overview of strategic management. Well done!

Figure Descriptions

Figure 1.3: Circular flow chart illustrating different aspects of strategic management. The center of the circle is labeled strategic management and strategic leadership. Moving clockwise, the first category is strategic analysis (i.e., Where are we?) and includes 4 blue boxes: analyze organizational performance, analyze external environment, analyze internal environment, and determine strategic issue and alternatives. Second category is strategy formulation (i.e., Where are we going?) and includes three light green boxes representing three levels of strategy and four dark green boxes representing strategies that are embedded into business-level strategy. Light green: formulate corporate-level strategy (where to play), formulate business-level strategy (how to win/right to win), and formulate functional-level strategy. Dark green: formulate innovation strategy, formulate sustainability and ethics strategy, formulate technology strategy, and formulate international strategy. Third category is strategy implementation (i.e., How do we get there?) and includes one orange box: implement strategy.

Figure 1.4: Inverted blue pyramid that is divided into six sections. The title of the chart reads "Strategic analysis; Where are we?" From top to bottom, the sections are: analyze organizational performance, analyze external environment, analyze internal environment, synthesize external and internal analysis, determine strategic issue, and determine strategic alternatives.

Figure 1.5: Green flow chart titled “Strategy formulation: where are we going?” The chart is three levels. Topmost level represents corporate-level strategy (i.e., where to play?). Middle level represents business-level strategies and their associated strategic business units (i.e., how to win?). A list titled “Right to win?” is connected to one of the business-level strategy boxes. The list includes innovation strategy, sustainability and ethics strategy, multinational strategy, and technology strategy. The bottommost level represents functional-level strategies and their associated functional business units.

Figure 1.6: A large, gray arrow curving upward from left to right contains three labels. Left part of the arrow is labeled intended strategy. Middle part of the arrow is labeled deliberate strategy. Right part of the arrow is labeled realized strategy. A smaller purple arrow juts out from the “intended strategy” part of the original arrow and points away. It is labeled unrealized strategy. Another small purple arrow comes the right, seemingly from nowhere, and merges with the original arrow between deliberate strategy and realized strategy. This small arrow is labeled emergent strategy.

Figure 1.7: Purple pie chart illustrating two main segments titled functional area focus (roughly 75%) and strategy focus (roughly 25%). Three boxes jut out from strategy focus: (1) participate in strategic analysis, (2) implement functional-level strategies that reflect corporate-level strategies, business-level strategies, and strategies embedded in business-level strategies, and (3) demonstrate strategic management competence needed for promotion.

Figure 1.8: Five purple pie charts representing career progression from first job to CEO. Each chart shows the portion of annual time spent on (1) managing and strategy, and (2) functional activities including accounting, finance, marketing, and operations. First job shows 90% functional activities and 10% managing and strategy. First promotion shows 75% functional activities and 25% managing and strategy. Business support unit manager shows 50% functional activities and 50% managing and strategy. VP/upper management shows 25% functional activities and 75% managing and strategy. CEO shows 10% functional activities and 90% managing and strategy.

Figure References

Figure 1.1: Elon Musk follows through on Tesla's Master Plan. Steve Jurvetson. 2016. CC BY 2.0. <https://flic.kr/p/HJfr8c>

Figure 1.2: Strategic leaders align strategic analysis, strategy formulation, and strategy implementation, much like fitting puzzle pieces together correctly. Kindred Grey. 2025. CC BY. Adapted from “Brain with a head outline and grey and blue puzzle pieces” by Raquel Mela (2019). https://commons.wikimedia.org/wiki/File:Brain_with_a_head_outline_and_grey_and_blue_puzzle_pieces.jpg

Figure 1.3: The analysis, formulation, implementation (AFI) framework. Kindred Grey. 2025. CC BY.

Figure 1.4: Strategic analysis. Kindred Grey. 2025. CC BY.

Figure 1.5: Strategy formulation. Kindred Grey. 2025. CC BY.

Figure 1.6: Intended, deliberate, emergent, realized, and unrealized strategies. Kindred Grey. 2025. CC BY.

Figure 1.7: Amount of time spent on strategy in your first position as a functional area expert for a large company. Kindred Grey. 2025. CC BY.

Figure 1.8: Amount of time spent on strategy as your career progresses in a large company. Kindred Grey. 2025. CC BY.

2. INTRODUCTION TO CASE ANALYSIS

Learning Objectives

After you have engaged with the concepts in this chapter, you will understand and be able to apply the following key case analysis concepts:

1. How the terms *case*, *case analysis*, *data*, *analysis*, *interpretation*, *evaluation*, *line of sight*, and *congruence* are used in the textbook
2. Case analysis process
3. Case analysis steps
4. Abbreviated case analysis steps

2.1 Introduction

In the previous chapter, you were introduced to strategic management as an area of practice in businesses and as a field of study. This chapter introduces you to case analysis. After an explanation of how some essential terms are used in the book, you then learn what is involved in conducting a case analysis—both full and abbreviated versions.

2.2 Case and Case Analysis

First, it is important to understand how the terms *case* and *case analysis* are used in the textbook.

Case

Imagine you are asked to read a case about a real company and that case contains real information about what the firm has faced. This may be a case from a well-known publisher, such as a Harvard Business case, or it could be an open-source case (free to you). You may even be asked to read a case about a hypothetical company that uses realistic but hypothetical data about the business. Hypothetical cases are sometimes used to illustrate especially sensitive areas of business that a real company would hesitate to disclose. Both real and hypothetical cases are written cases, which means they can cover only a limited timeframe. Some of the case data may be written as a narrative about the company, and other data may be presented as quantitative or qualitative data in tables, charts, and graphs, for example. Perhaps you have read cases like these during your business education so far.

Therefore, in the context of strategic management, **cases** are written scenarios about companies, such as Harvard Business cases or open-source cases, that present real business issues faced by firms. Sometimes they contain real facts about real companies, while other times, cases are written scenarios about a hypothetical company that uses realistic but hypothetical data.

Whether about real or hypothetical companies, cases are usually limited in the timeframe they cover. Cases often focus on a narrow range of company information to support students seeking in-depth understanding of an area of strategic management.

Case Analysis

Engaging in experiential learning by applying strategic management concepts and theories and analytical frameworks and tools to cases is an excellent way for you to learn “by doing.” Early in learning about strategic management, you may apply one concept and one analytical framework to a case. For example, you may apply what you learn about a firm’s external environment using a PESTEL framework (which you will learn more about in [Chapter 4](#)) to information about a real company. As your learning progresses, you may be asked to apply more of what you know about strategic management using multiple analytical frameworks.

Therefore, in strategic management, case analysis is a broad term used to encompass multiple possible approaches to conducting a strategic management review of a company. A **case analysis** is a thorough and methodical analysis, interpretation, and evaluation of a case or company.

There are two important things to notice about the term *case analysis*. The first is the use of the word *case*. As you have just seen, a case is a written scenario about a real or hypothetical company. In case analysis, a case can be a written scenario about a real or hypothetical company. If the case uses current real data about a real company, you can obtain this data in one of two ways. You can conduct research about a real company in the form of a desk review, meaning you do not meet with the leaders of the company. You gather data from sources to conduct a case analysis in this instance. The other option would be to provide consulting services to a real company, both collecting data about the company and using data the leaders of a company provide you to conduct the case analysis.

The second important thing to notice about case analysis is the use of the word *analysis*. Though the term *case analysis* only mentions analysis, the process of analysis includes three steps: analysis, interpretation, and evaluation. Analysis, interpretation, and evaluation are reviewed in detail below.

You can see that *case analysis* is an umbrella term that means applying strategic management concepts and theories and analytical frameworks and tools to analyze, interpret, and evaluate company information provided in a written scenario that uses real or hypothetical data about a company; case analysis can also be carried out in researching a company or working directly with a company through a consultancy project.

Case analysis is used as a pedagogical tool in strategic management because it requires you to step into the shoes of strategic leaders and managers and see the company from their perspective. By conducting case analysis, you strategically analyze a firm’s organizational performance and its external and internal environments. Then, by analyzing strategies, you learn how strategic leaders and managers formulate strategy. Finally, you consider strategy implementation by using the tools of strategic leaders and managers to assess the success of implemented strategies.

Key Takeaways

Cases are written scenarios about companies that present real business issues that real firms face. Cases may also focus on a hypothetical company that uses realistic but hypothetical data about the organization. *Case analysis* is an umbrella term that means applying strategic management concepts, and analytical tools to analyze, interpret, and evaluate company information that is provided through a written scenario that uses real or hypothetical data about a company, or researching a company; it’s also part of researching a company or working directly with a company through a consultancy project.

2.3 Data, Analysis, Interpretation, and Evaluation

When conducting a case analysis, it is important to consider the difference between data, analysis, interpretation, and evaluation and how they relate. Conducting a case analysis follows a structured process that involves analyzing data, interpreting the analysis, evaluating the analysis and interpretation, and ensuring line of sight and congruence.

The purpose of the following section is to introduce you to these ideas so they can serve as a reference for you as you continue your learning throughout the book. Subsequent chapters introduce analysis instruments that support you in conducting case analysis using many of the key strategic management analytical frameworks and tools. These analysis instruments rely on a robust application of the concepts of data, analysis, interpretation, evaluation, line of sight, and congruence.

Dictionary definitions of *analysis*, *interpretation*, and *evaluation* are narrow, and most methodological scholarship either uses these terms without explicit definitions or offers definitions that are ambiguous, overlapping, technical, or related to specific contexts. There is also little agreement between sources about the distinctions of these processes. Therefore, a different approach is needed to understand these ideas in the context of strategic management.

For the purposes of this textbook, these ideas are approached from a pragmatic and applied perspective, that considers how they support case analysis. They are informed by the experience of organizational executives who focus on strategic analysis, strategy formulation, and strategy implementation. They are also vetted by internal and external strategic management consultants to organizational leaders.

Each of these ideas—data, analysis, interpretation, and evaluation—is considered in turn to add conceptual clarity to the process of conducting a thorough case analysis. In practice, the distinctions between each idea may be less delineated, combining with and informing each other.

The first important term is *data*.

Data

Data is the information in the case being reviewed, the company being researched, or the company receiving consulting services. For example, data may include information such as whether a company is a domestic or multinational firm, what industry, market, and market segments in which the business operates, whose its major competitors are, and whether the company follows a centralized or decentralized management style, to name just a few.

Analysis

Analysis is the process and result of examining all the data available for the firm and identifying and classifying all the data for each category in a strategic management tool. Many cases contain a lot of data, and your task when conducting a case analysis is to sift through a large volume of data to determine which of the data is important and which data is to be placed into which strategic management tool. This requires a thorough understanding of the case and the strategic management framework you are applying.

For example, the PESTEL framework is one of the strategic management frameworks you use to analyze a company's external environment. The first and broadest level of a firm's external environment is the general environment, which consists of the societal events and trends that impact all firms in an industry including political, economic, sociocultural, technological, environmental, and legal factors. You will learn about a firm's external environment and how to analyze it in [Chapter 4](#). Imagine that you analyze a firm's external environment and identify a growing consumer preference for healthier food options that impacts the sales of the company's product. You also notice that phone app sales are increasing among customers over thirty-five. You then place both of

these observations in a PESTEL strategic management tool, identifying the growing consumer preference for healthier food options as a sociocultural factor and phone app sales increasing among customers over thirty-five as a technological factor.

To conduct an analysis of the data, follow these steps:

Step 1

- Methodically and thoroughly examine all the data available for the firm.

Step 2

- Identify all the data about the firm that the strategic management framework addresses.
- Question to ask: What information about the company relates to this strategic management framework?

Step 3

- Classify all the data about the company for each category in the strategic management tool.
- Question to ask: Where in the strategic management tool does this information best fit?

Step 4

- Complete the analysis section of a strategic management instrument.

Analyzing data is different than placing data from the company in the strategic management instrument. Analysis requires critical thinking and a thorough knowledge of the company that can only come from reading the case or company research multiple times.

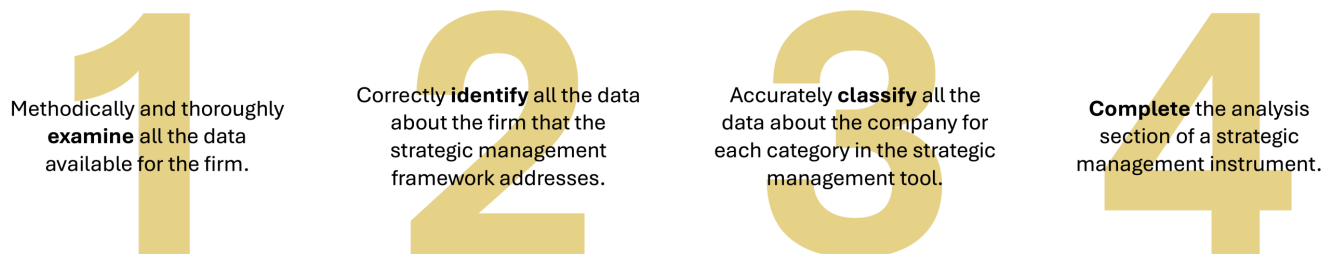


Figure 2.1: Analyze the data

So far, analyzing the data in the case has produced a large quantity of information by examining, identifying, and classifying all the data about the company. After analyzing an aspect of a firm using a strategic management framework (such as analyzing the general external environment using the PESTEL tool), you can narrow the focus by considering why the situation is occurring and its meaning for the company. Interpretation and evaluation begin to narrow the focus.

Interpretation

Once you have analyzed the data, it is possible to interpret the analysis.

Once you have analyzed the case, you now review your analysis. **Interpretation** is the process and result of examining the analysis to identify and explain relationships in the analysis as well as underlying root causes of the situation.

For example, when you review your analysis, you notice that food and drink sales are stronger on phone apps than those placed in the drive-through. When you examine the analysis in more detail, you notice that phone app sales are increasing among customers over thirty-five. When you consider this analysis along with a growing consumer preference for healthier food options, you may see a correlation between customers preferring healthier food that they can purchase on an app.

You should also consider which aspects of your analysis relate to each other and in what ways. When you consider the root causes of the increase in phone app usage in customers over thirty-five, you may find the underlying cause of this trend is that, for those over thirty-five, adoption of phone apps to order food requires a change in behavior, whereas those under thirty-five have been using phone apps for most purchases throughout their buying years. Changes in behavior always take more time.

Interpretation is not found in the case or company research. Interpretation is the process and result of applying critical thinking to the analysis conducted so far.

Interpret the analysis of the data by following these steps:

Step 1

- Examine the analysis.

Step 2

- Identify and explain whether, how, and in what ways the information in the analysis is related.
- Questions to ask:
 - How does one element of the analysis in the strategic management tool relate to another element of the analysis in the tool?
 - How does the analysis in each section of the strategic management framework relate to each other?
 - What elements of the analysis in the strategic management tool were expected?
 - What elements of the analysis in the strategic management tool were unexpected?
 - Are there incongruencies between the elements of the analysis in the strategic management tool?

Step 3

- Identify and explain underlying root cause(s) of the situation.
- Question to ask: What may be causing the information identified in the analysis?

Step 4

- Complete the interpretation section of a strategic management instrument.

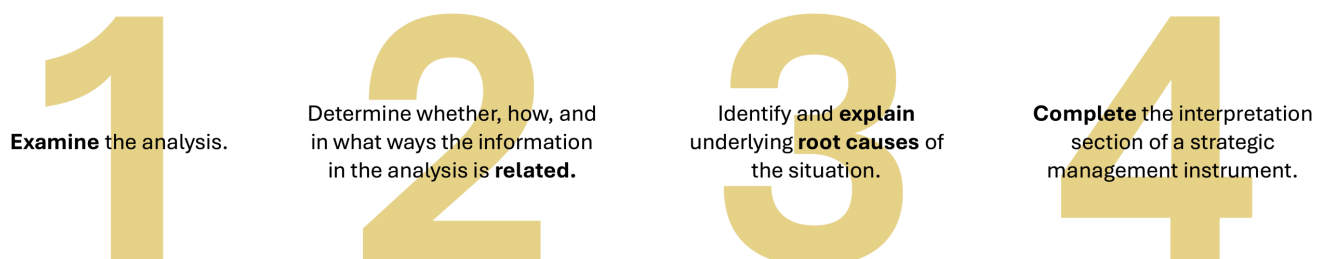


Figure 2.2: Interpret the analysis

Interpretation requires discernment and judgment. Answer the questions and complete the steps above that are relevant to the firm and the strategic management tool. It is not realistic or productive to answer every question and complete every step for each element of your analysis. The goal of interpretation is to begin to narrow the focus of your analysis of all the data on the company to that which is most important.

Evaluation

Once you have interpreted the analysis, the next step is to evaluate the information produced from the analysis and interpretation. Evaluation continues to narrow the focus of your analysis.

Evaluation is the process and result of examining the analysis and interpretation to identify and explain the meaning of the information to the company by considering its impact, relevance, and importance to the company and by identifying the company's current, potential, or needed assets, organizational capacity, and managerial ability that may support or mitigate the areas of highest impact, relevance, and importance for the firm.

In considering the interpretation you have conducted so far, you decide that because your primary target market segment is those 18–25 years old, the trend of increased usage of phone apps in those over thirty-five is likely to impact the business less, making the trend less relevant and important to this company. You also determine that knowing that the drive-through is used less frequently for ordering is important for the company because up to now it has made location decisions based on the need for a drive-through. This may be relevant and important to the company, potentially having a significant impact on its future expansion decisions. To consider a change in expansion strategy, the organization needs resources in marketing research, capital assessment, and technology development (including cybersecurity), to name just a few.

Like interpretation, evaluation is not found in the case or company research. Evaluation is the process and result of applying critical thinking to the analysis and interpretation conducted so far.

Follow these steps to evaluate the analysis and interpretation:

Step 1

- Examine the analysis and interpretation.

Step 2

- Identify and explain whether, how, and in what ways the information in the analysis and interpretation impacts the company.
- Questions to ask:
 - How does each element of the analysis and interpretation in the strategic management tool impact the company?
 - From a holistic point of view, looking across all the information in the analysis and interpretation in the strategic management tool, how does this information impact the company?

Step 3

- Identify and explain whether, how, and in what ways the information in the analysis and interpretation is relevant to the company.
- Questions to ask:
 - How is each element of the analysis and interpretation in the strategic management tool relevant to the company?
 - From a holistic point of view, looking across all the information from the analysis and interpretation in the strategic management tool, how is this information relevant to the company?

Step 4

- Determine how important the information is to the firm.
- Action to take (if helpful): Rank the information from the analysis and interpretation according to strength of importance, such as strong, moderate, or weak.

Step 5

- Identify the company's current, potential, or needed assets, organizational capacity, and managerial ability that may support or mitigate the areas of highest impact, relevance, and importance for the firm.
- Questions to ask:
 - What are the company's current, potential, or needed assets, that may support or mitigate the areas of highest impact, relevance, and importance for the firm?
 - What is the company's organizational capacity that may support or mitigate the areas of highest impact, relevance, and importance for the firm?
 - What managerial ability does the company possess that may support or mitigate the areas of highest impact, relevance, and importance for the firm?

Step 6

- Complete the evaluation section of a strategic management instrument.

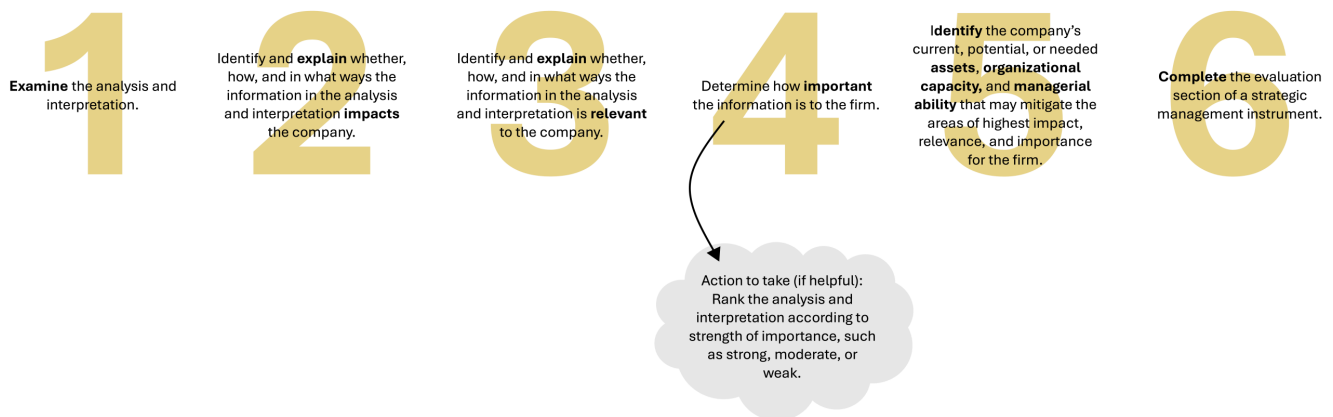


Figure 2.3: Evaluate the analysis and interpretation

Like interpretation, evaluation requires discernment and judgment. Answer the questions and complete the steps that are relevant to the firm and the strategic management tool. The goal of evaluation is to continue to narrow the focus of your analysis of all the data on the company to that which is most important.

Application

- Think about one of the times you enjoyed a project in your business education where you analyzed, interpreted, and evaluated data.
 - Can you identify some of the steps above in that project?
 - What was different in that project compared to the steps above?

Key Takeaways

Data is the information in the case being reviewed, the company being researched, or the company receiving consulting services. Analysis is the process and result of examining all the data available for the firm and identifying and classifying all the data for each category in a strategic management tool. Interpretation is the process and result of examining the analysis to identify and explain relationships in the analysis and underlying root causes of the situation. Interpretation is not found in the case or company research. Evaluation is the process and result of examining the analysis and interpretation to identify and explain the meaning of the information to the company by considering its impact, relevance, and importance to the company and by identifying the company's current, potential, or needed assets, organizational capacity, and managerial ability that may support or mitigate the areas of highest impact, relevance, and importance.

2.4 Line of Sight and Congruence

Strategic analysis requires that steps in the process have a direct and clear line of sight and strong congruence. The ideas of line of sight and congruence are similar yet distinct.

When thinking about analysis, interpretation, and evaluation through the lens of strategic analysis, confirm line of sight and congruence from three perspectives.

1. Within a strategic management tool, from analysis to interpretation to evaluation
2. Among strategic management frameworks
3. Across the entire case analysis

Line of Sight

Line of sight means there is a direct, unobstructed line between an observer and the object being observed. Imagine you are attending a match of your favorite women's tennis team, perhaps your university's team. Your seat is slightly raised from the seats in front of you, giving you an unobstructed view of your team winning. You have a clear and direct line of sight to players and the game. In strategic analysis, and in business generally, line of sight is used metaphorically to refer to a direct and clear logic connecting two or more concepts or ideas. In strategic analysis, you identify and state specifically what that line of sight is.

Investigate the questions below to identify and explain a direct and clear logic connecting two or more concepts or ideas.

- Is there a direct and clear logic connecting two or more ideas within an element of a strategic management tool during analysis, interpretation, or evaluation?
 - For example, when you consider a firm's external environment, you can use a PESTEL framework as a tool, which considers sociocultural factors, among others. Imagine you identify two sociocultural factors in your PESTEL analysis. One is a growing consumer preference for healthier food options and another is a shift in demographics, with more Muslims and Hindus living in the area. Ask yourself if there is a connection here. Identifying a line of sight between these two sociocultural factors may lead you to a connection between not only healthier food options but also anticipating a growing demand for halal, vegan, and vegetarian menu items.
- Is there a direct and clear logic connecting two or more ideas between elements of a strategic management tool?
 - For example, consider that you identify in your PESTEL analysis a shift in demographics with more Muslims and Hindus living in the area as a sociocultural factor and stronger food and drink sales on phone apps than those placed in the drive-through as a technological factor. Can you see a relationship between these? By identifying a line of sight between the sociocultural and technological factors, you may identify the need not only to offer more non-alcoholic drinks but also to show more images on your phone app for mango lassis, which may appeal to a broad audience.
- Is there a direct and clear logic connecting two or more concepts or ideas among strategic management frameworks?
 - For example, you use a PESTEL framework to analyze a firm's external environment and a VRIO framework for its internal environment (more on each of these in later chapters). Imagine that in your internal analysis of the business, you identify partnerships with organic and regenerative suppliers as a strategic resource. What lines of sight can you trace between your internal and external analyses? Perhaps you see a connection between organic and regenerative suppliers and a growing consumer preference for healthier food options. You recognize that here may not necessarily be a 100 percent overlap in these two elements of your analysis. After all, classic Oreos are vegan. You further understand that many consumers who are interested in healthier food seek out organic and regenerative food options. Drawing this line of sight across different strategic management frameworks may support the business in considering foregrounding its organic and regenerative products in its marketing, expanding its organic and regenerative options, or even acquiring a supplier.
- Is there a direct and clear logic connecting two or more concepts or ideas across the entire case analysis?
 - When you finish your entire case analysis, you consider all of your analysis, interpretation, and evaluation, looking for as many lines of sight as possible, just as you searched within and among strategic management tools. This time, you consider the whole case analysis. The more connections and lines of sight you identify, the more robust your case analysis.

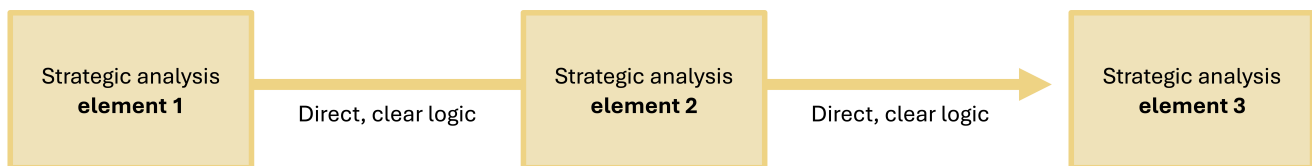


Figure 2.4: Confirm line of sight

Congruence

The concept of congruence also is important to case analysis.

Congruence means there is a one-to-one relationship or agreement between two or more things. There is harmony or compatibility between two things that are congruent. The two things do not necessarily have to be identical and in most cases are not exactly alike. Imagine you and your friend share similar taste in music. You both love a particular genre and like many of the same songs. However, you also dislike some of the songs your friend likes. Because your taste is compatible and you like more of the same songs as your friend than you dislike, your taste in music is congruent. In case analysis, congruence means there is a one-to-one agreement

or reconciliation between steps in the case analysis process or across an entire case analysis. All the main elements are compatible. Congruence is more relevant for some phases of case analysis.

Ensure there is robust congruence by considering the following steps.

Step 1

- Identify and explain how everything that is relevant in one aspect of the case analysis is also included in another aspect of the case analysis.
- Questions to ask:
 - Among specific steps in the case analysis, is everything that is relevant in one step of the case analysis also included in another step of the case analysis?
 - For example, as you learn in [section 2.6](#), the case analysis process includes multiple steps such as analyze a firm's organizational performance, external environment, and internal environment. Then you synthesize this analysis by conducting a SWOT (strengths, weaknesses, opportunities, and threats) analysis. It is important that all essential details that are relevant from the analysis of the firm's organizational performance, external environment, and internal environment are also present in the SWOT analysis.
 - Across the entire case analysis, is everything that is relevant in one step of the case analysis also included in another step of the case analysis?
 - For example, as you also learn in [section 2.6](#), the case analysis process consists of thirteen steps. Now ensure everything that is relevant in one step in the case analysis process is carried through and is present in all the steps in the entire case analysis. Step one focuses on ensuring all essential details are included among steps in the case analysis and across the entire case analysis.

Step 2

- Identify and explain how nothing that is relevant in one aspect of the case analysis is absent from another aspect of the case analysis.
- Prompts to consider:
 - Among specific steps in the case analysis, ensure nothing relevant in one step of the case analysis is absent from another step of the case analysis.
 - For example, ensure nothing that is relevant from the analysis of a firm's organizational performance, external environment, and the internal environment is omitted in the SWOT analysis.
 - Across the entire case analysis, ensure nothing relevant in one step of the case analysis is absent from another step of the case.
 - For example, now ensure nothing that is relevant in one step in the case analysis is omitted in another step in the case analysis. Review the entire case analysis to confirm each essential detail is carried through across all the steps in the entire case analysis process. Step two focuses on confirming that no essential details are omitted among steps in the case analysis and across the entire case analysis. As you conduct case analyses, what information is relevant to be included in each step of the case analysis and what information is important to be present across the entire case analysis will become clear.

You ensure congruence, which is a one-to-one reconciliation among and across all steps in the case analysis process, by making sure everything that is essential is included and nothing essential is omitted among and across all steps in the case analysis.

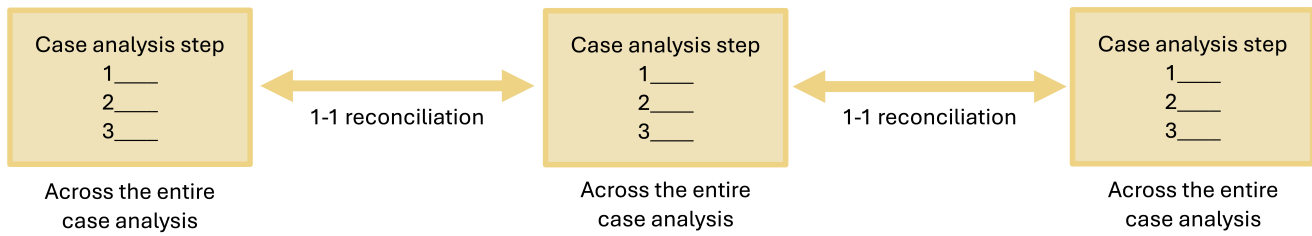


Figure 2.5: Confirm congruence

As you have just learned, line of sight and congruence are similar and distinct. You often assess both together in case analysis, and the difference can be a matter of emphasis. Line of sight focuses primarily on a direct and clear logic between ideas, and congruence focuses primarily on agreement, compatibility, and harmony between ideas. As you learn in [section 2.6](#), the final step in the case analysis process is presenting the case analysis. This is not a description or summary of all the preceding steps. This is a rich and robust narrative that presents the analysis, conclusions, and suggestions for future actions. The presentation needs to be logical and have a clear line of sight between all aspects of the case analysis. This ensures a rational, cohesive presentation. Ensuring congruence in the case analysis means the conclusions and recommendations are based on the analysis and the presentation does not suddenly introduce new and unexpected information that has not been previously supported by the analysis. It also ensures no essential information is omitted. Often in case analysis, when line of sight is strong, congruence is also robust, but this is not always the case. It is possible that either line of sight or congruence may be strong and the other weak. That is why it is important to understand how these ideas are related and different.

Now that you understand line of sight and congruence and have a clear conception of data, analysis, interpretation, evaluation, and how they relate, it is now possible to conduct case analysis.

Key Takeaways

Line of sight means there is a direct and clear logic connecting two or more concepts or ideas. Congruence means there is a one-to-one relationship between two or more things, with agreement, compatibility, and harmony between ideas. In case analysis, it means there is a one-to-one reconciliation between steps in the case analysis process or across an entire strategic analysis.

2.5 Case Analysis Process

[Chapter 1](#) introduced you to the subject of strategic management. In this chapter, you learn how to apply strategic management concepts, and analytical frameworks in conducting a case analysis.

Business is fundamentally a profession of doing, of action. To be successful, that action needs to be grounded in knowledge and evidenced-based decisions. To be industry leading, it needs to reflect inspiration, creativity, and insight.

Business is full of multiple dynamic tensions, and as an area of business, strategic management reflects many of these tensions. Strategic management embodies tensions between planning methodically and capitalizing on unexpected opportunities; between making decisions based on evidence and analytics or based on creativity and insight; between focusing on important details and seeing the bigger picture.

When conducting a case analysis, you use all of your capabilities, some of which are your preferred ways of operating and some that may challenge you. For example, though a successful career and life require the ability to consider both minute details and the big picture, most will naturally prefer one or the other, perhaps showing more skill with one.

In light of this potential difference in skills across expertise, strategic management and its application through case analysis is most often the focus of diverse and cross-functional teams. Such a team offers the advantage of a diverse range of topic expertise, such as accounting, business information technology and cybersecurity, finance, insurance and business law, human resource management, and marketing. It also utilizes a diverse range of talents and capabilities, ensuring, for example, that the team can focus on details and the big picture.

Case analysis starts with the objective data mining of company data and becomes more subjective as the process progresses through analysis, interpretation, and evaluation. A structured case analysis process incorporates both a micro, detail-oriented focus and a macro, big-picture orientation that considers the entire situation facing a firm.

Case analysis is central to strategic management. Conducting a case analysis follows a structured process. This requires a methodical approach that relies on a solid cross-functional understanding of business, thorough knowledge of the company, critical thinking, insight, judgment, intuition, and creativity.

First consider all the data in a company, and then gradually narrow the focus. Thoroughly analyze all the data available about the firm. Interpret and evaluate the information that is relevant and useful.

Because the ideas and process build upon each other, the early stages of conducting a case analysis require you to sequentially analyze the data, interpret the analysis, and evaluate the information produced so far through analysis and interpretation. As the review of a firm progresses, return to previous stages and consider the other ideas as well.

Key Takeaways

When conducting a case analysis, you use all of your capabilities, some that may be your preferred ways of operating and some that may challenge you. Strategic management and its application through case analysis is most often the focus of diverse and cross-functional teams. This takes advantage of a diverse range of topic expertise and capabilities. Case analysis begins with the objective data mining of company data and becomes more subjective as the process progresses through analysis, interpretation, and evaluation. A structured case analysis process incorporates both a micro, detail-oriented focus and a macro, big-picture orientation that considers the entire situation facing a firm. Case analysis is central to strategic management.

2.6 Case Analysis Steps

Utilize the following process to conduct a case analysis that follows a structured process. There are multiple steps, and conducting a case analysis in order is important. The overview presented here can be used as a reference as you conduct case analyses throughout the course. The following chapters discuss each step and the frameworks involved in detail.

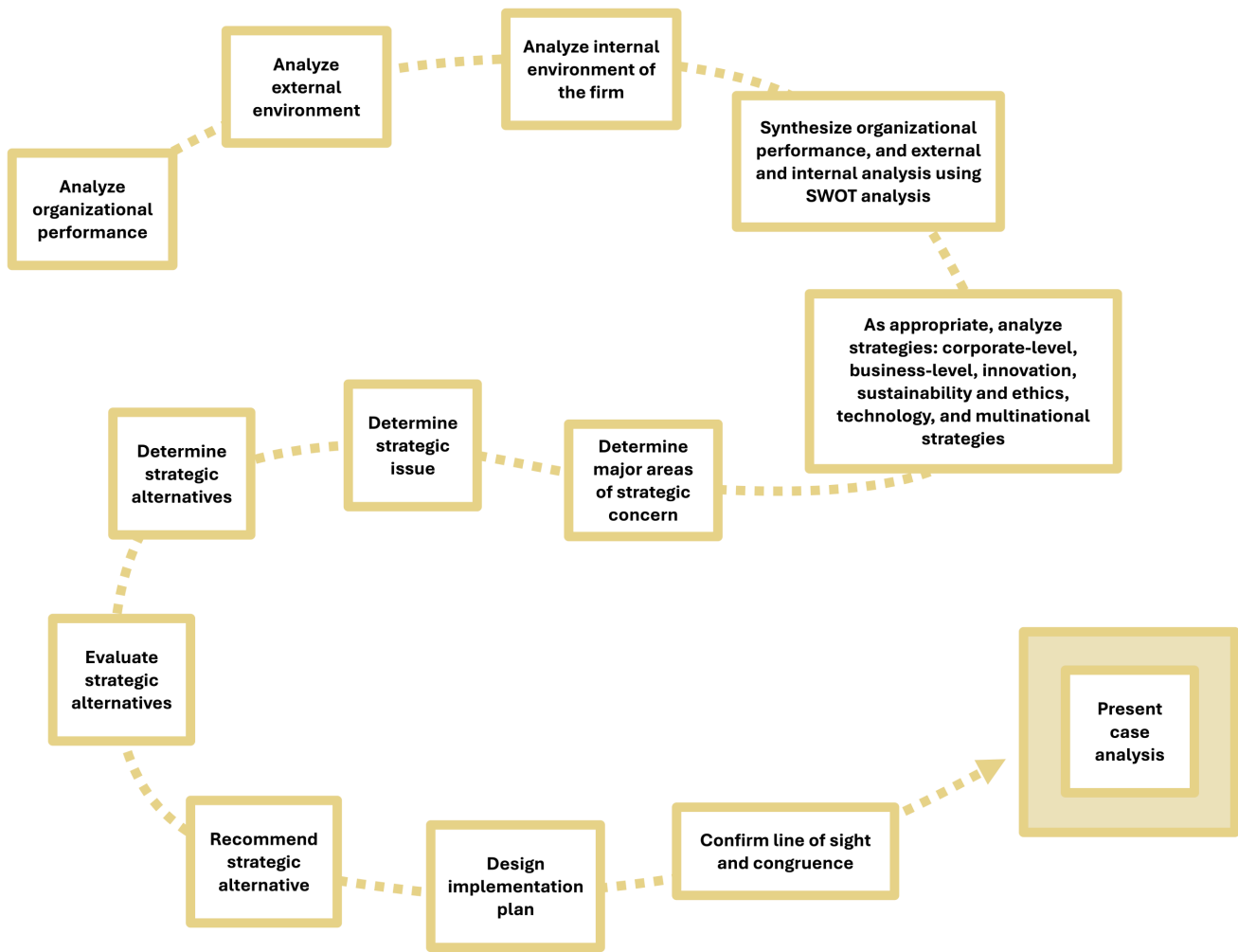


Figure 2.6: Case analysis

1. Analyze a firm's organizational performance.

- a. Use the organizational performance analysis instrument to analyze a firm's organizational performance.
 - i. Analyze, interpret, and evaluate the firm's mission, purpose, vision, values, and goals.
 - a. Evaluate line of sight and congruence among the firm's mission, purpose, vision, and values.
 - ii. Analyze, interpret, and evaluate the firm's financial position.
 - iii. Analyze, interpret, and evaluate the firm's market position.
 - iv. Analyze, interpret, and evaluate additional relevant quantitative measures of organizational performance.
 - v. Analyze, interpret, and evaluate a firm's balanced scorecard.
 - a. Evaluate line of sight and congruence among the measures in the balanced scorecard.
- b. Common-size data and present trends to ensure the analysis is meaningful.

2. Analyze the external environment.

- a. Use strategic management analytical frameworks to analyze, interpret, and evaluate the external environment of the company.
 - i. Use the PESTEL analysis instrument to analyze, interpret, and evaluate the general environment.
 - a. Ensure line of sight and congruence among the elements of the PESTEL analysis.
 - ii. Use the Porter's Five Forces analysis instrument to analyze, interpret, and evaluate the industry environment.
 - a. Ensure line of sight and congruence among the elements of the Porter's Five Forces analysis.

- iii. Use the strategic group analysis instrument to analyze, interpret, and evaluate the competitive environment.
- b. Ensure line of sight and congruence among all strategic management frameworks used.
- 3. **Analyze the internal environment.**
 - a. Use strategic management analytical frameworks to analyze, interpret, and evaluate the internal environments of the company.
 - i. Use the VRIO analysis instrument to analyze, interpret, and evaluate the firm's resources, capabilities, and core competencies.
 - a. Ensure line of sight and congruence among the elements of the VRIO analysis.
 - ii. Use the value chain analysis instrument to analyze, interpret, and evaluate the firm's primary and secondary activities.
 - a. Ensure line of sight and congruence among the elements of the value chain analysis.
 - b. Ensure line of sight and congruence between and among all strategic management frameworks used.
- 4. **Synthesize the organizational performance and the external and internal analysis using SWOT analysis.**
 - a. Synthesize the organizational performance and the internal and external analysis using a SWOT analysis.
 - b. Ensure line of sight and congruence between the analysis from the strategic management frameworks and the SWOT analysis.
- 5. **As appropriate to the case, analyze strategies: Corporate-level, business-level, innovation, sustainability and ethics, technology, and multinational strategies.**
 - a. Use strategic management analytical frameworks to analyze, interpret, and evaluate strategies.
 - b. Ensure line of sight and congruence within analysis of each strategy.
- 6. **Determine major areas of strategic concern.**
 - a. Identify the major areas of strategic concern from the SWOT and any additional analysis of strategies.
 - b. Ensure line of sight and congruence between the SWOT analysis and the major areas of strategic concern.
- 7. **Determine strategic issue.**
 - a. Determine the strategic issue from the major areas of strategic concern.
 - b. Ensure line of sight and congruence between the major areas of strategic concern and the strategic issue.
- 8. **Determine strategic alternatives.**
 - a. Determine strategic alternatives.
 - b. Ensure line of sight and congruence between the strategic issue and the strategic alternatives.
- 9. **Evaluate strategic alternatives.**
 - a. Determine criteria to evaluate the strategic alternatives.
 - b. Use criteria to evaluate the strategic alternatives.
 - c. Clearly indicate how the strategic alternatives meet the evaluation criteria.
- 10. **Recommend strategic alternative.**
 - a. Recommend one strategic alternative using the evaluation criteria.
- 11. **Design implementation plan.**
 - a. Design an implementation plan for the recommended strategic alternative.
- 12. **Confirm line of sight and congruence across the entire case analysis.**
- 13. **Write and/or present case analysis.**

2.7 Abbreviated Case Analysis Steps

When learning case analysis, students often conduct an abbreviated case analysis for their first case analysis. An abbreviated case analysis differs from the longer and more thorough case analysis detailed in [section 2.6](#) by omitting the following steps: (5) As appropriate to the case, analyze strategies: corporate-level, business-level, innovation, sustainability and ethics, technology, and multinational strategies; (9) Evaluate strategic alternatives; and (11) Design implementation plan.

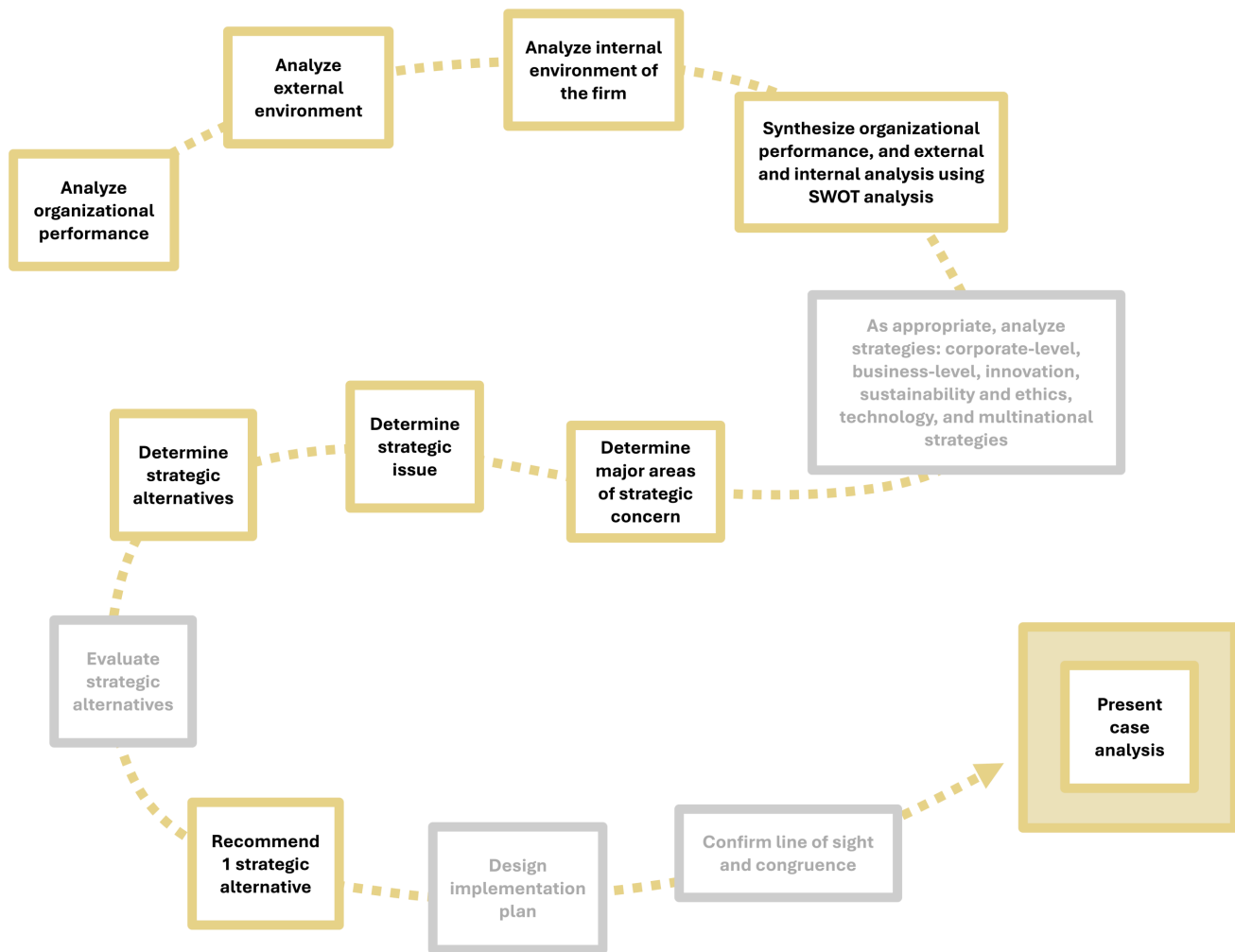


Figure 2.7: Abbreviated case analysis

Utilize the following process to conduct an abbreviated case analysis that follows a structured process.

1. Analyze a firm's organizational performance.

- a. Use the organizational performance analysis instrument to analyze a firm's organizational performance.
 - i. Analyze, interpret, and evaluate the firm's mission, purpose, vision, values, and goals.
 - a. Evaluate line of sight and congruence among the firm's mission, purpose, vision, and values.
 - ii. Analyze, interpret, and evaluate the firm's financial position.
 - iii. Analyze, interpret, and evaluate the firm's market position.
 - iv. Analyze, interpret, and evaluate additional relevant quantitative measures of organizational performance.
 - v. Analyze, interpret, and evaluate a firm's balanced scorecard.
 - a. Evaluate line of sight and congruence among the measures in the balanced scorecard.
- b. Common-size data and present trends to ensure the analysis is meaningful.

2. Analyze the external environment.

- a. Use strategic management analytical frameworks to analyze, interpret, and evaluate the external environment of the company.
 - i. Use the PESTEL analysis instrument to analyze, interpret, and evaluate the general environment.
 - a. Ensure line of sight and congruence among the elements of the PESTEL analysis.

- ii. Use the Porter's Five Forces analysis instrument to analyze, interpret, and evaluate the industry environment.
 - a. Ensure line of sight and congruence among the elements of the Porter's Five Forces analysis.
 - iii. Use the strategic group analysis instrument to analyze, interpret, and evaluate strategic groups.
 - b. Ensure line of sight and congruence among all strategic management frameworks used.
- 3. **Analyze the internal environment.**
 - a. Use strategic management analytical frameworks to analyze, interpret, and evaluate the internal environments of the company.
 - i. Use the VRIO analysis instrument to analyze, interpret, and evaluate the firm's resources, capabilities, and core competencies.
 - a. Ensure line of sight and congruence among the elements of the VRIO analysis.
 - ii. Use the value chain analysis instrument to analyze, interpret, and evaluate the firm's primary and secondary activities.
 - a. Ensure line of sight and congruence among the elements of the value chain analysis.
 - b. Ensure line of sight and congruence among all strategic management frameworks used.
- 4. **Synthesize the organizational performance and the external and internal analysis using SWOT analysis.**
 - a. Synthesize the organizational performance and the internal and external analysis using a SWOT analysis.
 - b. Ensure line of sight and congruence between the analysis from the strategic management frameworks and the SWOT analysis.
- 5. **Determine major areas of strategic concern.**
 - a. Identify the major areas of strategic concern from the SWOT and any additional analysis of company strategies.
 - b. Ensure line of sight and congruence between the SWOT analysis and the major areas of strategic concern.
- 6. **Determine strategic issue.**
 - a. Identify the strategic issue from the major areas of strategic concern.
 - b. Ensure line of sight and congruence between the major areas of strategic concern and the strategic issue.
- 7. **Determine strategic alternatives.**
 - a. Identify strategic alternatives.
 - b. Ensure line of sight and congruence between the strategic issue and the strategic alternatives.
- 8. **Recommend strategic alternative.**
- 9. **Confirm line of sight and congruence across the entire case analysis.**
- 10. **Write and/or present case analysis.**

Within the practical constraints of a university term, students are often asked to conduct a second, more thorough case analysis that includes the same information as an abbreviated case analysis with a few additional elements.

Application

- Data analytics is at the forefront of business. How does the structured process of case analysis fit into this current trend?

Key Takeaways

Case analysis follows a structured process. When first learning case analysis, students may conduct an abbreviated version as their first case analysis.

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2.8 Conclusion

Cases are written scenarios about companies that present real business issues that real firms face. Sometimes they contain real facts about real cases. Other times, cases are about a hypothetical company, using realistic but hypothetical data about the organization. *Case analysis* is an umbrella term that means applying strategic management concepts and analytical frameworks and tools to analyze, interpret, and evaluate company information that is provided through a written scenario; this information can also come from researching a company or working directly with a company through a consultancy project.

Conducting a case analysis follows a structured process that involves analyzing data, interpreting the analysis, evaluating the analysis and interpretation, and ensuring line of sight and congruence. Analysis is the process and result of examining all the data available for the firm and identifying and classifying all the data for each category in a strategic management tool. Interpretation is the process and result of examining the analysis to identify and explain relationships in the analysis and underlying root causes of the situation. Evaluation is the process and result of examining the analysis and interpretation to identify and explain the meaning of the information to the company by considering its impact, relevance, and importance to the company and by identifying the company's current, potential, or needed assets, organizational capacity, and managerial ability that may support or mitigate the areas of highest impact, relevance, and importance for the firm. Line of sight means there is a direct and clear logic connecting two or more concepts or ideas. Congruence means there is a one-to-one relationship between two or more things. When learning case analysis, students may conduct an abbreviated case analysis as their first case analysis, removing three steps from the full process.

Now that you have learned what strategic management and case analysis are in Part I, you focus on analyzing a firm's organizational performance and its external and internal environments in Part II.

Demonstrate Your Knowledge, Skills, and Competence

Use these questions to test your knowledge of the chapter.

1. Describe what a case is and what case analysis involves.
2. Explain data, analysis, interpretation, and evaluation and how they relate. Illustrate how these support a robust case analysis.
3. Describe line of sight and congruence. Explain how they are different. Illustrate how these support a robust case analysis.
4. Outline the case analysis steps. Explain the connections to the AFI framework.
5. Map out the steps in a case analysis. How steps can you recall without referring to the diagram? Now return to figure 2.6 and be sure you understand each element in the figure and their relationships.

You just demonstrated your expert knowledge of case analysis by considering these questions thoughtfully. Excellent work!

Figure Descriptions

Figure 2.1: Four steps of analyzing data shown in yellow. (1) Methodically and thoroughly examine all the data available for the firm. (2) Correctly identify all the data about the firm that the strategic management framework addresses. (3) Accurately classify all the data about the company for each category in the strategic management tool. (4) Complete the analysis section of a strategic management instrument.

Figure 2.2: Four steps of interpreting the analysis shown in yellow. (1) Examine the analysis. (2) Determine whether, how, and in what ways the information in the analysis is related. (3) Identify and explain underlying root causes of the situation. (4) Complete the interpretation section of a strategic management instrument.

Figure 2.3: Six steps of evaluating the analysis and interpretation shown in yellow. (1) Examine the analysis and interpretation. (2) Identify and explain whether, how, and in what ways the information in the analysis and interpretation impacts the company. (3) Identify and explain whether, how, and in what ways the information in the analysis and interpretation is relevant to the company. (4) Determine how important the information is to the firm. Action to take if helpful: Rank order the analysis and interpretation, according to strength of importance, such as strong, moderate, or weak tool. (5) Identify the company's current, potential, or needed assets, organizational capacity, and managerial ability that may mitigate the areas of highest impact, relevance, and importance for the firm. (6) Complete the evaluation section of a strategic management instrument.

Figure 2.4: Three yellow boxes each representing a different strategic analysis element. An arrow points from the first element to the second element, and then from the second element to the third element. The arrows represent direct, clear logic.

Figure 2.5: Three yellow boxes each representing a different case analysis step. A double sided arrow points between the first box and the second box. Another arrow points between the second box and the third box. The arrows represent direct, clear logic. 1-1 reconciliation. This process should be done across the entire case analysis.

Figure 2.6: Thirteen yellow boxes connected by a dashed path that leads to the final box titled “present case analysis.” (1) Analyze organizational performance. (2) Analyze external environment. (3) Analyze internal environment of the firm. (4) Synthesize organizational performance, and external and internal analysis using SWOT analysis. (5) As appropriate, analyze strategies: corporate level, generic business level, innovation, sustainability and ethics, technology, and multinational strategies. (6) Determine major areas of strategic concern. (7) Determine strategic issue. (8) Determine strategic alternatives. (9) Evaluate strategic alternatives. (10) Recommend strategic alternative. (11) Design implementation plan. (12) Confirm line-of-sight and congruence. (13) Present case analysis.

[Figure 2.7](#): Same flowchart as figure 2.6, except this one has four missing steps. The included steps are: (1) Analyze organizational performance. (2) Analyze external environment. (3) Analyze internal environment of the firm. (4) Synthesize organizational performance, and external and internal analysis using SWOT analysis. (6) Determine major areas of strategic concern. (7) Determine strategic issue. (8) Determine strategic alternatives. (10) Recommend strategic alternative. (13) Present case analysis.

Figure References

Figure 2.1: Analyze the data. Kindred Grey. 2025. CC BY.

Figure 2.2: Interpret the analysis. Kindred Grey. 2025. CC BY.

Figure 2.3: Evaluate the analysis and interpretation. Kindred Grey. 2025. CC BY.

Figure 2.4: Confirm line of sight. Kindred Grey. 2025. CC BY.

Figure 2.5: Confirm congruence. Kindred Grey. 2025. CC BY.

Figure 2.6: Case analysis. Kindred Grey. 2025. CC BY.

Figure 2.7: Abbreviated case analysis. Kindred Grey. 2025. CC BY.

PART II: ANALYZE ORGANIZATIONAL PERFORMANCE AND A FIRM'S EXTERNAL AND INTERNAL ENVIRONMENTS

In Part I, we introduced strategic management and case analysis. Part II continues to follow the AFI framework, expanding on the case analysis process as you learn how to analyze a firm's organizational performance and its external and internal environments.

In Chapter 3, you consider a company's organizational performance, which provides critical information about a firm's external and internal environments. You learn what mission, purpose, vision, and values mean to a company, why they are important, and how to analyze them. This chapter also discusses the difference between performance measures and benchmark measures and the importance of considering a range of measures to ensure a thorough and robust analysis. Therefore, you learn multiple approaches to analyze a company's organizational performance, focusing on and analyzing a firm's financial position, market position, and other relevant quantitative measures. You also learn a model for measuring organizational performance, the balanced scorecard, and how to analyze it to provide a more comprehensive view of a firm's organizational performance. Finally, you learn what a competitive advantage is and why it is central to strategic management.

In Chapter 4, you learn the strategic management concepts, and analytical tools that support strategically analyzing a firm's external environment. A firm's external environment provides a critical outside-in perspective and helps companies to determine attractive markets in which to operate. A firm's external environment includes those factors, forces, and competitive industry groups outside the firm's direct control. Part of understanding a firm's external environment is being familiar with the structure of its external environment. The chapter teaches you how to analyze the general environment, the industry environment, and the competitive environment. You also learn the role of external analysis in case analysis. The chapter concludes by having you use the PESTEL analysis instrument to analyze a firm's general environment, the Porter's Five Forces analysis instrument to analyze a firm's industry environment, and the strategic group analysis instrument to analyze a firm's strategic group.

In Chapter 5, you consider a company's internal environment, which provides a critical inside-out perspective of the firm. A company has direct control over its internal environment. You learn what resources, capabilities, and core competencies are and how these relate to creating and maintaining a competitive advantage. Next you learn what a resource-based view of a firm is and why it is important to organizations. The next topic, the VRIO framework, is derived from such a research-based view. You also learn how isolating mechanisms, including intellectual property, social complexity, and path dependence, serve as a value-added resource for organizations. After learning what a firm's value chain is and how it is used to identify strengths and weaknesses of an organization, you will be prepared to analyze the internal environment of a firm using a VRIO analysis instrument and a value chain analysis instrument. Analyzing both the external and internal environments of an organization provides a balanced and 360-degree analysis for the firm.

3. ANALYZE ORGANIZATIONAL PERFORMANCE

Learning Objectives

After engaging with this chapter, you will understand and be able to apply the following concepts.

1. Mission, purpose, vision, and values
2. Performance measures and benchmark measures
3. A range of organizational performance measures
4. Balanced scorecard
5. Competitive advantage

You will be equipped to analyze a firm's

1. Mission, purpose, vision, and values
2. Financial position
3. Market position
4. Other relevant quantitative data
5. Balanced scorecard

3.1 Introduction

In Part I, you were introduced to strategic management and case analysis. This chapter continues to follow the AFI framework, expanding on the case analysis process and teaching you how to analyze a firm's organizational performance.

You now know that strategic management's foundations rest in three questions:

1. Where are we?
2. Where are we going?
3. How are we going to get there?

You also know that these three questions align with the three major stages of strategic management according to the AFI framework: strategic analysis, strategy formulation, and strategy implementation. Strategic analysis addresses the broad question “Where are we?” Strategy formulation begins to answer “Where are we going?” Strategy implementation addresses the final question, “How are we going to get there?”

In this chapter, you learn key organizational performance measures and how to analyze them. You learn what mission, purpose, vision, and values mean to a company, why they are important, and how to analyze them. This chapter also discusses the difference between performance measures and benchmark measures and the importance of considering a range of measures to ensure a thorough and robust analysis. Therefore, you learn multiple approaches to analyze a company's organizational performance, focusing

on and analyzing a firm's financial position, market position, and other relevant quantitative measures. You also learn a model for measuring organizational performance, the balanced scorecard, and how to analyze it to provide a more comprehensive view of a firm's organizational performance. Finally, you learn what a competitive advantage is and why it is central to strategic management.

This is step one in case analysis.

1. Analyze a firm's organizational performance.

- a. Use the organizational performance analysis instrument to analyze a firm's organizational performance.
 - i. Analyze, interpret, and evaluate the firm's mission, purpose, vision, values, and goals.
 - a. Evaluate line of sight and congruence among the firm's mission, purpose, vision, and values.
 - ii. Analyze, interpret, and evaluate the firm's financial position.
 - iii. Analyze, interpret, and evaluate the firm's market position.
 - iv. Analyze, interpret, and evaluate additional relevant quantitative measures of organizational performance.
 - v. Analyze, interpret, and evaluate a firm's balanced scorecard.
 - a. Evaluate line of sight and congruence among the measures in the balanced scorecard.
- b. Common-size data and present trends to ensure the analysis is meaningful.

Throughout the text, we introduce analysis instruments to support your analysis. Use the organizational performance analysis instrument to analyze a firm's organizational performance.

Organizational performance analysis instrument

[Download an editable version](#) or [view this resource in Appendix 1](#).

3.2 Analyze Mission, Purpose, Vision, and Values

Collectively, a firm's mission, purpose, vision, and values set clear organizational direction that guides all firm decisions and strategies. Organizational leaders define these factors for the firm and then express them in statements for their stakeholders. It is important that there is a clear line of sight and congruence among these essential organizational elements. If there is no congruence or weak congruence between any or all of these, the organization will not have clear direction, and this can lead to poor decisions, weak strategies, and overall poor organizational performance. Of course, strong guiding statements do not guarantee superior firm performance. A company may have excellent mission, purpose, vision, and values and still make misguided strategic leadership decisions. However, this does not make it any less important for those four elements to be strong, clear, and congruent.

It is not enough for strategic leaders to just ensure that an organization's mission, purpose, vision, and values are aligned; they also need to align their leadership approach with these factors. Strategic leadership that is aligned to a company's mission, purpose, vision, and values has the potential to inspire employees, who feel the firm's leadership is authentic and that they are empowered to contribute meaningfully to the firm's performance. This powerful authenticity has the potential to lead an organization toward excellent performance.

Collectively, an organization's mission, purpose, vision, and values serve as the foundation for all strategic decisions. They inform every aspect of a business, both external and internal. For example, among other things, they inform marketing approaches, asset management approaches, and decisions to cooperate with other organizations. They also influence organizational structure, human resource policies, and organizational culture.

The primary emphasis for a firm defining and expressing these guiding factors is to capture the organization's distinctiveness. Missions, purposes, visions, and values that are both distinct and authentic have the potential to drive excellent performance.

The first step in analyzing a firm's organizational performance is to assess its mission, purpose, vision, and values. In analyzing them, the first important question to ask is whether they are effective. Then consider whether there is a clear line of sight among them and whether they are congruent. If the answer to either is no, recommend that the company revisit these and bring them into alignment.

Not only does there need to be a clear **line of sight** and **congruence** among the mission, purpose, vision, and values, strategies must align with them as well. If strategies do not align, they either need to be adjusted or dropped, or in some cases, the mission, purpose, vision, and values should be revised to stay relevant.

It is important to understand how mission, purpose, vision, and values relate and how they are distinct. It is most important to understand the concepts behind each and what each aims to accomplish because not all organizations consider and communicate through all four of the guiding statements. Some companies combine the ideas behind two of the factors, and sometimes companies use different names for the same ideas. When analyzing a company, it is more important to assess whether each broad concept is dealt with and communicated than whether a company uses each of these exact terms.

We now review each of these in turn.

Analyze Mission

Missions and mission statements are important for all firms. They are essential for industry leaders who seek to maintain their positions and drive continued success. When working to revitalize an organization, leaders often focus on reaffirming its commitment to a clear mission.

A **mission statement** explains why an organization exists. A well-crafted mission statement captures the essence of the organization and answers the questions "Why do we exist?" and "What is our purpose?" For example, a nonprofit might have a mission "to provide access to clean water in underserved communities," which clearly expresses why it exists. The mission defines the organization's role within society. Just as important as the firm's purpose is its identity, addressed in questions like "What defines us?" and "Who are we?" A mission is rooted in the firm's past foundation and current identity. Since a mission statement captures the essential elements of the company's identity from its founding to its reason to exist in the present, mission statements are often written in the present tense.

In practice, a mission statement also serves to inform key stakeholders why they should invest their trust, resources, and support in the organization. For an organization to succeed, it must gain the support of key stakeholders such as employees, owners, suppliers, partners, and customers.

For example, Google's mission is "to organize the world's information and make it universally accessible and useful" (Google.com). Early on, Google pursued this mission by developing a widely popular search engine. Today, the company continues to align with its mission through various strategic efforts, such as providing the Google Chrome browser, offering free email services through Gmail, and making books available for online browsing.

Deloitte offers professional services such as consulting, auditing, and advising to assist businesses in resolving difficult problems and accomplishing their objectives. In this regard, it is clear Deloitte has concentrated on its mission statement: "To make an impact that matters by delivering measurable, sustainable results to clients and communities" (Deloitte).

Another example is Peloton. Peloton makes fitness accessible by providing the most effective tools, software, content, and guidance. With its linked stationary bikes and streaming fitness classes, they engage in interactive at-home workouts and fitness technology. In efforts to strengthen its brand and direction, Peloton has focused on its mission statement: "Peloton uses technology and design to connect the world through fitness, empowering people to be the best version of themselves anywhere, anytime" (Peloton.com).

Mission statements are often brief and easy to remember. In the past, they tended to be much longer, sometimes spanning several paragraphs, which made it difficult for employees and other stakeholders to recall or recite them. Over time, companies have simplified their mission statements, making them shorter and more memorable. When employees know and embrace their organization's mission, it boosts their engagement and overall satisfaction. For instance, Nike's simple mission "to bring inspiration and innovation to every athlete in the world" (Nike.com) is easy for employees to internalize and work toward.

When you analyze a firm's mission statement, consider to what degree it addresses the criteria of a strong mission statement. It is not necessary that the mission statement meets every one of these criteria. After all, strong mission statements are short. Use this list as a guide to make your own assessment:

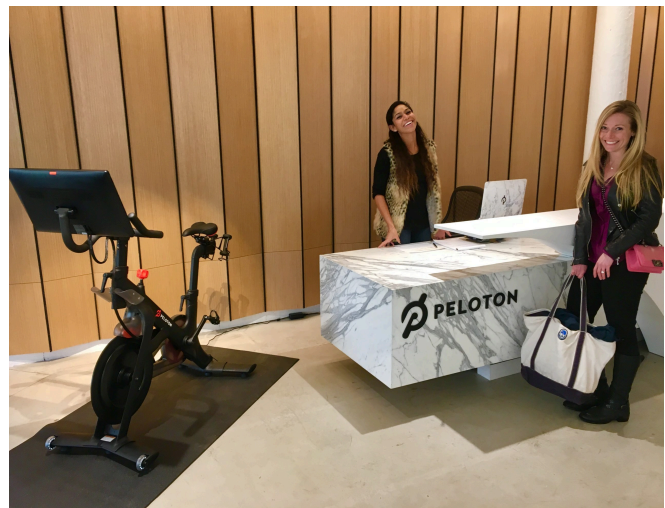


Figure 3.1: Peloton

- Does the mission statement explain why the organization exists?
- Does the mission statement define the organization's role within society?
- Is the mission statement rooted in the firm's past foundation and current identity?
- Does the mission statement capture the essential elements of the company's identity?
- Is the mission statement written in the present tense?
- Does the mission statement inform key stakeholders, such as employees, owners, suppliers, partners, and customers, why they should invest their trust, resources, and support in the organization?

The mission of an organization serves as a foundation for its purpose, vision, and values. We now turn our attention to an organization's purpose.

Analyze Purpose

In recent years, many organizations have increasingly embraced the concept of using a **purpose statement** to articulate their reason for existence beyond just profit-making, which differentiates them from mission statements.

Purpose statements are designed to inspire and unite stakeholders, ranging from employees to customers, around a central purpose. Unlike mission statements, purpose statements often focus on the broader impact an organization seeks to have on society or its industry. By highlighting the company's contributions beyond its products or services, purpose statements can help organizations foster trust, loyalty, and a sense of shared responsibility. Purpose statements often reflect a company's stance toward sustainability. Sometimes a company will publish a separate sustainability statement. Sustainability is reviewed in detail in [Chapter 10](#).

A well-crafted purpose statement also serves as a strategic guide, helping organizations navigate complex decisions by providing a clear framework for evaluating opportunities and challenges. When a company's actions and initiatives are aligned with its stated purpose, it ensures consistency in decision-making. This alignment fosters long-term success, as organizations are more likely to prioritize initiatives that resonate with their purpose and contribute to their broader goals. In turn, this can enhance the firm's reputation and attract not only customers but also partners and talent who share a similar vision for the future. With this focus on the current actions the company is taking, purpose statements are usually written in the present tense.

For example, PwC's purpose is to “build trust in society and solve important problems” (PwC.com). This statement reflects the company's commitment to addressing critical challenges facing global communities, positioning itself as a trusted partner in fostering societal progress. By aligning their operations and goals with a clearly defined purpose, organizations like PwC are better able to engage their workforce, attract like-minded clients, and create lasting, meaningful impact.

Not every company defines a purpose separate from its mission. Some companies address their purpose beyond profit-making in their mission statements. When analyzing a firm's broad guidance as it is communicated through its missions, purpose, vision, and values, it is most important to assess whether the company defines and articulates its purpose in addition to profit-making, whether this is expressed separately in a purpose statement, presented as part of the mission, or even included in another statement.

When you analyze a firm's purpose statement, consider to what degree it addresses the criteria of a strong purpose statement. As with your analysis of the firm's mission statement, it is not necessary that the purpose statement meets every one of these criteria. Use this list as a guide to make your own assessment:

- Does the purpose statement articulate a firm's reason for existence beyond just profit-making?
- Does the purpose statement focus on the broader impact an organization seeks to have on society or its industry?
- Is the purpose statement written in the present tense?
- Does the purpose statement inspire and unite stakeholders?
- Does the purpose statement foster trust, loyalty, and a sense of shared responsibility?
- If a company has not articulated a separate purpose statement, has it addressed the criteria above somewhere else?

With mission and purpose defined, company leaders define their vision and communicate this through a vision statement.

Analyze Vision

An organizational **vision statement** is a forward-looking or aspirational statement that captures what a company wants to achieve in the long run. It's meant to inspire and guide the organization, offering a clear sense of direction. A good vision paints a picture of a hopeful future, helping to align everyone around the same vision. Vision statements are usually concise, easy to understand, and motivate people by showing them what they're working toward. Unlike mission and purpose statements, they are usually written in the future tense.

“Where there is no vision, there is no hope”

—George Washington Carver

A compelling vision statement can be a powerful tool that leaders can use to energize and align the organization toward where it wants to be. A clear vision defines what the company aspires to become and helps to shape its strategies. For instance, LinkedIn's vision is to “[c]reate economic opportunity for every member of the global workforce” (LinkedIn.com). This succinct yet ambitious vision highlights the company's aspirations to reach every member of the global workforce and assist them by creating economic opportunities. Consequently, one might expect LinkedIn to feverishly pursue expansion of its offerings around the globe.

One might question the importance of vision statements. How much effect could they have, after all? More than fifty studies have demonstrated a relationship between vision statements and achieving desired outcomes (Kirkpatrick & Locke, 2012). Not all vision statements are good, and not all lead to success. Effective vision statements are generally clear, future focused, abstract and challenging, idealistic, concise, unique, and define success (Hauser, House, Kirkpatrick, & Locke, 2017).

While a well-defined vision can inspire employees, customers, and other stakeholders, strong and effective visions are relatively uncommon. Vision is the starting point of strategy. Strategy defines the roadmap of how an organization will move from where it is today to where it wants to be according to its vision.

An organization can't thrive if its mission and vision are not aligned. When a company's mission and vision point in different directions, confusion and inefficiency affect the strategy. For example, early in the development of some companies in the tech industry, their missions were focused on providing accessible and innovative products for consumers. However, as they grew, some shifted their visions toward dominating markets or expanding into unrelated areas, creating a conflict between what they originally stood for and what they aspired to become.

A more recent example comes from higher education. Many universities started with missions centered around providing quality education to students. As the need for research and innovation grew, the visions of some universities shifted to prioritize global research prestige. This created confusion among faculty: should they focus on teaching, as the mission suggests, or on research, as the vision demands? Even today, some institutions struggle to reconcile this tension, as the different emphases create competing priorities for faculty and staff.

Ultimately, organizations are most successful when mission and vision are aligned. A tech company that aims for both customer-centric innovation and market leadership, for example, will be more effective if its mission and vision work together to guide employees in the same direction despite having two potentially conflicting goals.

When you analyze a firm's vision statement, consider to what degree it addresses the criteria of a strong vision statement. As with your analysis of the firm's mission and purpose statements, it is not necessary that the purpose statement meets every one of these criteria. Use this list as a guide to make your own assessment:

- Is the vision statement a forward-looking or aspirational statement that captures what a company wants to achieve in the long run?
- Does the vision statement inspire and offer a clear sense of direction?
- Does the vision statement paint a picture of a hopeful future?
- Is the vision statement concise and easy to understand, with the potential to motivate people by showing them what they're working toward?
- Is the vision statement written in the future tense?
- Is the vision statement aligned with the mission statement?

Once a company has confirmed their current position with strong mission and purpose statements and articulated their aspirations for the future through their vision, they can then consider their values. A company's vision serves as the foundation for its values and goals, which in turn guide the organization toward achieving that vision.

Analyze Values

In addition to crafting mission, purpose, and vision statements, companies also create corporate **value statements** that define the core principles they stand by and expect their employees to uphold. These values are often showcased on company websites to communicate what the organization believes in and strives for.

Value statements are important because they not only guide internal culture but also influence how the company is perceived by stakeholders. Employees are expected to align with these values, and those who don't may find their tenure short-lived. Customers often choose companies whose values resonate with their own and firms that clearly communicate their principles. When Nike faced backlash over labor practices, the company revised its value system to emphasize fair labor conditions, showing how values impact both internal policies and public image. Likewise, Ben & Jerry's commitment to social justice can build strong brand loyalty. Values statements are usually written in the present tense.

Values are also tightly intertwined with strategic management. When formulating strategies and goals, companies must ensure alignment with their value statements. For example, if a strategy conflicts with a core value like sustainability, it must be reconsidered or adjusted. Companies like Tesla, which prioritizes environmental sustainability (Tesla.com), would likely reject strategies that compromise that value, even if profitable in the short term. Adhering to corporate values ensures that companies maintain their integrity while progressing toward their long-term goals.

Company	Values statement
KPMG	Integrity: We do what is right. Excellence: We never stop learning and improving. Courage: We think and act boldly. Together: We respect each other and draw strength from our differences. For Better: We do what matters.
Wells Fargo	We want to satisfy our customers' financial needs and help them succeed financially.
RSM	Respect and uncompromising integrity Succeeding together Excellence Impactful innovation Acting responsibly

Figure 3.2: Values and values statements

Companies like Microsoft emphasize values such as innovation (Microsoft.com), while others, like Patagonia, are known for promoting sustainability and environmental responsibility (Patagonia.com).

Some companies articulate both purpose and values statements, and some only define one. Purpose and values are similar and distinct. Purpose statements articulate the firm's reason for existence beyond just profit-making, instead focusing on the broader impact an organization seeks to have on society or its industry, such as AT&T's purpose statement, "Connecting people to greater possibility—with expertise, simplicity, and inspiration." Value statements define the core principles that companies stand by and expect their employees to uphold, such as RSM's value of impactful innovation. While purpose statements may explain the goals of the firm, the value statement explains why those goals are important. When analyzing a company, it is more important to assess whether the firm addresses the broader impact it seeks to have on society or its industry (purpose) and defines the core principles it stands by (values) than it is to focus on where exactly this is communicated.

When you analyze a firm's values statement, consider to what degree it addresses the criteria of a strong values statement. As with your analysis of the firm's mission, purpose, and vision statements, it is not necessary that the values statements meet every one of these criteria. Use this list as a guide to make your own assessment:

- Does the values statement define the core principles the firm stands by and expects its employees to uphold?
- Does the values statement have the potential to guide organizational culture and also influence how the company is perceived by stakeholders?
- Does the company articulate a separate sustainability statement?
- Is the purpose statement written in the present tense?

A company's values reflect their current commitment to a set of guiding principles. Values focus on where the company is headed by setting the parameters for the firm's goals. The company defines and executes its goals by remaining true to its values.

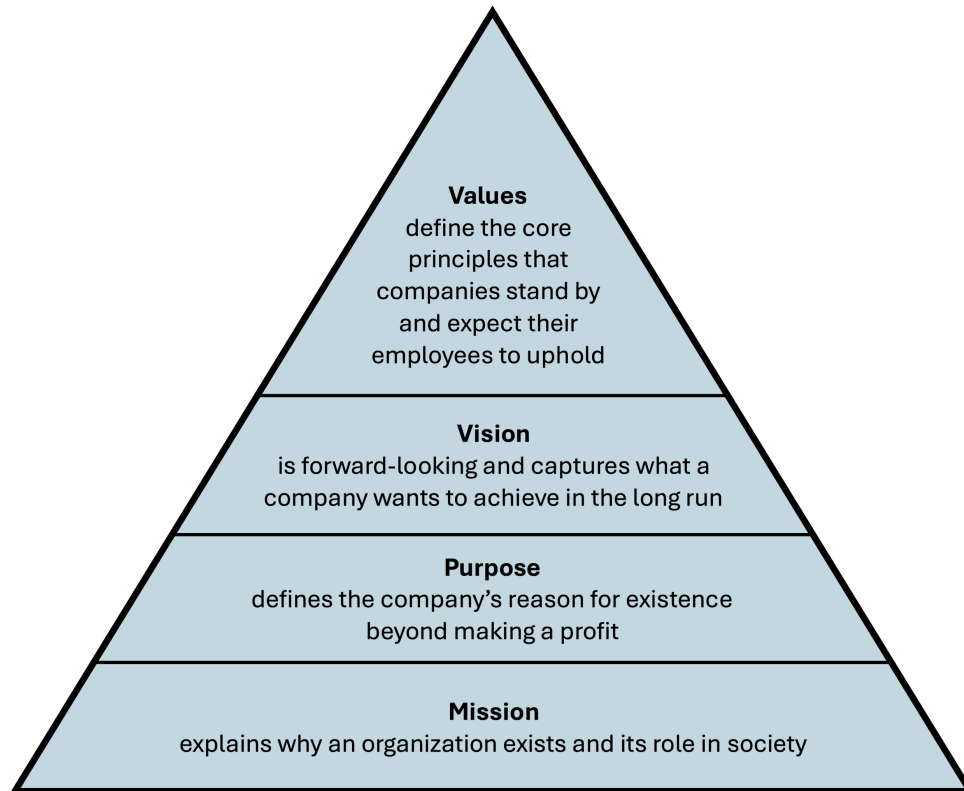


Figure 3.3: Analyze mission, purpose, vision, and values

Complete the section titled “Mission Purpose Vision Values” in the [organizational performance analysis instrument](#).

Application

- The same principles that guide successful organizations in defining their mission, purpose, vision, values, and goals can be just as useful for individuals. Thinking strategically about your personal aspirations and how you plan to achieve them can offer new insights and approaches. Consider applying these concepts to your own life to help clarify your goals, stay focused on your purpose, and map out the steps needed to move forward effectively.

Key Takeaways

Organizational leaders define the firm's mission, purpose, vision, and values then express them in statements for their stakeholders. These are usually published on company websites and easy to find. A mission statement explains why an organization exists. A firm's purpose statement articulates the reason for the company's existence beyond just profit-making. A vision statement is a forward-looking or aspirational statement that captures what a company or organization wants to achieve in the long run. Value statements define the core principles that companies stand by and expect their employees to uphold. It is important that there is a clear line of sight and congruence among these essential organizational elements. When analyzing an organization's mission, purpose, vision, and values, the first important question to ask is whether they are effective. Then ask whether there is a clear line of sight among them and whether they are congruent. If not, recommend that the company revisit these and bring them into alignment.

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3.3 Performance Measures and Performance Benchmarks

Once you have analyzed a firm's mission, purpose, vision, and values, next consider the firm's performance in others critical areas using comparative measures—specifically performance measures and performance benchmarks.

Performance measures are metrics used to track an organization's progress, such as profits, stock prices, or sales figures. These metrics provide insights but only offer a partial view of overall performance.

Performance benchmarks, on the other hand, provide context by comparing an organization's metrics to its previous results or to those of competitors. For example, a company showing a profit margin of 20 percent in 2024, might seem like a strong performance. However, if that same company had a profit margin of 35 percent in the previous year, and the industry average for 2024 was 40 percent, this new result would indicate a decline.

Application

- Consider the ways your performance is measured. How is your academic success measured? For example, your grades and GPA are performance measures. Your class standing is a measure of your academic standing as measured against other students in your class.
 - Think of other ways your performance is measured. Do you work out or play sports? Do you play a musical instrument or sing? Do you have a job? How is your performance measured in non-academic settings? What is the value of using both performance measures and performance benchmarks in evaluating your work?

Key Takeaways

Performance measures are metrics used to track an organization's progress, such as profits, stock prices, or sales figures. Performance benchmarks are standards or reference points used to evaluate an organization's metrics by comparing them to historical data, industry standards, or the performance of competitors. You can analyze a firm's performance using both performance measures and performance benchmarks.

3.4 Analyze a Firm's Financial and Market Positions and Other Relevant Quantitative Data

Once you have analyzed a firm's mission, purpose, vision, and values, the next step is to analyze a firm's financial and market positions and other relevant quantitative data.

We begin by analyzing a firm's financial position.

Analyze a Firm's Financial Position

An essential measure of organizational performance is a firm's financial landscape, which is visualized through analysis of financial data from the industry, competitors, and the firm.

Conducting a financial analysis of a firm is not always straightforward. The method and calculations are simple enough, and the key measures are reviewed below. The complexity lies in finding useful data, deciding which data is meaningful in this context, and presenting the data in an easily digestible format.

The challenge of grasping the complex nature of organizational financial performance stems from the conflicting views that can arise from using different benchmarks and metrics. For instance, the Fortune 500 ranks the largest U.S. companies based on sales, but these companies are not necessarily the best performers in terms of stock price growth. Due to their size, companies like Apple (as of 2024) would find it nearly impossible to double their revenue, whereas a smaller pharmaceutical company launching a new drug could see exponential revenue growth. In the late 1990s, many internet-based businesses experienced rapid sales and stock price growth despite posting losses. Investors who focused solely on sales growth suffered significant losses when the market shifted its attention to profits and stock prices plummeted.

Despite the problems with these metrics, almost all publicly traded companies discuss measures such as revenue and net income (Certo, Jeon, Raney, & Lee, 2024). This demonstrates the need for executives to carefully select a balanced yet manageable set of performance indicators to focus on, ensuring they capture a comprehensive picture without being swamped by excessive data.

Financial measures are key tools for evaluating an organization's profitability and overall effectiveness. These include essential metrics like return on assets (ROA), which measures how effectively a company turns its assets into profit. A high ROA suggests efficient asset use, while a low or negative ROA signals inefficiency. Additional financial measures include return on equity (ROE) and return on investment (ROI), which offer insight into how efficiently a company is using its resources.

Other popular financial indicators include earnings per share (EPS), net profits, and stock price, which together help answer the crucial question "How do we appear in the eyes of our shareholders?"

These financial metrics are typically featured in annual (10-K) and quarterly (10-Q) reports, providing stakeholders with a transparent snapshot of the organization's fiscal health. For these numbers to be meaningful, they need to be paired with relevant comparisons, such as the company's performance over time or industry benchmarks. For instance, in Tesla's 2022 annual report, the company highlighted its financial performance over the past five years, focusing on revenue growth, operating margins, and cash flow, which allowed shareholders to gauge the company's progress and future potential.

This method of financial analysis revolves around ratio analysis, which enables comparisons across companies or time periods, regardless of size or scale. Ratios like profit margins, debt-to-equity ratios, and asset turnover provide an even playing field for comparing firms across different operational scales.

"[W]hile we don't run the company worrying about the stock price in the short run, in the *long run* we consider our stock price a measure of our progress over time."

—Jamie Dimon, CEO of JP Morgan, April 8, 2024

"Our financial focus is on long-term, sustainable growth in free cash flows."

—Amazon Annual Report, 2020

"Trumpeting EBITDA is a particularly pernicious practice."

—Warren Buffett, 2002 Letter to Shareholders

Types of measures	Ratio	Formula	Purpose	Examples
Liquidity measures	Current ratio (CR)	Current assets / Current liabilities	Indicates ability to pay short-term obligations	Target uses CR to assess its ability to cover short-term obligations with its available assets.
Leverages measures	Debt ratio (DR)	Total liabilities / Total assets	Shows the proportion of assets financed through debt	Apple evaluates its DB to understand how much its assets are financed through debt.
Profitability ratios	Gross margin (GM)	Gross profit / Total revenue	Percentage of revenue remaining after direct costs	Starbucks uses GM to see the percentage of revenue left after covering direct costs like coffee beans and milk.
	Net profit margin (NPM)	Net profit / Net revenue	Shows profit earned per dollar of revenue	Netflix examines its NPM to determine profit per dollar after all expenses.
	Return on equity (ROE)	Net profit / Shareholder equity	Measures profitability relative to equity financing	Goldman Sachs reviews ROE to gauge how effectively it uses shareholders' equity to generate profits.
	Return on assets (ROA)	Net profit / Total assets	Assesses efficiency in using assets to generate profit	Tesla checks ROA to measure how efficiently it uses assets like factories to produce profits.
	Return on investments (ROI)	(Net profit / Investment cost) x 100	Assesses profitability relative to the cost of investment	Apple measures ROI for evaluating the success of new products.
Efficiency ratios	Inventory turnover (IT)	Cost of goods sold (COGS) / Average inventory	Indicates how efficiently inventory is managed	Walmart tracks IT to understand how quickly it sells and restocks products.
	Accounts receivable turnover (ART)	Net credit sales / Average accounts receivable	Assesses efficiency of accounts receivable management	Microsoft tracks ART to evaluate how quickly it collects payments from customers.
Market value	Market capitalization (MC)	Shares outstanding × Share price	Reflects the overall market value of the company	Amazon uses MC to understand its overall market value based on stock prices and shares.
	Earnings per share (EPS)	Net income / Number of outstanding shares	Shows the profitability attributed to each share of stock	Amazon tracks EPS to evaluate its profitability per shareholder.
	Net profit	Total revenue – Total expenses	Reflects the overall profit a company generates	Netflix analyzes net profits to evaluate a company's financial health.
	Stock price	The market valuation of one share of the company	Indicates how investors perceive the company's future performance	Microsoft monitors its stock price to track shareholder sentiment.

Figure 3.4: Finance ratios (bolded items indicate glossary terms)

Complete the section titled “Financial Position” in the organizational performance analysis instrument.

Analyze a Firm's Market Position

Analyzing a firm's market position assesses how a firm compares to its competitors within the market. Two common measures for evaluating a company's market position are market share and price–earnings (PE) ratio.

Market Share

Formula: Firm's Total Product Revenue / Total Revenue in the Industry

Market share reflects the percentage of the market controlled by a company. For example, if Netflix generates 35 percent of the total revenue in the global streaming industry, then its market share in that sector is 35 percent.

Price–Earnings (PE) Ratio

Formula: Stock Price / Earnings per Share (EPS)

The PE ratio shows how much investors are willing to pay for \$1 in earnings. If a company's stock is priced at \$50 per share and generates \$5 in annual earnings per share, the PE ratio is 10. A lower PE ratio suggests better value, while a higher PE ratio might indicate strong market confidence in the company's future growth prospects. For instance, a company like Tesla often has a high PE ratio due to market optimism about future earnings growth.

Complete the section titled “Market Position” in the organizational performance analysis instrument.

Analyze a Firm's Other Relevant Quantitative Data

Other data sets and trends can offer valuable insights. Trend analysis, for example, can reveal year-over-year changes in production volume or help forecast economic conditions. Insight can come from company-related data like customer satisfaction rates derived from surveys, employee satisfaction, strength of the brand, and innovation strengths (measured in new patents and new products launched). Demographic data can also be useful, such as forecasts for population growth. Analyzing the age and gender forecasts in a population can give important insights into potential new customers. Additionally, industry-specific data can offer useful benchmarks, enabling the analysis of a company's performance relative to average sector growth or innovation rates. By focusing on these different areas—financial, market-based, and general quantitative measures—organizations ensure they have a well-rounded view of their performance and are positioned for long-term success.

Complete the section titled “Other Quantitative Measures” in the organizational performance analysis instrument.

Video 3.1: What Is Organizational Performance? [01:56]

The video for this lesson explains how some organizations assess their organizational performance.

Access this YouTube video by scanning the QR code.



Key Takeaways

Analyze a firm's financial and market positions and other relevant quantitative data. Analyze financial data from the industry, competitors, and the firm. Competence with the finance measures in figure 3.4 is essential to conducting a financial analysis of a firm when you conduct a case analyses. Analyzing a firm's market position assesses how a firm compares to its competitors within the market. Two common measures for evaluating a company's market position are market share and price–earnings (PE) ratio. Also consider all other quantitative data that is relevant to the case, such a brand strength, employee satisfaction, or innovation.

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3.5 Use a Range of Measures to Address the Complexity of Organizational Performance

Analyzing firm performance is crucial in strategic management, as leaders need to understand how well their organization is performing to determine if any adjustments are necessary. However, there are many ways to measure performance, and opinions vary on which metrics matter most. The complexity lies in not just choosing the right measures but also interpreting outcomes, which may not always reflect the quality of decisions made. Sometimes, good decisions can lead to poor results due to unexpected circumstances, such as external crises. For instance, the COVID-19 pandemic disrupted many solid strategies that were previously thought to position organizations for success.

Using a range of performance measures and benchmarks is essential, as each provides different perspectives on how the organization is functioning. Without considering multiple angles, organizations risk missing key insights, which can lead to a skewed understanding of their true performance. To get an accurate picture, leaders must analyze performance from a variety of perspectives, ensuring they grasp both the strengths and weaknesses of their organization's progress.

With so many potential performance metrics and benchmarks, understanding an organization's performance can feel overwhelming. A study of restaurant companies' annual reports, for example, identified 788 different combinations of performance metrics and benchmarks used within just that one industry in a single year (Short & Palmer, 2003).

Leaders analyze their firm by evaluating their current position, focusing on trend examination, and comparing themselves with industry benchmarks or competitors. For example, return on assets (ROA) measures how effectively a company turns its assets into profit. A high ROA suggests efficient asset use, while a low or negative ROA signals inefficiency. This analysis goes beyond financial metrics, incorporating other performance indicators like product quality, employee satisfaction, retention, productivity, and customer satisfaction. For instance, Software as a Service (SaaS) is a cloud-based software delivery model where applications are hosted by a service provider and made available to users over the internet. Instead of purchasing and installing software on individual computers or servers, users subscribe to the software on a pay-as-you-go basis, often through monthly or annual plans. In SaaS companies like Netflix or Steam, monthly active users (MAU) is a crucial metric. Assessing various factors from multiple angles enables companies to gauge their overall performance.

Figure 3.5 shows a few additional key performance measures that are helpful when analyzing a company's organizational performance.

Metric	Formula/Definition	Purpose	Example use
Monthly active users (MAU)	Total individual users engaging with the service in a month	Tracks customer engagement and product stickiness	Netflix monitors MAU to gauge customer activity.
Customer acquisition cost (CAC)	Total cost of acquiring new customers / Number of new customers	Measures the efficiency of customer acquisition	Steam evaluates CAC to optimize marketing spending.
Churn rate	(Customers lost during a period / Total customers at the start) × 100	Identifies customer retention issues	Spotify analyzes churn to improve customer retention.
Lifetime value (LTV)	Average revenue per user (ARPU) × Average customer lifetime	Assesses the total value a customer brings	Slack uses LTV to understand long-term profitability.
Recurring revenue	Revenue from subscription services	Tracks stable, recurring income	Dropbox measures monthly recurring revenue (MRR).
Retention rate	(1 – Churn Rate) × 100	Measures customer loyalty over time	Zoom focuses on retention to maintain a steady user base.

Figure 3.5: Key measures for organizational performance

When you analyze organizational performance as part of conducting a case analysis, you use a range of measures, requiring a thorough knowledge of the case or company to select the measures that will be most useful. This also requires judgment.

Key Takeaways

When you analyze organizational performance as part of conducting a case analysis, you use a range of measures. Selecting the most useful measures requires a thorough knowledge of the case or company. It also requires judgment. Competence with the measures in figure 3.5 is essential to conducting an analysis of a firm for a case analysis.

3.6 Analyze a Firm's Balanced Scorecard

Understanding organizational performance requires a multidimensional approach. Just as a pilot must monitor multiple gauges, such as altitude, airspeed, and fuel level, managers must track various performance metrics to ensure their organizations stay on course. While various financial performance measures are essential indicators, they are only one component of the bigger picture.

To help managers assess performance beyond just financial measures, Harvard professors Robert Kaplan and David Norton developed the **balanced scorecard**. This tool encourages a broader evaluation of an organization's performance by focusing on multiple key areas. The balanced scorecard framework emphasizes a balance between financial indicators and other critical measures that influence long-term success.

The balanced scorecard suggests that managers track performance across four perspectives: financial, customer, internal business processes, and employee learning and growth. We reviewed the financial measures in [section 3.4](#). Here we focus on the additional measures in the balanced scorecard: customer measures, internal business processes measures, and employee learning and growth measures.

Analyze Customer Measures

Customer measures reflect how well a company attracts, satisfies, and retains customers. These measures answer the question “How do customers view us?” Examples include metrics like new customer acquisition rates, customer satisfaction scores, and repeat customer percentages.

For instance, Amazon emphasizes customer retention by offering services like Amazon Prime, which encourages loyalty through faster shipping, exclusive content, and personalized shopping experiences. Additionally, Amazon gathers extensive customer data to anticipate consumer needs and adapt its offerings accordingly.

Analyze Internal Business Process Measures

Internal business process measures focus on organizational efficiency and answer the question “What must we excel at?” Internal business process measures include production times, delivery efficiency, and new product development speed.

For example, Toyota's commitment to lean manufacturing focuses on reducing waste in its production processes. By streamlining assembly lines and improving supply chain coordination, Toyota continuously works to reduce the time it takes to manufacture vehicles while maintaining quality standards.

Analyze Learning and Growth Measures

Learning and growth measures provide insights into how an organization can continue to innovate and create future value. These metrics answer the question “Can we keep improving and adding value?” They often focus on employee development, innovation capabilities, and adapting to changing market conditions.

A company like Google, for example, prioritizes learning and growth by offering employees continuous opportunities for training and skill development. This not only keeps the workforce agile and innovative but also ensures that the company remains competitive in a fast-evolving tech landscape. Metrics in this category might include the number of new technologies introduced or the percentage of employees who undergo skill upgrades annually.

Scorecard dimension	Definition	Example
Financial measures	How a firm is performing financially	Return on assets (ROA) Return on equity (ROE) Return on investment (ROI) Stock price Profits
Customer measures	How well a company attracts, satisfies, and retains customers	Number of new customers Number of repeat customers Percentage of repeat customers
Internal business process measures	How efficient the organization is	Production times Delivery efficiency New product development speed Speed serving a customer
Learning and growth measures	How a business can continue to innovate and create future value	Average number of new skills learned by each employee every year

Figure 3.6: Analyzing organizational performance using the balanced scorecard

Complete the section titled “Balanced Scorecard” in the organizational performance analysis instrument.

Adding the measures considered in the balanced scorecard to those reviewed in the preceding sections offers a more thorough analysis of organizational performance.

Application

- The balanced scorecard provides a well-rounded view, helping managers understand where the organization stands and where improvements can be made. Similarly, individuals can apply this framework to evaluate their personal performance and growth across these same dimensions. Complete the following table for yourself.

Scorecard dimension	Ask yourself
Financial measures	After graduation, what are my initial strategies to improve my personal wealth? Do I have student loans to repay? Do I have cash reserves, for example in a savings account? Do I have good credit and the ability to assume new debt to start a business or buy a home? Do I have current investments? What is my strategy to begin saving for retirement?
Customer measures	How strong is my professional network? How might I strengthen this and use it more effectively? What contacts can I make and strengthen while I am still attending university? How can I use my online professional network more effectively?
Internal business process measures	What have I learned from my university education and current work experience about completing work efficiently to a high standard? How has the time it takes me to complete assignments and work tasks improved? How could I improve this time further? What is my plan to accomplish this? What have I learned about myself when working with others and in teams? How could I improve my teamwork further? What is my plan to accomplish this?
Learning and growth measures	What new skills do I plan to develop now for the future? What licenses and certifications do I plan to obtain? Am I planning to earn a graduate degree? What growth and development goals do I have that relate to living a well-rounded life that may indirectly influence my career, such as emotional, mental, behavioral, and physical health goals or hobbies and friendships?

Figure 3.7: Apply the balanced scorecard to yourself

Key Takeaways

The balanced scorecard offers a comprehensive framework for executives to evaluate their organization's achievements across four critical dimensions: financial, customer, internal processes, and learning and growth.

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3.7 Competitive Advantage

Although financial metrics like accounting measures and stock market returns provide insight into a firm's short-term performance, they often fail to capture long-term success. These indicators can be misleading, as they are influenced by random market fluctuations. A company might experience a stroke of good fortune that results in high profits despite having a weak strategic position. On the other hand, a company with solid business fundamentals may suffer temporary setbacks and report disappointing profits. Another limitation of relying solely on these measures is that some companies, especially in growth phases, intentionally reinvest profits to fuel future expansion. This means their financial statements may not reflect their true health, even if they are thriving.

In strategic management, the focus often shifts from these financial measures to the concept of competitive advantage. This can be better understood through economic value creation (EVC), a concept that measures the difference between what a customer is willing to pay for a product (WTP) and the cost of producing that product.

$$\text{EVC} = \text{WTP} - \text{Cost}$$

In this equation, WTP is the maximum amount a customer would pay, while cost represents the expense the firm incurs to produce the product. The price a consumer actually pays is not included in this calculation.

Economic value creation can vary between companies, even when they sell similar products. This is because production costs and customers' willingness to pay may differ from one firm to another. Consequently, some firms generate more economic value than their competitors, leading to differences in competitive standing.

A company is said to have a **competitive advantage** when its economic value creation exceeds that of its competitors. For example, if Firm A and Firm B produce similar goods, but Firm A creates more economic value (either through lower production costs, higher customer willingness to pay, or both), then Firm A holds a competitive advantage over Firm B. The magnitude of this advantage is the difference in the economic value created by each firm.

Competitive advantage is valuable for several reasons. Unlike profits and stock prices, which are influenced by market volatility, competitive advantage reflects deeper, more stable dynamics. If a firm increases its competitive advantage, it means either its costs have decreased, consumers' willingness to pay has increased, or both, signaling true strategic improvement.

Additionally, competitive advantage accounts for the success of firms that reinvest their earnings; a company might report minimal accounting profits because it reinvests heavily in innovation or product development, yet it can still have a strong competitive posi-

tion if its economic value creation remains high. For example, if Firm A reinvests most of its profits back into the business, it may report low accounting profits, but its competitive advantage could grow, as customers see more value in its product.

In practice, economic value creation is a more widely used and recognized concept than similar measures like economic value added (EVA), especially when discussing competitive advantage in strategic management. EVC focuses more directly on the relationship between customer value and production costs, making it a useful tool for understanding long-term strategic success.

Competitive advantage is the unique characteristics and capabilities of a firm that allow a firm to outperform its competitors.

Key Takeaways

In analysis carried out for strategic management, the focus often shifts from financial measures to the concept of competitive advantage. A company is said to have a competitive advantage when its economic value creation exceeds that of its competitors. Competitive advantage is the unique characteristics and/or capabilities of a firm that allow a firm to outperform its competitors. This advantage can be better understood through economic value creation (EVC), a concept that measures the difference between what a customer is willing to pay for a product (WTP) and the cost of producing that product ($EVC = WTP - \text{Cost}$).

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3.8 Conclusion

By analyzing a wide range of areas related to organizational performance in this chapter, you are now able to provide a more comprehensive analysis of a firm's organizational performance. The process begins with analysis of a firm's mission, purpose, vision, and values. When analyzing organizational performance data, it is useful to consider a wide range of performance measures and benchmark measures to ensure you capture a thorough and robust picture of the firm. Analyze a firm's financial position, its market position, and other relevant quantitative measures. Analyze a company's balanced scorecard, including customer measures, internal business process measures, and employee learning and growth measures. This thorough review of an organization's performance supports a more holistic view of their operations and informed evidenced-based decisions that promote sustained success. This approach helps managers understand where the organization stands and where improvements can be made. Analyzing a firm's organizational performance produces analysis that relates to both the external and internal environments of the company. A company has a competitive advantage if its economic value creation exceeds that of its competitors. Competitive advantage reflects deeper, more stable dynamics.

Analyzing a firm's organizational performance is the first step in case analysis. In the next chapter, we turn our attention to analyzing a company's external environments.

Demonstrate Your Knowledge, Skills, and Competence

Use these questions to test your knowledge of the chapter:

1. Describe mission, purpose, vision, and values and how they are similar and distinct. Do companies always define each one? Discuss the most useful way to approach these when you conduct a case analysis.
2. Explain performance measures and performance benchmarks. Give an example of each, and explain how your examples illustrate each.
3. Review figure 3.4 to ensure you understand how to use each measure in case analysis. Test your knowledge by writing down each ratio and filling in the type of measure, the formula, and its purpose without referring to the figure. If there are any areas you need to study further, we encourage you to do this now, as they will be highly useful throughout the rest of the course.
4. Describe market share and PE ratio. Explain how they are used to analyze a firm's market position.
5. What other types of relevant quantitative data may be useful when you conduct a case analysis? Explain their roles in case analysis.
6. Discuss why using a range of measures is important when you analyze a case.
7. Review figure 3.5 to ensure you understand how to use each organizational performance measure in case analysis. Test your knowledge by writing down each metric and filling in the formula and its purpose without referring to the figure. If there are any areas you need to study further, we encourage you to do so now.
8. Describe what a company's balanced scorecard measures and why this is a useful tool. Explain how considering alternative measures in addition to financial measures is useful and how this gives a broader measure of an organization's performance.
9. Discuss competitive advantage. Explain the concept, the formula, and its role in strategic management.

You are now competent at analyzing a firm's organizational performance. Congratulations!

Figure Descriptions

Figure 3.3: Blue pyramid divided into four horizontal sections. From top to bottom, the sections are labeled values, vision, purpose, and mission. Values define the core principles that companies stand by and expect their employees to uphold. Vision is forward-looking and captures what a company wants to achieve in the long run. Purpose defines the company's reason for existence beyond making a profit. Mission explains why an organization exists, and its role in society.

Figure References

Figure 3.1: Peloton. Steve Jurvetson. 2017. CC BY 2.0. https://commons.wikimedia.org/wiki/File:Peloton_HQ_reception_area.jpg

Figure 3.3: Analyze mission, purpose, vision, and values. Kindred Grey. 2025. CC BY.

4. ANALYZE THE EXTERNAL ENVIRONMENT

Learning Objectives

After engaging with this chapter, you will understand and be able to apply the following concepts.

1. The external environment of a company
2. The structure of the external environment
3. The general environment of an organization
4. The industry environment of a company
5. The competitive environment of a firm
6. The role of external analysis in case analysis

You will be equipped to analyze a firm's

1. Industry, market, and market segment
2. General environment using the PESTEL analysis instrument
3. Industry environment using the Porter's Five Forces analysis instrument
4. Competitive environment using the strategic group mapping analysis instrument

4.1 Introduction

As you have learned, strategic management and case analysis follow a structured process through strategic analysis, strategy formulation, and strategy implementation. Case analysis begins with analyzing a company's organizational performance, which you learned in [Chapter 3](#).

In this chapter, you learn the strategic management concepts and theories and the analytical frameworks and tools that support strategically analyzing a firm's external environment. This includes understanding what is included in a firm's external environment and how the environment is structured. You learn how to analyze the general environment, the industry environment, and the competitive environment. You also learn the role of external analysis in case analysis, as analyzing the external environment of a company provides a critical outside-in perspective and helps companies to determine attractive markets in which to operate.

4.2 The External Environment

Before you can analyze the external environment of a company, you must first know what makes up the external environment and why analyzing it is important. All organizations operate in an external environment. The **external environment** includes everything outside a company that influences its ability to create and sustain a competitive advantage. The forces, factors, and actions of competitors that operate in a firm's external environment are all outside the direct control of a firm.

Understanding a firm's external environment is crucial because it is a source of opportunities that can be harnessed to support a firm's competitive advantage. The external environment is also a source of threats that must be mitigated to ensure continued company success.

Key Takeaways

The external environment includes everything outside a company that influences its ability to create and sustain a competitive advantage. The forces, factors, and actions of competitors that operate in a firm's external environment are all outside the direct control of a firm. The external environment is a source of opportunities that can be harvested to support a firm's competitive advantage and threats that must be mitigated to ensure continued company success.

4.3 The Structure of the External Environment

In strategic management, the structure of a firm's external environment consists of the general environment, the industry environment, and the competitive environment. This section introduces analytical instruments you use to support your analysis of each of these elements.

The General Environment

The first and broadest level of a firm's external environment is the **general environment** (also known as the macro environment). The general environment consists of the societal events and trends that impact all firms in an industry, including political, economic, sociocultural, technological, environmental, and legal factors. The PESTEL framework is the strategic management framework used to analyze the general environment. The factors in an organization's general environment are the furthest away from the firm in origin, and the firm has the least influence over these factors.

The Industry Environment

The second level of the external environment is the **industry environment**, and it is narrower in focus. Sometimes the industry environment is referred to as the task environment. A firm's industry environment consists of the forces that exert influence and pressure over the firm's entire industry. To assess the market attractiveness and profit potential of the industry, you use a Porter's Five Forces analysis instrument to analyze the bargaining power of suppliers, the bargaining power of buyers, the threat of substitute products, the threat of new entrants, and the rivalry among existing competitors. In contrast to the factors in the general environment, the forces and dimensions in an organization's industry environment are closer in proximity to the firm, and the firm has more influence over these forces.

The Competitive Environment

The third level of the external environment is the **competitive environment**, and it is the narrowest in focus, consisting of companies that pursue similar strategies in the same industry—strategic groups. A firm has the most influence over the dynamic influences in its competitive environment.

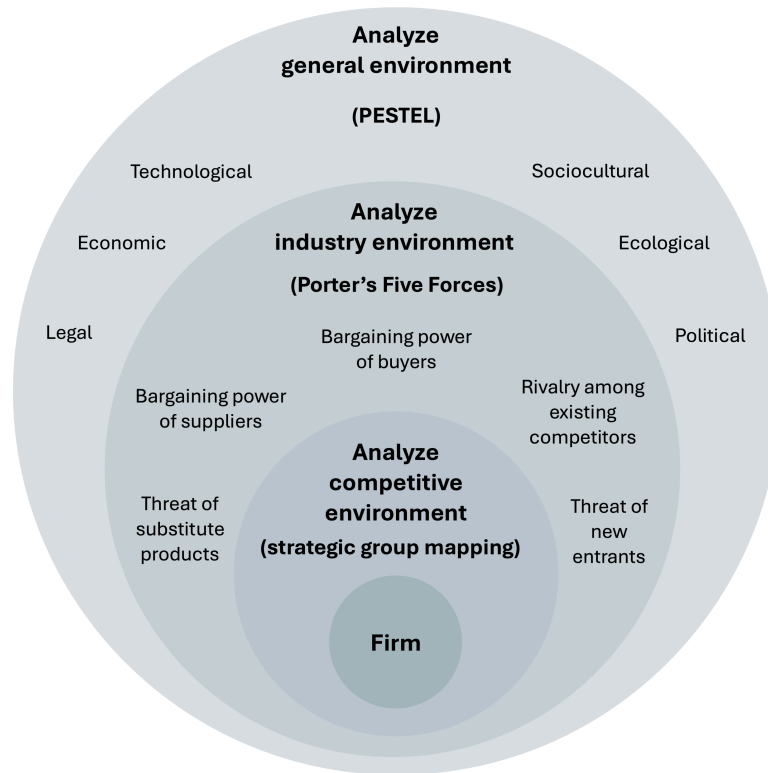


Figure 4.1: Analyze the external environment

Key Takeaways

The external environment consists of the general environment, the industry environment, and the competitive environment. The first and broadest level of a firm's external environment is the general environment, which consists of the societal events and trends that impact all firms in an industry, including political, economic, sociocultural, technological, environmental, and legal factors. The PESTEL framework is the strategic management framework used to analyze the general environment. The second level of the external environment is the industry environment, which is narrower in focus and consists of the forces that exert influence and pressure over the firm's entire industry: the bargaining power of suppliers, the bargaining power of buyers, the threat of substitute products, the threat of new entrants, and the rivalry among existing competitors. Porter's Five Forces framework is the strategic management tool used to analyze the industry environment. The third level of the external environment is the competitive environment, which is the narrowest in focus and consist of companies that pursue similar strategies in the same industry.

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4.4 Define the Industry, Market, and Market Segment

Before you can analyze a firm's external environment, you must determine the firm's industry, its market, and the market segment it is focusing on. A firm's industry, market, and market segments play a crucial role in shaping strategy and performance. **Industry** is a group of organizations, businesses, companies, or firms that compete in the marketplace for profit, engaging in similar business activities and producing or selling similar products or services. A **market** refers to the overall pool of potential customers for a product or service within a specific industry, and a **market segment** is a distinct group within a market that is identified by shared characteristics like demographics, needs, or behaviors.

Companies in an industry are related in their main activities (the activities that generate the most revenue for the firm). For example, many companies finance their products. Automakers finance automobiles, and technology firms finance new technology products. Finance is an important business support unit for the company and one that new business graduates may join and manage. However, finance is not the main activity of either an automaker or a technology firm, so neither belongs to the finance industry. Automakers are members of the auto industry, and technology firms are members of the technology industry.

It is important to consider industry and competitor analysis when considering the company's positioning and performance. Let's consider Chipotle.

Chipotle is considered to be in the food service industry, which places it alongside all types of restaurants, from other fast-food restaurants, such as McDonald's, to exclusive restaurants and even institutional cafeterias, such as those found on university campuses, and catering services. Although it is accurate that Chipotle is in the food service business, this is not a useful industry to consider for most analyses of Chipotle. The restaurant industry is another possibility. This includes all types of restaurants, from other fast-food restaurants, such as Kentucky Fried Chicken, to exclusive restaurants, such as Ruth's Chris Steak House. This is likely still too broad to be helpful in analyzing Chipotle. Considering restaurants that serve Mexican food is another potential perspective. This would include food trucks and local Mexican restaurants. Again, this is likely too broad.

A more pragmatic and useful approach is to consider what other restaurants Chipotle directly competes against. Additional choices still need to be made to determine Chipotle's direct competitors. A **competitor** is a business within the same industry that offers similar products or services and competes for customers.



Figure 4.2: Chipotle

Competitors selling products that customers tend to buy one at a time may compete for the same customer, with only one competitor winning. This applies to products that garner high brand loyalty from customers. This happens in different circumstances, such as when competitors sell products that are expensive relative to their customer's ability and willingness to pay. For example, for many buyers, a vehicle is a major purchase, and many customers have high brand loyalty to vehicle makers. Many customers buy only one vehicle at a time. In this case, one competitor wins the sale of the vehicle. Phones, being less expensive than vehicles, are typically purchased more frequently by customers, but they still tend to show strong brand loyalty to manufacturers. Again, only one competitor wins.

When businesses sell products or services that are less expensive relative to their customer's ability and willingness to pay, a company is competing for customers at each decision point and each point of sale. This is especially true for consumable goods, such as food. In the case of eating at fast-food restaurants, although many customers have brand loyalty, many customers eat at multiple fast-food restaurants.

This complicates the identification of Chipotle's industry, market, and market segment. Chipotle's direct competitors could include all fast-food restaurants. On the other hand, Chipotle could be seen as competing directly with Mexican fast-food restaurants. Additional competitors could be restaurants that focus on fresh ingredients or Mexican grills that serve fresh food. All of these are competitors, to varying degrees.

Chipotle's most direct competitors include Qdoba Mexican Eats, Moe's Southwest Grill, Baja Fresh Mexican Grill, and Rubio's Coastal Grill. Chipotle also competes, but less directly, with Taco Bell. Finally, other fast-food restaurants, such as Wendy's and McDonald's are more distant competitors.

When considering Chipotle's market and market segment, there are several important considerations to keep in mind. Remember: a market refers to the overall pool of potential customers for a product or service within a specific industry, and a market segment is a distinct group within a market that is identified by shared characteristics like demographics, needs, or behaviors.

An important element of defining the market and market segments correctly is the determination of the size of the market and its growth rates. If a company defines its market and market segments too narrowly, the firm may celebrate a high market share but may also miss out on opportunities in the broader market. If a company defines its market too broadly, there could be a mismatch between what the company can really offer and what the market demands. Companies must avoid trying to be everything to everyone. It is also important to define the company's total market, accessible market, and strategically relevant market (SRM). For strategic analysis, formulation, and implementation, the strategically relevant market is the main framework to use when assessing the market size and growth rates, the market dynamics, markets trends, and market attractiveness.

From a strategic management perspective, it is pragmatic and useful approach to consider what restaurant subsector Chipotle inhabits. The restaurant industry has many subsectors, including fast food, fast casual, casual, full-service, and fine dining. Chipotle can be considered to operate in the fast casual sector of the restaurant industry. Chipotle's market includes fast casual Mexican restaurants. Chipotle's strategically relevant market can be defined as urban and suburban customers who want quick customizable Mexican-inspired food in a casual dining atmosphere. Chipotle's market segment is college students and younger millennials, aged 18–30, who want a healthy meal that is sustainably sourced at a reasonable price point. Customers value convenience, such as being able to access Chipotle through digital platforms, and transparency in food sourcing.

Ideally, every company wants to operate in an attractive market. One important factor that determines the attractiveness and profit potential of different industries is the size of the market—more specifically, the size of the firm's strategically relevant market. A big market is more attractive because there is more demand and more space for various companies to succeed. A second important factor of market attractiveness is the growth rates of the market. A growing market offers growth opportunities for various companies and competitors in an industry, whereas growth in a stagnating or even declining market can only be achieved by taking market share away from competitors. Typically, companies analyze past growth rates as the compound annual growth rate (CAGR). A robust and data-driven forecast of the market's future CAGR is critical when determining the attractiveness and profit potential of an industry. Beyond the size and growth rates, firms need to understand the industry dynamics in their industry.

Every company that engages in the process of strategy formulation must gain a full understanding of the industry in which the firm operates as well as its market, market segments, and the dynamics affecting the company. This allows the firm to determine the strategic opportunities and threats that the industry, market, and market segments present to the firm, as well as the firm's strengths and weaknesses that may be leveraged to address these opportunities and threats.

Following the logic of the “3 Cs” of industry players, a firm needs to thoroughly analyze its competitors, its customers, and its company. As it relates to a firm's external environment, a firm's competitors include the industry in which a firm operates. A firm's customers make up the firm's markets and market segments. The company includes all the internal dynamics of the firm, which is covered in the next chapter, which focuses on analyzing the internal environment.

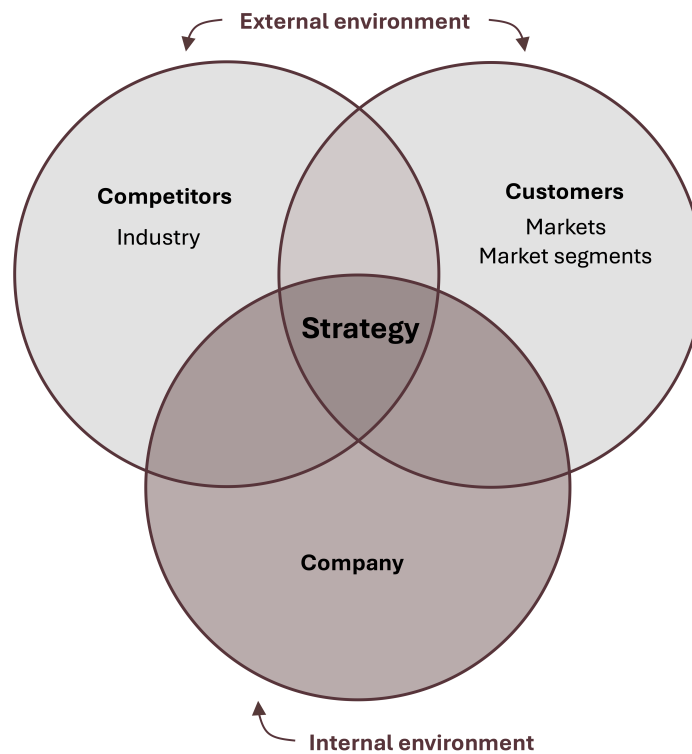


Figure 4.3: The 3 Cs and strategy

Understanding a firm's industry, market, strategically relevant market, and market segment are essential when analyzing a company. When you conduct a case analysis, begin by defining the firm's industry, market (especially its strategically relevant market), and its market segment.

Application

- Now that you have seen an example of Chipotle's industry, market, and market segment, identify and discuss the industry, market, and market segment for one of your favorite restaurants.

Key Takeaways

A firm's industry, market, and market segments play a crucial role in shaping strategy and performance. An industry is a group of businesses that engage in similar business activities and that produce or sell similar products or services. A market refers to the overall pool of potential customers for a product or service within a specific industry, and a market segment is a distinct group within a market that is identified by shared characteristics like demographics, needs, or behaviors.

4.5 Analyze the General Environment

The **general environment** is the broadest level of the external environment of a firm and includes societal events and trends that impact all firms in an industry.

Although factors in a company's general environment are the furthest away from the firm and include those factors that the firm has the least influence over, these factors influence the success of a business. Executives must continuously scan and monitor developments in the general environment.

An organization's general environment presents both opportunities and threats. For example, the rapidly changing landscape of technology, with developments in AI and cloud computing, offers potential opportunities for many companies. Advances in solar and wind power also can be sources of opportunities in the external environment as many companies move toward goals of net-zero emissions.

The general environment is also a source of threats that must be mitigated to ensure continued company success. For example, wars pose threats to supply chains. Changing tariffs on imports threatens trade balances. Successfully navigating these external forces is key to ensuring a company's sustained success and maintaining its competitive position.

The PESTEL Framework

The **PESTEL** framework is the strategic management framework that you use to analyze the general environment. Each letter of the acronym PESTEL represents a factor in the general environment: political, economic, sociocultural, technological, environmental, and legal.

There are many elements that make up each factor in the PESTEL framework. Figure 4.4 and the explanation following it include an illustrative list of elements that make up each PESTEL factor.

Political	Economic	Sociocultural	Technological	Environmental	Legal
Type of law: administrative law = governmental regulation	Economic growth	Population growth / decline / density	Level of technology	Impact of climate crisis	Type of law: Statutory law = passed by Con- gress Case law = adjudi- cated in courts
Tax regulations	Inflation rates	Age, gender, and ethnicity distribution	Life cycle of technology	Weather	Level of law: national, state, local
Immigration regulations	Exchange rates	Attitudes toward inclusiveness	Level of technological innovation	Natural disasters	Import / export laws
Foreign trade regulations	Interest rates	Role of family in society	Rate of new technology development	Pollution	Antitrust laws
Health and safety regulation (OSHA)	Stability / volatility of stock market(s)	Health consciousness	Internet infrastructure: urban vs. rural	Recycling infrastructure	Copyright and patent laws
Presidential executive orders	Household disposable income	Lifestyle attitudes	Communications infrastructure: urban vs. rural	Regenerative agriculture	Consumer protection laws

Political	Economic	Sociocultural	Technological	Environmental	Legal
Political stability	Job market growth	Cultural attitudes	Digital divide / access to new technology	Availability of organic products as supplies	Labor laws
Political corruption	Unemployment rates	Career attitudes	Automation and robotics	Availability of recycled products as supplies	Antidiscrimination laws
Degree of political division	Gross domestic product	Risk vs. safety focus	Generative AI, cloud and quantum computing, augmented reality (AR) and virtual reality (VR)	Renewable energy infrastructure	Environmental laws

Figure 4.4: PESTEL framework

Political

The political factor in the PESTEL framework focuses on the ways in which governments shape businesses.

It can be easy for students first learning the PESTEL framework to confuse the political category with the legal category. We review the legal factor later in this section. One distinction is that governmental regulations are best categorized as political.

To understand governmental regulations that are best categorized as political and how this differs from what is best categorized as legal, it is helpful to briefly review how government regulation is created through the federal executive branch of government because this is the governmental regulation the PESTEL framework's political factor concerns.

In the U.S., there are three branches of government: the executive, legislative, and judicial. There are also three levels of government: federal, state, and local. There are multiple types of law, and they are created through different governmental processes by different branches of government.

Federal executive governmental agencies, such as the Occupation Safety and Health Organization (OSHA), make administrative law. The **administrative law** made by governmental agencies form the basis of federal governmental regulations. Administrative law that regulates business is binding, and companies must follow it. A few of the governmental regulations that business must follow are tax regulations, immigration regulations, foreign trade regulations, and OSHA regulations that address employee health and safety.

In addition to promulgating regulations, the federal executive branch of government in the U.S. also issues presidential executive orders. For example, a July 9, 2021, **presidential executive order** by then-President Joe Biden titled "Executive Order on Promoting Competition in the American Economy" directly impacts businesses. Statutory and case law are reviewed under the legal section of the PESTEL framework.

Types of governmental regulation differ in different countries. When U.S. companies operate outside of the United States, it is important for company legal teams to understand under what conditions U.S. regulations apply and when regulations of the other country apply.

In addition to governmental regulation and presidential orders, there are other aspects of the general environment that are impacted by political factors. Corruption and political instability in a country can also impact the general environment.

Economic

The economic segment of the PESTEL framework focuses on the broad economic events and trends that impact the general environment. These include, and are not limited to, the degree of growth in the economy, inflation rates, exchange rates, and interest

rates. It also includes the recent and long-term stability or volatility of the stock market(s). The amount of available household disposable income impacts the general environment. The job market is an essential element of the economic picture of the general environment. This includes job market growth and unemployment rates. The gross domestic product (GDP) of a country is also an important indication of the economic factor for the general environment.

Sociocultural

The sociocultural factor in the PESTEL framework includes a society's culture, norms, and values. A sociocultural aspect to consider when analyzing the general environment is composition of the population, including population growth and decline and its density. Considering the percentage of the population that lives in urban, suburban, and rural communities is valuable. It is also valuable to analyze the age, gender, and ethnic distribution across a population. Perspectives can vary among different groups.

Understanding attitudes and values across multiple dimensions of the population can give a helpful picture of the sociocultural factor of the PESTEL framework. Consider attitudes and values toward the role of family in society and health consciousness. Attitudes and values about work-life balance and general lifestyle, as well as attitudes and values toward careers, can be important sociocultural factors to consider.

Changing values at work that are relevant for business now could be:

- Desire and expectation to partially work from home (hybrid work)
- Rights movements like #BLM or #MeToo
- Heightened sensitivity regarding climate change and expectations that business plays its role in fighting it
- Individualism continuing to grow

Analyzing the tolerance for risk can also be helpful when assessing the sociocultural factor of the PESTEL framework.

Technological

Technology influences the general environment in multiple ways. The level of technology in the general environment is important, as is the life cycle of technology. The life cycle of technology, which covers the commercial journey of a new technology from development and growth to decline, may have an influence on the level of technological innovation, which influences the rate of new technology development. Technology is dependent upon the appropriate infrastructures to enable its use. Consider internet and communications infrastructures and how urban and rural environments impact these. The digital divide considers access to technology along geographical and socioeconomic lines. Automation has been important for a while. Robotics is a growing technology that influences the technological factor of the PESTEL framework. Specific new technologies are always important, such as generative artificial intelligence (AI), cloud and quantum computing, augmented reality (AR), and virtual reality (VR).

Environmental

Environmental factors are important when analyzing the general (or macro) environment. The climate crisis is an essential focus of this factor. Weather and natural disasters impact the general environment. Pollution has a large impact. Although many share a value to reuse, repurpose, and recycle, there can be significant variations in the infrastructures that support these values and activities. Regenerative agriculture seeks to balance the needs for food production and the needs of the environment. As more consumers become interested in organic and recycled products, the market for securing organic and recycled supplies is increasing. As many companies set carbon-neutral or net-zero goals, the demand for green energy sources is increasing. The infrastructure to support green energy is an important aspect of the environmental factor for the PESTEL framework.

Legal

In addition to administrative law and presidential executive orders discussed above under the political factor, there is statutory law that is passed by the legislative branch of government, Congress. There also is case or common law that is based on cases adjudicated in the judicial system, the courts. Case law sets precedents that guide future actions. Both types of law must be followed and are categorized under the legal factor of the PESTEL tool. In addition to understanding where law is made, it is also useful to understand at what level of government the law has been passed—federal, state, or local—because this indicates the jurisdiction of the law. Some of the federal law that impacts businesses include import and export laws, antitrust laws, and copyright and patent laws. Federal laws that govern consumer protection, labor, and antidiscrimination are also crucial focuses of the legal factor. Federal environmental laws address ways businesses interact with the environment.

Now that you understand the PESTEL framework, it is time to conduct an analysis of the general environment. The PESTEL analysis instrument introduced below supports you when you conduct an analysis of PESTEL factors in the general environment. Once you have conducted the analysis, the instrument structures your interpretation of the analysis and your evaluation of the analysis and interpretation. You then make recommendations to the firm based on your analysis, interpretation, and evaluation.

The first step when you analyze the general environment using the PESTEL analysis instrument is to analyze the case data related to each PESTEL factor.

PESTEL analysis instrument

[Download an editable version](#) or [view this resource in Appendix 2](#).

Analyze Data about the General Environment

Step 1

- Methodically and thoroughly examine all the data available about the general environment that relates to each PESTEL factor: political, economic, sociocultural, technological, environmental, and legal.

Step 2

- Identify and classify all the data about the general environment that relates to each PESTEL factor: political, economic, sociocultural, technological, environmental, and legal.
- Questions to ask:
 - What information about the general environment relates to each PESTEL factor?
 - In which PESTEL factor does this information fit best?

Step 3

- Complete the analysis section of the PESTEL analysis instrument.

Be specific about what data in the case applies to each of the PESTEL factors. Your analysis needs to focus on the present and specific organizational context and must address what is happening with this firm, at this time, in this place, and under these circumstances. Avoid making general statements that apply either to many industries or to this company always.

For example, imagine you are analyzing Ford Motor Company, and you are considering the impact of governmental regulations and policy on sales. Avoid statements like, “Governmental regulation impacts sales.” This statement applies to many industries and has applied to Ford for some time. Although the statement is true, being more specific is helpful. Instead, you may analyze the influence of governmental regulations and policy on Ford, writing something along the lines of “The IRS \$7,500 tax credit for new plug-in electric vehicles (EVs) or fuel cell vehicles (FCVs) influenced Ford sales in 2023 by X%. President Trump’s retrenching of governmental support for clean technologies threatens Ford’s sales of EVs and FCVs.” It takes a thorough knowledge of the case to be able to provide this much more robust analysis of the influence of political regulation and policy on Ford. Continue to analyze the influence of governmental regulation and policy on Ford until you have exhausted an analysis of all the data in the case that relates to the political factor. When you have exhausted your analysis of the influence of the political factor on Ford, move onto analyzing the economic, sociocultural, technological, environmental, and legal factors. This level of detail in your analysis supports the next steps in the analysis process: interpretation and evaluation.



Figure 4.5: Ford

After completing your analysis related to each PESTEL factor, your next step is to interpret the analysis.

Interpret the Analysis

Step 1

- Examine the analysis of each PESTEL factor: political, economic, sociocultural, technological, environmental, and legal.

Step 2

- Identify and explain whether, how, and in what ways the information in the analysis is related.
- Questions to ask:
 - How does your analysis within each PESTEL factor relate?
 - How do the political factors relate?
 - How do the economic factors relate?
 - How do the sociocultural factors relate?
 - How do the technological factors relate?
 - How do the environmental factors relate?
 - How do the legal factors relate?
 - How does your analysis in each PESTEL factor relate to your analysis of other PESTEL factors?
 - For example: How does your analysis of the political factor relate to your analysis of the legal factor? Continue this until you have considered all combinations of factors that are relevant to the case.
 - What elements of your analysis of PESTEL factors were a surprise?
 - Are there incongruencies between the elements of analysis of PESTEL factors?

Step 3

- Identify and explain underlying root cause(s) of the situation.
- Question to ask:
 - What may be causing the information identified in your analysis of PESTEL factors?

Step 4

- Complete the interpretation section of the PESTEL analysis instrument.

The next step is to evaluate the interpretation of your analysis.

Evaluate the Analysis and Interpretation

Step 1

- Examine the analysis and interpretation you have just completed.

Step 2

- Identify and explain whether, how, and in what ways the information in the analysis and interpretation in the PESTEL analysis instrument impacts the industry and company.
- Questions to ask:
 - How does each element of the analysis and interpretation in the PESTEL analysis instrument impact the industry and company?
 - From a holistic point of view, looking across all the information in the analysis and interpretation in the PESTEL analysis instrument, how does the information impact the industry and company?

Step 3

- Identify and explain whether, how, and in what ways the information in the analysis and interpretation PESTEL analysis instrument is relevant to the industry and the company.
- Questions to ask:
 - How is each element of the analysis and interpretation in the PESTEL analysis instrument relevant to the industry and company?
 - From a holistic point of view, looking across all the information in the analysis and interpretation in the PESTEL analysis instrument, how is the information relevant to the industry and company?

Step 4

- Determine how important the information is to the industry and the firm.
- Action to take (if helpful):
 - Rank the analysis and interpretation PESTEL analysis instrument according to strength of importance, such as strong, moderate, or weak.

Step 5

- Identify the company's current, potential, or needed assets, organizational capacity, and managerial ability that may support or mitigate the areas of highest impact, relevance, and importance for the firm.
- Questions to ask:
 - What are the company's current, potential, or needed assets that may support or mitigate the areas of highest impact, relevance, and importance for the firm?
 - What is the company's organizational capacity that may support or mitigate the areas of highest impact, relevance, and importance for the firm?
 - What managerial ability does the company possess that may support or mitigate the areas of highest impact, relevance, and importance for the firm?

Step 6

- Complete the evaluation section of PESTEL analysis instrument.

The final step is to recommend action to the firm based on your analysis, interpretation, and evaluation.

Recommend Action to the Firm

Step 1

- Make recommendations to the company to leverage opportunities in the general environment.

Step 2

- Make recommendations to the company to mitigate threats in the general environment.

Step 3

- Place the recommendations in the instrument in the section titled "Recommendations."

A PESTEL framework takes a snapshot of the general environment. Building on this snapshot, the PESTEL analysis instrument enables you to interpret the analysis, evaluate the analysis and interpretation, and make recommendations to the firm. This transforms a PESTEL analysis from a static picture of the general environment to a dynamic process that considers the elements within the PESTEL analysis, which is much more helpful to a firm than a static snapshot.

When you analyze a case, use the strategic management framework and the analysis instrument to support your analysis. The goal is not to complete every aspect of the analysis instrument with the same degree of information. The goal is to thoroughly analyze the data in the case.

When you analyze a case, you analyze the specific PESTEL factors present in the case. Each factor in a case does not necessarily impact the case to the same degree. For example, you may find that the political, sociocultural, technological, and legal factors have the greatest influence on a case and that economic, sociocultural, technological, and environmental factors influence another case.

We have now considered the general environment, which is the first and broadest level of a firm's external environment. We also reviewed the PESTEL framework, which is the strategic management framework that is used to analyze the general environment. You have completed a PESTEL analysis using the PESTEL analysis instrument. It is now time to turn your attention to the next level of the external environment: the industry environment.

Application

- Choose one of your favorite companies.
 - Apply the PESTEL framework to that company.
 - Give an example of each factor, and explain how your examples illustrate each PESTEL factor.
 - Use the PESTEL analysis instrument to structure your analysis, interpretation, and evaluation. What recommendations would you make to the company based on your analysis?

Key Takeaways

The PESTEL framework is the strategic management framework that you use to analyze the general environment. Each letter of the acronym PESTEL represents a factor in the general environment: political, economic, sociocultural, technological, environmental, and legal.

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4.6 Analyze the Industry Environment

The **industry environment** is the second level of the external environment, and it is narrower in focus than the general environment. Sometimes the industry environment is referred to as the task environment.

The industry environment is important because it includes the dynamics that shape the profit potential and market attractiveness of an industry and the influence of direct competitors on a firm. How profitable a firm may be in an industry is important for many reasons. When company executives are considering entering a new industry, the market attractiveness and profit potential of the industry is essential information. The industry environment also considers the impact of direct competitors. Understanding the industry environment can help executives decide where in an industry to position a company. This is also valuable information when a firm is deciding whether to divest a company in an industry.

The Porter's Five Forces Framework

The Porter's Five Forces (P5) framework is the strategic management framework used to analyze the industry environment. The Porter's Five Forces framework was introduced in a 1979 article by Michael Porter of Harvard Business School.

The framework considers five forces in an industry that influence the profit potential and industry attractiveness in the industry. Executives of companies currently competing in the industry and those considering entering or exiting an industry utilize the Porter's Five Forces framework to make essential decisions.

The framework is made up of four factors on the outside surrounding a central factor (see figure 4.6). The four outside factors represent opportunities and threats to existing companies in the industry and those firms considering entering or exiting the industry. Executives of companies already competing in the industry need to continuously scan the industry environment and analyze these opportunities and threats. Businesses considering entering or

exiting the industry consider these factors when making their decision. Rivalry among existing competitors, which is in the center of the Porter's Five Forces framework, represents the relationships of companies currently competing in the industry.

Porter's Five Forces framework is a dynamic framework, as the forces interrelate and impact each other. When none of the five forces work to undermine profits, then the profit potential of the industry is strong. If all the forces work to undermine profits, then the profit potential of the industry is weak. Most industries fall between these extremes.

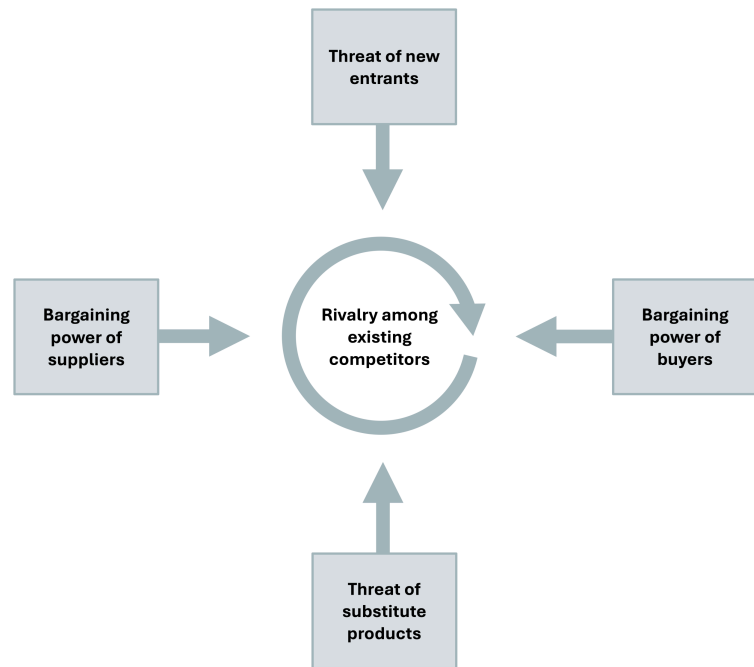


Figure 4.6: Porter's Five Forces framework

Bargaining Power of Suppliers

When suppliers have a high bargaining power, there is less industry profit potential, and when suppliers have a low bargaining power, there is more industry profit potential.

High Bargaining Power of Suppliers Means Less Industry Profit Potential

When suppliers have greater leverage over the competitors in an industry than the competitors in the industry have over the suppliers, then the bargaining power of suppliers is high. Suppliers can increase their prices either incrementally or suddenly. A price increase from suppliers reduces competitors' profit margins and can have a detrimental impact on their success. Suppliers can also analyze the potential value of entering the market as a competitor.

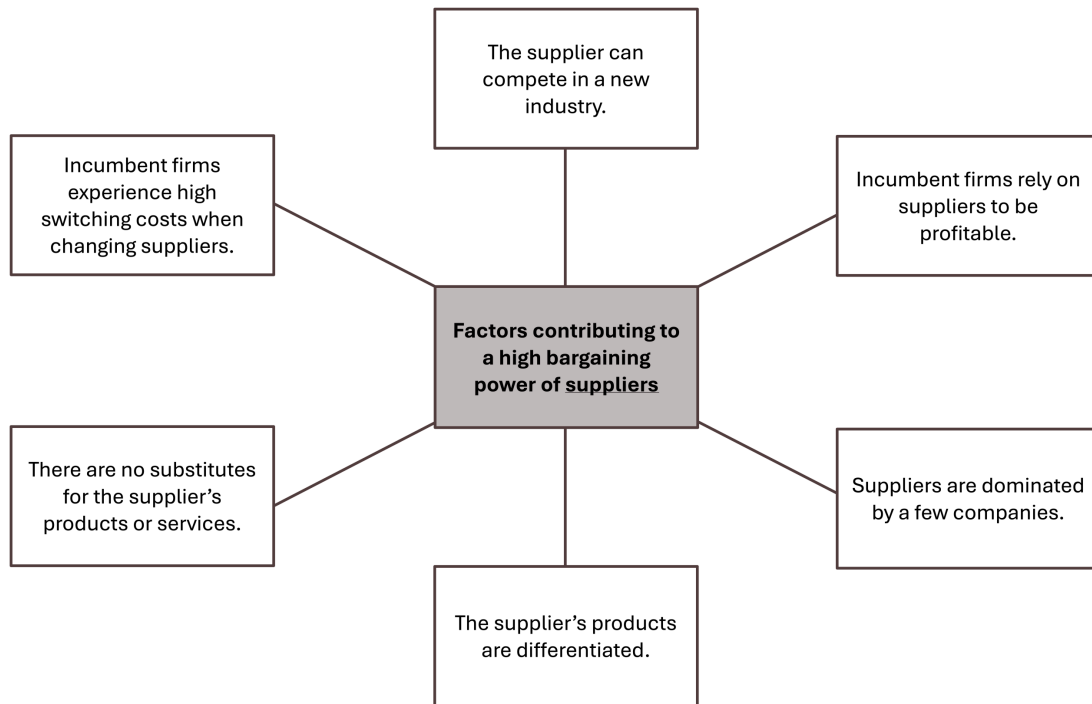


Figure 4.7: High bargaining power of suppliers

As seen in figure 4.7, there are multiple factors that contribute to suppliers in an industry having high bargaining power, including the following.

1. Incumbent firms experience high switching costs as they change suppliers.

When incumbent firms experience high switching costs when changing suppliers, this gives the current supplier a high bargaining power. There are many reasons an incumbent firm may experience high switching costs. For example, a company may experience financial switching costs due to a disruption in supply chains during a change in suppliers. Firms may also experience high psychological switching costs when they have longstanding and productive relationships with suppliers that enable quick resolutions of any potential problems. In both instances, the supplier has a high bargaining power over the incumbent firm.

2. There are no substitutes for the supplier's products or services.

When there are no substitutes for the supplier's products or services, the current supplier has a high bargaining power. Imagine a company that has no immediate alternatives of suppliers to choose from. Until other suppliers arrive in the market, the current supplier has a monopoly on the company's supply, giving the supplier very high bargaining power.

3. The supplier's products are differentiated.

When the supplier's products are differentiated, the supplier has multiple product lines, meaning a single product is a smaller portion of the supplier's total business. In this case, the supplier is less dependent on a single product and can afford to hold out for favorable prices, distribution contracts, or other conditions. This gives the current supplier a high bargaining power.

4. The supplier can compete in the new industry.

When the supplier can compete in the new industry, it is possible for the supplier to enter the industry as a competitor to incumbent firms. This gives the current supplier a high bargaining power because incumbent firms are motivated to keep out a new competitor.

5. Incumbent firms rely on suppliers to be profitable.

When incumbent firms rely on suppliers to be profitable, any changes to the supply quantity, quality, and availability will have an immediate impact on the incumbent firm's bottom line. In this case, the current supplier has a high bargaining power.

6. Suppliers are dominated by a few companies.

When suppliers are dominated by a few companies, incumbent firms have fewer choices of suppliers. This gives the current supplier a high bargaining power.

Low Bargaining Power of Suppliers Means More Industry Profit Potential

When suppliers have less leverage over the competitors in the industry than the competitors in the industry have over the suppliers, then suppliers have less bargaining power. Suppliers may need to lower their prices to remain suppliers to the industry. This strengthens competitors' profit margins and increases the probability of their success.

Bargaining Power of Buyers

Buyers are the customers to the industry's incumbent firms. When buyers have a high bargaining power, there is less industry profit potential, and when buyers have a low bargaining power, there is more industry profit potential.

High Bargaining Power of Buyers Means Less Industry Profit Potential

When buyers have greater leverage over the competitors in an industry than the competitors in the industry have over the buyers, then the competitors may be forced to lower their prices or increase the quality of their products. This weakens competitors' profit margins and makes them less likely to be prosperous. The power of buyers increases when they demand a lower price or higher-quality product because this impacts the profit margin of the industry's incumbent firms. Buyers can also analyze the potential value of entering the market as a competitor.

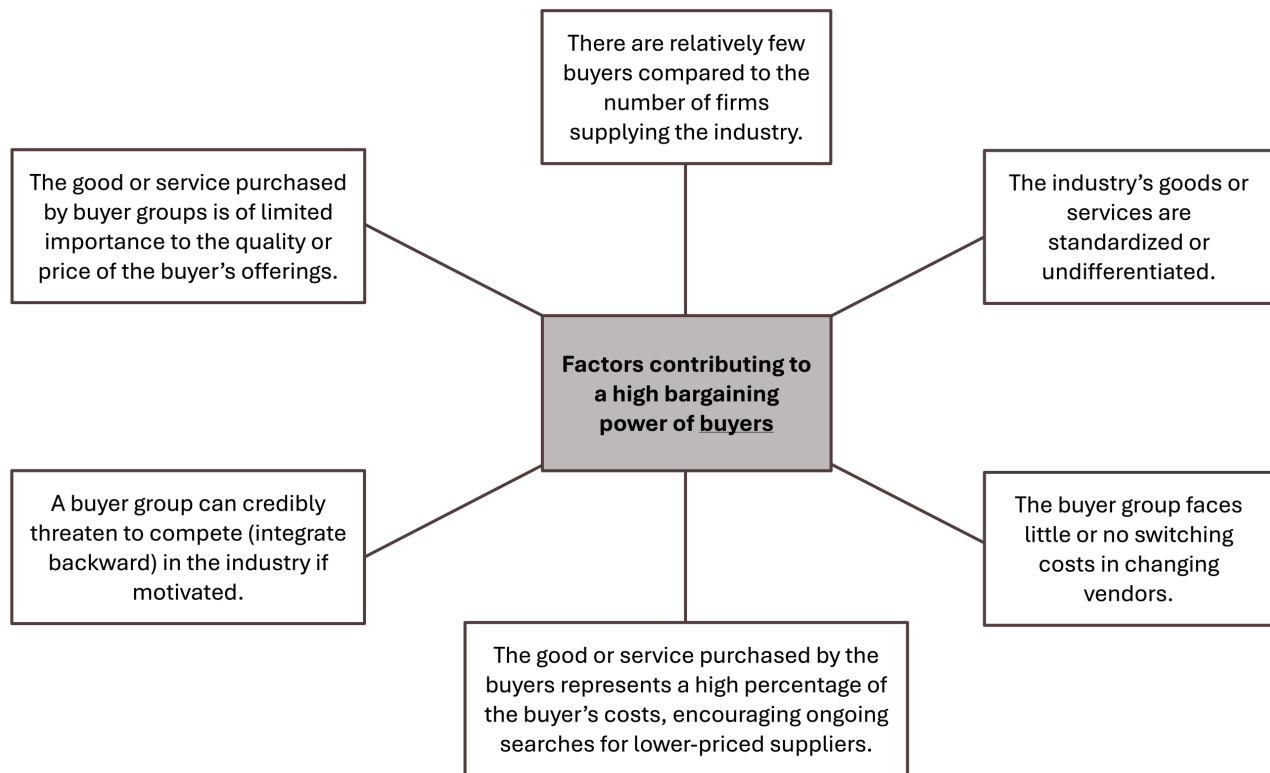


Figure 4.8: High bargaining power of buyers

Low Bargaining Power of Buyers Means More Industry Profit Potential

When buyers have less leverage over the competitors in an industry than the competitors in an industry have over the buyers, then competitors can raise their prices and enjoy greater profits.

Industry Concentration

Both suppliers and buyers have more bargaining power in concentrated industries. Industry concentration refers to the extent to which large firms dominate an industry; since there are both suppliers and buyers in highly concentrated industries, both benefit from greater concentration.

One way to measure industry concentration is to examine the percentage of total industry output that is produced by the four biggest competitors. An industry has a high concentration when the four biggest competitors in an industry represent 80 percent to 100 percent of the total industry output. When the four biggest competitors have a total industry output of 50 percent to 79 percent, the industry has a medium concentration. An industry has a low concentration when the four biggest competitors in an industry represent less than 50 percent of the total industry output.

Threat of Substitute Products

A **substitute** is a product or service that comes from outside the existing industry but fills the same need for existing industry customers while offering some additional value. Because they are products or services from outside the industry, substitute products may come close to meeting the current customer need but by a different means. Sometimes substitute products generate a new

demand for a product or service that did not previously exist in the industry. A substitute product or service is not the same thing as a product or service offered by a competitor, which is covered under competitive rivalry.

High Threat of Substitutes Means Less Industry Profit Potential

A high threat of substitutes limits the price incumbent firms can charge for their goods. Therefore, a high threat of substitutes reduces industry profit potential.

Sometimes substitutes are so effective that they disrupt the industry, meaning that all or most of the industry demand for the previous product or service becomes obsolete. For example, navigation systems were a big market with products like TomTom that sold many different navigation devices. Customers also paid substantial premiums for cars with an in-built navigation system. With the emergence of Google Maps, Wayz, Apple Maps, and other navigation apps that are part of everyone's smart-phone, the market has shrunk significantly. Navigation apps on smart-phones have substituted dedicated navigation devices, disrupting the industry. An industry that is threatened by such a disruption due to possible substitute products and services is unattractive.

Low Threat of Substitutes Means More Industry Profit Potential

A low threat of substitutes has little impact on the price incumbent firms can charge for their products and services. A low threat of substitutes increases industry profit potential.

Threat of New Entrants

New entrants are companies that are not currently competitors in the industry but may become **competitors** in the future. A primary difference between the threat of substitutes and the threat of new entrants in the Porter's Five Forces framework is that the threat of substitutes concerns products or services that come from outside the industry but fill the same need for existing industry customers while offering some additional value, while the threat of new entrants analyzes the threat of companies that are not currently competitors in the industry but may become competitors in the future. The more profit potential an industry has, the more attractive it is to potential new entrants.

High Threat of New Entrants Means Less Industry Profit Potential

There are many factors that contribute to a high threat of new entrants. The three previous forces we have considered—threat of substitute products, bargaining power of buyers, and bargaining power of suppliers—can contribute to a high threat of new entrants. When suppliers consider entering the market as a competitor, they become a threat as a new entrant. When buyers consider entering the market as a competitor, they become a threat as a new entrant. The company that makes a substitute product or service is likely to become a new entrant. This illustrates the interrelationships of the forces in the Porter's Five Forces framework.

Low Threat of New Entrants Means More Industry Profit Potential

There are barriers that reduce the threat of potential new entrants to existing firms in the industry. These are referred to as entry barriers.

Potential barrier	Relation
Economies of scale	When the scale needed for the lowest possible production cost is high, the threat of entry is lowered.
Capital requirements	When capital requirements to enter a new industry is high, the threat of entry is lowered.
Advantages independent of size	When incumbent firms possess high levels of brand loyalty, favorable locations, proprietary technology, cumulative learning and experience, and preferential access to supplies and distribution channels, the threat of entry is lowered.
Switching costs	When switching costs are high, the threat of entry is lowered.
Network effects	When network effects are present, the threat of entry is lowered.
Government policy	When governmental policy restricts competition, the threat of entry is lowered.
Expected retaliation	When a new entrant expects incumbent firms to retaliate, such as by initiating a price war when they enter the industry, the threat of entry is lowered.

Figure 4.9: Entry barriers to new entrants

Economies of Scale

Economies of scale are cost advantages that firms with large outputs have because they can spread their fixed costs across more units of production. Some of these fixed costs include, but are not limited to, many of the functional business units, such as finance, accounting, human resource management, information technology, and sales and marketing. They also may be able to capture some efficiencies by using technology in more innovative ways and creating a more specialized work force. When the scale needed for the lowest possible production cost is high for a potential new entrant into the industry, the threat of entry is lowered.

Capital Requirements

Capital requirements are related to economies of scale. Capital requirements include the investment required to enter a new industry. When capital requirements to enter a new industry are high, the threat of entry is lowered.

Advantages Independent of Size

Incumbent firms in an industry have advantages independent to size. Some of these include high levels of brand loyalty, favorable locations, and proprietary technology. In addition to these advantages, incumbent firms also have the advantage of the cumulative learning and experience they have acquired from being successful in their industries. They may also have established preferential access to supplies and distribution channels. When incumbent firms possess high levels of brand loyalty, favorable locations, proprietary technology, cumulative learning and experience, and preferential access to supplies and distribution channels, the threat of entry is lowered.

Switching Costs

Switching costs are the costs that customers incur when they switch from one vendor to another. Switching costs are most often monetary. They can also be psychological. When a customer is loyal to a brand and switches to another brand, there can be a psychological cost to the customer in switching to the new vendor. There are mental or emotional barriers to making a switch. Brand loyalty is a classic example. Customers of music streaming platforms might resist switching to a competitor because of familiarity and comfort with the service they use. A Spotify customer may be hesitant to switch to Apple Music and may experience a drain on their mental energy as they navigate the learning curve of using a new system. They may also experience an emotional drain as

music platform loyalty may be shared by friends and their friends may not be using the new service. When switching costs are high, the threat of entry is lowered.

Network Effects

Network effects are the positive effects one user has on other users of a product or service. The stronger the network effect, the higher the value of a product or service when the number of users increases. Network effects can be encouraged through friends and families. They can also be encouraged through social media and the use of influencers to be associated with a product or service. When network effects are present, the threat of entry is lowered.

Government Policy

Governmental policy can have either positive or negative effects on the threat of potential new entrants to an industry. When governmental policy encourages competition, the threat of entry is raised. When governmental policy restricts competition, the threat of entry is lowered.

Expected Retaliation

Incumbent firms with longevity in an industry have the capacity to enter and withstand a price war when a new firm enters the industry. The new entrant may not have the capacity to withstand this tactic. The fact that incumbent firms may enter a prolonged price war is an example of expected retaliation. The expected retaliation must be credible to deter a potential new entrant to an industry. When a new entrant expects incumbent firms to retaliate, such as by initiating a price war when they enter the industry, the threat of entry is lowered.

Rivalry among Existing Competitors

Unlike the four aspects on the outside of the Porter's Five Forces framework, which represent opportunities and threats to existing companies in the industry and opportunities for firms considering entering or exiting the industry, rivalry among existing competitors represents the relationships of companies currently competing in the industry.

Competition among rival firms in an industry can be intense. Companies seek to differentiate their products and services from those of their competitors.

Differentiation is how a company makes its products distinct from its competitors. How Apple makes a Mac distinct from a PC and an iPhone different from a Galaxy phone are examples of differentiation.

Businesses use a variety of marketing approaches to communicate the ways in which their products and services are differentiated from those of their competitors. Companies also compete in a highly competitive market through new offerings and price cuts to maintain and attract new customers. High levels of rivalry in an industry reduce the profit potential of the industry.

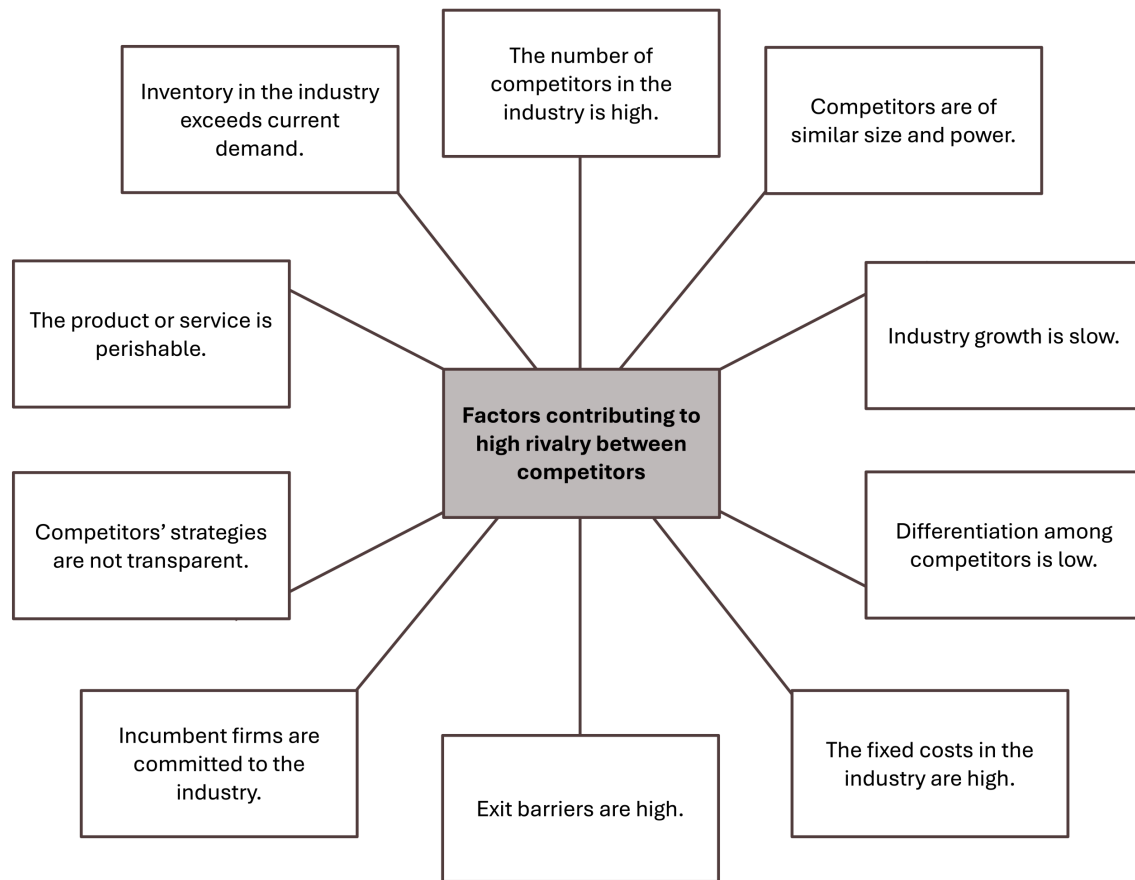


Figure 4.10: High rivalry between competitors

As the arrows in the Porter's Five Forces framework show, the four forces on the outside of the framework—the bargaining power of suppliers, and the bargaining power of buyers, the threat of substitutes, and the threat of new entrants—all exert pressure on the rivalry of competitors.

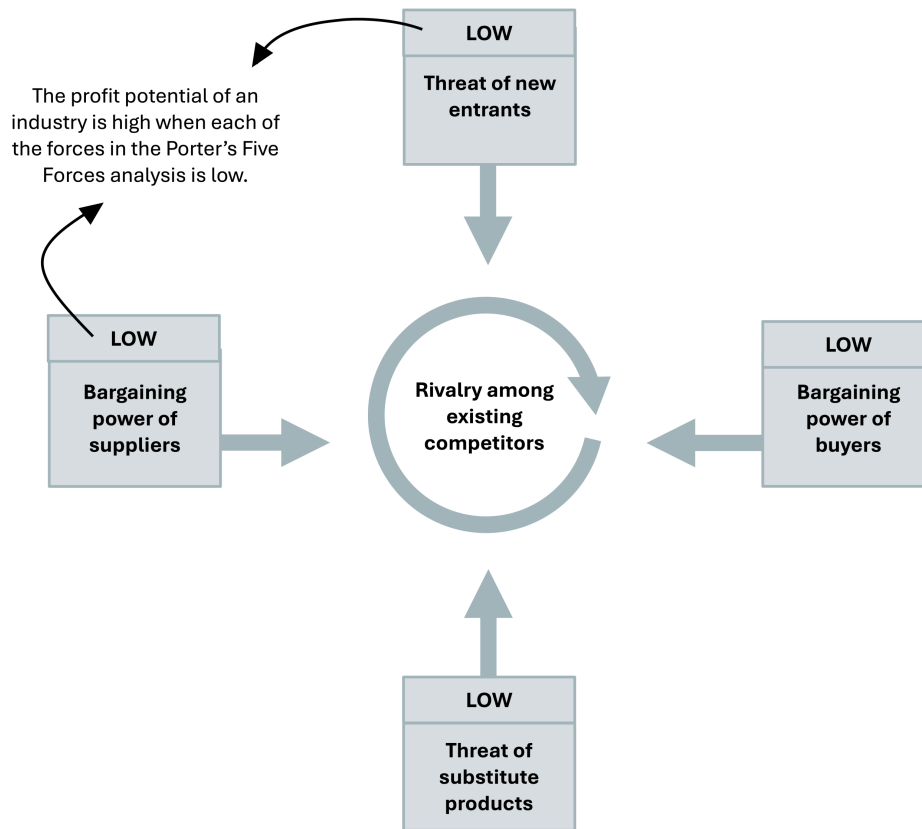


Figure 4.11: Porter's Five Forces and profit potential

When the five forces are low, then the profit potential and market attractiveness of the industry is strong.

Now that you understand the Porter's Five Forces framework, it is time to conduct an analysis of the industry environment using the Porter's Five Forces analysis instrument included in Appendix 3. The instrument structures your interpretation of the analysis and your evaluation of the analysis and interpretation, enabling you to then make recommendations to the firm based on your analysis, interpretation, and evaluation.

Porter's Five Forces analysis instrument

[Download an editable version](#) or [view this resource in Appendix 3](#).

Follow a similar process as that outlined in [section 4.5](#) for the PESTEL analysis.

The Porter's Five Forces framework is a valuable framework for analyzing the industry environment. It is most productive to consider each aspect of the framework in turn. A Porter's Five Forces analysis is generally framed as analyzing more dynamic features of the external environment than does the PESTEL framework. This is because the five elements of the framework are dynamic and inter-related.

In using the Porter's Five Forces analysis instrument, you interpret the analysis, evaluate the analysis and interpretation, and make recommendations to the firm, which is made more effective thanks to the dynamic nature of Porter's Five Forces analysis.

Collaboration

Porter's Five Forces framework is useful, but it has limitations. The Porter's Five Forces framework assumes the amount of profit potential in an industry is fixed and that, if a firm is to make more profit, it must take that profit from a rival, a supplier, or a buyer. This is not always the case. Some companies collaborate, which creates a larger pool of profit that benefits all parties in the collaboration. Collaboration is reviewed in greater detail in [Chapter 9](#).

Analyze Customers' Current and Future Needs

While Porter's Five Forces analysis covers the customer perspective through the perspective of the buying power of buyers, companies need to embark on an even more specific and thorough analysis of customers' current and future needs to formulate strategy. Every strategy developed must allow the firm to meet or exceed customer needs better than its competitors. Hence, a robust understanding of present and future customer needs is critical for the success of every strategy. The firm must understand who its current and future main customers are. Which market segments, customer groups, and main customers will drive strategic success for the firm? Will the firm serve a variety of smaller customers, or will its future success depend on winning with a few industry-leading customers?

When formulating strategy with a clear right to win, winning with customers is the guiding star of strategy formulation. Hence, the firm must understand the following customer-related key areas.

- Who are the main customers with whom the firm's future success stands and falls? Who are the industry leaders and drivers in the market that command a high market share that the firm needs to win?

For example, BASF Care Chemicals' business (producing chemical ingredients for the home and personal care industry) relied heavily on a few key customers like Procter & Gamble, Unilever, L'Oreal, Johnson & Johnson, and Colgate, among others. Without winning with these key customers, BASF's Care Chemicals business would never be able to reach its visions and strategic objectives.



- Understand and estimate the share of wallet the firm holds with the most important customers who will drive its success. The share of wallet is a metric that measures how much of a customer's spending goes toward a particular company compared to its competitors. The share of wallet indicates the depth of a client relationship and how well a firm is performing with key customers and against its competitors. A typical strategic objective is to increase the share of wallet with key customers.
- For all customers, but especially the above key customers, the firm must understand the customers' strategy. Where will key customers go, and how can the firm's customers strategize through their own products and services? The firm wants to help its (key) customers implement their strategy, which makes the firm a strategic partner and key supplier.

Staying with the BASF Care Chemicals example, Unilever's corporate strategy revolves around sustainability leadership. Integrating the innovation of sustainable and environmentally friendly chemical ingredients into BASF's Care Chemicals strategy aligns the firm's strategy with the strategy of key customers in the market, allowing BASF to form a strategic partnership with key customers and helping them to reach their own strategic objectives.

- What are the customers' met and unmet needs? The firm wants to understand the key customers' current and future needs. It is important to understand unmet customer needs because they present an opportunity to drive competitive differentiation by offering solutions for currently unsolved customer problems. This approach also links closely to innovation management as one element of business strategy.
- What are the principle buying factors in the market, and what is the main source for competitive differentiation (like price, technology, innovation, customer service, product portfolio, etc.)?
- What is the cost to serve versus the willingness to pay for key customers?

The process for finding answers to the above strategic questions is called customer exploration. This process of understanding potential and existing customers to uncover their needs, preferences, and buying behaviors is a critical step in developing a customer-centric business strategy. Customer exploration allows organizations to align their products, services, and strategy with what their target customers truly value and are willing to pay for. In a dynamically evolving business environment, successful companies prioritize customer exploration as a continuous activity. It informs product innovation, improves customer relationships, and provides a competitive advantage by adapting to market changes and to shifting customer expectations. Primary and secondary market research are used to better understand customer needs as a guiding star of strategy development.

An easy and effective approach to customer exploration is simply asking key customers what they expect from the firm. Seeking input from key customers is essential for a successful strategy. These input and feedback mechanisms include direct surveys or polls, online reviews and ratings, social media interactions and the use of "big data." Another important approach in customer exploration is customer journey mapping. This involves tracking the steps a customer takes when interacting with the firm, from initial awareness to post-purchase behavior. A customer journey map highlights the customer's pain points and areas of opportunity that can be integrated into the strategy development as a means to identify opportunities and threats in the industry.

Application

- Use the same example of one of your favorite companies that you used with the PESTEL framework in [section 4.5](#).
 - Now apply the Porter's Five Forces framework to that company.
 - Give an example of each force, and explain how your examples illustrate each Porter's Five Forces force.
 - Use the Porter's Five Forces analysis instrument to structure your analysis, interpretation, and evaluation. What recommendations would you make to the company based on your analysis?

Key Takeaways

The Porter's Five Forces framework is the strategic management framework used to analyze the industry environment. The Porter's Five Forces framework considers five forces in an industry that influence the profit potential and industry attractiveness of that industry: the bargaining power of suppliers, the bargaining power of buyers, the threat of substitute products, the threat of new entrants, and the rivalry among existing competitors. Porter's Five Forces framework is useful, but it has limitations. The Porter's Five Forces framework assumes the amount of profit potential in an industry is fixed and that, if a firm is to make more profit, it must take that profit from a rival, a supplier, or a buyer. This is not always the case. Some companies collaborate, which creates a larger pool of profit that benefits all parties in the collaboration. While Porter's Five Forces analysis covers the customer perspective through the perspective of the buying power of buyers, companies need to embark on an even more specific and thorough analysis of customer's current and future needs to formulate strategy. Customer exploration is the process of understanding potential and existing customers to uncover their needs, preferences, and buying behaviors. It is a critical step in developing a customer-centric business strategy, allowing organizations to align their products, services, and strategy with what their target customers value and are willing to pay for.

4.7 Analyze the Competitive Environment

The third level of the external environment is the **competitive environment**, and it is the narrowest in focus, consisting of companies that pursue similar strategies in the same industry. A firm has the most influence over the dynamic influences in its competitive environment.

Strategic Group

A company is a member of a strategic group, which includes firms that pursue similar strategies in the same industry. A **strategic group** consists of industry competitors that have similar characteristics to each other and differ in important ways from the companies in other strategic groups. Each firm in the strategic group seeks to create and sustain a competitive advantage. There are important differences among strategic groups, such as research and development investment, the use of technology and technology innovation, product differentiation, distribution channels, and even customer service approaches.

Firms in the same strategic group are direct competitors. Competition tends to be more intense among firms in the same strategic groups, which is known as intragroup rivalry. Competition among different strategic groups is intergroup rivalry and is less intense than intragroup rivalry.

To create and sustain a competitive advantage, executives need to know as much as they can about their competitors. This includes understanding their direct competitors in their strategic group as well as dynamics among strategic groups. This analysis supports decisions about where to position a firm relative to its competitor. When considering strategic moves, the strategies being considered or implemented by other members of a strategic group are often the best examples for executives to consider. The strategies pursued by firms in other strategic groups are alternative paths to success and can inform a firm's strategic choices.

Strategic Group Mapping

Strategic group mapping is the strategic management framework used to analyze strategic groups. It analyzes performance differences among clusters of firms in the same industry. Figure 4.13 shows a strategic group map for the competitive environment of the American automotive industry.

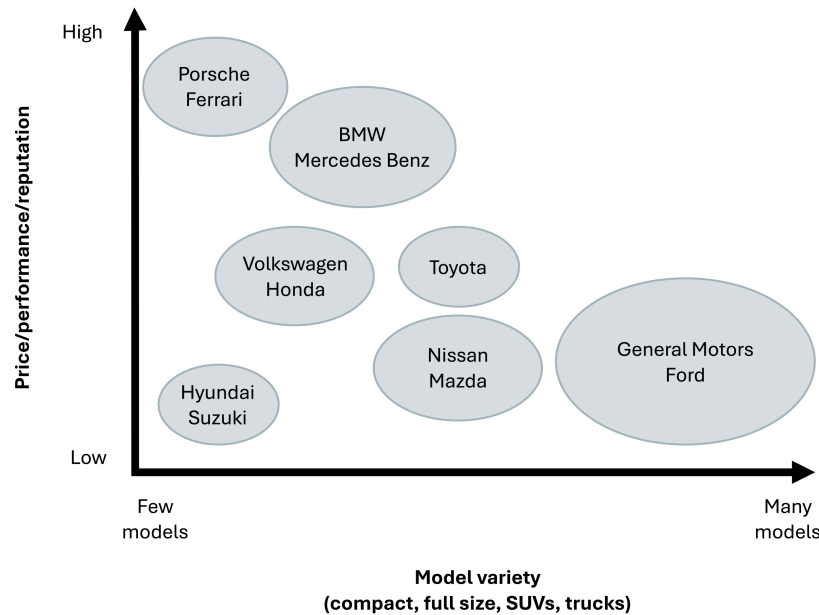


Figure 4.13: Strategic group mapping

Analyzing strategic groups using the strategic group mapping analysis instrument follows Porter's Five Forces analysis well because there are similarities between the rivalry among existing competitors in the Porter's Five Forces analysis and strategic groups in strategic group mapping.

Strategic groups in most industries differ along a few essential dimensions. To map competitors in the same industry into strategic groups, follow these steps:

1. Identify the most important dimensions that characterize the strategic groups. These represent company commitments that are both difficult and costly to reverse. They include, but are not limited to, product price, product line, research and development investment, the use of technology and technology innovation, product differentiation, distribution channels, and even customer service. This varies by industry.
2. Choose two dimensions from this list of the most important dimensions that characterize the strategic groups.
3. Map these two dimensions. Use an X (horizontal) for one dimension, with low on the left and high on the right. Use a Y (vertical) axis for the other dimension, with low at the bottom and high at the top.
4. Graph the firms in the strategic group based on these two dimensions using bubbles.
5. Indicate the market share of each firm by the size of its bubble.
6. Circle those firms with the most in common.

An example of a common X- and Y-axis pair is price and product line. Another common example for one of the axes is business-level strategy.

Strategic group mapping analysis instrument

[Download an editable version](#) or [view this resource in Appendix 4](#).

When you conduct a case analysis, you use the strategic group mapping analysis instrument to analyze strategic groups, following a similar process as outlined for the PESTEL analysis. The strategic group mapping analysis instrument structures your analysis.

Analyze Competitors' Strategy and Expected Competitive Moves Using a SOAR Analysis

The strategic group framework provides important information as to the most relevant and most important competitors of the firm. Additional competitive intelligence with information about the main competitors and rivals is necessary and important in anticipating competitors' next strategic moves. The firm needs to integrate assumptions about these strategic moves into the formulation of the firm's own strategy. For example, in strategy formulation, it is critical to know if a main competitor intends to enter or leave market segments of strategic importance for the firm. In addition, understanding whether competitors are doing well or not or whether they want to grow aggressively or are satisfied with their current both present critical input to the formulation of a meaningful and robust strategy.

The SOAR framework provides a systematic approach to analyzing and understanding the expected strategic moves of main competitors. SOAR is an acronym that stands for strategy of the rival, objectives of the rival, assumptions of the rival, and resources of the rival.

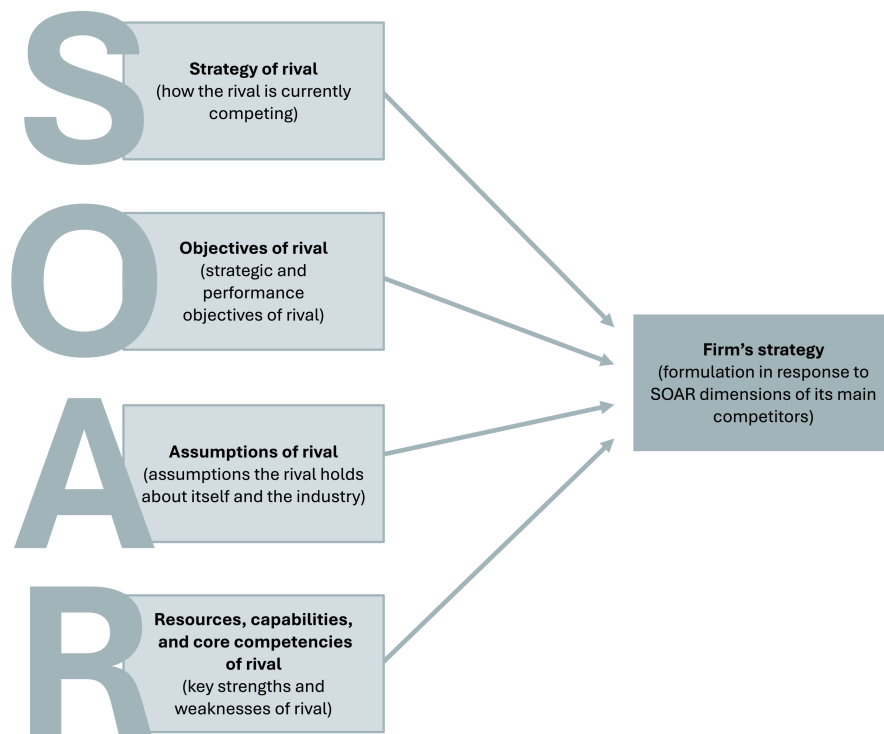


Figure 4.14: SOAR framework

S: Strategy of the Rival

A robust understanding of a competitor's expected strategic moves starts with the analysis of the competitor's current strategy. The firm needs to understand the strategic importance of its own targeted market and market segments to understand the strategy of the competitor. The firm also wants to understand the competitiveness of its rivals today and in the future.

O: Objectives of the Rival

In the second step, the firm analyzes the strategic and performance objectives of its competitor. What are the business aims of the competitor for individual business support units and as a whole? What are the competitor's objectives for regional and global markets? This will help the firm further understand how intense future rivalry may be and the implications for future market attractiveness.

A: Assumptions of the Rival

In the third step, the firm analyzes the assumptions that a competitor holds about itself and the industry. What is the competitor's definition of the market, and what are the competitor's assumptions regarding the development of the market and the industry? Are there any historical (emotional) ties to the business? Are there any national influences that would impact the competitor's strategy and competitive actions? What is the competitor's attitude to risk?

R: Resources, Capabilities, and Core Competencies of the Rival

In the fourth step, the firm looks at the resources, capabilities, and core competencies of its rival. The firm wants to understand the strengths and weaknesses of the competitor as well as their possible market exit barriers. For example, knowing that the competitor faces high possible market exit barriers means that it will be more challenging for the firm to push this specific competitor out of the market as part of its own strategy.

Understanding these four elements of the SOAR analysis helps the firm to integrate these dimensions of its main competitors into its own new strategy. This includes answers to these questions:

- Is the competitor happy with the present situation?
- How will the competitor act in all probability?
- What changes could appear in the strategy of the competitor?
- In which areas is the competitor vulnerable?
- Which strategic actions of the firm would provoke a serious strategic response from the competitor?
- Which strategic move would trigger the strongest counterreaction?

After conducting a thorough SOAR analysis, the firm has a much better understanding of competitive moves and responses that the firm needs to integrate into its own strategy formulation process. This allows the firm to make a well-informed decision regarding the strategic "battlefield" in relation to its main competitors.

The idea that a company chooses its battlefield is based on the premise that ideally, a firm wants to offer distinct resources, capabilities, and core competencies to unique markets and market segments. A company aims to avoid a strategy that leads to an overlap in resources, capabilities, and core competencies and/or overlaps in markets and market segments with its competitors.

A firm wants to avoid a strategy that leads the firm to operate in markets and market segments with strong competitive rivalries. The company also aims to avoid competing in the same markets with firms with similar resources, capabilities, and core competencies.

Ideally, the firm wants to avoid a strategy that leads to an overlap in both market segments and resources with its competitors. A strategy that leads the firm to operate in markets and market segments with strong competitive rivalries and compete in the same markets as firms with similar resources, capabilities, and core competencies is a less attractive strategic choice.

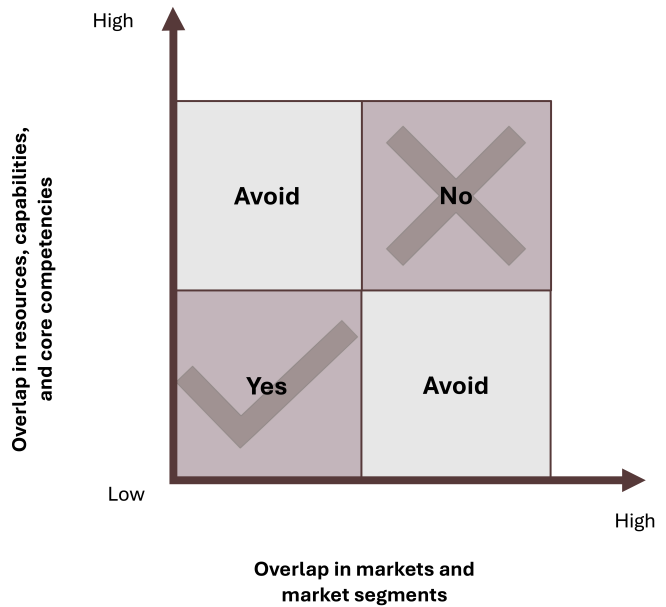


Figure 4.15: Choice of battlefield

Application

- Use the same example of one of your favorite companies that you used with the PESTEL and Porter's Five Forces frameworks.
 - Now apply strategic group mapping to that company.
 - Who are the company's closest competitors?
 - Use the strategic group mapping analysis instrument to structure your analysis, interpretation, and evaluation. What recommendations would you make to the company based on your analysis?

Key Takeaways

A company is a member of a strategic group, which includes firms that pursue similar strategies in the same industry. Strategic group mapping is the strategic management framework used to analyze strategic groups. The SOAR framework provides a systematic approach to analyzing and understanding the expected strategic moves of main competitors. SOAR is an acronym that stands for strategy of the rival, objectives of the rival, assumptions of the rival, and resources of the rival. A firm wants to offer distinct resources, capabilities, and core competencies to unique markets and market segments.

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4.8 External Environment in Case Analysis

Analyzing the external environment is the second step of case analysis:

2. Analyze the external environment.

- a. Use strategic management analytical frameworks to analyze, interpret, and evaluate the external environment of the company.
 - i. Use the PESTEL analysis instrument to analyze, interpret, and evaluate the general environment.

- a. Ensure line of sight and congruence between and among the elements of the PESTEL analysis.
- ii. Use the Porter's Five Forces analysis instrument to analyze, interpret, and evaluate the industry environment.
 - a. Ensure line of sight and congruence among the elements of the Porter's Five Forces analysis.
- iii. Use the strategic group mapping analysis instrument to analyze, interpret, and evaluate the competitive environment.
 - b. Ensure line of sight and congruence among all strategic management frameworks used.

4.9 Conclusion

The external environment includes everything outside a company that influences its ability to create and sustain a competitive advantage. The forces, factors, and actions of competitors that operate in a firm's external environment are all outside the direct control of a firm. The structure of the external environment consists of the general environment, the industry environment, and the competitive environment. Before you analyze a firm's external environment, determine its industry, its market, and the market segment it is focusing on. The general environment consists of the societal events and trends that impact all firms in an industry, including political, economic, sociocultural, technological, environmental, and legal factors. The PESTEL framework is the strategic management framework used to analyze the general environment with the PESTEL analysis instrument. The industry environment is narrower in focus. The Porter's Five Forces tool analyzes the industry environment. When you conduct a case analysis, you use a Porter's Five Forces analysis instrument to analyze the market attractiveness and profit potential of the industry by considering the bargaining power of suppliers, the bargaining power of buyers, the threat of substitute products, the threat of new entrants, and the rivalry among existing competitors. Analyze customers' current and future needs. When you conduct a case analysis, you must analyze the competitive environment by considering strategic groups with the strategic group mapping analysis instrument. Lastly, case analysis involves analyzing competitors' strategy and expected competitive moves using a SOAR analysis.

Demonstrate Your Knowledge, Skills, and Competence

Use these questions to test your knowledge of the chapter:

1. Discuss a firm's external environment. Describe what specifically it includes.
2. Describe the three levels of a company's external environment and the focus of each.
3. Discuss why defining a company's industry, market, and market segment is important when conducting a case analysis.
4. Describe the PESTEL factors. Explain the difference between political forces and legal forces.
5. Describe the five forces in Porter's Five Forces analysis and how they relate. Explain what influences the profitability and market attractiveness, both positively and negatively, of each force.
6. Discuss how analyzing customer current and future needs offers an additional dimension to analyzing a company's industry environment.
7. Describe a business's strategic group and how analyzing this can be helpful. Explain what you may consider for the X-axis and Y-

axis.

8. Describe the SOAR framework and how this is used in an external analysis of a firm.

Analyzing a company's external environment is now on your list of skills. Well done!

Figure Descriptions

Figure 4.1: Diagram composed of four concentric circles with varying shades of blue. The innermost circle is labeled “Firm”. Surrounding it, the next circle is labeled as “Analyze competitive environment (strategic group mapping).” Surrounding it, the next circle is labeled “Analyze industry environment (Porter’s five forces)” and includes the threat of substitute products, bargaining power of suppliers, bargaining power of buyers, rivalry among existing competitors, and the threat of new entrants. Surrounding it, the next circle is labeled “Analyze general environment (PESTEL)” and includes legal, economic, technological, sociocultural, ecological, and political.

Figure 4.3: Venn diagram consisting of three overlapping purple circles. The top left circle is labeled “Competitors” and includes the subheading “Industry.” The top right circle is labeled “Customers” and includes the subheadings “Markets” and “Market segments.” The bottom circle is labeled “Company,” and where all three circles intersect, it is labeled “Strategy.” The two top circles represent the “External environment.” The bottom circle represents the “Internal environment.”

Figure 4.6: Central cycle representing “Rivalry among existing competitors” surrounded by four blue boxes on each side of the circle. The boxes are connected to arrows that point to the central cycle. Clockwise, the boxes read: (1) threat of new entrants, (2) bargaining power of buyers, (3) threat of substitute products, and (4) bargaining power of suppliers

Figure 4.7: Factors contributing to a high bargaining power of suppliers: (1) The supplier can compete in a new industry. (2) Incumbent firms rely on suppliers to be profitable. (3) Suppliers are dominated by a few companies. (4) The supplier’s products are differentiated. (5) There are no substitutes for the supplier’s products or services. (6) Incumbent firms experience high switching costs when changing suppliers. This graphic is purple.

Figure 4.8: Factors contributing to a high bargaining power of buyers: (1) There are relatively few buyers compared to the number of firms supplying the industry. (2) The industry’s goods or services are standardized or undifferentiated. (3) The buyer group faces little or no switching costs in changing vendors. (4) The good or service purchased by the buyers represents a high percentage of the buyer’s costs, encouraging ongoing searches for lower-priced suppliers. (5) If a buyer group can credibly threaten to compete (integrate backward) in the industry if motivated. (6) The good or service purchased by buyer groups is of limited importance to the quality or price of the buyer’s offerings. This graphic is purple.

Figure 4.10: Factors contributing to high rivalry between competitors: (1) The number of competitors in the industry is high. (2) Competitors are of similar size and power. (3) Industry growth is slow. (4) Differentiation among competitors is low. (5) The fixed costs in the industry are high. (6) Exit barriers are high. (7) Incumbent firms are committed to the industry. (8) Competitors strategies are not transparent. (9) The product or service is perishable. (10) Inventory in the industry exceeds current demand. This graphic is purple.

Figure 4.11: Central cycle representing “Rivalry among existing competitors” surrounded by four blue boxes on each side of the circle. The boxes are connected to arrows that point to the central cycle. Clockwise, the boxes read: (1) Low threat of new entrants, (2) Low bargaining power of buyers, (3) Low threat of substitute products, and (4) Low bargaining power of suppliers. Note: The profit potential of an industry is high when each of the forces in the Porter’s five forces analysis is low.

Figure 4.13: First quadrant of an X-Y axis with blue circles representing different automotive brands. The x-axis represents model variety (compact, full size, SUVs, trucks) and the y-axis represents price, performance, and reputation. At the higher end of the price/

performance/reputation axis with fewer models are Porsche and Ferrari. BMW and Mercedes Benz are positioned slightly lower and offer more models. Volkswagen and Honda are situated in the mid-range of price/performance/reputation and in the low-range of model variety. Toyota, Nissan, and Mazda have mid-to-low range price/performance/reputation and mid-range model variety. General Motors and Ford are placed closer to having many models but with lower price/performance/reputation. Hyundai and Suzuki are positioned at the lower end of both axes, indicating low price/performance/reputation and fewer models.

Figure 4.14: On the left, four blue boxes representing each letter of S O A R are vertically aligned. “S” stands for “Strategy of rival,” focused on how rivals are currently competing. “O” is for “Objectives of rival,” concerning strategic and performance objectives of the rival. “A” represents “Assumptions the rival holds about itself and the industry.” “R” refers to “Resources, capabilities, and core competencies of rival,” indicating key strengths and weaknesses of the rival. Arrows from each of these four boxes point to a single box on the right labeled “Firm’s strategy,” which is a formulation in response to SOAR dimensions of its main competitors.

Figure 4.15: First quadrant of an X-Y axis with four purple boxes. The x-axis represents overlap in markets and market segments and the y-axis represents overlap in resources, capabilities, and core competencies. Both axis range from low to high. Low overlap in markets and low overlap in resources is marked yes. High overlap in markets and high overlap in resources is marked no. High overlap in markets and low overlap in resources is marked avoid. Low overlap in markets and high overlap in resources is marked avoid.

Figure References

Figure 4.1: Analyze the external environment. Kindred Grey. 2025. CC BY.

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Figure 4.3: The 3 Cs and strategy. Kindred Grey. 2025. CC BY.

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Figure 4.6: Porter's Five Forces framework. Kindred Grey. 2025. CC BY.

Figure 4.7: High bargaining power of suppliers. Kindred Grey. 2025. CC BY.

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Figure 4.10: High rivalry between competitors. Kindred Grey. 2025. CC BY.

Figure 4.11: Porter's Five Forces and profit potential. Kindred Grey. 2025. CC BY.

Figure 4.12: BASF Care Chemicals. Ikar.us. 2022. CC BY 3.0. https://commons.wikimedia.org/wiki/File:BASF_erleben_Tor2.jpg

Figure 4.13: Strategic group mapping. Kindred Grey. 2025. CC BY.

Figure 4.14: SOAR framework. Kindred Grey. 2025. CC BY.

Figure 4.15: Choice of battlefield. Kindred Grey. 2025. CC BY.

5. ANALYZE THE INTERNAL ENVIRONMENT

Learning Objectives

After engaging with this chapter, you will understand and be able to apply the following concepts and theories to your analysis of the internal environment of a firm.

1. Resources, capabilities, and core competencies and how these relate to creating and maintaining a competitive advantage
2. The resource-based view of a firm and why it is important to organizations
3. The VRIO framework and how it is based on the resource-based view of a firm
4. The ways isolating mechanisms serve as a value-added resource for organizations, including intellectual property, social complexity, and path dependence
5. A firm's value chain and how it is used to identify strengths and weaknesses of an organization

You will be equipped to analyze the internal environment of a firm using:

1. A VRIO framework using the VRIO analysis instrument
2. A value chain analysis using the value chain analysis instrument

5.1 Introduction

You now understand how the AFI framework provides a structured process for managing strategy. You also know that the analysis phase of strategic management answers the question “Where are we?” and includes analyzing a firm's organizational performance, external environment and internal environment, synthesizing the external and internal analysis, and determining a firm's strategic issue and strategic alternatives. The analysis phase of strategic management provides an important starting point for strategy formulation.

You have now analyzed a company's organizational performance, which provides critical information about a firm's external and internal environments. You have also analyzed a company's external environment, which provides a critical outside-in perspective and helps companies to determine attractive markets in which to operate. A firm's external environment includes those factors, forces, and competitive industry groups outside a firm's direct control. Analyzing a firm's external environment supports identifying a company's opportunities and threats.

In this chapter, you consider a company's internal environment, which provides a critical inside-out perspective of the firm. A company has direct control over its internal environment. Analyzing both the external and internal environments of an organization provides a balanced and 360-degree analysis for the firm. You also learn what resources, capabilities, and core competencies are and how these relate to creating and maintaining a competitive advantage. Next you learn the resource-based view (RBV) of firms. Then you learn what the VRIO framework is and how it is based on the resource-based view of a firm. You also learn the ways isolating mechanisms, including intellectual property, social complexity, and path dependence, serve as a value-added resource for organizations. The chapter explains a firm's value chain before teaching you to analyze the internal environment of a firm using

a VRIO analysis instrument and a value chain analysis instrument. Analyzing a firm's internal environment supports identifying a company's strengths and weaknesses.

5.2 Analyze the Internal Environment

Analyzing the **internal environment** of a firm provides critical information about key features internal to the organization over which the company has direct control.

A company has direct control over its internal resources, capabilities, and core competencies. An internal analysis of a firm identifies whether a company has the appropriate internal resources, capabilities, and core competencies to perform well and be competitive in attractive industries, markets, and market segments. The internal analysis helps to identify which internal resources, capabilities, and core competencies a firm needs to develop internally or acquire externally to be successful in the chosen markets.

At the end of the day, an organization needs to make sure that it has differentiating resources, capabilities, and core competencies that will drive a competitive advantage and will allow the organization to meet customer needs better than its competitors. While it is not possible for an organization to be superior to all its competitors in all relevant resources, capabilities, and competencies, it is important to identify and leverage a few success-critical factors that are unique to the organization, superior to its competitors, and relevant for the customers' buying decisions. The starting point of the internal analysis is a thorough understanding of the relevant resources, key capabilities, and core competencies of the firm and how they are different from each other.

An internal analysis also identifies where value is added in a firm's value chain.

While analyzing a firm's external environment helps determine a company's opportunities and threats, analyzing a company's internal environment helps determine strengths and weaknesses of the company that it needs to consider in the strategy formulation process. Strengths can be leveraged to address opportunities in the market and to counteract threats. Weaknesses need to be addressed through the internal development or external acquisition of competencies if they are relevant and important for success in the market.

Key Takeaways

The internal environment of a firm consists of resources, capabilities, and core competencies. Companies have direct control over their internal environments.

5.3 Resources, Capabilities, and Core Competencies

Resources, capabilities, and core competencies can all serve as the source of competitive differentiation in a winning strategy. Hence, they make up the basic building blocks of strategy, and it is important to start with a thorough understanding of these concepts and the differences between them.

Resources are the tangible or intangible assets that an organization owns. Tangible resources are resources that can be seen, touched, and quantified. These include physical assets, such as a firm's property, plant, land, buildings, labor, supplies, equipment, capital, and cash. Intangible resources are difficult to see, touch, or quantify. Intangible resources include the knowledge and skills of employees, a firm's reputation, brand equity, intellectual property, and a firm's corporate culture.

For example, NVIDIA has strong strategic intangible resources, such as expert employee knowledge and skills and a positive and empowering corporate culture.

A strategic resource is a resource that has the potential to drive competitive differentiation and that can serve as a source of sustainable competitive advantage. Both tangible and intangible resources can be the source of a sustainable competitive advantage and are therefore strategic in nature.

For example, BASF is the world's largest chemical company and has strategic tangible resources, such as huge fully integrated chemical plants that allow the company to manage the complete chemical value chain with synergies and economies of scale. On the other hand, Apple excels in its strategic intangible resources. Success-critical intangible resources are often the decisive strategic differentiator as it relates to corporate culture, innovation strength, and superior skills of the workforce as strategic resources.



Figure 5.1: BASF

Capabilities refer to what the organization can do with its tangible and intangible resources. Capabilities are the outcome and result of organizations using, bundling, managing, and leveraging their resources in a way that drives competitive differentiation and that adds value to its customers. Capabilities are born out of the resources that a firm has, and they are developed over time. A firm's capabilities are its organizational and managerial abilities to orchestrate a diverse set of resources and deploy them strategically. Since different firms have different approaches for resources utilization, it is possible that different firms with similar resources have different capabilities.

NVIDIA uses its leadership excellence to effectively capitalize on its intangible resources of expert knowledge and skills and its positive and empowering corporate culture to create strategic capabilities such as designing highly parallel GPUs that can process many tasks simultaneously and developing frameworks like CUDA to enable programmers to take full advantage of its GPUs. These related capabilities drive NVIDIA's competitive differentiation and adds value for its customers.

Core competencies are unique strengths embedded deep within a firm that allow the firm to differentiate its products and services from those of its rivals, creating higher value for the customer or offering products and services of comparable value at lower cost. Core competencies comprise a deep proficiency that enables a company to deliver unique value to customers. They embody the organization's collective learning and help the firm to branch into a wide variety of related markets. If they are truly differentiating, they are hard for competitors to copy or procure. Core competencies play a key role in formulating strategy because they define the firm's position and competitive advantage, and they create a sustainable competitive advantage for a company.

Returning to NVIDIA, the company has a core competency of leading the industry in AI computing. This is a deeply embedded and unique strength that allows NVIDIA to differentiate its products and services from those of its rivals and create higher value for its customers.

The term **dynamic capability** refers to an organization's ability to continually use its existing resources to create new core competencies and enhance, upgrade, and improve existing capabilities to win with customers and beat competition.

NVIDIA has a dynamic capability of capitalizing on its intangible resources such as employee expert knowledge and skills and its positive and empowering corporate culture to rapidly innovate using the latest technology to create new solutions and bring those solutions to the market ahead of its competitors.

The process of developing core competencies is sophisticated and requires strong leadership, a robust strategy, and management expertise. The first step of identifying and leveraging core competencies is to isolate key abilities and hone them into organization-wide strengths. It is important to compare them with other firms with the same skills to ensure that the firm is developing unique competencies. After that, the firm needs to develop an understanding of what competencies customers value, investing accordingly to develop and sustain the valued competencies. Hence, core competencies need to be customer-perceivable and valued by the cus-

tomers. Then the organization can create an organizational roadmap that sets goals for competence building, pursuing alliances, acquisitions, and licensing arrangements that will further build the organization's core competencies. It is advisable to encourage communication and involvement in core competency development across the organization. Non-core competencies can be outsourced or divested to free up resources that can be used to deepen the firm's core competencies.

Consumer giant Procter & Gamble identified the five core competencies below that meet the criteria and that make them the premier marketing company in the world (us.pg.com).

1. Consumer understanding. Uncovers the unarticulated needs of consumers.
2. Innovation. Translates consumer desires into new products.
3. Brand-building. Shapes purpose-inspired, benefit-driven brands.
4. Go-to-market capabilities. Reaches retailers and consumers at the right place and time.
5. Scale. Drives efficiency and consumer value.



Figure 5.2: P&G

Unilever is one of P&G's main competitors and identifies the three differentiating strengths below as Unilever's core competencies (unilever.com). Firms often refer to their core competencies by different terms. When you analyze a firm's core competencies, it is most important that you understand what a core competency is and are able to recognize it, whether the company refers to its core competencies as core competencies, differentiating strengths, or some other term.

1. Powerful portfolio of leading category and brand positions
2. Strong presence in growth markets of the future
3. The global leader in sustainable business



Figure 5.3: Unilever

These examples of P&G and Unilever illustrate how different companies that are direct rivals within the same industry determine different core competencies.



Figure 5.4: Coca-Cola

The Coca-Cola Company describes its core competencies as the ability to lead the world's most sophisticated system of independent bottling partners while creating value for retail and restaurant customers (coca-cola.com).

These examples illustrate that core competencies need to go beyond topics that just sound good or that are just a wishlist of what a company wants to be. Core competencies need to be specific to the firm, relevant to customers, and capable of beating competition.

Lastly, let us consider how the concepts of resources, capabilities, and core competencies are connected and how they work together. The starting point is the firm's resources, which are the tangible and intangible assets that a firm possesses to create value. However, just having physical assets is not sufficient to create a sustainable competitive advantage for a firm. The firm needs to use resources and translate them to customer-perceivable value that is relevant for customers' buying decisions and that drives competitive differentiation.

This is where capabilities and core competencies come into play. Capabilities include the firm's ability and aptitude to perform a certain task. A capability is a combination of personal and technical skills, knowledge, processes, tools, and behaviors that are critical to an organization's success and future needs.

Core competencies focus on the application of organizational capabilities. The core competencies ultimately drive strategic success in the competitive arena.

Hence, a firm needs to define, refine, and continuously enhance its resources and capabilities to command core competencies that will drive a sustainable competitive advantage. If the firm does this successfully, it will win in its chosen markets and will be rewarded with a competitive advantage and superior financial performance. The positive financial results will then be reinvested in further honing the firm's resources and capabilities that will lead to sustainably differentiating core competencies.

Application

- Consider your own personal resources, capabilities, and core competencies as they relate to your future career in business.
 - Describe the tangible resources you have. Your university degree will be one tangible resource. What other tangible resources do you have that will support your business career?
 - Describe the intangible resources you have. The knowledge you gain earning your university degree will be one intangible resource. What other intangible resources do you have that will support your business career?
 - Discuss the capabilities you have. What capability will you create by organizing, using, bundling, managing, and leveraging your degree and knowledge in a way that gives you a competitive differentiation in the job market? What other capabilities do you have that will support your business career?
 - Discuss your personal core competencies. What are your unique strengths that are deeply embedded in your behavior and mindset that allow you to differentiate your talents and skills from other job applicants that will create a higher value for your employer?
 - Rank your dynamic capability. Describe your ability you have to continually use your existing resources to create new core competencies and to enhance, upgrade, and improve your existing capabilities to continuously improve your employability.
 - Consider this assessment of your own personal resources, capabilities, and core competencies when you analyze the resources, capabilities, and core competencies of firms.

Key Takeaways

Resources are the tangible or intangible assets that an organization owns. Tangible resources are resources that can be seen, touched, and quantified, like a firm's property, plant, land, buildings, labor, supplies, equipment, capital, and cash. Intangible resources are difficult to see, touch, or quantify. Intangible resources include the knowledge and skills of employees, a firm's reputation, brand equity, intellectual property, and a firm's corporate culture. Both tangible and intangible resources can be sources of sustainable competitive advantages and strategic in nature. Capabilities refer to what the organization can do with its tangible and intangible resources. Capabilities are the outcome and result of organizations using, bundling, managing, and leveraging its resources in a way that drives competitive differentiation. Core competencies are unique strengths embedded deep within a firm that allow a firm to differentiate its products and services from those of its rivals, creating higher value for the customer or offering products and services of comparable value at lower cost. Core competencies are a deep proficiency that enable a company to deliver unique value to customers. Dynamic capability refers to an organization's ability to continually use its existing resources to create new core competencies and to enhance, upgrade, and improve existing capabilities to win with customers and beat competition.

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5.4 Resource-Based View and the VRIO Framework

By now, you know that strategy can be described as a firm's answer to three critical strategic questions that every organization needs to answer:

1. Where to play?
2. How to win?
3. Right to win?

Regarding the first two questions, “Where to play?” is addressed at the corporate level and “How to win?” is addressed at the strategic business unit level. The third question, “Right to win?”, is considered by the specific strategies that are embedded into business-level strategies at the strategic business unit level, which include innovation strategy, sustainability and ethics strategy, technology

strategy, and multinational strategy. Corporate-level strategy, business-level strategy, and these embedded strategies are all dealt with in detail in subsequent dedicated chapters. All three questions drive the firm's formulation of a roadmap and action plan toward sustained superior performance.

Addressed at the strategic business unit level, how to win in a firm's chosen market is largely driven by the firm's ability to develop a winning strategy around its resources, capabilities, and core competencies that are superior to those of its competitors and that will create value for the firm's customers. Overall the "How to win?" question addresses the firm's search for a sustainable competitive advantage.

Considering how a firm's resources, capabilities, and core competencies can be marshalled to create and sustain a competitive advantage leads to a series of new questions that will help a company define how to win in its specific strategies that are embedded into business-level strategies at the strategic business unit level.

1. Which of these resources, capabilities, and core competencies make a firm truly unique?
2. Where and how can a firm find its unique selling proposition (USP), which is the essence of what makes the firm's product or service better than its competitors?
3. What does the firm do both well and in a superior way?
4. What do the company's customers want?
5. What does the firm do better than its competitors?
6. What are the main sources and drivers for the firm's competitive differentiation?

A helpful framework to find answers to these critical strategy questions is the **VRIO framework**, which is based on the resource-based view of a firm.

According to the resource-based view, a firm can achieve a sustainable competitive advantage if it possesses resources, capabilities, and core competencies that are:

- Valuable
- Rare
- Hard to imitate (inimitable)
- Organized to capture value

A resource, capability, or core competency that meets all four requirements can provide a sustainable competitive advantage around which the firm should build its strategy.

	V VALUABLE	R RARE	I INIMITABLE	O ORGANIZED
Competitive disadvantage	✗			
Competitive parity	✓	✗		
Temporary competitive advantage	✓	✓	✗	
Unrealized competitive advantage	✓	✓	✓	✗
Sustainable competitive advantage	✓	✓	✓	✓

Figure 5.5: The VRIO framework

Analyze the Internal Environment of a Firm Using the VRIO Framework

The VRIO framework is a flowchart.

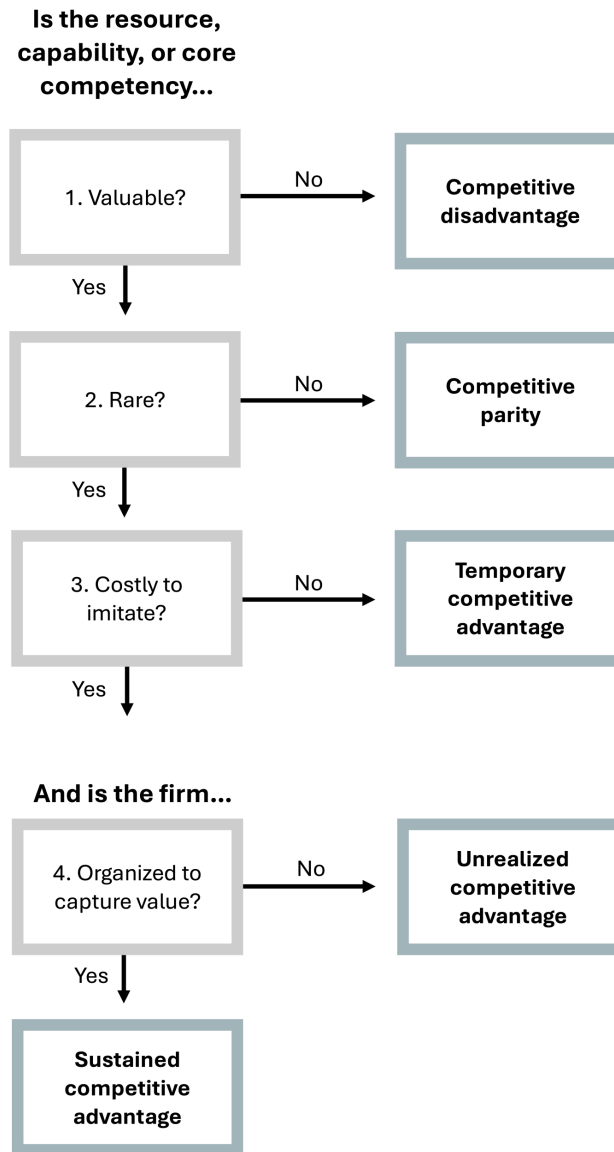


Figure 5.6: VRIO framework flowchart

The first step in using the VRIO framework is to identify a firm's resources, capabilities, and core competencies and list these in the lefthand column of the table, as shown in figure 5.5. Assess each resource, capability, and core competency to determine whether it is valuable, rare, hard to imitate, and organized to capture value. Stop when you answer "no" to the resource, capability, or core competency being valuable, rare, or costly to imitate. Do not continue along the flowchart once you have answered "no" for anything. Use the VRIO decision tree to analyze resources, capabilities, and core competencies, not a firm's products, services, or the firm.

After learning what a VRIO analysis is and how to analyze the internal environment of a firm, the chapter walks you through an example using a VRIO analysis.

Valuable

The first criterion in the VRIO framework is value. When you analyze a firm's internal environment using a VRIO framework, the question to consider is whether a resource, capability, or core competency is valuable.

If a firm has no resources, capabilities, and core competencies that are valuable to the customer, the firm will fail. If customers do not see value in what the company brings to the market, they will simply walk away from the company and give their business to the organization's competitors that offer something that the customers value; in this case, the firm is at a competitive disadvantage. The strategic conclusion is that, if a firm does not have valuable resources, capabilities, and core competencies, the company cannot formulate differentiating strategies that are embedded into business-level strategies at the strategic business unit level, and therefore does not have a strategic right to win. The firm needs to internally develop or externally acquire resources, capabilities, and core competencies that its customers value.

It is unlikely that you'll analyze a firm with no resources, capabilities, or core competencies, as it is impossible to survive in the market if none of these elements are valuable. When you analyze a firm's internal environment using a VRIO framework, it is more likely that you may find a particular resource, capability, or core competency that is not valuable. If you assess that a resource, capability, or core competency is not valuable, then place a "no" in the flowchart under "Valuable" and stop. This places the company at a competitive disadvantage.

When you assess the resource, capability, or core competency as valuable, then place a "yes" in the flowchart under "Valuable" and move on to assess whether that resource, capability, or core competency is rare.

Rare

The second criterion in the VRIO framework is rarity. When you analyze a firm's internal environment using a VRIO framework, the second question to consider is whether a resource, capability, or core competency is rare. You consider this question only for those resources, capabilities, and core competencies that are valuable.

If a firm's competitors also command resources, capabilities, and core competencies that offer the same value for customers, the firm does not offer anything unique and differentiating but only matches competitor offerings. This puts the firm at competitive parity with its competitors. While this is surely a better strategic position than not offering any value at all, the company has followed a "me too" strategy, and that is not enough to drive competitive differentiation. It is not recommended that a firm builds its strategy around resources, capability, and core competencies that are valuable but not rare, as this only leads to competitive parity in the market. The strategic conclusion is that a firm needs to develop or acquire resources, capabilities, and core competencies that are unique in the market and that truly drive competitive differentiation that is perceivable by the firm's customers. If a firm has no resources, capabilities, and core competencies that are rare, then the whole firm is at competitive parity. It is unlikely to survive long.

When you analyze a firm's internal environment using a VRIO framework, it is more likely that you find some particular resources, capabilities, and core competencies that are rare and some that are not. If you assess that one of these elements is valuable but not rare, then place a "no" in the flowchart under "Rare" and stop. This resource, capability, or core competency places the company at a competitive parity. When you assess the resource, capability, or core competency as rare, then place a "yes" in the flowchart under "Rare" and move on to assess whether that resource, capability, or core competency is hard to imitate.

Hard to Imitate (Inimitable)

The third criterion in the VRIO framework is being hard to imitate, or inimitable. When you analyze a firm's internal environment using a VRIO framework, the third question to consider is whether a resource, capability, or core competency is hard to imitate. You consider this question only for those resources, capabilities, and core competencies that are valuable and rare.

When a firm has resources, capabilities, and core competencies that are valued by the customer and rare, this is obviously much better than the “me too” strategy mentioned earlier. The firm enjoys a temporary competitive advantage because it offers something that its competitors do not currently offer. However, in a dynamic and highly competitive market environment, competitors constantly monitor the success of the firm. Competitors do not want to lose market share, and if they have the opportunity to quickly emulate and imitate the successful offering of the firm, they will do this to catch up and regain lost market share. This means the company only enjoys a temporary competitive advantage as long as competitors have not yet imitated their successful approach. As soon as competitors emulate, duplicate, and imitate their solutions, the firm will lose its competitive advantage. The strategic conclusion is that a firm needs to command resources, capabilities, and core competencies that are rare, valuable, and hard to copy by competitors.

If a firm has no resources, capabilities, and core competencies that are hard to imitate, it will remain competitive only until competitors imitate these elements. When you analyze a firm's internal environment using a VRIO framework, it is more likely that you may find particular elements that are not hard to imitate and some that are hard to imitate. If you assess that a resource, capability, or core competency is not hard to imitate, then place a “no” in the flowchart under “Inimitable” and stop. Being hard to imitate places the company at a temporary competitive advantage. When you assess the resource, capability, or core competency as hard to imitate, then place a “yes” in the flowchart under “Hard to Imitate” and move on to assess whether that resource, capability, or core competency is organized to capture value.

Organized to Capture Value

The fourth and final criterion in the VRIO framework concerns whether a firm is organized to capture value. You consider this question only for those resources, capabilities, and core competencies that are valuable, rare, and hard to imitate. A resource, capability, or core competency is organized to capture value when the firm has organizational systems, processes, and structures in place to capitalize on the resource, capability, or core competency for a competitive advantage.

A firm that commands resources, capabilities, or core competencies that are valuable, rare, and hard to imitate is in a better strategic position than those that do not have such characteristics. However, the presence of valuable, rare, and hard to imitate factors is not enough for long-term success. Companies that have valuable, rare, and hard to imitate resources, capabilities, or core competencies have yet to fully realize their full competitive advantage. They have an unrealized competitive advantage.

The firm also needs to leverage those and translate them into specific activities and strategic action. It needs to organize its business model in a way that enables the firm to translate the valuable, rare, and hard to imitate resources into a competitive advantage and superior firm performance. The company does this by having organizational systems, processes, and structures in place to capitalize on the resource, capability, or core competency for a competitive advantage.

The strategic conclusion is that a firm needs to make good use of its valuable, rare, and hard to imitate resources, capabilities, or core competencies. It takes leadership effort, strategic insight, and decisive managerial action to leverage the potential of winning in the market into truly superior financial performance. Only when resources, capabilities, and core competencies meet all the VRIO criteria does the firm have a sustainable competitive advantage to build a winning strategy.

Just as it is unlikely that a firm only no resources, capabilities, and core competencies that are valuable, it is also unlikely that one hundred percent of a firm's characteristics meet all four criteria of valuable, rare, hard to imitate, and organized to capture value. When you analyze a firm's internal environment using a VRIO framework, it is more likely that you may find a particular resource,

capability, or core competency that does not meet all four criteria and some that do. If you assess that a resource, capability, or core competency is not organized to capture value, then place a “no” in the flowchart under “Organized to capture value” and stop. This resource, capability, or core competency gives the company an unrealized competitive advantage. The firm has the potential to move that resource, capability, or core competency into a sustainable competitive advantage if it can organize to capture the value of that resource, capability, or core competency.

When you assess the resource, capability, or core competency to be organized to capture, then place a “yes” in the flowchart under “Organized to capture value.” This places the firm at a sustainable competitive advantage.

Using the VRIO framework helps companies to identify all of their resources, capabilities, and core competencies and the few truly differentiating ones that are the source of sustainable competitive advantage. These few resources, capabilities, and core competencies form the basis of a winning strategy.

A VRIO analysis instrument is offered below to support your analysis.

VRIO analysis instrument

[Download an editable version](#) or [view this resource in Appendix 5](#).

Now let's take an example of one of your favorite restaurants. Perhaps it is a place you go to hang out with your friends.

Resource Capability Core competency	Valuable	Rare	Inimitable	Organized to capture value	Competitive implication
Outdoor dining	Y	N			Competitive parity
Secret sauce	Y	Y	N		Temporary competitive advantage
Fresh seafood	Y	Y	Y	N	Unrealized competitive advantage
Local reputation	Y	Y	Y	Y	Sustained competitive advantage

Figure 5.7: VRIO of your favorite restaurant

Imagine that your favorite restaurant has outdoor dining. You and everyone you know loves this. This is valuable. Now let's consider if outdoor dining is rare. Because you attend university in a small university town in a favorable climate, outdoor dining is not rare. Most restaurant in town offer outdoor dining. Therefore, the competitive implication for outdoor dining is that it affords the restaurant competitive parity with other restaurants in town. This is important information for the restaurant because they need to maintain outdoor dining to remain competitive in this town. Imagine the restaurant is faced with a decision to expand their indoor seating at the expense of no longer offering outdoor dining. This is an unwise choice because that would put them at a competitive disadvantage in relation to their competitors. Now imagine that your favorite restaurant is in a large city with weather seldom favorable to outdoor dining. In that context, your assessment of outdoor dining would be different. When using a VRIO framework, your analysis is always context specific.

Now let's say the restaurant has a secret sauce that has a bit of local notoriety. It is valuable and rare because no other local restaurant has a similar sauce, even though it is not hard to imitate. Do you like to try to make something at home that you have eaten in a restaurant? If another local restaurant wanted to invest in replicating or even improving upon the secret sauce, they could. The secret sauce is not inimitable, and the competitive implication is that the secret sauce is a temporary competitive advantage.

Imagine your favorite restaurant occasionally has fresh ocean seafood but not on a regular day of the week and without a consistent selection. You and your friends love fresh ocean seafood and often go to your favorite restaurant hoping there will be a fresh ocean seafood offering that day. Often you are disappointed. Your small university town is not near the ocean, and there are currently no food services delivering fresh seafood to the area. Fresh ocean seafood is valuable, rare, and hard to imitate. However, the restaurant has not organized to capture the full value of this resource because of the insufficient supply chain. This is an unrealized competitive advantage. Understanding this, your favorite restaurant decides to start internally sourcing fresh ocean seafood. They buy a refrigerated truck and employ someone to drive once a week to the ocean and bring back a reliable menu of fresh ocean seafood. Once they have established the viability and profitability of this approach, the restaurant gradually adds more days. They have now organized to capture the full potential of this menu item and have the potential to change this unrealized competitive advantage to a sustained competitive advantage.

Now let's say that your favorite restaurant has a strong local reputation. It is not only your and your friends' favorite restaurant but also a favorite spot for most locals. This is valuable, rare, hard to imitate, and organized to capture value. The restaurant's strong consistently positive local reputation is a sustained competitive advantage. The restaurant needs to continue to focus on and invest in this to be sure it maintains this market position. Once reputation is tarnished, it is hard to recover it.

When you conduct a VRIO analysis, use the VRIO analysis instrument to structure your analysis, interpretation, and evaluation. The goal is not to find an example of each of the possible competitive implications but to list the firm's resources, capabilities, and core competencies and then evaluate them.

Application

- Conduct a VRIO analysis for your own resources, capabilities, and core competencies as a student. What is your USP? What makes you employable as an applicant for internships and positions after graduation?
- Use your favorite professional sports team. Does your team have any resources, capabilities, and core competencies that would drive a right to win in its respective league?
- Let's now apply the VRIO analysis to a company. Use the same example of one of your favorite companies that you used with the PESTEL, Porter's Five Forces, and strategic group mapping in the previous chapter. Now apply the VRIO framework to that company. Use the VRIO analysis instrument to structure your analysis, interpretation, and evaluation. What recommendations would you make to the company based on your analysis?

Key Takeaways

According to the resource-based view (RBV), a firm can achieve a sustainable competitive advantage if it possesses resources, capabilities, and core competencies that are valuable, rare, hard to imitate (inimitable), and organized to capture value. A resource, capability, or core competency that meets all four requirements can provide a sustainable competitive advantage around which the firm should build its strategy. A VRIO analysis helps companies identify the few truly strategic and differentiating resources, capabilities, and core competencies that the firm can use to build its winning strategy. A winning strategy needs a convincing answer to the question of how a firm wants to win in its chosen markets. Doing the same as competitors is not good enough. Offering something that the customers do not truly value is not good enough. A firm must systematically analyze which resources, capabilities, and core competencies they have

in place to win in the market, and they need to determine which of these elements must be further developed, honed, or added through internal development or external acquisition.

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5.5 Isolating Mechanisms

The VRIO framework shows the importance of protecting a firm's competitive advantage. Building a firewall or a “moat” around the firm's “castle” (its competitive advantage), moves the firm's strategic position from temporary or unrealized to sustainable competitive advantage. Isolating mechanisms are important ways of sustaining a firm's competitive advantage and making it hard or, for a certain time, even impossible or illegal for competitors to imitate the winning offerings of the firm.

Isolating Mechanisms and Their Significance in Business Strategy

The primary objective of a firm is to achieve a sustainable competitive advantage, where a unique resource, capability, or core competency provides a lasting edge over competitors. The duration of this advantage varies by industry. In rapidly evolving sectors like information technology or fast fashion, maintaining a competitive advantage for even a year can be considered successful. Conversely, in more stable industries, a sustainable competitive advantage may endure much longer. However, no firm can maintain a competitive advantage indefinitely with its current resources, capabilities, and core competencies since competitors are always striving to gain their own competitive advantage.

To prolong a competitive advantage, a firm must prevent competitors from replicating the resource, capability, or core competency that provides this edge. To do this, a firm needs to utilize isolating mechanisms, which are crucial for firms to sustain competitive advantage. **Isolating mechanisms**, also known as barriers to imitation, explain why firms can maintain a stable stream of economic profits and why intra-industry differences persist over time. They protect individual firms from competition within a particular strategic group or while the firms are uniquely positioned in the industry.

Isolating mechanisms include intellectual property, social complexity, and path dependence, all of which reduce the likelihood of imitation and help firms maintain their competitive advantage longer. Integrating purposeful decisions regarding isolation mechanisms into the development of a firm's strategy ensures that key decisions concerning resource acquisition, development, and allocation cannot be easily imitated, thereby prolonging and sustaining the firm's competitive advantage.

Intellectual Property

Intellectual property (IP) is one of the most important and impactful ways of creating isolating mechanisms. It refers to creations of the mind, such as inventions, literary and artistic works, designs, symbols, names, and images used in commerce. It encompasses the legal rights that individuals or organizations have over their intellectual creations, granting them control and protection from unauthorized use by others. Intellectual property refers to the legal rights concerning intellectual activity in the industrial, scientific, literary, and artistic fields. These rights allow creators or owners to benefit financially from their creations, providing a vital incentive for innovation and creative output.

In the context of business strategy, IP plays a crucial role in building competitive advantage. By securing exclusive rights to new technologies, designs, and creative works, companies can protect their market positions and prevent competitors from replicating their products or services, making this advantageous resource, capability, or core competency hard to imitate. Protecting intellectual property is especially important for companies whose business strategy includes a focus on differentiation, formulating and implementing a strategy to distinguish itself in the market by responding to consumer preferences for luxury items. The company competes primarily by offering products or services that are perceived as unique or superior by customers. Protecting intellectual property also is important for companies where innovation plays an important role. These companies invest significant resources into innovative products, services, and other solutions to drive competitive differentiation, and they obtain a significant return on investment through their intellectual property rights.

There are four important types of intellectual property that firms use to sustain and protect competitive advantage: patents, trademarks, copyrights, and trade secrets.

Patents

A U.S. patent gives the inventor the right to exclude others from making, using, offering for sale, or selling an invention or importing it into the U.S. ([uspto.gov](https://www.uspto.gov)). A patent grants property rights by a sovereign authority to an inventor. In the U.S., the U.S. Patent and Trademark Office (USPTO) is this responsible authority and has issued more than ten million patents. U.S. patents are effective only within the U.S. and its territories and possessions. They do not protect U.S. firms operating abroad. Globally operating U.S. firms must research the intellectual property rights of other nations and apply for protection to their governing authorities.

The patent provides the inventor exclusive rights to the patented process, design, or invention for a designated period in exchange for a comprehensive disclosure of the invention. Patents protect inventions from direct imitation for a limited period of time. Most patents are valid for twenty years in the U.S. from the date the application was filed with the USPTO.

Patents can be further categorized into utility patents, design patents, and plant patents. Utility patents, or patents for invention, issue legal protection to people who invent a new and useful process, an article of manufacture, a machine, or a composition of matter. Utility patents are the most common type of patent, with more than 90 percent of patents issued by the U.S. government belonging to this category. Design patents are patents issued for original, new, and ornamental designs for manufactured products. Design patents protect the design or look of something. The invention to which the design belongs must be original. Plant patents go to anyone who produces, discovers, and invents a new kind of plant capable of reproduction.

The number of patents successfully filed by a company is a good indicator of its innovation power. For example, German chemical company BASF spent more than \$2.3 billion on research and development and filed more than a thousand patents in 2023 ([BASF.com](https://www.basf.com)).

In the pharmaceutical industry, IP is so important that the strength of a company's innovation pipeline drives the company evaluation. Intellectual property is a critical asset and strategic resource in business, company valuation, mergers, acquisitions, and partnerships. Companies with strong IP portfolios are often valued higher because their intangible assets can generate sustained revenue streams and superior financial performance. Effective management of IP, including obtaining, defending, and licensing intellectual property rights, is essential for any knowledge-based business aiming to maintain long-term profitability and growth.

Examples of patents include Apple's iPhone, whose patent referred to it only as "electronic device." The patent for the signature device of the twenty-first century tells you almost nothing about it. In its entirety, Apple's patent for the original iPhone, listed simply as an "electronic device," says only that it is an "ornamental design of an electronic device, as shown and described" (popularmechanic.com).

If we look way back, Thomas Edison is one of the most famous inventors in history, and his work still has a significant mark on the world. The light bulb is one of the most famous inventions. He also worked with the phonograph, motion picture camera, and storage battery. Thomas Edison was awarded 1,093 U.S. patents (2,332 if you include his foreign patents). Edison's record wasn't surpassed until 2003, 72 years after Edison's final patent application, by Shunpei Yamazaki who holds over 12,587 patents worldwide as of 2024. Yamazaki is the president and founder of a research and development firm in Tokyo, Semiconductor Energy Laboratory Co., Ltd. As of 2024, Samsung is the company that holds the most patents granted, with over 6,377 in the U.S. For decades, IBM has been a leader in U.S. patents applications, filing over 10,000 U.S. patent applications.

Trademarks

Despite the lack of words, you immediately recognize the two trademarks in figure 5.8. You also have various associations right away when you see them. You may think of late-night food after a night out with friends and a technology company that sells leading-edge gadgets that you want and need. This example shows you the importance of trademarks as a way to differentiate a firm from its competitors.

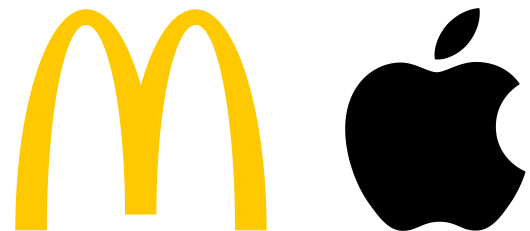


Figure 5.8: Easily recognizable trademarks

A trademark is a type of intellectual property consisting of a recognizable sign, design, or expression that identifies a product or service from a particular source and distinguishes it from others. A trademark owner can be an individual, business organization, or any legal entity. Trademarks are important because they help an organization stand out and build an identity in the marketplace. They are not only well known; they also play a crucial role in brand identity and consumer recognition.

Copyright

Copyright is a type of intellectual property that grants the creator of an original work exclusive rights to its use and distribution for a specified amount of time. This legal right allows the creator to control how the work is used, including reproduction, distribution, adaptation, and public performance.

Below are some important examples of copyrights in the U.S.

- Literary works like novels, poems, articles, and other written content
- Musical works like compositions, including any accompanying lyrics
- Dramatic works like plays and scripts
- Pictorial, graphic, and sculptural works like paintings, drawings, sculptures, and photographs
- Motion pictures like movies, TV shows, and videos
- Sound recordings like music, spoken word, and other sounds
- Architectural works like designs of buildings and structures

These examples illustrate the broad scope of copyright protection, which is essential for safeguarding the rights of creators and promoting creativity and innovation.

Trade Secrets

A trade secret is a type of intellectual property that consists of confidential business information which provides a company with a competitive edge. This information can include formulas, practices, processes, designs, instruments, patterns, or compilations of information that are not generally known or readily ascertainable by others. The owner of a trade secret must take reasonable measures to keep this information secret to maintain its economic value.

Below are some important examples of trade secrets in the U.S.

- Coca-Cola's Recipe: The formula for Coca-Cola is one of the most famous trade secrets. It has been kept confidential since the drink was invented in 1863.
- Google's Search Algorithm: Google's algorithm for ranking web pages is a closely guarded secret that gives the company a significant advantage in the search engine market.
- KFC's Secret Blend of Herbs and Spices: The recipe for KFC's chicken, which includes a blend of eleven herbs and spices, is another well-known trade secret.
- McDonald's Big Mac Special Sauce: The recipe for the special sauce used in McDonald's Big Mac is also a trade secret.

Trade secrets are crucial for businesses, as they protect valuable information that can give them a competitive advantage in the market. By keeping this information confidential, companies can maintain their unique position and continue to innovate.

Social Complexity

Social complexity is another isolating mechanism. The web of relationships within a firm, as well as connections, relationships, and partnerships of the organization with key external stakeholders like customers and suppliers, can be tough for competitors to replicate. For instance, the vital relationships that firm members establish with strategic suppliers or the long-standing relationships of the firm's account managers with procurement managers can create a unique condition that rivals cannot duplicate. Building trust, mutual understanding, and alignment makes it easier to do business. This social capital serves as an enabler of productive relationships that lowers transaction costs between the firm and other stakeholders. This social complexity acts as a barrier to imitation and can extend a firm's competitive edge. Such complexity can arise from networks and partnerships both on an organizational level and on the level of individual relationships between key members of the firm and its stakeholders.

Path Dependence

Path dependence is also an isolating mechanism. The journey a firm undertakes to achieve a competitive advantage can also act as a barrier to imitation. Past decisions that have shaped a firm's current position can be challenging for other firms to replicate. The accumulated learning and experience gained along this historical path are not easily duplicated. This concept, known as path dependence, serves as an isolating mechanism, preventing competitors from attaining the same market position. For instance, Warby Parker's early decision to build relationships with various suppliers and adopt a "buy one, give one" strategy, where a pair of glasses is donated for every pair sold, created a loyal base of suppliers and customers in the online eyewear industry. Replicating this strategy would likely be prohibitively expensive for competitors.

Video 5.1: Understanding Intellectual Property (IP) [02:14]

The video further explains intellectual property.

Access this YouTube video by scanning the QR code.

**Application**

- Going back to your favorite sports team, which form of IP do you recognize and see in action?
- Assume that you are an inventor and you want to protect your IP. What are the necessary steps to do so? Please visit the website of the U.S. Patent and Trademark Office at <https://www.uspto.gov>.

Key Takeaways

Isolating mechanisms are barriers to imitation that prevent competitors from replicating the resource, capability, or core competency that provides a sustainable competitive advantage that is critical to a firm's strategy. They drive long-lasting competitive differentiation that cannot be easily imitated or emulated by competitors. Isolating mechanisms include intellectual property (IP), social complexity, and path dependence, all of which reduce the likelihood of imitation and help firms maintain their competitive advantage longer. Intellectual property is a success-critical isolation mechanism to extend and protect the competitive advantage that a firm enjoys. Intellectual property refers to creations of the mind, such as inventions, literary and artistic works, designs, symbols, names, and images used in commerce. The targeted search and integration of IP strategies in support of the firm's chosen business model is an important element of internal analysis and resource-based strategy development that builds strategy around the strategic resources, capabilities, and core competencies of a firm that provide long-lasting and sustainable competitive differentiation. There are four important types of intellectual property: patents, trademarks, copyrights, and trade secrets. A patent grants property rights by a sovereign authority to an inventor. In the U.S., the U.S. Patent and Trademark Office (USPTO) is this responsible authority. A trademark is a type of intellectual property consisting of a recognizable sign, design, or expression that identifies a product or service from a particular source and distinguishes it from others. Copyright is a type of intellectual property that grants the creator of an original work exclusive rights to its use and distribution for a specified amount of time. A trade secret is a type of intellectual property that consists of confidential business information which provides a company with a competitive edge. This information can include formulas, practices, processes, designs, instruments, patterns, or compilations of information that are not generally known or readily ascertainable by others. Social complexity is another isolating mechanism. The web of relationships within a firm, as well as connections, relationships, and partnerships of the organization with key external stakeholders like customers and suppliers, can be tough for competitors to replicate. Path dependence is also an isolating mechanism, as the journey a firm undertakes to achieve a competitive advantage can also act as a barrier to imitation. Past decisions that have shaped a firm's current position can be challenging for other firms to replicate. The accumulated learning and experience gained along this historical path are not easily duplicated.

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5.6 Analyze the Value Chain

A value chain represents the full life cycle of a product or service, usually in the form of a series of consecutive steps detailing the creation of a finished product, from its initial design to its arrival at a customer's door. The chain identifies where value is added at each step in the process. The term was introduced by Harvard Business School professor Michael Porter in his 1985 book *Competitive Advantage: Creating and Sustaining Superior Performance*. A value chain framework is a model that describes the series of activities a business undertakes to create and deliver a product or service to a customer.

Value chain analysis (VCA) is another important tool of internal analysis. It provides a systematic overview of all major business functions of the company. When you analyze the value chain, divide business functions into primary activities and support activities.

Primary activities include the business activities that are immediately necessary and basic for any business to operate. This includes inbound logistics of raw materials being purchased and warehoused until they are used in the manufacturing process during business operations. After producing their respective products, they are shipped to the customer using outbound logistics supported by marketing and sales and by customer service as customer-facing key activities.

In contrast to primary activities, business support activities are not immediately customer-facing or related to the core business operations. Support activities include the management of the company, financing, and legal activities as part of the firm's infrastructure. Business support activities also involves human resource management, innovation management, and technology development, which includes research and development. Finally, procurement is an important support activity.

All primary and support activities need to be well aligned for a company to be successful in the market and to generate positive margins and profits.

Figure 5.9 depicts an overview of a company's primary and support activities.

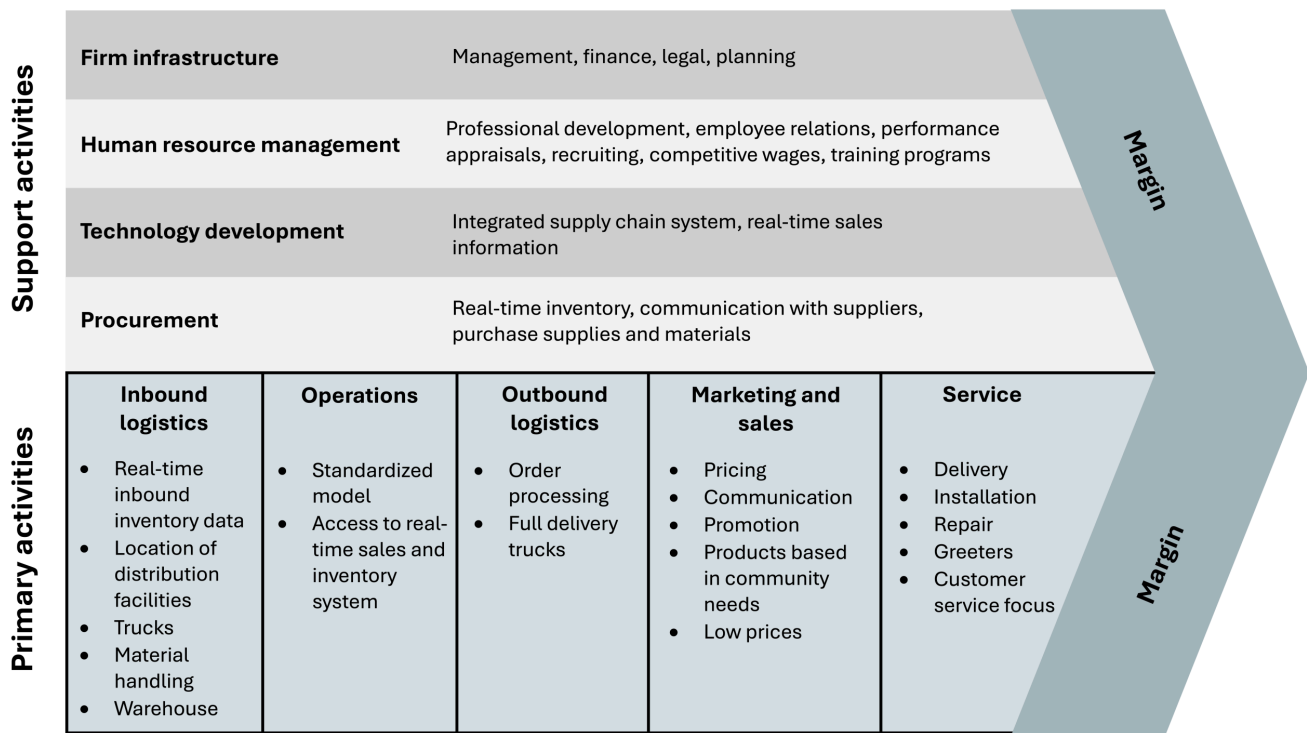


Figure 5.9: Primary and support activities

There are three main steps to conducting a value chain analysis.

- Identify primary and support activities that add value to the firm's final product or service.
- Analyze all primary and support activities with the objective of reducing costs or increasing value through appropriate and strategy-supporting activities.
- Recognize the most valuable activities. Today, competitive advantage is often derived from technological improvements or innovation.

A pragmatic approach for using value chain analysis for strategy formulation is “cost out, value in,” which indicates a focus on bringing costs down while building the value it delivers to customers. Executives use value chain analysis to implement best practices throughout the firm, particularly for high value activities that drive strategic success and competitive differentiation. Products, components, processes, and activities can be redesigned to facilitate speedier and more economical manufacturing or assembly. High-cost activities can be reallocated and outsourced to external value chains to be performed more cheaply and efficiently by vendors and contractors. Resources can also be reallocated to address activities tied to the most important purchase criteria for the firm's customers. Finally, productivity-enhancing and cost saving technological improvements can be adopted in support of margins and productivity.

It is important and critical to identify firm-specific strengths and weaknesses through the process. Primary and support activities that affirm key strengths need to be exploited and leveraged, enhancing their ability to effectively drive competitive differentiation as a key element of strategy.

On the other hand, primary and support activities that have been identified as key weaknesses need to be addressed as well. Weaknesses that are success-critical and that impact competitive positioning and customer expectations need to be corrected by internal development or the external acquisition of needed resources, capabilities, and core competencies. Weaknesses in business func-

tions that are not success-critical do not necessarily need to be addressed internally, as they possibly present an opportunity to outsource the weak elements to third party suppliers that are better suited for them because they are specialized in those areas.

A good example of such an outsourcing process is that many companies outsource their payroll activities to a third-party supplier. Unless you are a payroll services provider, payroll is neither a core competency of companies nor a factor that is important for winning in the market. Hence, there are opportunities to save money by outsourcing non-key activities to third-party suppliers. This process is covered by a long-standing strategic trend of companies focusing on their core competencies. Not every company can be the best in performing all primary and support functions of the value chain. As a consequence, companies focus on the business functions that are critical for winning in the market and that are mainly customer-facing, while outsourcing and reallocating resources away from non-key activities in its value chain.

Use the value chain analysis instrument when you analyze a firm's value chain.

Value chain analysis instrument

[Download an editable version](#) or [view this resource in Appendix 6](#).

Analyzing a firm's internal environment using the VRIO analysis instrument and the value chain analysis instrument gives you a full assessment of a firm's strengths and weaknesses. The value chain analysis reveals the ways a firm is organized to capture value—one of the criteria in the VRIO analysis. Strengths that have been identified in the value chain analysis become possible candidates for a sustainable competitive advantage. The VRIO analysis answers whether strengths identified in the value chain analysis meet all criteria to constitute a sustainable competitive advantage.

Video 5.2: Strategic Management: Value Chain Analysis [04:41]

The video for this lesson further discusses value chain analysis.

Access this YouTube video by scanning the QR code.



Application

- Conduct a value chain analysis for your favorite sports team. Which are the most important primary and support activities? Which ones are less important? Which activities, if any, would you outsource to a third party?
- You probably have used the services of an airline and/or a car rental agency. What were your positive and negative experiences? How could a value chain analysis help to identify the strengths and weaknesses for these businesses?
- Let's now apply the value chain analysis to a company. Use the same example of one of your favorite companies that you used above with the VRIO analysis.
 - Now apply the value chain framework to that company.

- Use the value chain analysis instrument to structure your analysis, interpretation, and evaluation. What recommendations would you make to the company based on your analysis?

Key Takeaways

A value chain represents the full life cycle of a product or service, usually presented as a series of consecutive steps that go into the creation of a finished product, from its initial design to its arrival at a customer's door. The value chain analysis is another important tool of internal analysis, providing a systematic overview of all major business functions of the company. When you analyze the value chain, divide business functions into primary activities and support activities. The primary activities include the business activities that are immediately necessary and basic for any business to operate. This includes inbound logistics of raw materials being purchased and warehoused until they are used in the manufacturing process during business operations. After producing their respective products, they are shipped to the customer using outbound logistics supported by marketing and sales and by customer service as customer-facing key activities. In contrast to primary activities, business support activities are not immediately customer-facing or related to the core business operations. Support activities include the management of the company, financing, and legal activities, which all make up the firm's infrastructure. It also includes human resource management, technology development, and innovation management. Finally, procurement is an important support activity. The chain identifies where value is added at each step in the process.

A value chain analysis is a powerful tool to identify strengths and weaknesses in a firm's main business functions. It provides ideas to push costs out of the business and drive more value creation by focusing on success-critical and strategically important business functions while reallocating resources away from less important functions. This can drive the strategy away from trying to be "everything to everyone" to instead focus on a few selected core competencies that the company performs really well; in turn, that will drive competitive differentiation. Use the value chain analysis instrument when you analyze a firm's value chain.

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5.7 Conclusion

Resources, capabilities, and core competencies are the backbone of strategy development in terms of how a firm can win in its chosen markets. If these elements are unique, customer-perceivable, and relevant for customers' buying decisions, the company will win. If a company has resources, capabilities, and core competencies that provide a sustainable competitive advantage, the company has a strategic right to win and should build its strategy around these few unique characteristics. The resource-based view and the VRIO analysis help companies to identify these few success-critical and truly differentiating strategy drivers.

Isolating mechanisms are powerful elements of resources, capabilities, and core competencies that often meet all VRIO criteria. Value chain analysis provides a systematic analysis of all primary and support business functions that help the company to identify strengths that can be leveraged and weaknesses that need to be addressed in the development of a new strategy. A focus on core competencies helps companies to position themselves for success with a guideline of "costs out, values in."

Demonstrate Your Knowledge, Skills, and Competence

Use these questions to test your knowledge of the chapter:

1. Discuss a firm's internal environment. Describe what specifically it includes.
2. Describe a firm's resources, capabilities, and core competencies and how they relate. What is dynamic capability?
3. Explain the resource-based view and how this relates to a VRIO analysis.
4. Describe a VRIO framework and how to use it. Explain the role of resources, capabilities, and core competencies in a VRIO analysis. What are the different levels of competitive advantage, and how do these relate to your analysis of the VRIO factors? Describe how a VRIO can be considered a flowchart.
5. Describe isolating mechanisms and how they support creating a competitive advantage. Explain the three main categories of isolating mechanisms. Discuss the three types of intellectual property.
6. Discuss a value chain, and describe how you use this to analyze a firm's internal environment. Describe the difference between support and primary activities. Discuss how this relates to a firm's profit margins.

You are now skilled at analyzing a company's internal environment. Congratulations!

Figure Descriptions

Figure 5.5: Table illustrating the VRIO framework. Columns are labeled "V," "R," "I," and "O." and shown in blue. Rows are labeled "Competitive disadvantage," "Competitive parity," "Temporary competitive advantage," "Unrealized competitive advantage," and "Sustainable competitive advantage." Each cell in the table contains either a checkmark or an "X," indicating whether the characteristic is met. Competitive disadvantage: not valuable. Competitive parity: valuable but not rare. Temporary competitive advantage: valuable and rare but not inimitable. Unrealized competitive advantage: valuable, rare, and inimitable, but not organized. Sustainable competitive advantage: valuable, rare, inimitable, and organized.

Figure 5.6: Blue flowchart to determine type of competitive advantage based on characteristics of the resource or capability. If the resource or capability is valuable, rare, and costly to imitate and the firm is organized to capture value, then it's sustained competitive advantage. If the resource is not valuable, it's competitive disadvantage. If the resource is valuable but not rare, it's competitive parity. If the resource is valuable and rare but not costly to imitate, it's temporary competitive advantage. If the resource is valuable, rare, and costly to imitate but the firm is not organized to capture value, it's unrealized competitive advantage.

Figure 5.9: Support activities: Firm Infrastructure (management, finance, legal, planning), Human Resource Management (professional development, employee relations, performance appraisals, recruiting, competitive wages, training programs), Technology Development (integrated supply chain system, real-time sales information), Procurement (real-time inventory, communication with suppliers, purchase supplies and materials). Primary activities: Inbound logistics (real-time inbound inventory data, location of distribution facilities, trucks, material handling, warehouse), Operations (standardized model, access to real-time sales and inventory system), Outbound Logistics (order processing, full delivery trucks), Marketing and Sales (pricing, communication, promotion, products based in community needs, low prices), Service (delivery, installation, repair, greeters, customer service focus). Support activities are stacked on top of Primary activities. Both sections have a Margin on the right in the shape of an arrow. This graphic is blue.

Figure References

Figure 5.1: BASF. A Frank99. 2006. Public domain. https://en.m.wikipedia.org/wiki/File:BASF-Logo_bw.svg

Figure 5.2: P&G. KarimKoueider. 2019. Public domain. https://en.wikipedia.org/wiki/File:Procter_%26_Gamble_logo.svg

Figure 5.3: Unilever. Sean Biehle. 2006. CC BY-SA 2.0. <https://flic.kr/p/agZWP>

Figure 5.4: Coca-Cola. Sean. 2008. CC BY-ND 2.0. <https://flic.kr/p/4PR8Xw>

Figure 5.5: The VRIO framework. Kindred Grey. 2025. CC BY.

Figure 5.6: VRIO framework flowchart. Kindred Grey. 2025. CC BY.

Figure 5.8: Easily recognizable trademarks. Left: McDonald's. 2006. Public domain. https://commons.wikimedia.org/wiki/File:McDonald%27s_Golden_Arches.svg. Right: Rob Janoff. 1978. Public domain. https://en.m.wikipedia.org/wiki/File:Apple_logo_black.svg

Figure 5.9: Primary and support activities. Kindred Grey. 2025. CC BY.

PART III: SYNTHESIZE ANALYSIS AND DETERMINE A FIRM'S STRATEGIC ISSUE

Part I introduced you to strategic management and case analysis. In Part II, you learned how to analyze a company's organizational performance and its external and internal environments. Now in Part III, you learn how to synthesize the analysis you have conducted and how to determine a firm's strategic issue.

6. SYNTHESIZE ANALYSIS AND DETERMINE A FIRM'S STRATEGIC ISSUE

Learning Objectives

After you have engaged with the concepts in this chapter, you will understand and be able to apply the following key strategic management concepts.

1. The SWOT framework
2. How a SWOT framework is used in strategic management
3. How to synthesize analysis using a SWOT framework
4. What a strategic issue is and why it is important
5. How to determine major areas of strategic concern
6. How to determine a firm's strategic issue
7. How to determine strategic alternatives
8. How to evaluate alternatives
9. How to develop an implementation plan to execute the recommended strategic alternative
10. How to confirm line of sight and congruence across the entire case analysis

You will be equipped to

1. Analyze the analysis you have completed so far, and complete a SWOT analysis
2. Determine major areas of strategic concern
3. Determine a strategic issue
4. Determine strategic alternatives, evaluate them, and recommend one
5. Determine line of sight and congruence throughout the entire case analysis
6. Write an implementation plan for your recommended strategic alternative
7. Write and/or present your case analysis

6.1 Introduction

In this chapter, you learn what a strengths, weakness, opportunities, and threats (SWOT) framework is and how it is used in strategic management to synthesize the analysis you have conducted so far. You learn how to determine a firm's major areas of strategic concern and its strategic issue. You learn how to determine strategic alternatives, evaluate them, and recommend one. You learn how to how to determine line of sight and congruence throughout the entire case analysis and how to write an implementation plan for your recommended strategic alternative. This culminates in your learning how to write and present your case analysis.

6.2 SWOT Framework

A SWOT framework is a tool used to categorize a firm's strengths, weaknesses, opportunities, and threats, typically portraying them in a grid with four quadrants. Strengths and weaknesses are on the top of the grid, and opportunities and threats are on the bottom of the grid.

In contexts other than the strategic management process, organizations use a SWOT framework as a standalone tool.



Figure 6.1: SWOT framework

Application

- Consider your search for a professional position after you graduate. Perhaps you already have plans.
 - Are you aiming to join a large company as a subject expert in accounting and information systems, business information technology and cybersecurity, finance, insurance and business law, hospitality and tourism management, human resource management, business management, management consulting and analytics, entrepreneurship, innovation and technology management, marketing, or real estate?
 - Does working with a smaller enterprise appeal to you more?
 - Perhaps you are planning on a more entrepreneurial path. Do you have a plan to start your own company? Maybe you already are an entrepreneur. You may be heading into consulting.
 - What are your current strengths that will support your success in your career plans? Do you have any weaknesses that you can mitigate to ensure your success? What are the external opportunities that you can capitalize on? Are there any threats to your plans that you can plan around?
 - Place your strengths and weaknesses in the top of a SWOT tool and the external opportunities and threats you may face in the bottom of a SWOT framework.

Key Takeaways

A SWOT framework is a tool used to categorize a firm's strengths, weaknesses, opportunities, and threats. The framework is typically visualized as a grid, with strengths and weaknesses on the top of the grid and opportunities and threats are on the bottom of the grid.

6.3 How a SWOT Framework Is Used in Strategic Management

In strategic management, a SWOT framework is used to **synthesize** the analysis you have conducted so far. Synthesize means to review, critically examine, and combine diverse elements into a coherent whole. Synthesis is combining different concepts to create a new understanding, making a new whole from individual parts.

Think of a time when you wanted to make a large purchase. You gathered and analyzed a wide range of data, considered the relationships of that data, and decided what to buy based on your research. Perhaps you purchased a computer or another electronic device for school. Did you investigate different brands? Did you consider the type of chip? How important was RAM to you? Perhaps weight and size were important. What about price? You synthesized a lot of information to arrive at a decision based on your analysis.

To conduct a SWOT in strategic management, you synthesize the analysis you have conducted so far about a firm's organizational performance, external environment, and internal environment. This means to review, critically examine, and combine the diverse elements of your previous analysis into a coherent concept.

When you synthesize the current analysis using a SWOT framework, this is referred to as a SWOT analysis. You are not returning to the case to conduct additional analysis from the case when you use a SWOT framework.

In strategic management, a SWOT framework is never used as a standalone tool. It is used only after you have completed your analysis of a company, when it is time to synthesize your analysis. In strategic management, once you have completed your SWOT analysis, you use your completed SWOT analysis to determine the firm's **strategic issue**.

Key Takeaways

At this stage of strategic management, you analyze and synthesize the analysis you have conducted so far to complete the SWOT analysis. In strategic management, a SWOT framework is never used as a standalone tool, but as a way to determine the firm's strategic issue from the analysis so far.

6.4 Synthesize Analysis Using a SWOT Framework

To conduct a robust SWOT analysis, begin by assessing which elements of the analysis you have conducted so far represent strengths, weaknesses, opportunities, and threats. This gives you a draft of a SWOT analysis. The next step is to synthesize the information in this draft. Once you confirm line of sight and congruence, you have a final SWOT analysis.

Determine Strengths, Weaknesses, Opportunities, and Threats

The first step in conducting a SWOT analysis is to identify strengths, weaknesses, opportunities, and threats in the elements you have analyzed thus far in the process. Then you place your previously conducted analysis into the correct categories of a SWOT analysis.

In strategic management, it is important to place the analysis that relates to the external environment of the firm in the bottom half of the grid, as they are opportunities and threats. External analysis addresses those issues external to a company and outside a firm's control—the opportunities and threats a company faces.

Then place the analysis you have conducted so far about the company's internal environment on the top of the SWOT framework as strengths and weaknesses. This is because internal analysis addresses those issues internal to a company and within a firm's control. Issues within a company's control are the company's strengths and weaknesses.



Figure 6.2: Synthesize analysis using a SWOT framework

Let's consider the analysis you have conducted so far. You do not place every aspect of your analysis into your SWOT analysis. Decide which elements of your analysis impact the firm the most, are most relevant to the company, and are most important to the company. The **evaluation** step in the analysis you have conducted so far supports you in this assessment. Deciding which elements to place in the SWOT framework requires critical thinking and judgment.

Organizational Performance

In [Chapter 3](#), you learned how to analyze a firm's organizational environment. You used the [organizational performance analysis instrument](#) to analyze a company's mission, purpose, vision, values, and goals. You analyzed a firm's financial position, its market

position, and other relevant quantitative measures. You also analyzed an organization's balanced scorecard. Your analysis of a firm's organizational performance produces information that relates to both the external and internal environments of a firm.

Synthesis begins with the examination of your analysis of the firm's organizational performance, enabling you to decide which elements of your analysis relate to the company's external environment and which elements relate to the firm's internal environments. For example, you may decide that your analysis of a firm's market position relates primarily to the external environment and your analysis of the company's balanced scorecard may relate predominantly to the internal environment. This requires critical thinking and judgment.

Next decide whether those elements of your organizational performance analysis that relate primarily to the external environment represent opportunities or threats. Place those elements that you assess as opportunities in the opportunities box of your SWOT analysis. Place those elements that you assess as threats in the threats box of your SWOT analysis.

Then decide whether those elements of your organizational performance analysis that relate primarily to the internal environment represent strengths or weaknesses. Place those elements that you assess as strengths in the strengths box of your SWOT analysis. Place those elements that you assess as weaknesses in the weaknesses box of your SWOT analysis.

Now that you have analyzed your analysis of the firm's organizational performance and placed this into the correct boxes of your SWOT analysis, you are now ready to move on to analyzing your external analysis.

External Analysis

In [Chapter 4](#), you learned how to analyze the external environment of a company. You used the [PESTEL analysis instrument](#) to analyze the general environment and the [Porter's Five Forces analysis instrument](#) to analyze the industry environment. You used the [strategic group mapping analysis instrument](#) to analyze a firm's strategic group. The findings from your external analysis are placed in the bottom half of the grid as opportunities and threats because external analysis addresses those issues outside a firm's control.

First decide whether the elements of your external analysis represent opportunities or threats. Place those elements from your analysis of the external environment that you assess as opportunities in the opportunities box of your SWOT. Place those elements from your analysis of the external environment that you assess as threats in the threats box of your SWOT.

Now that you have placed your analyses of the firm's organizational performance and external analysis into your SWOT, you are now ready to move onto analyzing your internal analysis.

Internal Analysis

In [Chapter 5](#), you learned how to analyze the internal environment of a company. You used the [VRIO analysis instrument](#) to analyze a firm's resources, capabilities, and core competencies and the [value chain analysis instrument](#) to analyze a company's primary and secondary activities. The findings from your internal analysis are placed in the top half of the grid as strengths and weaknesses because internal analysis addresses those issues within a firm's control.

First decide whether the elements of your internal analysis represent strengths or weaknesses. Place those elements from your internal analysis that you assess as strengths in the strengths box of your SWOT. Place those elements from your internal analysis that you assess as weaknesses in the weaknesses box of your SWOT.

You have now analyzed the analysis you have conducted so far in the case analysis process, deciding which elements of your analysis impact the firm the most, are most relevant to the company, and are most important to the company. After critical examination, you placed those elements of your analysis that relate to the external environment on the bottom of your SWOT analysis as opportunities and threats and those aspects of your analysis that relate to the internal environment on the top of your SWOT analysis as strengths and weaknesses. This step of conducting your SWOT analysis provides you with a draft SWOT analysis.

Synthesize SWOT Analysis

As you are learning, it is never sufficient in case analysis to simply place information into a framework. You must use critical thinking and judgment to make decisions. The same is true for synthesizing your previous analysis using a SWOT analysis.

Now that you have completed a draft SWOT analysis, you **synthesize** the analysis you have placed in your draft.

To synthesize the analysis in your draft SWOT analysis, stand back and review the SWOT analysis. Think of it from a holistic perspective. Critically examine each element of your previous analysis that you have now placed into your draft SWOT analysis. Combine elements of your draft that relate. Work with your draft SWOT analysis until you have a succinct and concise analysis that represents all the essential elements of your draft SWOT analysis.

Confirm Line of Sight and Congruence

Once you have synthesized your analysis in the draft of your SWOT analysis, determine a clear **line of sight** and **congruence** between the analysis from the strategic management frameworks and your SWOT analysis.

A few questions to consider include:

- Is there a clear line of sight between the analysis from the strategic management frameworks and the SWOT analysis?
 - Is there a clear logic behind how the analysis from the strategic management frameworks supports the SWOT analysis?
 - Is there a clear logic behind what analysis from the strategic management frameworks is placed in which category of the SWOT analysis?
- Is there congruence between the analysis from the strategic management frameworks and the SWOT analysis?
 - Ensure that everything that is included in your SWOT analysis is included in an analysis instrument.
 - Ensure that nothing is present in your SWOT analysis that is not included in an analysis instrument.

This gives you your final SWOT analysis.

This is step four in case analysis.

4. Synthesize the organizational performance and the external and internal analysis using SWOT analysis.

- a. Synthesize the organizational performance and the internal and external analysis using a SWOT analysis.
- b. Ensure line of sight and congruence between the analysis from the strategic management frameworks and the SWOT analysis.

It is only from a robust SWOT analysis that it is possible to determine a firm's strategic issue.

Video 6.1: SWOT Analysis [02:02]

The video for this lesson discusses SWOT Analysis.

Access this YouTube video by scanning the QR code.

**Application**

- Let's apply the SWOT analysis to a company. Use the same example of one of your favorite companies that you used with the PESTEL, Porter's Five Forces, strategic group mapping, VRIO, and value chain analyses in the previous two chapters.
 - Place your analysis from the external environment (PESTEL, Porter's Five Forces, strategic group mapping) on the bottom of the SWOT grid as opportunities and threats.
 - Place your analysis from the external environment (VRIO and value chain analysis) on the top of the SWOT grid as strengths and weaknesses. This gives you your draft SWOT analysis.
 - Synthesize the information in your SWOT analysis and confirm line of sight and congruence to determine your final SWOT analysis.

Key Takeaways

To conduct a SWOT analysis, begin by accurately assessing which elements of the analysis you have conducted far represent strengths, weaknesses, opportunities, and threats. Place the analysis that relates to the external environment of the firm in the bottom half of the grid as opportunities and threats because external analysis addresses those issues outside a firm's control. Place the analysis you have conducted so far that relates to the internal environment of the company on the top of a SWOT framework as strengths and weaknesses because internal analysis addresses those issues within a firm's control. This gives you a draft SWOT analysis. Then synthesize the analysis in your draft. Confirm line of sight and congruence. Now you have a final SWOT analysis. It is only from a robust SWOT analysis that it is possible to determine a firm's strategic issue.

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6.5 Strategic Issue: What It Is and Why It Is Important

In addition to synthesizing organizational performance and external and internal analysis, executives and analysts use a SWOT analysis to begin the process of identifying a firm's strategic issue. You also use a SWOT analysis to determine a firm's strategic issue when conducting a case analysis. Before considering how a SWOT analysis is used to begin determining a firm's strategic issue, it is first important to understand what a strategic issue is and why it is important.

Strategic Issue

We briefly introduced the concept of a strategic issue in the first chapter. We now cover its important role for any firm in greater detail.

A firm's **strategic issue** is the most important, urgent, broad, and long-term matter that the company is facing. Strategic issues are the result of multiple causes in multiples areas of a business and require significant organizational talent and resources to resolve. Addressing a strategic issue moves a firm toward its mission, purpose, and vision and should therefore be congruent with its values. A strategic issue focuses on the present and specific organizational context, and considers what is happening with this firm, at this time, in this place, and under these circumstances.

Let's unpack this definition:

A firm's strategic issue is the most important, urgent, broad, and long-term matter that the company is facing.

The first thing to notice is that the definition refers to one strategic issue. We distinguish between major areas of strategic concern, and a firm's strategic issue. Firms likely have more than one major area of strategic concern. Addressing multiple areas of strategic concern in one strategic issue has the advantage of clearly determining the relationships between the major areas of strategic concern. However, there is no one right answer to whether a company can have multiple strategic issues. It is more important to accurately capture all that is going on strategically for a firm than it is to be concerned with whether the firm's strategic challenge is expressed as one or multiple strategic issues. We find it easiest to learn one approach at a time. Therefore, we present multiple areas of strategic concern written in one strategic issue.

A strategic issue is the most important concern that the company is facing. A strategic issue is not a trivial matter. It is very important and must be addressed. A strategic issue also is urgent. If the strategic issue is not addressed, there are likely serious consequences for the company. These could include loss of market share, loss of industry position, or even death. A strategic issue is broad. It captures the big picture of what the firm is facing. A strategic issue is long term. It is not something the company can deal with immediately.

Strategic issues are the result of multiple causes in multiples areas of a business and require significant organizational talent and resources to resolve.

Notice here that a strategic issue has multiple causes in multiples areas of a business. This means that strategic issues are complex, with related and overlapping causes. Because of their complex nature, they have significant impact across multiple areas of a company. Their complexity also means that they are not easily or quickly resolved. They require both talent and resources to address, and a company must be committed to solving them.

Addressing a strategic issue moves a firm toward its mission, purpose, and vision and should be congruent with its values.

Everything a firm does needs to be aligned to its mission, purpose, vision, and values.

A strategic issue focuses on the present and specific organizational context, addressing what is happening with this firm, at this time, in this place, and under these circumstances.

There is no one right formula for the structure of a strategic issue. When learning to identify a strategic issue, one good way to write a strategic issue is to begin with “How can [firm's name] ...”

When first learning what a strategic issue is, it is easy to write a strategic issue that is either too narrow or too broad. There are several reasons why a strategic issue may be too narrow. Many business students concentrate on functional areas such as business information technology, accounting, human resources, and entrepreneurship. This functional expertise is a strong asset when beginning a business career, but it can also narrow focus and sometimes lead to strategic issues that are aligned with a particular business function, such as marketing.

Another reason for identifying a strategic issue that is too narrow is the way that business education polishes skills in identifying problems and then immediately identifying solutions. This is an important skill in business. However, in strategic management, problems are identified through analyzing a company using strategic management tools. From those, a strategic issue is identified. Then strategic alternatives offer solutions to the issue. The extra step of identifying a broad concern from the problem is not necessarily unique to strategic management, but it may be a less-polished skill for many business students who have spent their business educations honing their skills in immediately identifying solutions. In strategic management, you analyze a case to identify the problem, then you determine a strategic issue before you move on to recommending solutions in the form of strategic alternatives.

Strategic issues that are too narrow often contain an action. Actions and solutions are identified later in the process as strategic alternatives.

When a strategic issue is too narrow and needs to be amended, a common response can be to then write a strategic issue that is too broad. If a strategic issue applies to all companies, then it is too broad. For example, a strategic issue reading “How can [firm's name] make a profit?” is too broad because that is relevant to all companies, not just the firm that is being analyzed.

If a strategic issue always applies to the company being analyzed, not just right now, then the strategic issue is too broad. For example, if a technology company is being analyzed, then “How can [firm's name] remain an industry leader in technology?” is too broad because this will always be relevant to the company being analyzed.

That is why a robust strategic issue must address what is happening with this firm, at this time, in this place, and under these circumstances, which can help focus a strategic issue that is too narrow or too broad. It focuses on the current context of the company being analyzed.

Companies with strong strategic management talent, processes, resources, and strategic leaders are more likely to be able to continuously address strategy in a dynamic and ongoing way. This positions them to amend their strategy incrementally to remain

industry leaders. Failing to continue to invest in strategic management and leadership can lead to a company losing its position as an industry leader. Even industry leaders face significant challenges from their external and internal environments.

More often, strategic issues arise from shifts in the general environment, the industry environment, and the competitive environment, from organizational crises, or from other circumstances that are either unforeseen or which the company is insufficiently prepared to address. In these cases, failing to address a strategic issue quickly and thoroughly can lead to firm decline or even death.

Video 6.2: Strategic Issues [01:57]

The video for this lesson discusses strategic issues.

Access this YouTube video by scanning the QR code.



Key Takeaways

A firm's strategic issue is the most important, urgent, broad, and long-term matter that the company is facing. Strategic issues are the result of multiple causes in multiple areas of a business and require significant organizational talent and resources to resolve. Addressing a strategic issue moves a firm toward its mission, purpose, and vision and should be congruent with its values. A strategic issue focuses on the present and specific organizational context, addressing what is happening with this firm, at this time, in this place, and under these circumstances.

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6.6 Determine Major Areas of Strategic Concern

Now that it is clear what a strategic issue is and why it is important, it is possible to begin determining a firm's strategic issue. There are multiple ways to do so, and as with the number of strategic issues or the wording of a strategic issue, there is no one right approach. Regardless of the specific approach you use to determine a strategic issue, it is essential that you base your strategic issue on your completed SWOT analysis. A strategic issue must reflect the analysis you have conducted so far of organizational performance and the external and internal environments, which you have now synthesized in your SWOT analysis.

When learning to determine a strategic issue, it can be tempting to rush to define a strategic issue for a firm without using a structured approach. As you work with a case, you may begin to see areas a firm needs to address. Deciding a strategic issue without basing it on robust analysis is not a reliable or sufficient method. Strategic issues must be grounded in the thorough and robust analysis you have conducted so far using strategic management frameworks and your SWOT analysis.

Since students new to strategic management often benefit from having a specific process to follow to determine a strategic issue, we now review one approach to determine a strategic issue. First determine themes in your SWOT analysis. Use these themes to determine a firm's major areas of strategic concern. Then confirm line of sight and congruence between the themes in your SWOT analysis and the major areas of strategic concern.

Determine Themes in Your SWOT Analysis

To determine a firm's major areas of strategic concern, first determine themes in your SWOT analysis. Critically think about each strength, weakness, opportunity, and threat in your SWOT analysis, then identify which ones relate and how they relate.

A few questions to consider include:

Are there themes within the categories?

- In the strengths?
- In the weaknesses?
- In the opportunities?
- In the threats?

Are there themes between the categories?

- Between any two, three, or four of the categories: strengths, weaknesses, opportunities, threats?



Keep working with your SWOT analysis until all strengths, weaknesses, opportunities, and threats are assigned to a theme.

Figure 6.3: Determine themes in your SWOT analysis

Let's use an example to illustrate this process. Imagine that you have determined three themes in your SWOT analysis: competition, innovation, and technology.

Determine Major Areas of Strategic Concern

Next determine **major areas of strategic concern** from the themes you have just identified in your SWOT analysis. Major areas of strategic concern are the most urgent aspects of strategy that a firm needs to address immediately to ensure company success now and in the future.

Ensure each major area of strategic concern is mutually exclusive from the others, making them each distinct.

The number of major areas of strategic concern is determined by the analysis of the company's current situation. Three is a good guideline because most companies are facing at least three major areas of strategic concern, and three major areas of strategic concern are likely the most a firm can effectively attend to at one time.

In our example, the three themes in your SWOT analysis—competition, innovation, and technology—are the major areas of strategic concern.

Finally, confirm the line of sight and congruence between the themes in your SWOT analysis and the major areas of strategic concern.

A few questions to consider include:

- Is there a clear line of sight between the SWOT themes and the major areas of strategic concern?
 - Is it clear how the SWOT themes support the major areas of strategic concern?
- Is there congruence between the SWOT themes and the major areas of strategic concern?
 - Ensure that everything that is included in your SWOT themes is included in the major areas of strategic concern.
 - Ensure that nothing present in your SWOT themes is omitted in the major areas of strategic concern.

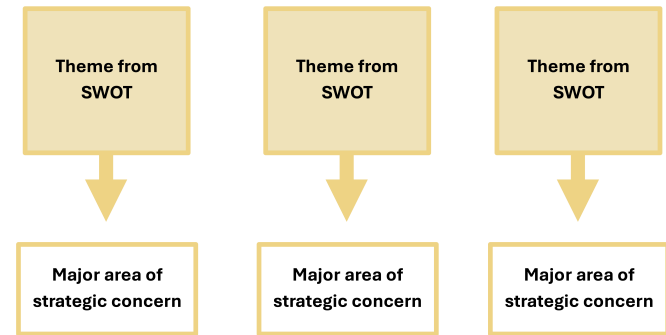


Figure 6.4: Major areas of strategic concern

This is step six in case analysis.

6. Determine major areas of strategic concern.

- a. Identify the major areas of strategic concern from the SWOT analysis and any additional analysis of strategies.
- b. Ensure line of sight and congruence between the SWOT analysis and the major areas of strategic concern.

We move to step 6 of case analysis because step 5 is “as appropriate to the case, analyze strategies: corporate level, business level, innovation, sustainability and ethics, technology, and multinational strategies.” That step addresses information that may be considered when determining a strategic issue but is not central to learning how to determine a strategic issue, so it is omitted here.

Application

- Consider your SWOT analysis that you completed above.
 - Determine themes in your SWOT analysis.
 - Determine three major areas of strategic concern from the themes in your SWOT analysis.
 - Confirm the line of sight and congruence between the themes in your SWOT analysis and the major areas of strategic concern.

Key Takeaways

A strategic issue must reflect the analysis you have conducted so far of organizational performance and the external and internal environments, which you have now synthesized in your SWOT analysis. To determine a strategic issue, determine themes in your SWOT analysis, then identify major areas of strategic concern from the themes you identified in your SWOT analysis. Major areas of strategic concern are significant strategic areas that a firm needs to address immediately to ensure company success now and in the future. Each major area of strategic concern must be mutually exclusive. Aim for about three major areas of strategic concern. Lastly, confirm line of sight and congruence between the themes in your SWOT analysis and the major areas of strategic concern.

6.7 Determine a Strategic Issue

Now that you have determined three major areas of strategic concern, it is possible to continue with the process of identifying a firm's strategic issue. First, rank the major areas of strategic concern, placing them in descending order of importance to the firm. Then identify the relationships between the major areas of strategic concern, and write phrases that capture these relationships. Place the phrases between the major areas of strategic concern. This is your draft strategic issue.

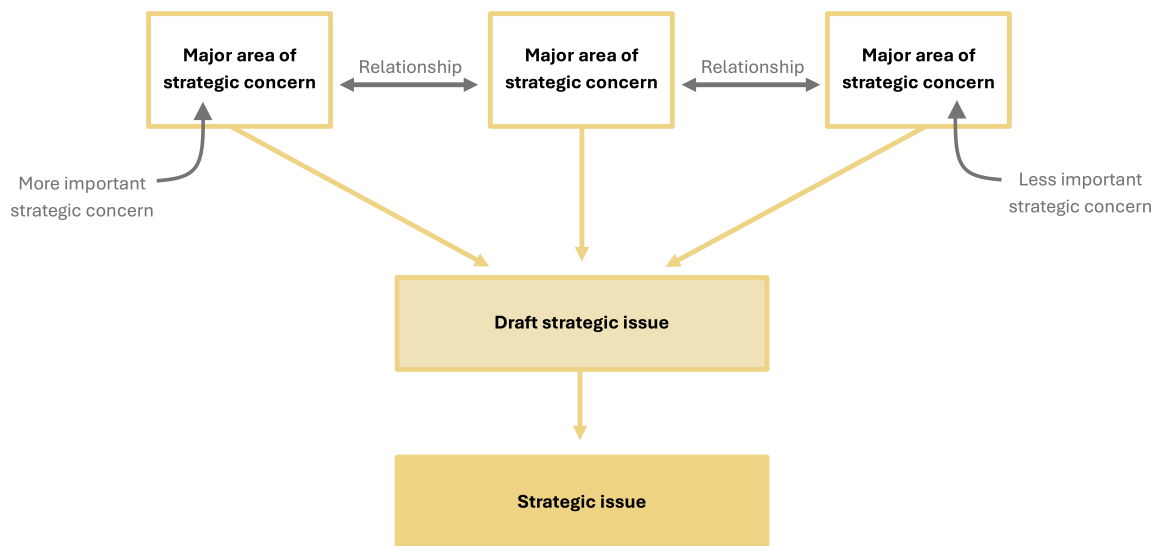


Figure 6.5: Identify a strategic issue

Confirm line of sight and congruence between the major areas of strategic concern and the draft of the strategic issue.

A few questions to consider include:

- Is there a clear line of sight between the major areas of strategic concern and the draft strategic issue?
 - Is there a clear logic between the major areas of strategic concern and the draft?
- Is there congruence between the major areas of strategic concern and the draft strategic issue?
 - Ensure that everything that is included in your major areas of strategic concern is included in the draft.
 - Ensure that nothing present in your major areas of strategic concern is omitted in the draft strategic issue.

Review the draft of the strategic issue from a macro, big-picture orientation that considers the entire situation facing the firm. Stand back and critically think about your draft strategic issue from a holistic perspective and finalize it based on your in-depth knowledge of the case.

This is step seven in case analysis.

7. Determine strategic issue.

- a. Determine the strategic issue from the major areas of strategic concern.
- b. Ensure line of sight and congruence between the major areas of strategic concern and the strategic issue.

In our example, you determined that competition, innovation, and technology are the major areas of strategic concern. Let's say you rank these in order of importance to the case as follows: innovation, technology, and competition.

Now you determine the relationship between the major areas of concern: firm needs to innovate so that it can address technology and deal with competition. This is your draft strategic issue.

Now stand back and critically think about your draft strategic issue from a holistic perspective and finalize it based on your in-depth knowledge of the case. Your final strategic issue may be "How can [company] continue to innovate so that it can successfully capitalize on rapidly changing technology in an increasingly competitive market?" In choosing this focus, you have moved from a draft strategic issue to a more refined and final strategic issue.

You arrived at this final strategic issue through your in-depth knowledge of the case. You know that the company is a leader in innovation, so you frame innovation as something they are going to continue to do.

You also know that, although they are a leader in innovating to use existing and especially new technology, developing new technology is not aligned to their mission and vision. Therefore, you frame your final strategic issue as capitalizing on rapidly changing technology. You know they want to use the latest technology but not develop it.

Finally, you know that, while their market position has been historically strong, they have had some very recent challenges to their market position from some new companies in the market. You frame the final strategic issue as competing in an increasingly competitive market.

Application

- Consider your major areas of strategic concern that you determined above.
 - Rank the major areas of strategic concern, placing them in descending order of importance to the firm.
 - Identify the relationships between the major areas of strategic concern, and write phrases that capture these relationships.
 - Place the phrases between the major areas of strategic concern. This is your draft strategic issue.
 - Confirm line of sight and congruence between the major areas of strategic concern and the draft strategic issue.
 - Determine your final strategic issue.

- Explain how your strategic issue meets each key aspect in the definition of a strategic issue:
 - The most important, urgent, broad, and long-term matter that the company is facing. Strategic issues are the result of multiple causes in multiples areas of a business and require significant organizational talent and resources to resolve. Addressing a strategic issue moves a firm toward its mission, purpose, and vision and should be congruent with its values. A strategic issue focuses on the present and specific organizational context, addressing what is happening with this firm, at this time, in this place, and under these circumstances.

Key Takeaways

To identify a firm's strategic issue from the major areas of strategic concern, rank the major areas of strategic concern, placing them in descending order of importance to the firm. Identify the relationships between the major areas of strategic concern, and write phrases that capture these relationships, placing the phrases between the major areas of strategic concern. This arrangement is your draft strategic issue. Confirm line of sight and congruence between the major areas of strategic concern and the draft strategic issue. Review the draft from a macro orientation that considers the entire situation facing the firm. Critically think about your draft strategic issue from a holistic perspective, and finalize it based on your in-depth knowledge of the case.

6.8 Determine Strategic Alternatives

Once you have determined a strategic issue, the next step in case analysis is to identify strategic alternatives that address the issue. A strategic alternative is an action that addresses and has the potential to resolve every aspect of a strategic issue.

All strategic alternatives resolve the same strategic issue, just in different ways. Strategic alternatives address root causes; they do not address or mask symptoms. Strategic alternatives are forward-looking. They do not fix yesterday's problems. Strategic alternatives are realistic in both practical and ethical senses. They are economically viable. It is important that strategic alternatives are well developed and explained so they can be implemented by the firm.

Identify at least three strategic alternatives that address all areas in the strategic issue. Then confirm line of sight and congruence between the strategic issue and the strategic alternatives.

A few questions to consider include:

- Is there a clear line of sight between the strategic issue and the strategic alternatives?
 - Is there a clear logic between the strategic issue and the strategic alternatives?
- Is there congruence between the strategic issue and the strategic alternatives?
 - Ensure that everything that is included in the strategic issue is addressed by each strategic alternative.
 - Ensure that nothing present in the strategic issue is omitted by each strategic alternative.

Most often, complete and immediate resolution of the strategic issue may not be realistic. Because strategic issues are complex and the result of multiple causes, strategic alternatives may begin by mitigating the circumstances causing the strategic issue or by aiming to improve the situation if a full resolution is not immediately possible.

In our example, you determined the firm's strategic issue to be "How can [company] continue to innovate so that it can successfully capitalize on rapidly changing technology in an increasingly competitive market?" Next determine three strategic alternatives that address the strategic issue. This requires critical thinking and judgment and a thorough knowledge of the case.

One strategic alternative may be "partner with [technology company]." From your knowledge of the case, you know which company the firm is likely to consider. You also know that the firm you are analyzing is not in direct competition with the technology company, so a partnership may be a viable option to explore. It could be mutually advantageous for both companies. Perhaps you also know that the firm engages in a variety of cooperative relationships with other firms, so their culture would support such an alternative.

Another strategic alternative may be "invest heavily in talent acquisition and succession planning specifically aimed at innovation leaders." You know from your knowledge of the case that the founders of the company remain their corporate leaders and are instrumental in setting the culture of innovation in the firm. However, while this hands-on approach was a key to their early success, the firm's age and maturity and changing market conditions mean it is time to ensure the company's early success can continue into the future.

A third strategic alternative may be "backwardly integrate into their value chain and acquire [technology company]." You know that one of their current suppliers is a small technology company that may be inclined to consider this option. This would require the firm to change their mission and vision to align with becoming a producer of the technology rather than just a consumer of it.

This is step eight in the case analysis process.

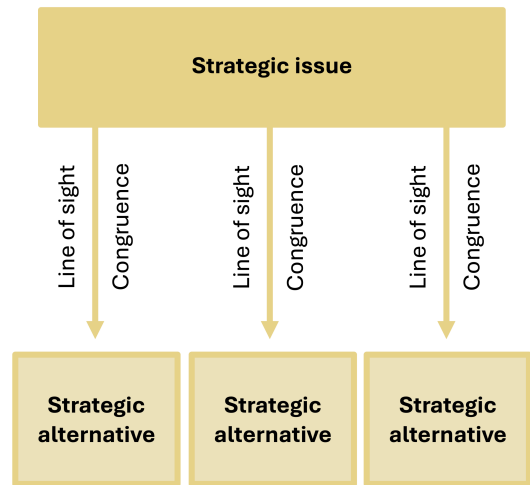


Figure 6.6: Strategic alternatives

8. Determine strategic alternatives.

- a. Determine the strategic issue from the major areas of strategic concern.
- b. Ensure line of sight and congruence between the major areas of strategic concern and the strategic issue.

Application

- Consider your strategic issue that you determined above.
 - Identify three strategic alternatives that address all areas in the strategic issue. Explain how each strategic alternative addresses all areas in the strategic issue.
 - Confirm line of sight and congruence between the strategic issue and the strategic alternatives.

Key Takeaways

A strategic alternative is an action that addresses and has the potential to resolve every aspect of a strategic issue. All strategic alternatives resolve the same strategic issue, just in different ways. Strategic alternatives address root causes, are forward-looking, are realistic practically and ethically, are economically viable, and can be implemented by the firm. Aim for about three strategic alternatives.

6.9 Evaluate Strategic Alternatives

Once you have determined three strategic alternatives, you need to recommend one. If you are conducting an abbreviated case analysis, you likely will not evaluate your three strategic alternatives.

If you evaluate the strategic alternatives, first identify the criteria you plan to use to evaluate the strategic alternatives. The criteria may vary depending on the specifics of the company being analyzed and may include, but are not limited to, the degree to which the strategic alternative resolves the strategic issue. Sometimes complete and immediate resolution of the strategic issue may not be realistic.

Another criterion to consider when evaluating strategic alternatives is whether they are consistent with the firm's mission, purpose, vision, and values. Consider whether the strategic alternatives are consistent with the external and internal environments of the firm. Strategic alternatives should also be consistent with existing or needed firm resources, capabilities, and core competencies, and they should create a competitive advantage for the firm. Another criterion to consider is whether the strategic alternatives add value to the firm overall.

Whether strategic alternatives are financially realistic for the firm and how they impact a firm's profitability also are important. Ask whether the strategic alternatives are realistic given the economic resources of the firm, as recommending a strategic alternative that a firm cannot fund is not helpful. Consider whether the strategic alternatives enable the firm to earn a profit by asking if they add value and increase price or if they add value without increasing costs. In addition, you must consider whether the strategic alternatives improve profitability.

Use the table below to evaluate the strategic alternatives against the criteria you choose. Delete criteria that you do not use, and add criterion that you use that do not appear in the table. Include a robust description of whether and in what ways each strategic alternative meets each criterion.

Criteria	Strategic alternative 1	Strategic alternative 2	Strategic alternative 3
1. Resolves the strategic issue			
2. Is congruent with the firm's mission, purpose, vision, and values			
3. Is consistent with the external environment			
4. Is consistent with the internal environment			
5. Is consistent with the existing or needed firm resources, capabilities, and core competencies			
6. Creates a competitive advantage for the firm			
7. Adds value			
8. Is realistic given available funding			
9. Enables the firm to earn profit. (A) Adds value and increases price (B) Adds value without increasing cost			
10. Improves profitability			

Figure 6.7: Evaluate strategic alternatives

The last task for the strategic alternatives is to explain how each alternative meets the evaluation criteria. Give a full and clear explanation.

This is step nine in the case analysis process.

9. Evaluate strategic alternatives.

- a. Determine criteria to evaluate the strategic alternatives.
- b. Use criteria to evaluate the strategic alternatives.
- c. Clearly indicate how the strategic alternatives meet the evaluation criteria.

Application

- Consider your strategic alternatives that you determined above.
 - Use figure 6.7 to identify criteria to evaluate the strategic alternatives.
 - Explain how each strategic alternative meets the evaluation criteria.

Key Takeaways

Once you have determined three strategic alternatives, you need to recommend one, which is achieved by evaluating the alternatives (unless you are conducting an abbreviated case analysis). If you evaluate the strategic alternatives, identify the criteria you plan to use to evaluate them. The criteria may vary depending on the specifics of the company being analyzed. Use the criteria to evaluate each alternative, explaining how each strategic alternative meets the evaluation criteria.

6.10 Recommend a Strategic Alternative

Once you have determined three strategic alternatives, you now recommend one. If you conduct an abbreviated case analysis, you may not have used criteria to evaluate your strategic alternatives. In this case, use critical thinking to recommend the best strategic alternative. You may still explain why you chose the strategic alternative that you did. If you use criteria to evaluate your strategic alternatives, explain how the strategic alternative you recommend best meets the criteria used.

This is step ten in the case analysis process.

10. Recommend strategic alternative.

- a. Recommend one strategic alternative using the evaluation criteria.

Application

- Consider how each strategic alternative meets the evaluation criteria you used above.
- Recommend a strategic alternative that best meets the criteria you use.
- Explain how the strategic alternative you recommend best meets the criteria you use.

Key Takeaways

Once you have determined three strategic alternatives, you now recommend one either using critical thinking or criteria you identify.

6.11 Design an Implementation Plan

Now that you have recommended one strategic alternative, you may design an implementation plan to execute the recommended strategic alternative. As with the criteria to evaluate the strategic alternatives, implementation plans may vary depending on the specifics of the company being analyzed.

Implementation plans may include assumptions regarding implementation of the strategic alternative, such as changes in demand, price, and costs that factor in competitor reactions, customers' willingness to pay a higher price, and realistic cost projections.

Implementation plans outline an implementation timeline that may include stages of the implementation plan, duration of each stage of the implementation plan, activities in each implementation stage, duration of activities in each implementation stage, and who is responsible for each activity.

New resources required will likely be addressed by an implementation plan. These include financial resources, such as available cash, stocks, and loans. The human resources of time and talent are also important. Other resources to consider are whether the firm has sufficient facilities and appropriate technology.

When designing an implementation plan, it is helpful to consider whether new or revised value chain activities are needed. Likewise, ask if new resources, capabilities, or core competencies are required. Consider whether changes are needed in organization structure or firm infrastructure, such as new positions and restructuring. Changes in organizational systems, such as incentive programs that will support the success of changes, may be helpful.

Use the table below to design the implementation plan against the criteria you choose. Delete criteria that you do not use, and add criteria that you use that do not appear in the table. Place a robust description of whether and in what ways the strategic alternative you recommend to be implemented meets each criterion.

This is step eleven in the case analysis process.

11. Design implementation plan.

- a. Design an implementation plan for the recommended strategic alternative.

Criteria	Recommended strategic alternative
1. Assumptions regarding implementation of the strategic alternative (a) Changes in demand (b) Price and costs that factor in competitor reactions (c) Customers' willingness to pay a higher price (d) Realistic cost projections	
2. An implementation timeline (a) Stages of the implementation plan (b) Duration of activities in each implementation plan (c) Activities in each implementation plan (d) Duration of activities in each implementation plan (e) Who is responsible for each activity	

Criteria	Recommended strategic alternative
3. New resources required (a) Financial (available cash, stocks, loans) (b) Human (c) Facilities (d) Technology	
4. New or revised value chain activities	
5. New resources, capabilities, or competencies required	
6. Changes needed in organization structure	
7. Changes needed in firm infrastructure (a) New position needed (b) Restructuring	

Figure 6.8: Design an implementation plan

Application

- Consider the strategic alternative you recommended above.
 - Use figure 6.8 and design an implementation plan.

Key Takeaways

Now that you have recommended one strategic alternative, you may design an implementation plan to execute the recommended strategic alternative. As with the criteria to evaluate the strategic alternatives, implementation plans may vary depending on the specifics of the company being analyzed.

6.12 Confirm Line of Sight and Congruence across the Entire Case Analysis

Line of sight and congruence are important throughout the case analysis process. Up to now, you have considered line of sight and congruence within a strategic management tool, among strategic management frameworks, and between steps in the case analysis process. It is now time to assess line of sight and congruence across the entire case analysis. Review the entire strategic analysis, ensure there is direct and clear logic connecting all elements in the strategic analysis, and confirm there is a one-to-one relationship between two or more things.

This is step twelve in the case analysis process.

12. Confirm line of sight and congruence across the entire case analysis.**Application**

- Review the entire strategic analysis you have conducted on one of your favorite companies.
- Confirm there is line of sight and congruence across your entire analysis.

Key Takeaways

As a final check, assess line of sight and congruence across the entire case analysis.

6.13 Write and/or Present the Case Analysis

Now that you have conducted a case analysis, you will likely write it as an assignment and/or present it. A case analysis is not a data dump of every point of information produced. It is a presentation of a coherent and logical narrative.

This is step thirteen in the case analysis process.

13. Write and/or present case analysis.**Application**

- Review the entire strategic analysis you have conducted on one of your favorite companies.
- Determine a coherent and logical narrative to present your analysis.
- Discuss how you can avoid your case analysis being a data dump of every point of information you produced.

Key Takeaways

When you have completed your analysis, write it as an assignment and/or present it.

6.14 Conclusion

In strategic management, a SWOT framework is used to synthesize the analysis you have conducted so far. When you synthesize the analysis using a SWOT framework, this is referred to as a SWOT analysis. In strategic management, a SWOT framework is never used as a standalone tool. It is used only after you have completed your analysis of a company to synthesize that analysis. In strategic management, once you have completed your SWOT analysis, you use your completed SWOT analysis to determine the firm's strategic issue.

A firm's strategic issue is the most important, broad, long-term, and urgent matter that the company is facing. Strategic issues are the result of multiple causes in multiples areas of a business. They require significant organizational talent and resources to resolve. Addressing a strategic issue moves a firm toward its mission and vision while supporting its values. A strategic issue addresses what is happening with this firm, at this time, in this place, and under these circumstances. It is focused on the present and specific context.

To determine a strategic issue, determine themes in your SWOT analysis, determine major areas of strategic concern, write a draft strategic issue, and finalize it based on your knowledge of the case. Determine strategic alternatives, which are actions that address and have the potential to resolve every aspect of a strategic issue. Evaluate and recommend a strategic alternative, develop an implementation plan to implement your recommended strategic alternative, and present your case analysis.

Demonstrate Your Knowledge, Skills, and Competence

Use these questions to test your knowledge of the chapter:

1. Describe a SWOT framework and how it is utilized in strategic management. Explain why you place your external analysis on the bottom of the grid and your internal analysis on the top of the grid. Discuss why a SWOT analysis is never used as a standalone tool in strategic management.
2. Unpack the definition of a strategic issue to be sure you understand all its critical elements.
3. Describe how you determine the major areas of strategic concern for a firm.
4. Describe how to use major areas of strategic concern to identify a company's strategic issue.
5. Describe the criteria you may use to evaluate a firm's strategic alternatives and how you would use these to recommend a strategic alternative.
6. Describe the criteria you may use to design an implementation plan.
7. Describe what confirming line of sight and congruence across the entire case analysis involves and why this is essential to a robust case analysis.

By answering these questions, you have demonstrated your thorough knowledge of how to synthesize your analysis and determine a firm's strategic issue. This is essential to robust case analysis. Well done!

Figure Descriptions

[Figure 6.2](#): Internal analyses for strengths and weaknesses include organizational performance, VRIO, and VCA. Strengths: strong resources, strong capabilities, strong core competencies, competitive advantages, and primary and secondary activities. Weaknesses: missing/weak resources, missing/weak capabilities, missing/weak core competencies, competitive disadvantages, primary and secondary activities, and weaknesses in the general, industry, and competitive environments. External analyses for opportunities and threats include organizational performance, PESTEL, P5, and strategic mapping. Opportunities: opportunities in the general, industry, and competitive environments, and industry opportunities. Threats: threats in the general environment and industry threats. This graphic is yellow.

[Figure 6.3](#): Four separate yellow boxes representing strengths (S1, S2, and S3), weaknesses (W1, W2, and W3), opportunities (O1, O2, and O3), and threats (T1, T2, and T3).

[Figure 6.5](#): Three major areas of strategic concern (most important to least important), each have a relationship with each other. These three areas point to “Draft strategic issue”, which then points to “Strategic issue.” This graphic is yellow.

[Figure 6.6](#): Strategic issue points to three separate strategic alternatives, each of the three arrows represents line-of-sight and congruence. This graphic is yellow.

Figure References

Figure 6.1: SWOT framework. Kindred Grey. 2025. CC BY.

Figure 6.2: Synthesize analysis using a SWOT framework. Kindred Grey. 2025. CC BY.

Figure 6.3: Determine themes in your SWOT analysis. Kindred Grey. 2025. CC BY.

Figure 6.4: Major areas of strategic concern. Kindred Grey. 2025. CC BY.

Figure 6.5: Identify a strategic issue. Kindred Grey. 2025. CC BY.

Figure 6.6: Strategic alternatives. Kindred Grey. 2025. CC BY.

PART IV: FORMULATE CORPORATE- AND BUSINESS-LEVEL STRATEGY

In Part I, you learned about strategic management and how to conduct a case analysis. You analyzed a company's overall organizational performance and its external and internal environments in Part II. Then in Part III, you learned how to synthesize the analysis you conducted so far using a SWOT analysis, enabling you to determine a firm's strategic issue and strategic alternatives. This completed the strategic analysis focus of the AFI framework.

We begin our exploration of strategy formulation in Part IV by considering corporate-level strategy and business-level strategy. Then in Part V, you learn four strategies that are embedded in business-level strategy: innovation strategy, sustainability and ethics strategy, technology strategy, and multinational strategy.

7. FORMULATE CORPORATE-LEVEL STRATEGY

Learning Objectives

After you have engaged with the concepts in this chapter, you will understand and be able to apply the following key strategic management concepts.

1. Corporate-level strategy
2. Synergy and its role in corporate-level strategy
3. Related and unrelated diversification as a means of addressing corporate-level strategy
4. The relationship between diversification and financial performance
5. Ways a company diversifies, including internal development, strategic alliances, joint ventures, and mergers and acquisitions
6. Ways a firm reverses diversification, including retrenchment and divestment
7. What an industry value chain is and its application to corporate-level strategy
8. Vertical integration as a means of addressing corporate-level strategy
9. Geographical scope as a means of addressing corporate-level strategy
10. Portfolio planning
11. How to analyze a firm's corporate-level strategy
12. Why corporate-level strategy is important to business-level graduates

You will be equipped to analyze a firm's corporate-level strategy.

7.1 Introduction

You have now completed your strategic analysis. You analyzed a company's overall organizational performance and its external and internal environments. You synthesized the analysis using a SWOT analysis and determined the firm's strategic issue and strategic alternatives.

This chapter focuses on how firms use strategic analysis to formulate strategy. You learn strategy formulation beginning at the broadest level of a firm—the corporate level. Then in the next chapter, you learn about business-level strategy, which is the strategy all firms formulate at the **strategic business unit** level. In Part V, you learn about four strategies that are embedded in business-level strategy: innovation strategy, sustainability and ethics strategy, technology strategy, and multinational strategy.

Firms use strategic analysis to formulate strategy. When you conduct a case analysis, you analyze the strategies companies have formulated for their effectiveness and congruence with the firm's mission, purpose, vision, and values as well as their other strategies.

In this chapter, you learn about corporate-level strategy, synergy, and the role synergy plays in corporate-level strategy. Next you learn how diversification, including related and unrelated diversification, is used by firm executives to address corporate-level strategy. Then you learn how company leaders use vertical integration, including forward vertical integration and backward vertical integration, to address a firm's corporate-level strategy. You also learn how geographical scope is used to address a company's cor-

porate-level strategy. Additionally, you learn about portfolio planning and the BCG matrix, a model for assessing a firm's portfolio. Finally, you learn how corporate-level strategy is relevant to new business graduates.

7.2 Corporate-Level Strategy

Let's begin by explaining corporate-level strategy.

Where Are We Going?

Recall that there are three stages to the strategic management process—strategic analysis, strategy formulation, and strategy implementation—and each stage aligns with a foundational question of strategic management. You have now completed your strategic analysis, which addresses the question “Where are we?” Strategy formulation begins to answer “Where are we going?” Lastly, strategy implementation addresses “How are we going to get there?” Corporate-level strategy is the first strategy you learn, and like all strategy formulation, it addresses the question of where a firm is going.

C-Suite and Board of Directors

There are three levels of strategy in an organization: corporate-level, business-level, and functional-level. Strategy is formulated at all three levels. Corporate-level strategy is the broadest level of strategy. The corporate level of a company consists of the C-suite, and if the company is large enough, it includes the board of directors.

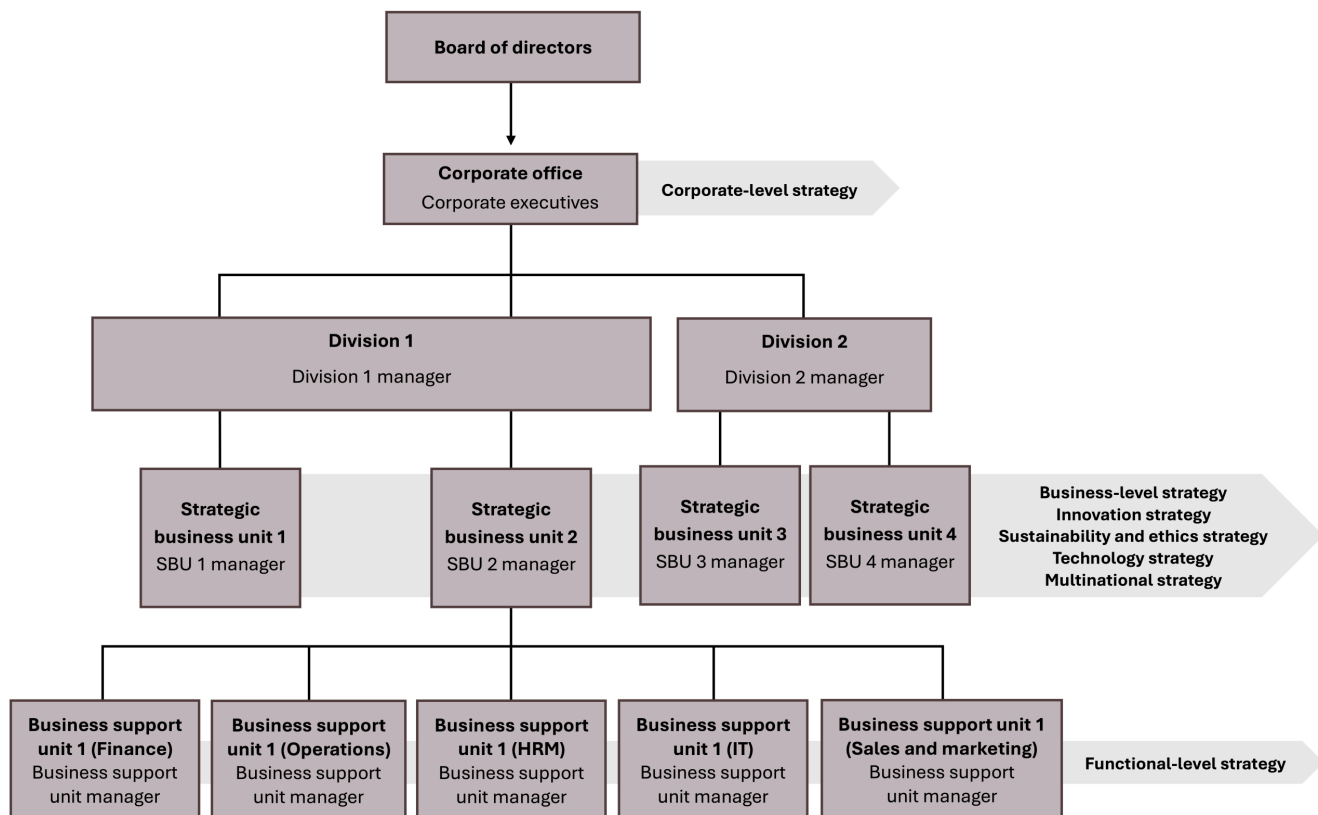


Figure 7.1: Three levels of strategy

Strategy can be described as a firm's answer to three critical strategic questions that every organization needs to answer. "Where to play?" is answered at the corporate level with corporate-level strategy. "How to win?" is addressed in strategic business units by business-level strategy, and the third question, "Have we earned a right to win?", is addressed by strategies that are embedded in business-level strategy, such as innovation strategy, sustainability and ethics strategy, technology strategy, and multinational strategy.

Where to Play?

"Where to play?" investigates where the firm is going to compete, considering which industries, markets, market segments, businesses, and regions in which the firm wants to operate (or play). This is largely determined by the firm's assessment of the attractiveness and profit potential of alternative markets, market segments, and businesses and the synergies between them. The answers to the question of where to play also provide important solutions to issues related to the allocation of limited company resources to different businesses. In this sense, it is also important for every organization to decide where *not* to play. Overall, "where to play" strategy can be described as the firm's search for markets and market segments that are attractive today and in the future.

Therefore, formulating corporate-level strategy focuses on where a firm is going—its direction for the future. Corporate-level strategy is the broadest level of strategy and is the responsibility of senior executives and the board of directors. Corporate-level strategy further answers the question where a company is going to "play": where it is going to compete.

Volatile, Uncertain, Complex, and Ambiguous (VUCA) Environment

When executives analyze their organizational environments, they consider factors that relate to both the external environment and the internal environment of the firm. The external analysis focuses on an outside-in perspective of the firm. The internal analysis focuses on an inside-out perspective of the firm. You analyze companies through these same lenses when you conduct a case analysis.

When strategic management leaders and managers formulate strategy, they focus on an outside-in perspective. All successful strategies are driven by outside-in perspectives, including corporate-level and business-level strategy as well as the strategies embedded in business-level strategies, such as innovation, sustainability and ethics, technology, and multinational strategies.

This means that companies need to carefully monitor their external environment, analyzing trends and developing strategies that are forward-looking. Firms must navigate an external environment that is volatile, uncertain, complex, and ambiguous (VUCA), where change and disruption have become the new normal.

Volatility refers to rapid and unpredictable changes in the environment and can include many things, such as sudden shifts in consumer demand, disruptive technology like the rise of AI, and fluctuating stock prices. Uncertainty means lack of clear information and predictability and may include things such as the effects of climate change and unanticipated competitor moves like the launch of a new product or service. Complexity occurs when there are many interrelated factors and one area changes, causing long-ranging ripple effects; this makes it challenging to fully understand and manage the possible ramifications of proposed actions. The global supply chain responding to tariffs is an excellent example of complexity. Finally, ambiguity means there are multiple correct answers with various tradeoffs, making decision-making a challenge; it can also mean there are multiple interpretations to the same situation, making finding a correct answer challenging. Companies that conduct business globally face significant ambiguity, including customer reactions to foreign products and the impact of foreign regulations.

A VUCA environment is characterized by all these factors intertwined, further complicating strategic analysis, strategy formulation, and strategy implementation. As you know, strategic management is a structured process to analyze, evaluate, and interpret information to support evidenced-based decisions. The data-driven decisions of strategic management all occur in a VUCA environment.

Synergy

Corporate-level strategy seeks ways to generate synergy. Synergy means that the whole is greater or better than the sum of its parts. In business, **synergy** occurs when two or more strategic business units or businesses perform more effectively together than they do independently. To review, a strategic business unit is a fully functional unit of a business that has its own vision and direction and may be part of a larger organizational unit like a division. It may be based on markets served, products offered, or regions served. Smaller firms may have only one strategic business unit, and large corporations may have multiple. Firms gain synergy in various ways, such as by sharing administrative overhead expenses like accounting, human resources, and sales and marketing when two business units are combined. This is an opportunity to capture operational efficiency.

Focus

Corporate-level strategy is a companywide strategy that focuses on creating and maintaining a firm's competitive advantage by creating synergy within and between multiple **industries, markets, market segments**, and businesses, across multiple industry value chain(s), and in different geographical locations. The industry value chain concept is reviewed in [section 7.4](#).

Therefore, corporate-level strategy focuses on these questions:

1. In what industries, markets, market segments, and businesses should a firm operate? This is a question of diversification.
2. In what stage of the industry value chain(s) should the company participate? This is a question of vertical integration.
3. Where should the organization compete geographically? This is a question of geographical scope.

Application

- Firms operate in a VUCA environment, and so do individuals.
 - Think about your job search.
 - Identify and discuss how you will face a volatile, uncertain, complex, and ambiguous environment when you try to secure a position after graduation.

Key Takeaways

Like all strategy formulation, corporate-level strategy addresses the broad question of where a firm is going. Corporate-level strategy is the broadest level of strategy and is the responsibility of senior executives and the board of directors. Corporate-level strategy further answers the question where a company is going to compete. Corporate-level strategy is a companywide strategy that focuses on creating and maintaining a firm's competitive advantage by creating synergy within and between multiple industries, markets, market segments, and businesses, across multiple industry value chain(s), and in different geographical locations. Diversification refers to the question of what industries, markets, market segments, and businesses firms should operate in. Vertical integration considers the stage of the industry value chain(s) at which the company should participate. Geographical scope refers to the question of where an organization should compete in the world.

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7.3 Diversification

In what industries, markets, market segments, and businesses a firm should operate is a question of diversification.

Let's first clarify the distinction between differentiation and diversification.

Differentiation

Differentiation is how a company makes its products distinct from its competitors. Apple makes a Mac distinct from a PC and an iPhone different from a Galaxy phone.

Diversification

Diversification refers to how a company simultaneously deals with different products and services in different industries, markets, market segments, and businesses. After the firm decides which industries, markets, market segments, and businesses it wants to operate in, it then decides which products and services it is going to offer.

For example, Apple's range of products—desktop computers, laptops, iPhones, iPads, and watches—represent product diversification. Another example of product diversification is L'Oréal. L'Oréal initially focused on hair products and diversified its product lines to include skincare and cosmetics.

It is diversification, not differentiation, that is the focus of corporate-level strategy. There is a strong business case for diversification. Diversification helps with the firm's risk management because the firm doesn't “put all of its eggs in one



Figure 7.2: L'Oréal

basket.” Through diversification, a company spreads its risk by participating in different industries, markets, market segments, and businesses. Beyond risk management, diversification allows the firm to leverage its resources, capabilities, and core competencies into different industries, which drives growth for the firm.

There are multiple types of diversification to consider. You will likely consider diversification from multiple points of view throughout your business education. As it relates to corporate-level strategy, we focus on two types of diversification: related diversification and unrelated diversification. One important subcategory is geographic diversification. In corporate-level strategy, geographical diversification is covered in questions of geographical scope.

To understand related and unrelated diversification, it is helpful to understand single business firms and dominant business firms first.

Single Business Firm

A **single business firm** is a firm that derives 95 percent or more of its revenues from one business.

Dominant Business Firm

A **dominant business firm** derives between 70 percent and 95 percent of its revenues from one business.

Related Diversification

Related diversification refers to expanding into new and similar markets, market segments, and businesses in a new industry that has similarities to a firm's current industry or industries. In contrast to a single business firm or a dominant business firm, a company that engages in a related diversification strategy receives less than 70 percent of its revenues from a single business and the remaining revenue from a business or businesses that are related to the primary business. Related diversification also encourages and supports synergies.

For example, Unilever was originally a soap manufacturer but engaged in related diversification by expanding its product line to include personal care such as skincare like Vaseline lotion and Axe deodorant.

Unrelated Diversification

Unrelated diversification refers to expanding into new markets, market segments, and businesses in a new industry that has little or no similarities to a firm's current industry or industries. In contrast to a single business firm or a dominant business firm, a company that engages in an unrelated diversification strategy receives less than 70 percent of its revenues from a single business and the remaining revenue from a business or businesses that are unrelated to the primary business. Unrelated diversification has positive impacts on the firm's risk management because it expands into new markets, market segments, and businesses. On the other hand, this approach does not involve synergies, one of the main drivers of corporate strategy.

For example, Unilever also engaged in unrelated diversification by expanding into food products such as Hellmann's mayonnaise and Magnum ice cream.

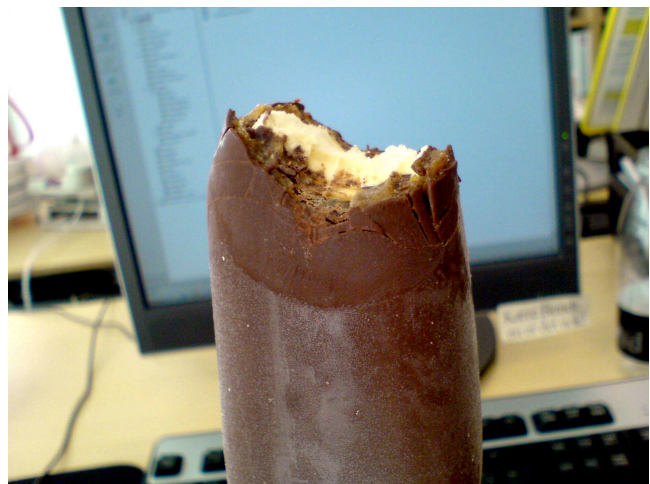


Figure 7.3: Magnum ice cream bar

Amazon started as an online bookstore before expanding into different sectors, such as streaming services (Prime Video) and grocery stores (Whole Foods). Google initially started as a search engine and then diversified its services to include Google Drive, where users can store files, photos, and more. Additionally, Google expanded into advertising with Google Ads. Sony initially focused on electronics but has expanded its products line to movies and music production.

In contrast to single and dominant business firms, firms that engages in both related and unrelated diversification strategy receives less than 70 percent of their revenues from a single business. Both related and unrelated diversification require significant resources to execute. Related diversification is considered less risky and often produces greater profit potential. This is because the company already has expertise with the industry that it can apply to the new products and services. However, there are times when expanding into a new industry taps into significant profits.

Diversification and Financial Performance

When considering whether to enter new businesses in new industries, consider how attractive the new industry is. New business in new industries must have strong profit potential to make the risk worth taking.



Figure 7.4: Google

In choosing between related or unrelated diversification, it is useful to analyze the external environment of the firm. As you learned in [Chapter 4](#), a PESTEL analysis gives an analysis of the general environment and a Porter's Five Forces analysis provides an analysis of the industry environment. You also analyzed strategic groups as a way of analyzing the competitive environment. Together, these analyses support an evidenced-based decision about related or unrelated diversification.

Is unrelated diversification better or worse than related diversification? While this needs to be answered on a company-specific basis, there is a sweet spot between both forms of diversification that leads to the highest financial performance.

The graph in figure 7.5 suggests that there is an optimal degree of diversification, and in most cases, related diversification is associated with the strongest firm performance. High and low levels of diversification are generally associated with lower overall performance, while moderate levels of diversification are associated with higher firm performance. This implies that companies that focus on a single business, as well as companies that pursue unrelated diversification, often fail to achieve additional value creation. Firms that compete in single markets could potentially benefit from economies of scope by leveraging their core competencies into adjacent markets.

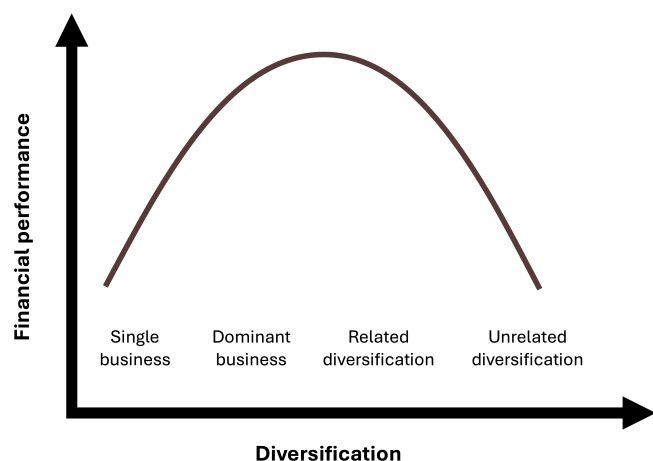


Figure 7.5: Diversification and financial performance

Ways Firms Diversify

Now that we have reviewed related and unrelated diversification and the impact of diversification on financial performance, let's consider ways to diversify. To explore ways that firms choose to diversify, we introduce a make-contract-create-acquire continuum, illustrated in figure 7.6.

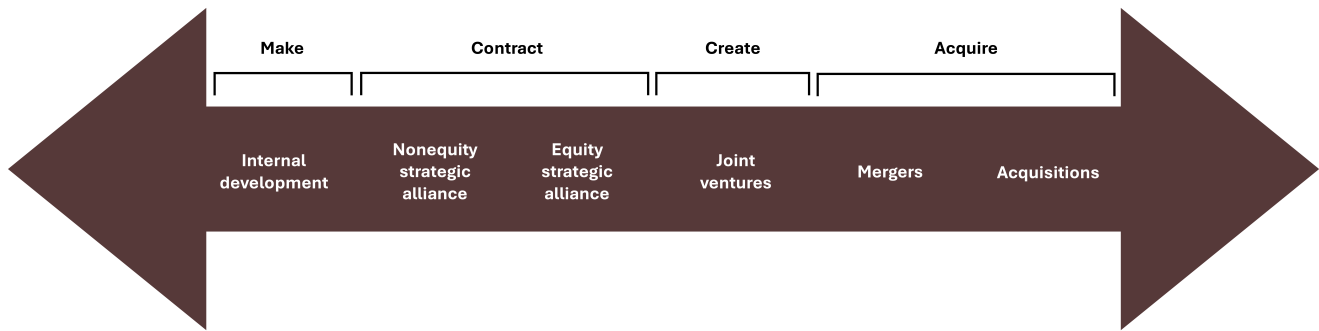


Figure 7.6: How to diversify

Companies may diversify by using internal development to make their own products or to design new services. They also may enter into contracts with other companies to achieve diversification. This includes nonequity and equity alliances. Firms can diversify by creating a new company through a joint venture. Finally, companies may acquire additional companies as a means of diversification through mergers and acquisitions.

Make: Internal Development

When considering different ways to diversify, organizations may use **internal development** to make their own new products or design new services by leveraging their existing resources and expertise.

Apple is an example of a company that often uses internal development to diversify its products and services.

Companies can also develop and launch whole new business lines through internal development. For example, Microsoft expanded from mostly software development to offering full tech solutions by diversifying its offerings through internal development, producing products like Microsoft Teams for collaboration and Azure for cloud services.



Figure 7.7: Apple



Figure 7.8: Microsoft

Contract: Strategic Alliances

Strategic alliances are mutually beneficial contractual relationships between two organizations, allowing them to work together on specific goals while maintaining their independence. Strategic alliances are an example of horizontal integration. Nonequity and equity strategic alliances are both means of diversification.

Equity Strategic Alliance

An **equity strategic alliance** is created when one company contracts with another company to purchase a certain equity percentage of the other company.



Figure 7.9: Panasonic's President, Naoto Noguchi, and Tesla's Chief Technology Officer, JB Straubel

For example, in 2010, Panasonic invested \$30 million in the automaker Tesla by purchasing shares of Tesla common stock in a **private placement**, which is a sale of stock to preselected investors rather than on a public exchange. The purpose of this equity strategic alliance was to build a stronger relationship between Panasonic and Tesla. Panasonic was able to expand its footprint in the electric vehicle market. Tesla was able to improve its battery packs and reduce its costs through Panasonic's market position as one of the world's leading battery cell manufacturers. The relationship between the two companies continues to this day.

Figure 7.9 depicts Panasonic Energy Company President Naoto Noguchi presenting Tesla Chief Technology Officer JB Straubel with the first production lithium-ion cells manufactured at Panasonic's facility in Suminoe, Japan.

Nonequity Strategic Alliance

Nonequity strategic alliances are created when two or more companies enter a contractual relationship to pool their resources and capabilities together. These alliances allow companies to expand their networks and improve their services without requiring equity stakes from other organizations.

Turkish Airlines, for example, has established a number of non-equity strategic alliances with other carriers, including Air Canada, United Airlines, and Lufthansa. Through these non-equity strategic alliances, Turkish Airlines is able to keep its independence while expanding the range of routes it offers and enhancing passenger connection.

Create: Joint Ventures

In addition to embracing internal development and strategic alliances, two organizations also may diversify by creating an entirely new company. An example of this is a joint venture.



Figure 7.10: Turkish Airlines

Joint ventures are established when two companies establish a new shared entity. For example, when two parent companies, Company A and Company B, create a child company, Company C, this is a joint venture. Each partner is invested in the new venture and shares joint responsibility for the new entity's success. Joint ventures are another example of diversification through horizontal integration.

In 2007, Hulu was initially established as a joint venture between NBCUniversal, the Walt Disney Company, Providence Equity, and 21st Century Fox. These companies came together to create Hulu, a streaming platform that provides TV shows, movies, and original content.

When both Company A and Company B own 50 percent of the child company, this is a **50-50 joint venture**.

For example, in 2012, Microsoft and General Electric Healthcare signed an agreement to create Caradigm, a new company. Microsoft and General Electric Healthcare each owned 50 percent. The purpose of this joint venture was to develop and market an open healthcare intelligence platform through the creation of Caradigm. Microsoft had the technical capability, and General Electric Healthcare had the expertise with healthcare. This is an example of a 50-50 joint venture.

Subsequently, in 2016, General Electric Healthcare bought out Microsoft's share in the company, and in 2018, General Electric Healthcare sold Caradigm to Inspirata. This illustrates how joint ventures may serve a current corporate strategy until the company must respond to a dynamic market and choose to engage in other forms of diversification and divestment.

If Company A owns 70 percent and Company B owns 30 percent, the joint venture is a **majority-owned joint venture**.

For example, until recently, China required all manufacturing operations to be at least 50 percent Chinese owned. In 2003, BMW and Chinese automobile manufacturer Brilliance Auto Group entered a 50-50 joint venture to produce and sell BMW vehicles in China. When Chinese regulations changed, the relationship between BMW and Brilliance Auto Group changed. In 2022, the two firms entered into a majority-owned joint venture, with BMW owning 75 percent of the joint venture. This is another example of how relationships between firms change. A PESTEL analysis is a good strategic management framework to assess changing governmental regulations in the general (macro) environment.

Acquire: Mergers and Acquisitions (M&A)

Finally, firms may acquire another company as a method of diversifying. Mergers and acquisitions are means of acquiring another company. Both are examples of horizontal integration.

A **merger** occurs when two companies of similar size voluntarily join forces and create a new, singular business.

For example, in 1999, Exxon and Mobil merged to create ExxonMobil, the largest publicly traded oil company in the world. Both companies were about the same size and decided to join together voluntarily. By merging, they combined their expertise, resources, and market power. This helped them become more efficient and competitive in the global oil and gas industry. The merger allowed ExxonMobil to grow stronger and lead the market in exploration, refining, and energy production.

Acquisitions occur when one company buys another company, absorbing the purchased company into the buyer. Acquisitions are more common than mergers.



Figure 7.11: Marriott

For example, in 2016, Marriott bought Starwood Hotels and Resorts Worldwide, making them part of the Marriott International company and creating the world's largest hotel chain.

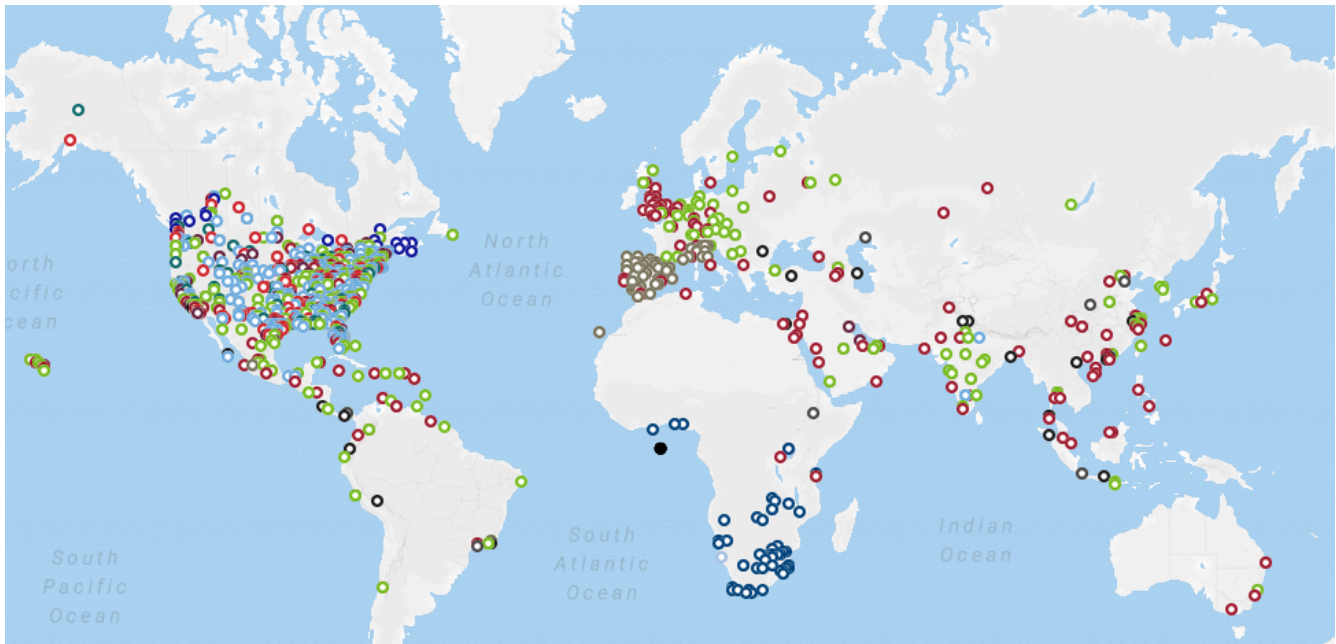


Figure 7.12: Marriott hotels

In 2017, Amazon bought Whole Foods Market. In 2023, Microsoft acquired Activision Blizzard, a video game **holding company**. A holding company's primary business is holding a controlling interest in the securities of other companies.

We consider joint ventures, strategic alliances, and mergers and acquisitions again in [Chapter 9](#) when we focus on innovation, as these are mechanisms that allow firms to innovate through cooperation.

Reducing and Reversing Diversification

Continuously assessing and managing diversification includes evaluating a firm's current offering of products and services and assessing the potential value of changing the firm's current offerings by expanding into additional products and services. A firm also may consider reducing or divesting the offerings of its current product and service lines.

Retrenchment

Business borrowed the term *retrenchment* from warfare. In the wars of the early twentieth century, battles were fought using trench warfare. When an attacking army reached a trench, the defending army fell back to the next trench. This was called retrenchment, which allowed the retreating army to refortify its position. The partial retreat was an effort to remain in the battle with the goal of winning the battle.

In business, **retrenchment** is a reduction in size and product offerings to continue to make profits. It is also referred to as downsizing or rightsizing, which often requires laying off employees.

Divestment

When reducing a company's size and offerings is insufficient to address the company's strategic goals, then **divestment** may be an option. Selling an unprofitable business or product line can be a way of reversing diversification. Companies may divest complete product lines and businesses. They may also sell part of a company. Selling part of a company, such as a division of strategic business unit, is known as a **spinoff**.

Application

- Think about some of the companies you have studied in your business education.
 - Discuss an example of related diversification, and explain why it is an example of a related diversification.
 - Describe an example of unrelated diversification, and explain why it is an example of unrelated diversification.
 - Use the make-contract-create-acquire continuum to give examples of the ways a firm may diversify. Give an example of internal development, nonequity strategic alliance, equity strategic alliance, joint venture, merger, and acquisition. Explain how your examples are examples of diversification.
 - Discuss an example of retrenchment, and explain how this is a way a company can reduce its diversification.
 - Describe an example of divestment, and explain how this is a way a company can reverse its diversification.

Key Takeaways

Differentiation is how a company makes its products distinct from its competitors. Diversification refers to how a company simultaneously deals with different products and services in different industries, markets, market segments, and businesses. A single business firm is a firm that derives 95 percent or more of its revenues from one business. A dominant business firm derives between 70 percent and 95 percent of its revenues from one business. Related diversification is expanding into new and similar markets, market segments, and businesses in a new industry that has similarities to a firm's current industry or industries. A company that engages in a related diversification strategy receives less than 70 percent of its revenues from a single business and the remaining revenue from business related to the primary business. Unrelated diversification is expanding into new markets, market segments, and businesses in a new industry that has little or no similarities to a firm's current industry or industries. A company that engages in an unrelated diversification strategy receives less than 70 percent of its revenues from a single business and the remaining revenue from business unrelated to the primary business. There is an optimal degree of diversification, and in most cases, related diversification is associated with the strongest firm performance. Companies may diversify by using internal development to make their own products or design new services. They also may enter into contracts with other companies to achieve diversification through nonequity and equity alliances. Firms can diversify by creating a new company through a joint venture. Finally, companies may acquire additional companies as a means of diversification through mergers and acquisitions. Sometimes companies need to reduce their diversification through retrenchment, which is reverse diversification through divestment or spinoffs.

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7.4 Vertical Integration

As you recall, corporate-level strategy is a companywide strategy that focuses on creating and maintaining a firm's competitive advantage by creating synergy within and between multiple industries, markets, market segments, and businesses, across multiple industry value chain(s), and in different geographical locations.

To consider at what stage of the industry value chain(s) a company should participate requires an understanding of industry value chains and how analyzing them relates to corporate strategy.

A supply chain and an industry value chain are related ideas.

Supply Chain

A **supply chain** includes the steps of product production from multiple entities, from raw materials to the final delivered product. Using jewelry production as an example, valuable metals such as gold, silver, and platinum are extracted from mines. Mining companies ship these to suppliers, who shape the raw materials. Then, manufacturing companies design the products in workshops, where they also do quality control. After this process, the produced jewelry is distributed to retailers, who market and sell them to customers and offer customer support and service.

Industry Value Chain

An **industry value chain** considers the ways a firm adds value to each step (or “node”) in the production process.

Analyze an Industry Value Chain

[Chapter 4](#), “Analyzing the Internal Environment,” considered several strategic management frameworks, including the VRIO and value chain analyses. A company value chain analysis examines internal company practices and their optimization relative to creating value for customers and a sustainable competitive advantage for the firm. An **industry value chain analysis** differs in that it emphasizes value creation as it examines the production stages, from raw material procurement to the delivery of the final product.

An industry value chain analysis examines each node of a product’s value chain to analyze value creation at each. Among other things, these nodes include sourcing of raw materials, costs associated with production and distribution, and characteristics that drive customers’ willingness to pay for the product. Aspects of each node have the ability to impact total costs and expected margins of the final delivered product. An industry value chain analysis is used to identify opportunities for increased profit through, for example, more effective cost control pricing, product positioning, and product distribution strategies.

Imagine an industry value chain for the production of gourmet cakes. In figure 7.13, the value chain includes the following nodes: wheat farmer, wheat processing plant, dairy farmer, dairy processing plant, baking facility, distribution, and bistro. To analyze the value chain, analyze each level or node for the value added to the overall process of producing gourmet cakes. This includes an analysis of the profit margin of each step in the process.

The stage of the industry value chain(s) at which the company should participate is a question of business integration—more specifically, vertical integration.

Business Integration

Business integration is the process of combining different components of a business into a unified and cohesive operation. There is horizontal and vertical integration.

Horizontal Integration

Horizontal integration is business expansion that focuses on relationships with another company in the same business line.

Continuing with our example of a value chain for producing gourmet cakes, let’s now consider horizontal integration. An example of horizontal integration would be a wheat processing plant merging with or acquiring another wheat processing plant. If a wheat processing plant significantly expands its capacity so that it takes up more market share, this internal development can also be a form of horizontal integration. If a distributor merged with another distributor or a bistro acquired another bistro, these would also be examples of horizontal integration.

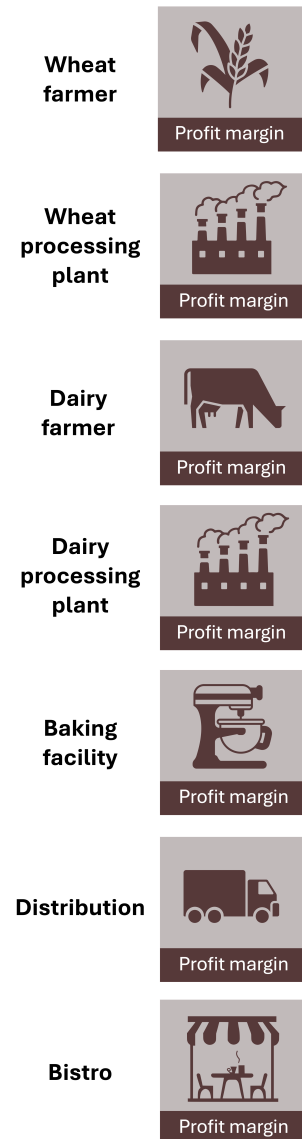


Figure 7.13: Industry value chain for the production of gourmet cakes

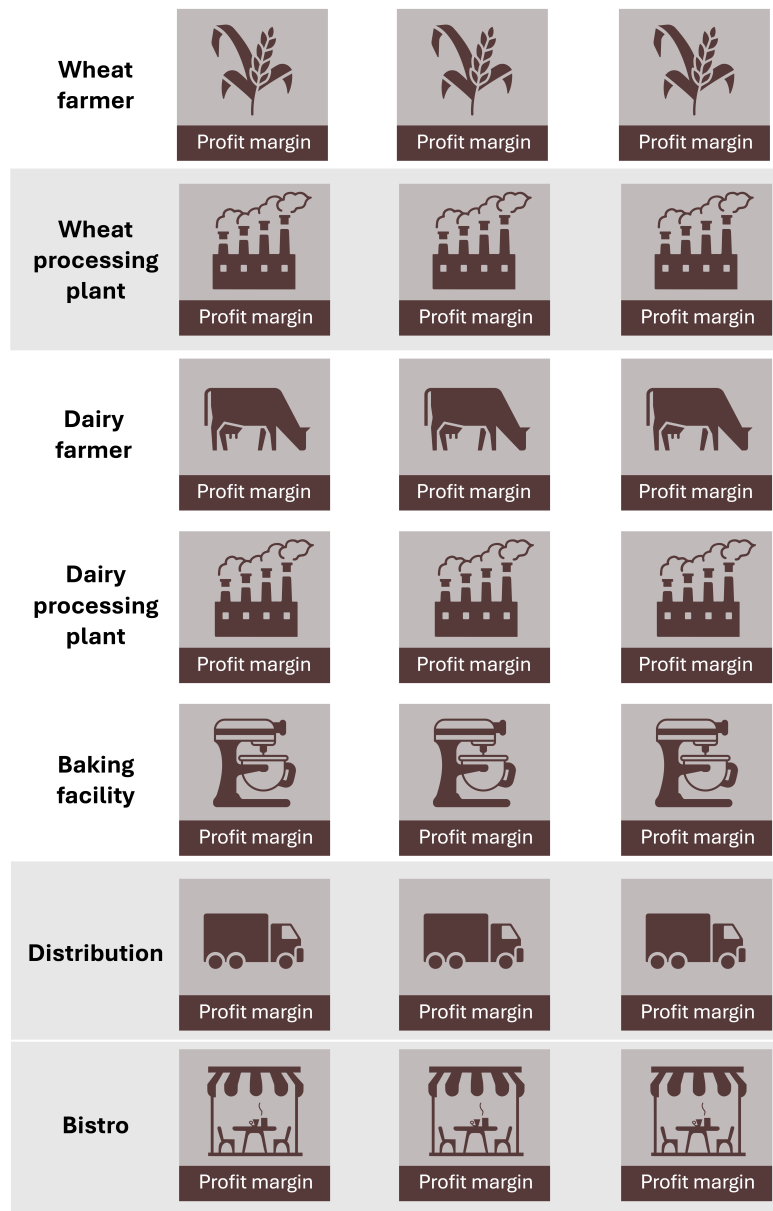


Figure 7.14: Horizontal integration

Vertical Integration

Vertical integration is a business expansion strategy where a company takes control over one or more stages in the production or distribution of its products.

Continuing with our example of a value chain for producing gourmet cakes, an example of vertical integration would be any business along the vertical dimension of the value chain deciding to diversify into another business along the vertical dimension of the value chain such as a dairy processing plant diversifying by opening a baking facility.

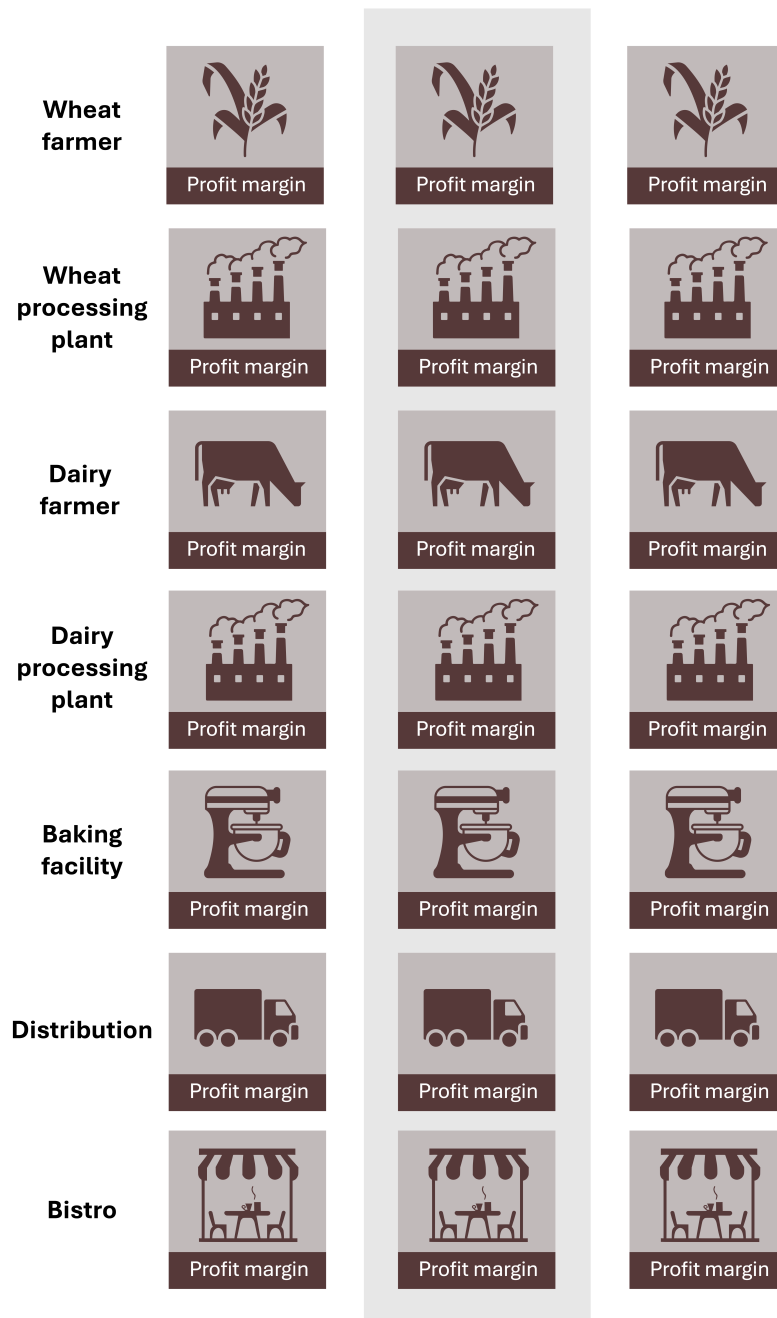


Figure 7.15: Vertical integration

Backward Vertical Integration

Backward vertical integration occurs when a firm moves backward along the industry value chain and enters a supplier's business. For example, Volkswagen purchased turbine manufacturing facilities to guarantee consistent supply of parts for its power generation equipment.

In our example of a value chain for producing gourmet cakes, a dairy processing plant purchasing a dairy farm is an example of backward vertical integration. If the bistro decided to change its business model from purchasing gourmet cakes to making them in-house, that also would be an example of backward vertical integration. This would be a significant change for the bistro. The bistro would need the physical space and equipment to make cakes, it would need to hire talented patisserie chefs, and it would need to establish relationships with suppliers to ensure they had reliable supplies to make the cakes.

These decisions are supported by an industry chain analysis. In [Chapter 4](#), you learned that one of the four elements of a Porter's Five Forces analysis is the bargaining power of suppliers. Analyzing the bargaining power of suppliers is also important when considering backward vertical integration. Using multiple strategic analysis tools informs an evidenced-based decision whether to choose a backward vertical integration approach.

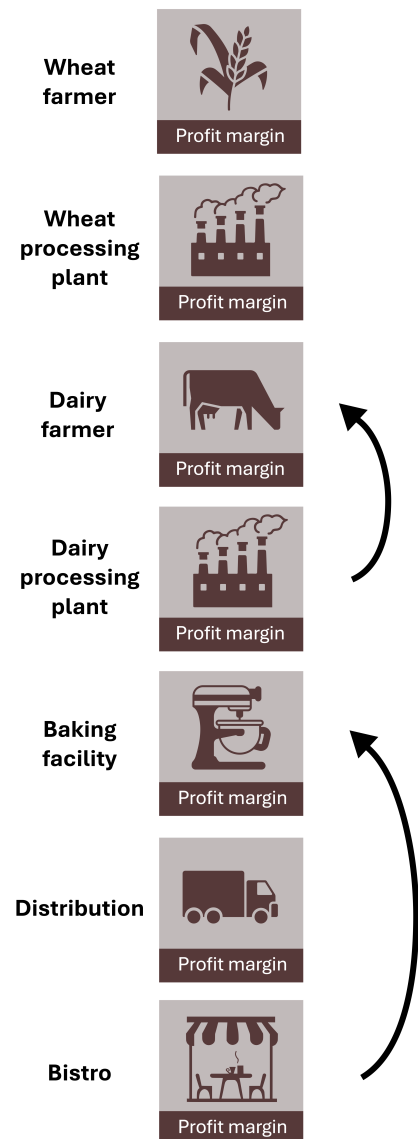


Figure 7.16: Backward vertical integration

Forward Vertical Integration

When a company moves further forward down the industry value chain and enters a buyer's business, that is **forward vertical integration**. When a microbrewery purchases a pub, that is an example of forward vertical integration. Amazon's acquisition of Whole Foods is another example.

In our example of a value chain for producing gourmet cakes, the baking facility deciding to distribute the cakes would be example of forward vertical integration. Many companies outsource business activities that do not contribute to their core competencies, hiring organizations that specialize in goods delivery, such as Fedex. Amazon is an example of a company that brought delivery back in-house. This is a good strategic choice for Amazon due to the importance of delivery and the percentage of its online shopping business that relies on delivery. Companies that require special delivery conditions for their products, which may be fragile or heat sensitive, sometimes provide their own deliveries. Paxton & Whitfield, a London cheesemonger, provides its own overnight deliveries in recyclable ice packs. In our example, an industry value chain analysis may convince the baking facility that it is worth the investment to deliver its own cakes.

In [Chapter 4](#), you learned that another of the four elements of a Porter's Five Forces analysis is the bargaining power of buyers. Analyzing this power is important when considering forward vertical integration. Using multiple strategic analysis tools informs an evidenced-based decision whether to choose a forward vertical integration approach.

Vertical integration, both backward and forward, occurs when a company controls different stages along the industry value chain. When considering a company's position in the industry value chain(s), a firm evaluates its current position and assesses the potential value of expanding through backward and forward vertical integration. The firm also evaluates the benefits of contracting its presence in the chain(s) and changing its portfolio either incrementally or radically with a combination of retaining, expanding, and reducing positions in the industry value chain(s).

Conducting an industry value chain analysis allows corporate executives to make evidenced-based decisions about which stage of the industry value chain the firm should occupy. Combining a value chain analysis and a Porter's Five Forces analysis gives a strong evidence base to decide how to manage a firm's position along its value chain(s).

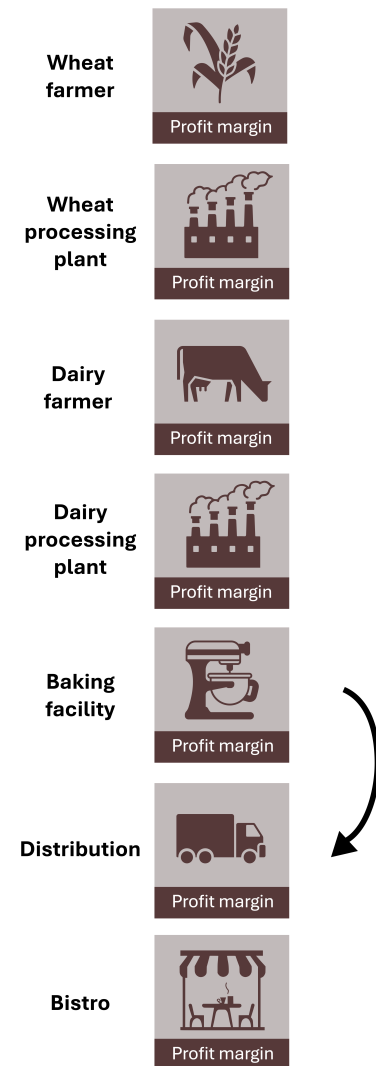


Figure 7.17: Forward vertical integration

Application

- Continue to think about some of the companies you have studied in your business education.
 - Discuss an example of backward vertical integration, and explain why it is an example.
 - Discuss an example of forward vertical integration, and explain why it is an example.

Key Takeaways

Vertical integration is a business expansion strategy where a company takes control over one or more stages in the production or distribution of its products. Backward vertical integration occurs when a firm moves backward along the industry value chain and enters a supplier's business. When a company moves further forward along the industry value chain and enters a buyer's business, that is forward vertical integration. Vertical integration, both backward and forward, occurs when a company controls different stages along the industry value chain. An industry value chain considers the ways a firm adds value to each step in the production process. Conducting an industry value chain analysis allows corporate executives to make evidenced-based decisions about which stage of the industry value chain the firm should occupy. Combining an industry value chain analysis with a Porter's Five Forces analysis is a robust approach to formulating strategy.

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7.5 Geographical Scope

So far, we have discussed corporate-level strategy based on synergy and the industry value chain. There is a third factor to consider. Where the organization should compete geographically is a question of **geographical scope**—where geographically firms provide their products and services.

Companies evaluate the potential benefits of offering their products and services in local, regional, national, and multinational markets. Formulating multinational strategy is considered in detail in [Chapter 12](#).

Companies evaluate geographical markets for their current line of products or for new lines of products. When considering where the firm will provide its products and services, it evaluates its current geographical markets and assesses the potential value of expanding into new geographical markets; it also evaluates the value of changing its portfolio either incrementally or radically with a combination of retaining, expanding, and reducing their offering geographically.

The question of where to provide products and services is important for brick-and-mortar businesses. It is equally essential for companies that offer either all or a portion of their products and services online. For example, when a company expands its market through online sales, it must address many new issues, such as transportation for delivering its products. U.S.-based companies that expand into a wider local market within a state may encounter different local laws and regulations, such as differences in taxation. Expanding into new U.S. states requires knowledge of both federal and state laws, such as those that govern labor practices. International expansion considers a wide range of factors and is the topic of [Chapter 12](#).

Application

- Continue to think about some of the companies you have studied in your business education.
 - Discuss an example of forward geographical scope, and explain why it is an example of a geographical scope.

Key Takeaways

Geographical scope refers to where geographically firms compete, providing their products and services. Companies evaluate the potential benefits of offering their products and services in local, regional, national, and international markets. Sometimes a company needs to alter its businesses and product lines either incrementally or radically while retaining its current offering, expanding through diversification, and reducing or divesting the products and services it offers. This is a process of portfolio planning, which we will consider next.

7.6 Portfolio Planning

A firm's **business portfolio** consists of all the products and services it sells, all the business it is in, and all the market segments, markets, and industries in which it participates.

An essential part of continuously assessing and managing corporate-level strategy includes portfolio planning. Portfolio planning addresses how a firm should manage its portfolio of businesses, like strategic business units or divisions, to achieve synergy and create value. It also addresses how the parent company adds value to its business divisions and strategic business units.

There are many models to describe business portfolios. The Boston Consulting Group (BCG) matrix is a framework that supports portfolio planning.

The Boston Consulting Group (BCG) Matrix

The BCG matrix is designed to help companies decide how to prioritize their different businesses. A company with multiple strategic business units needs to make important decisions as to which strategic business units are the most attractive, which will receive more resources than other strategic business units, which will receive new investments, and which are not attractive enough anymore and need to be divested.

These questions touch on the topic of corporate portfolio management. Ideally, a corporation wants to operate successful businesses in attractive markets. Following this logic, the BCG matrix uses the market growth rate as an indicator of how attractive the strategic business unit's market is. The relative market share is used as an indicator of how well the business or strategic business units are doing in the specific market. A high relative market share means that the business is doing well compared to its competitors. Ideally, a corporation wants a relatively high market share in attractive markets, as measured by market growth rates.

The BCG matrix maps a firm's businesses along two dimensions. The first is relative market share, and the second is market growth rate. This produces four quadrants, each with its own symbol: dog, cash cow, question mark, and star. To use the BCG matrix, first plot a firm's business units or product lines along these two dimensions, and then decide whether it is best to liquidate them, reinvest their profits into other product lines, or significantly invest in them.

Dogs

The Boston Consulting Group uses the term *pet* for the quadrant most commonly referred to as dogs (bcg.com). For fans of dogs or any pet, either name is unfortunate, as dogs in the BCG matrix are those businesses or product lines that have a low relative market share and a low market growth rate. Dogs are strong candidates for liquidation, divestment, or repositioning in the portfolio.

Cash Cows

Cash cows have a high relative market share and a low market growth rate. Cash cows are best “milked” for cash to reinvest. These businesses or product lines have poor performance potential. Therefore, profits from cash cows are best diverted to business and product lines with more profit potential.

Question Marks

Question marks have a low relative market share and a high market growth rate. Executives decide whether to invest in them or divest them, depending on their potential profit.

Stars

Stars have a high relative market share and a high market growth rate. Because of their high profit potential, companies should significantly invest in stars.

Limitations to the BCG Matrix

Like many portfolio planning tools, the BCG matrix has limitations. The positioning and attractiveness of different strategic business units is influenced by many complex factors, but relative market share and market growth rate oversimplifies this. The BCG is best used as a broad first indication of the positioning and attractiveness of different strategic business units. Once a BCG matrix has been applied to a firm's businesses, it is important to then consider other relevant factors that influence the positioning and attractiveness of different strategic business units before a decision is made to divest, reinvest profits, or invest in the product line.

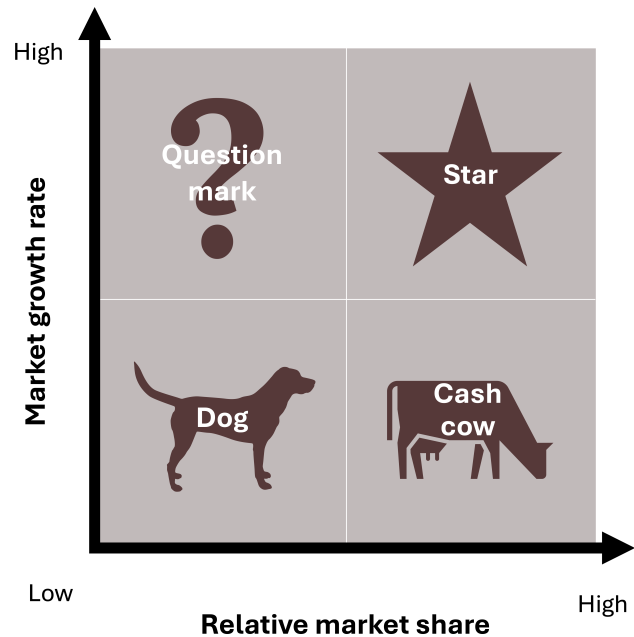


Figure 7.18: The BCG matrix

Key Takeaways

A firm's business portfolio consists of all the products and services it sells, and all the business it is in, all the market segments, markets, and industries in which it participates. The Boston Consulting Group (BCG) matrix is a framework that supports portfolio planning by assessing the positioning and attractiveness of different strategic business units that make up a firm's portfolio. The BCG maps a firm's businesses along two dimensions: relative market share and market growth rate. This produces four quadrants, each with its own symbol: dog, cash cow, question mark, and star. Dogs are businesses with a low relative market share and a low market growth rate. Dogs are strong candidates for liquidation, divestment, or repositioning in the portfolio. Cash cows have a high relative market share and a low market growth rate. Profits from cash cows are best diverted to business and product lines with more profit potential. Question marks have a low relative market share and a high market growth rate. Executives decide whether to invest in them or divest them, depending on their potential profit. Stars have a high relative market share and a high market growth rate. Because of their high profit potential, companies should significantly invest in stars. Like most tools, the BCG has limitations, such as oversimplifying portfolio planning.

7.7 Analyze Corporate-Level Strategy

Corporate executives and boards of directors focus on formulating corporate-level strategies. When you conduct a case analysis, you analyze a firm's corporate-level strategy. This is step six in the case analysis process.

6. As appropriate to the case, analyze strategies: Corporate-level, business-level, innovation, sustainability and ethics, technology, and multinational strategies.

- a. Use strategic management analytical frameworks to analyze, interpret, and evaluate strategies.
- b. Ensure line of sight and congruence within analysis of each strategy.

Key Takeaways

Analyze a firm's corporate-level strategy when you conduct a case analysis for strategy formulation.

7.8 Why Corporate-Level Strategy Is Important to Business Graduates

Because corporate-level strategy operates at the highest level of a firm, it may appear distant or irrelevant to the work of recent business graduates. However, that is not the case. For business graduates starting as business support unit managers in support business units of large companies, such as marketing managers, corporate-level strategy has a direct influence on the implementation of functional-level strategy, which is a key responsibility for functional managers. In formulating corporate-level strategies, corporate executives and divisional or strategic business unit managers may solicit data analysis from functional business managers, such as managers of business information technology, accounting, and human resource management.

As a companywide strategy that focuses on creating and maintaining a firm's competitive advantage by creating synergy within and between multiple industries, markets, market segments, and businesses, across multiple industry value chain(s), and in different geographical locations, corporate-level strategy must reflect current, accurate, and relevant data analysis that only business support unit managers have direct access to. Therefore recent graduates are an essential part of ensuring a firm's successful corporate-level strategy.

Business graduates joining smaller companies will spend more time working closely with executives responsible for corporate-level strategy from the start. Business graduates that enter either internal or external consulting roles require a high level of competence with corporate-level strategy to communicate to corporate executives how their consulting projects fit into the overall corporate-level strategy of the firm. For business graduates who already are or will become entrepreneurs, fluency with corporate-level strategy is essential to establishing and growing a successful firm.

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7.9 Conclusion

Formulating a firm's corporate-level strategy focuses on finding a direction for the firm's future. Corporate-level strategy is the broadest level of strategy and is the responsibility of senior executives and the board of directors, who must answer the question of where the firm is going to compete. Corporate-level strategy is a companywide strategy that focuses on creating and maintaining a firm's competitive advantage by creating synergy within and between multiple industries, markets, market segments, and businesses, across multiple industry value chain(s), and in different geographical locations. In what industries, markets, market segments, and businesses a firm should operate is a question of diversification. At what stage of the industry value chain(s) the company should participate is a question of vertical integration. Where the organization should compete geographically is a question of geographical scope. The BCG matrix is one framework that addresses portfolio planning.

Demonstrate Your Knowledge, Skills, and Competence

Use these questions to test your knowledge of the chapter:

1. Describe corporate-level strategy. Who is responsible for corporate-level strategy? What questions does it answer? How does it relate to a VUCA environment? What is the role of synergy in corporate-level strategy?
2. Describe diversification and its role in corporate-level strategy. Explain how diversification begins to answer a primary focus of corporate-level strategy: in what industries, markets, market segments, and businesses a firm should operate. Explain how diversification can contribute to a company's competitive advantage.
3. Discuss related diversification and how this relates to a single business firm and a dominant business firm. Give an example.
4. Discuss unrelated diversification. Give an example.
5. Explain the relationship between diversification and financial performance.
6. Use the make-contract-create-acquire continuum to describe the ways a firm may diversify.
7. Describe the ways a company may reduce or reverse diversification. Give an example of each.
8. Describe an industry value chain, how you analyze it, and why this is useful.
9. Describe horizontal integration, and give an example.
10. Discuss vertical integration and its role in corporate-level strategy. Explain how vertical integration begins to answer a primary focus of corporate-level strategy: the stage of the industry value chain(s) at which the company should participate. Explain how vertical integration can contribute to a company's competitive advantage.
11. Describe backward vertical integration and how this indicates the stage of the industry value chain(s) at which the company should participate.
12. Discuss forward vertical integration and how this indicates the stage of the industry value chain(s) at which the company should participate.
13. Describe how geographical scope relates to corporate-level strategy. Explain how geographical scope can contribute to a company's competitive advantage.
14. Explain the purpose of portfolio planning.
15. Explain the BCG matrix and its limitations.
16. Describe how competence with corporate-level strategy is relevant and important to you.

Now you are competent with corporate-level strategy. Your hard work has paid off!

Figure Descriptions

Figure 7.1: Purple hierarchical organizational chart displaying the structure of a company's management and strategic planning. At the top is a rectangle labeled "Board of directors." Below this, another rectangle labeled "Corporate office (corporate executives)." This level of hierarchy represents corporate-level strategy. Below this, two rectangles are labeled "Division 1 (division 1 manager)" and "Division 2 (division 2 manager)." Below this, there are four SBU boxes (each with one manager). There are two SBU boxes beneath Division 1 and two SBU boxes beneath Division 2. This level of hierarchy represents business-level strategy, innovation strategy, sustainability and ethics strategy, technology strategy, and multinational strategy. Below the SBUs are five "Business support Unit 1" boxes, dedicated to finance, operations, human resources (HRM), IT, and sales and marketing, each managed by their own business support unit manager. This level of hierarchy represents functional level strategy.

Figure 7.5: First quadrant of an X-Y graph. The x-axis represents diversification and the y-axis represents financial performance. The graph features a purple parabolic curve that opens downwards. From left to right, the curve is labeled (1) single business (low diversification and low financial performance), (2) dominant business (slightly higher diversification and high financial performance), (3) related diversification (moderate diversification and high financial performance), and (4) unrelated diversification (high diversification and low financial performance).

Figure 7.6: Horizontal purple arrow pointing in both directions. From left to right, the main sections of the arrow are (1) Make (includes internal development), (2) Contract (includes nonequity strategic alliance and equity strategic alliance), (3) Create (includes joint venture), and (4) Acquire (includes mergers and acquisitions).

Figure 7.13: Illustration of the stages of a supply chain, presented vertically in a column. Each stage includes an icon and a profit margin. Stages from top to bottom: wheat farmer, wheat processing plant, dairy farmer, dairy processing plant, baking facility, distribution, and bistro. This graphic is purple.

Figure 7.14: Illustration of the stages of a supply chain, presented vertically in a column. Each stage includes an icon and a profit margin. Stages from top to bottom: wheat farmer, wheat processing plant, dairy farmer, dairy processing plant, baking facility, distribution, and bistro. This is repeated three times (i.e., there are three wheat farmers, below that are three wheat processing plants, below that are three dairy farmers, and so on). Three stages are highlighted horizontally: wheat processing plant, distribution, and bistro. This graphic is purple.

Figure 7.15: Illustration of the stages of a supply chain, presented vertically in a column. Each stage includes an icon and a profit margin. Stages from top to bottom: wheat farmer, wheat processing plant, dairy farmer, dairy processing plant, baking facility, distribution, and bistro. This is repeated three times (i.e., there are three wheat farmers, below that are three wheat processing plants, below that are three dairy farmers, and so on). One entire supply chain is highlighted vertically. This graphic is purple.

Figure 7.16: Illustration of the stages of a supply chain, presented vertically in a column. Each stage includes an icon and a profit margin. Stages from top to bottom: wheat farmer, wheat processing plant, dairy farmer, dairy processing plant, baking facility, distribution, and bistro. An upward black arrow begins at the dairy processing plant and points to the dairy farmer. Another black arrow begins at the bistro and points up towards the baking facility. This graphic is purple.

Figure 7.17: Illustration of the stages of a supply chain, presented vertically in a column. Each stage includes an icon and a profit margin. Stages from top to bottom: wheat farmer, wheat processing plant, dairy farmer, dairy processing plant, baking facility, distribution, and bistro. A black arrow begins at the baking facility and points down towards distribution. This graphic is purple.

Figure 7.18: First quadrant of an X-Y axis with four purple boxes. The x-axis represents relative market share and the y-axis represents market growth rate. Both axis range from low to high. Low relative market share and low market growth rate is marked dog. High relative market share and high market growth rate is marked star. High relative market share and low market growth rate is marked cash cow. Low relative market share and high market growth rate is marked with a question mark.

Figure References

Figure 7.1: Three levels of strategy. Kindred Grey. 2025. CC BY.

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Figure 7.17: Forward vertical integration. Kindred Grey. 2025. CC BY. Includes the following icons from the Noun Project ([Noun Project license](#)): Wheat (sentya irma, 2024, <https://thenounproject.com/icon/wheat-7330935>), factory (Kevin, 2022, <https://thenounproject.com/icon/factory-5053342>), cow (Laymik, 2019, <https://thenounproject.com/icon/cow-2717641>), stand mixer (I'm Vattie, 2024, <https://thenounproject.com/icon/stand-mixer-6983675>), box truck (Andrianxia, 2024, <https://thenounproject.com/icon/box-truck-6945195>), and cafe (Ruby, 2023 <https://thenounproject.com/icon/cafe-6111062>)

Figure 7.18: The BCG matrix. Kindred Grey. 2025. CC BY. Includes the following icons from the Noun Project ([Noun Project license](#)): Cow (Laymik, 2019, <https://thenounproject.com/icon/cow-2717641>) and Dog (Daniel Ducrocq, 2013, <https://thenounproject.com/icon/dog-14830>)

8. FORMULATE BUSINESS-LEVEL STRATEGY

Learning Objectives

After engaging with this chapter, you will understand and be able to apply the following concepts.

1. Business-level strategy
2. Strategic market position (cost leadership and differentiation)
3. Strategic market size (focused and broad)
4. Six business-level strategies
5. Focused cost leadership
6. Broad cost leadership
7. Focused differentiation
8. Broad differentiation
9. Best-cost strategy
10. Blue ocean strategy
11. Stuck in the middle
12. Limitation of business-level strategies
13. Why business-level strategy is important to business graduates

Upon completion of this chapter, you will be equipped to analyze a firm's business-level strategy.

8.1 Introduction

In the previous chapter, you learned about the broadest level of strategy, corporate-level strategy. In this chapter, we begin to narrow the focus with business-level strategy.

After an introduction to business-level strategy, you learn the two dimensions along which strategic business unit managers formulate business-level strategy. The first addresses a firm's strategic market position, which includes cost leadership and differentiation approaches. The second addresses a firm's strategic market size, which can concentrate on a narrow, niche market segment (focused approach) or a wider market (broad approach). These two dimensions produce six business-level strategies: focused cost leadership, broad cost leadership, focused differentiation, broad differentiation, and two hybrid strategies known as best cost and blue ocean. Then you learn the risks of a firm not clearly formulating a business-level strategy and getting stuck in the middle. Next you learn how to analyze a firm's business-level strategy. Finally, you consider why business-level strategy is important to business graduates.

8.2 Business-Level Strategy

Let's begin by considering what business-level strategy is.

Where are we going?

You now understand that there are three stages to the strategic management process: strategic analysis ("Where are we?"), strategy formulation ("Where are we going?"), and strategy implementation ("How do we get there?"). Like all strategy formulation, business-level strategy addresses the question of where a firm is going.

Strategic Business Unit

While corporate-level strategy is the broadest level of strategy and is formulated at the corporate level of a company, business-level strategy is the strategy of a strategic business unit.

A **strategic business unit** is a fully functional unit of a business that has its own vision and direction and may be part of a larger organizational unit like a division. It may be based on markets served, products offered, or regions served.

Each strategic business unit has its own vision and direction it pursues through one business-level strategy. Smaller firms that have only one strategic business unit have only one business-level strategy. In large companies with more than one strategic business unit, different strategic business units may have different business-level strategies. Therefore, large corporations that have more than one strategic business unit potentially have multiple business-level strategies. Let's revisit our diagram that depicts the three levels of strategy to now consider how business-level strategy fits into the larger picture of strategy in an organization.

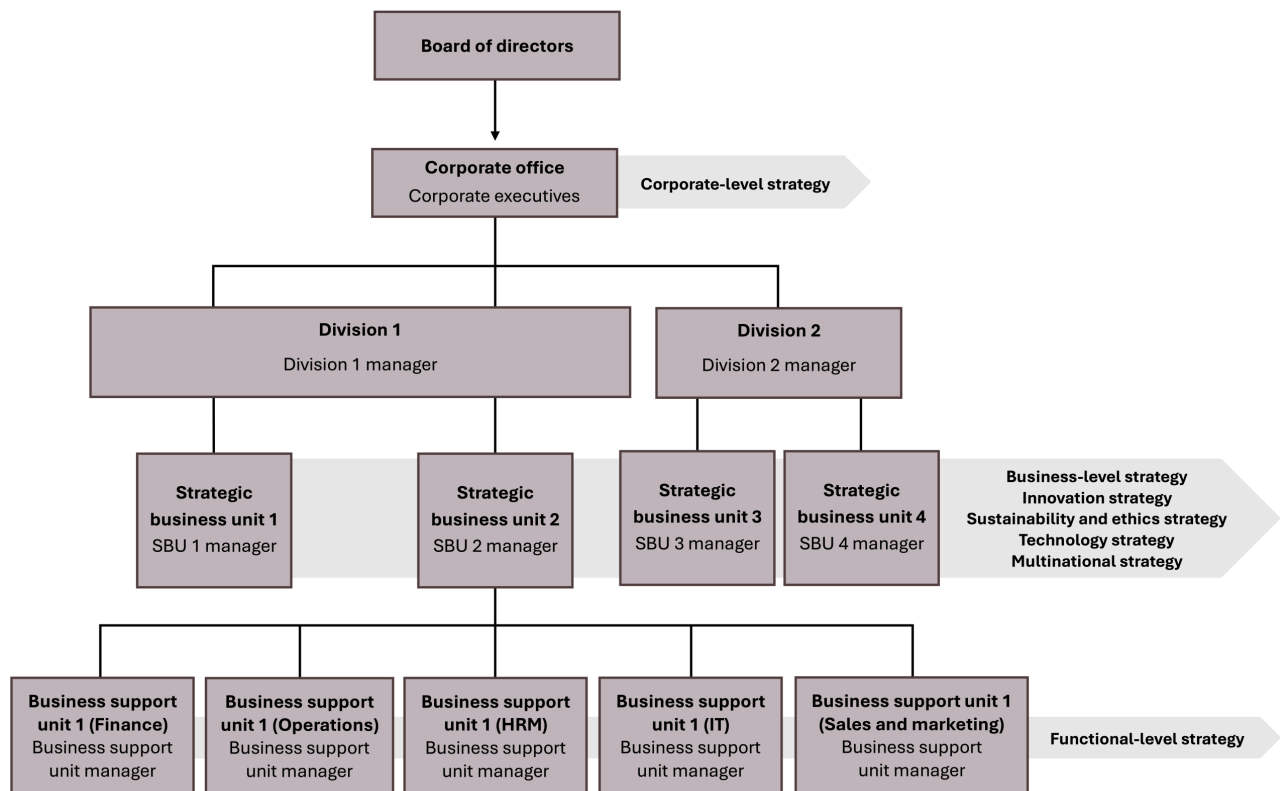


Figure 8.1: Three levels of strategy

How to win?

How a firm wins in its chosen markets is largely driven by the firm's ability to develop a winning strategy around its resources, capabilities, and core competencies that are superior to those of its competitors and that will create value for the firm's customers. Overall, the “How to win?” question addresses the firm's search for a sustainable competitive advantage.

Volatile, Uncertain, Complex, and Ambiguous Environment

As you now know, when executives analyze their organizational environments, they consider factors that relate to both the external environment and the internal environment of the firm. The external analysis of the general, industry, and competitive environments focuses on an outside-in perspective of the firm. The internal analysis of a firm's resources, capabilities, core competencies, and value chain focuses on an inside-out perspective of the firm. When you conduct a case analysis, you analyze companies through these same lenses.

When strategic management leaders and managers formulate strategy, they focus on an outside-in perspective. All successful strategies are driven by outside-in perspectives. [Chapter 7](#) discussed how this is true for corporate-level strategy. An outside-in perspective is equally important to business-level strategy and the strategies embedded into business-level strategies.

Strategic leaders and managers carefully monitor the external environment of their companies, analyze trends, and develop strategies that are forward-looking. Regardless of the level of strategy being formulated, firms must navigate an external environment that is volatile, uncertain, complex, and ambiguous (VUCA), where change and disruption are the new normal.

Focus

Both corporate-level strategy and business-level strategy focus on the markets and market segments in which a firm competes. Corporate-level strategy is broader in focus, aimed at creating synergy across businesses and industries.

Business-level strategy is narrower in focus. Business-level strategy is the strategy of a strategic business unit. A business-level strategy is a general way of positioning a company within an industry for gaining a competitive advantage by defining how a firm competes head-to-head against similar products and services in its market and market segments. In contrast, corporate-level strategy considers what industries and markets a firm should operate in and how to create synergy between them. Both focus on markets and market segments, but the focus is different. It is important the business-level strategy is congruent with and supports corporate-level strategy.

Determining a firm's business-level strategy involves making decisions about how to best serve specific groups of customers, address their unique needs, and provide solutions that stand out from competitors. At its core, business-level strategy is about identifying who the firm will serve, what needs it will meet, and how it will go about satisfying those needs in a way that delivers value.

Who Are Our Customers?

The first step in crafting a business-level strategy is understanding who the company is trying to serve. Every organization must carefully define its target market and market segments. For smaller companies, this might involve focusing on a single customer group, while larger organizations may develop different strategies for each of its markets and market segments. Understanding the customers being served is critical, as it guides the firm in tailoring its offerings and competitive approach to meet specific needs.

What Customer Needs Do We Meet?

Next, a business-level strategy must address what customer needs will be met. This step involves identifying the core problems or desires of the company's target market and market segments. Successful firms invest heavily in understanding these needs, often through market research, customer feedback, and competitive analysis. Whether customers are looking for affordability, innovation, reliability, or premium quality, the firm must clearly identify what drives purchasing decisions. The ability to accurately define and prioritize customer needs is essential to developing a strategy that resonates with the target market.

How Do We Satisfy Customer Needs?

Finally, the business must decide how it will satisfy its customers' needs and desires. This involves choosing the methods the firm will use to deploy its strategic resources, capabilities, and core competencies to deliver value to customers. The choice of how needs will be satisfied is closely tied to the firm's internal resources, capabilities, and core competencies. From a thorough knowledge of its customers, firms develop business-level strategies.

Business-level strategy leads to decisions about how to deploy a firm's resources, capabilities, and core competencies to best serve specific groups of customers, address their unique needs, and provide solutions that stand out from competitors. It is essential the firm keeps customers as a primary focus in deciding business-level strategies. Aligning a firm's resources, capabilities, and core competencies to business-level strategies includes decisions about product design, marketing, pricing, distribution, and customer service. An organization must define and continuously improve its business-level strategy because they are not necessarily static. They can change, especially in response to VUCA environments.

Strategic leaders and managers choose from a limited number of business-level strategies that are available to all companies. Despite companies choosing from a common pool of business-level strategies, all strategy should be specific and differentiating, and companies must implement them in ways that reflect their specific company conditions.

As you learn in Part V, there are strategies that are embedded into business-level strategies. We cover four of them in the book: innovation strategy, sustainability and ethics strategy, technology strategy, and multinational strategy. Therefore, the overall strategies that are formulated and implemented at the strategic business unit level are a combination of a company's chosen business-level strategy and the ways in which it embeds a combination of other strategies (such as innovation strategy, sustainability and ethics strategy, technology strategy, and multinational strategy) into their business-level strategy. This nuanced combination of strategies gives a company a distinctive competitive edge.

Next, we consider a business-level strategy framework.

Application

- Consider the job(s) you have now or have had so far. Answer these questions for that company:
 - Who are the company's customers?
 - What customer needs does the company meet?
 - How does the company satisfy customer needs?

Key Takeaways

Just as strategy formulation asks the question “Where are we going?”, business-level strategy asks the question “How to win?” and functions at the strategic business unit level. Determining a firm's business-level strategy involves making decisions about how to best serve specific groups of customers, address their unique needs, and provide solutions that stand out from competitors. Business-level strategy focuses on how to compete within an organization's chosen market and market segments to create and sustain competitive advantage. Business-level strategy addresses a firm's strategic market position, cost leadership and differentiation, and its strategic market size, focused or broad.

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8.3 Business-Level Strategy Framework

Firms formulate business-level strategies by making critical decisions on two fundamental dimensions. The first of these decisions is defining the firm's strategic market position. The second decision that firms make concerns the company's strategic market size. Both dimensions require a thorough understanding of the firm's customers, and both dimensions address which customers are being targeted.

These decisions combine to create business-level strategies and are represented in the business strategy framework as depicted in figure 8.2. The text that follows walks you through the business-level strategy framework.

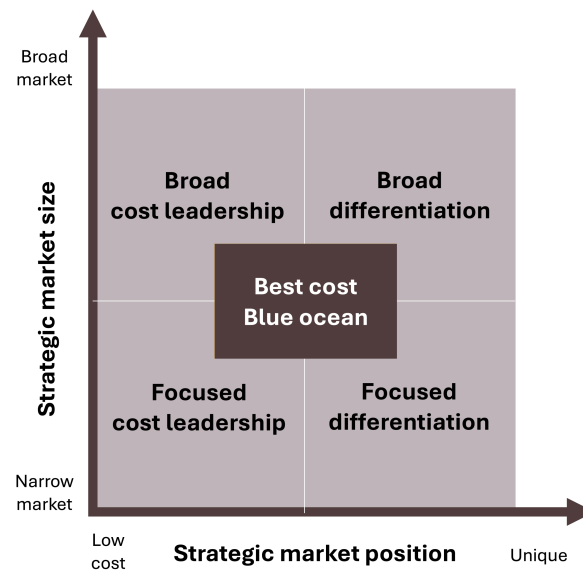


Figure 8.2: Business-level strategy framework

Next we consider a firm's strategic market position, which involves cost leadership and differentiation. Then we turn our attention to a company's strategic market size, which concerns whether it competes in a broad market or a focused market segment.

Key Takeaways

Firms formulate business-level strategies by defining the firm's strategic market position and strategic market size.

8.4 Strategic Market Position: Cost Leadership and Differentiation

The first critical strategic decision in defining the firm's business-level strategy is deciding its strategic market position. The strategic market position addresses how the firm distinguishes itself in its chosen market and market segments, either through addressing consumer preferences for low-cost alternatives or by addressing consumer preferences for luxury items. Strategic market position is sometimes referred to as the source of competitive advantage or as just strategic position.

Cost Leadership

When a firm distinguishes itself in the market by responding to consumer preferences for low-cost alternatives, the company competes primarily by being the lowest-cost producer or provider in its chosen market. The goal is to offer products or services that are of an equal or similar value to competitors' products or services at a lower price than them. This is called a **cost leadership** approach, and it appeals to cost-conscious customers.

A cost leadership strategic market position involves a firm striving to become the lowest-cost producer or provider in its chosen market or market segment while still offering products or services that meet customer expectations. Successful cost leadership leverages operational efficiencies, scale, and cost control measures to reduce production and distribution costs.

Companies achieve cost leadership through a combination of strategic initiatives focused on reducing costs across various areas of their operations. One common approach is leveraging **economies of scale** to achieve efficiency, where firms produce in large quantities to lower the average cost per unit. Economies of scale are created when the costs of offering goods and services decrease as a firm sells more items. This occurs because expenses are distributed across a greater number of items.

Automation, outsourcing, and streamlined processes also play crucial roles in keeping production costs low. Firms often simplify product offerings, standardize processes, and minimize waste to reduce overhead. Moreover, firms pursuing cost leadership often invest heavily in supply chain optimization, negotiating better terms with suppliers and seeking out more affordable raw materials. This relentless focus on cost-cutting allows companies to maintain their profit margins while offering lower prices to customers, creating a competitive advantage.

Firms that pursue cost leadership focus on achieving operational efficiency, leveraging economies of scale, and controlling overhead costs. This strategy is particularly effective in industries where price is the primary driver of customer decisions, such as retail, transportation, or basic consumer goods. Cost leaders streamline their supply chains and keep operating costs low to offer lower prices than competitors.

Large companies often choose to pursue a cost leadership strategic market position, and they keep their prices down by demanding price concessions from suppliers. The firm then passes some of these savings on to customers in the form of reduced prices in its stores. Typically, firms following a cost leadership approach spend little on advertising, market research, or research and development.

The key to this strategic market position is maintaining profitability through low costs while offering value that resonates with price-sensitive customers. However, it is important for firms to avoid compromising on quality to a degree that alienates their customer base. The challenge is striking a balance between being cost-competitive and delivering acceptable value.

A cost leadership approach works well when price competition among rival sellers is vigorous, identical products are available from many sellers, there are few ways to differentiate industry products, most buyers use the product in the same way, and buyers incur low costs in switching among sellers. The primary driver of a cost leadership approach is cost, which is most influenced by the cost of input factors and economies of scale.

For example, Walmart strategically positions itself in the market by using a cost leadership strategic market position. It has mastered this position by streamlining its supply chains and keeping operating costs low to offer lower prices than competitors. The key to success in cost leadership is maintaining cost advantages without sacrificing quality, which can erode the firm's competitive position if not carefully managed.

Advantages

Cost leadership offers several advantages for companies that can successfully implement it. One of the most significant benefits is that it allows firms to maintain a competitive position by offering lower prices than competitors, which can attract a larger share of price-sensitive customers. By being the lowest-cost producer, a firm can set its prices below industry averages, making it difficult for rivals to compete without sacrificing profitability. Additionally, cost leadership can provide companies with a buffer during economic downturns or periods of weak demand. When consumers are more cautious with their spending, companies with lower costs can continue to thrive by offering affordable alternatives, which can allow them to maintain their sales volume even when higher-priced competitors suffer. The emphasis on efficiency also makes firms well positioned to withstand price competition from rivals.

Another advantage is the potential for greater profitability through economies of scale and operational efficiency. Firms that achieve cost leadership often benefit from producing goods or services at high volumes, which spreads fixed costs over a larger number of units, reducing the per-unit cost. This can lead to higher margins, even when selling at lower prices. Furthermore, cost leaders are often more resistant to price wars in which competitors continually lower prices in pursuit of market share; they can resist because they have the financial flexibility to absorb lower margins without significantly harming their bottom line. This abil-

ity to maintain profitability while keeping prices low enables cost leaders to undercut competitors in highly competitive markets. High profits are possible if a cost leader has a high market share.

Disadvantages

Cost leadership also has several disadvantages that firms must be aware of. One major risk is the potential for lower perceived value by customers. If a firm focuses solely on reducing costs, it may neglect product quality, innovation, or customer service, leading customers to perceive the product as inferior. In industries where customers value features, brand loyalty, or innovation, cost leadership can backfire if the firm sacrifices these elements in pursuit of cost reduction. Additionally, firms pursuing cost leadership are highly vulnerable to changes in the cost structure, such as rising raw material prices, labor costs, or supply chain disruptions, especially in a VUCA environment. If a firm's cost advantage erodes due to external factors, it may struggle to compete, particularly if it cannot quickly adjust its prices or improve efficiency.

Another disadvantage of cost leadership is that it can lead to complacency and a lack of differentiation. Firms focused on cutting costs may not invest enough in research and development, marketing, or customer experience, which can prevent them from adapting to changing market conditions. Competitors might develop innovations or create brand loyalty that cost leaders cannot match. In such cases, cost leadership may become unsustainable if competitors can offer superior products at a similar price point. Additionally, cost leadership is often imitable, meaning competitors can adopt similar cost-cutting measures, eroding the initial firm's advantage.

Another disadvantage includes customer perceptions of quality. Just offering cheaper products is not sufficient to succeed at a cost leadership strategy. If customers perceive the quality of the product as no longer of the same or similar value, they are likely to take their business to a competitor. Sacrificing quality to a level that cost-conscious customers no longer perceive as acceptable can erode the firm's competitive position if not carefully managed.

Another disadvantage for cost leaders is reliance on large sales volumes. When sales decline, so do profits because the profit margin is low. Cost leaders often offset this risk by selling recession-proof products like groceries, healthcare, and other essentials. Firms that follow a cost leadership strategy are slow to respond to market changes because low investment in research and development can lead to a sluggishness to detect market changes, which can be a disadvantage. Large volumes of sales are required for cost leaders because profit margins are slim. Lastly, the need to keep expenses low might lead cost leaders to be slow in detecting key environmental trends.

Differentiation

When a firm distinguishes itself in the market by responding to consumer preferences for luxury items, the company competes primarily by offering products or services that are perceived as unique or superior by customers. This is referred to as a **differentiation** approach.

Firms that choose a differentiation approach offer products or services that have unique features or attributes. They aim to create higher value than competitors' products or services. They invest heavily in advertising in general and brand building in particular.

Firms that choose a differentiation approach add value to the products and services they offer. They are responsive to customer preferences, and this can increase costs. They invest in research and development and innovation. Their customers are willing to pay a premium for products and services because of distinct product features, customer service, and the perception that the product is superior to those offered by competitors. The primary driver of the differentiation approach is value, and this is most influenced by product features, customer service, and perception of quality.

A differentiation approach involves offering products or services that are perceived as unique or superior by customers, allowing firms to stand out in the marketplace. Companies pursuing this approach focus on developing features, quality, brand identity, or customer experiences that go beyond what competitors offer. By doing so, they hope to attract customers who are willing to pay a premium for these distinctive qualities. This approach is particularly effective in industries where customers value innovation, quality, customization, or specialized expertise over just price.

Instead of competing on price, the objective is to create a product or service that customers are willing to pay a premium for because it meets needs in ways that rivals cannot easily replicate. Companies that follow a differentiation approach often offer cutting-edge technology, superior design, and a strong brand identity. Differentiation can be achieved through various means, including innovation, superior customer service, or the creation of a prestigious brand image. However, this strategic market position often requires significant investment in research and development, marketing, and customer engagement.

A differentiation approach works well when firms differentiate their products and services in ways that are difficult for rivals to duplicate or imitate, such as through company reputation, long-standing relationships with buyers, and a unique product or service image. Differentiating along these dimensions creates substantial switching costs that lock in buyers. Patent-protected product innovation and relationship-based customer service can also be success factors for a company following a differentiation strategy. Differentiation also works well when there are many ways that differentiation can have value to buyers and there is rapid change in the product's technology and features.

For example, Apple exemplifies the differentiation approach to strategic market position by offering cutting-edge technology, superior design, and a strong brand identity.

Advantages

Differentiation offers significant advantages to firms that can successfully execute it. One of the primary benefits is the ability to command premium prices for products or services, as customers are often willing to pay more for offerings they perceive as unique or superior. This premium pricing not only boosts profit margins but also allows companies to reinvest in continuous innovation, marketing, and customer service. For example, Tesla has been able to charge significantly higher prices than traditional automakers due to the perceived value of its cutting-edge technology, superior design, and sustainable approach to transportation.

Another advantage of differentiation is the potential for strong brand loyalty. When customers feel that a company offers something truly distinctive, whether it's exceptional quality, innovative features, or a unique experience, they are more likely to remain loyal to the brand. This loyalty can reduce price sensitivity, making customers less likely to switch to a competitor, even if that competitor offers a lower price. For example, buyer loyalty is extremely common for smartphone users.

Disadvantages

A differentiation approach also comes with its challenges. One of the most significant disadvantages is the higher cost structure associated with maintaining differentiation. Companies must invest heavily in research and development, marketing, and customer service to ensure that their products or services remain distinct and relevant in the marketplace. This constant need for innovation can strain resources, especially if competitors begin to catch up or replicate similar features.

Another disadvantage is the risk of imitation by competitors. In highly competitive markets, rivals may quickly copy the features or innovations that originally differentiated the product. As competitors adopt similar technology, designs, or service enhancements, the perceived uniqueness of the original product may diminish over time. This can erode the firm's competitive advantage, forcing it to lower prices or further invest in differentiation to maintain its market position.

Another disadvantage is that customers' own perception of quality is a crucial element in them continuing to buy luxury items. If a company following a differentiation approach offers discounts that are too deep, this can have negative ramifications on customers' perception of the quality of its offerings.

Video 8.1: Differentiation Strategy [04:28]

The video discusses differentiation strategy.

Access this YouTube video by scanning the QR code.

**Application**

- In the next sections, you are asked to apply what you learn about business-level strategies to companies not discussed in the text. Think about companies you know and like, rather than looking up examples online. By applying your knowledge about business-level strategies to these companies, you lock in your learning.
 - Describe three companies not discussed in the text that follow a cost leadership approach to strategic market position. Explain your rationale.
 - Discuss the advantages and disadvantages of following a cost leadership approach for these companies.
 - Describe three companies not discussed in the text that follow a differentiation approach to strategic market position. Explain your rationale.
 - Discuss the advantages and disadvantages of following a differentiation approach for these companies.

Key Takeaways

The first critical strategic decision when deciding a firm's business-level strategy is to define the firm's strategic market position. When a firm distinguishes itself in the market by responding to consumer preferences for low-cost alternatives, the company competes primarily by being the lowest-cost producer or provider in its chosen market. The goal is to offer products or services that are of an equal or similar value to competitors' products or service at a price lower than competitors. This is called a cost leadership approach, and it appeals to cost-conscious customers. While cost leadership provides a competitive edge, it can lead to diminished product quality or innovation, resulting in lower perceived value by customers if the focus on cost-cutting becomes too extreme. The cost leadership strategic market position is highly sensitive to external cost changes, such as rising raw material prices or supply chain disruptions, and such a firm is often susceptible to imitation by competitors, which can erode the firm's competitive advantage. Firms pursuing this strategic market position must carefully balance cost reduction with maintaining enough value in their offerings to satisfy customers. Companies that can navigate these challenges effectively can enjoy sustained profitability, but those that rely too heavily on cost cutting without innovation or differentiation may find themselves outpaced by more adaptable competitors.

When a firm distinguishes itself in the market by responding to consumer preferences for luxury items, the company competes primarily by offering products or services that are perceived as unique or superior by customers. This is referred to as a differentiation approach. Differentiation offers firms substantial advantages in terms of premium pricing and customer loyalty, but it also requires significant

investment and exposes the firm to competitive threats. Companies that follow a differentiation approach benefit from strong customer relationships and pricing power but must also navigate the high costs of maintaining their unique offerings and the risk of competitors imitating their innovations. Differentiation is a dynamic strategic market position that requires constant innovation, deep market understanding, and a sustained commitment to providing superior value to customers. While it can lead to long-term success, firms must continuously evolve to protect their differentiated position in the market. Differentiation allows firms to charge higher prices by offering unique products or services that customers perceive as superior, fostering strong brand loyalty and reducing price sensitivity. Differentiation requires significant investment in research and development, marketing, and customer service to maintain the perceived uniqueness of the offering, which can strain profitability over time. Competitors can erode a firm's competitive advantage by imitating the features or innovations that initially set the differentiated product apart, forcing the firm to continuously innovate to stay ahead.

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8.5 Strategic Market Size: Broad and Focused

The second critical decision that firms make when deciding their business-level strategy concerns the company's strategic market size. Like the firm's strategic market position, a company's strategic market size is also a decision based on the firm's customers. The strategic market size defines whether the firm will target a broad market, serving many customer segments, or a narrow market, focusing on a specific niche market segment.

If the approach is broad, the target market is broad, meaning most people within that industry buy the product or service. If the approach is focused, the target market is narrow, and the product or service is not meant for most people in the industry. Sometimes strategic market size is referred to as scope of operations or competitive scope.

Broad

A **broad approach to strategic market size** targets large markets, typically encompassing a wide range of customer groups. These strategies aim to appeal to as many customers as possible by offering products or services designed to meet diverse customer needs and preferences. By leveraging economies of scale and broad market reach, firms employing this approach seek to dominate their industry and build a strong competitive position. Broad approaches are often associated with significant operational scale, extensive distribution networks, and the ability to serve a diverse customer base efficiently. The goal of a broad strategic market size is to achieve widespread market penetration and long-term sustainability by serving the needs of a diverse customer base.

For example, Walmart targets in a broad strategic market. Its products appeal to a large and diverse customer base.

Advantages

One advantage of a broad strategic market size is the ability to achieve economies of scale. By serving a large customer base, firms can lower their per-unit costs through higher production volumes, enabling them to price competitively.

Another advantage of a broad approach is the potential for extensive market coverage and revenue generation. By targeting large, diverse markets, firms can access multiple customer groups, maximizing their sales potential.

A third advantage is that broad approaches also help firms build brand recognition and customer loyalty. A well-recognized brand that appeals to a wide audience can establish connections with customers and help to secure a firm's competitive position.

Additionally, firms that adopt a broad strategic market size benefit from reduced dependency on any single customer groups. This diversification allows them to be more resilient to changes in consumer preferences or economic conditions.

Finally, broad approaches enable firms to create or maintain entry barriers for competitors. Extensive market coverage, brand equity, and economies of scale make it challenging for new entrants to compete effectively, reinforcing the firm's market dominance.

Disadvantages

One major disadvantage of a broad strategic market size is the complexity of managing operations. Serving a large and diverse market requires extensive resources, including multiple product lines, varied distribution channels, and significant administrative oversight. This operational complexity can result in inefficiencies and higher costs.

Another disadvantage is the risk of diluted focus. Broad approaches often require firms to cater to the general needs of many customer groups, which may prevent them from meeting the specific needs of individual groups. This lack of specialization can leave the firm vulnerable to competitors employing focused approaches that target niche market segments more effectively.

Staying competitive across a wide market often requires substantial resources, which can strain profitability. In industries with intense competition, this challenge is even more pronounced.

Expanding a brand to appeal to a broad audience can also dilute its identity. When a firm attempts to serve too many customer groups, it risks alienating its core audience. For example, luxury brands that adopt a broad approach may lose their exclusive appeal, reducing their differentiation from competitors.

Finally, firms pursuing a broad strategic market size face intense competition from other large players targeting the same markets. This competition can lead to price wars, reduced profit margins, and challenges in sustaining a competitive advantage. A broad approach to strategic market size requires continuous effort to remain relevant and efficient in highly contested markets.

Focused

A **focused approach to strategic market size** targets specific niche markets segments. Focused strategic market segments allow firms to understand and cater to the specific needs of a niche market segment, fostering customer loyalty by offering tailored products or services that meet the unique demands of their target market segment. By concentrating on a narrow market segment, firms that follow a focused approach can reduce direct competition, but the small size of the niche market segment limits long-term growth opportunities and may constrain economies of scale. Focused strategic market segments are highly vulnerable to changes in customer preferences and can be threatened by larger competitors entering the niche market segment, leveraging their resources and scales to replicate or surpass the focused firm's offerings. Focused approaches allow firms to serve niche market segments with precision and build customer loyalty, but they also come with risks, such as limited market size, vulnerability to market shifts, and the threat of competition from larger rivals. Firms pursuing focused strategic market segment must stay vigilant in maintaining their unique value proposition while being prepared to adapt to changes in their niche market segment.

For example, Apple follows a focused approach to strategic market size. They serve a market segment that is interested in high quality products with the latest technology.

Advantages

One of the primary advantages of a focused approach is that they allow firms to deeply understand and cater to the specific needs of a niche market segment. By concentrating on a well-defined customer segment, companies can offer tailored products or services that align closely with the preferences, behaviors, and demands of their target market segment. This precision leads to stronger customer loyalty, as the specialized nature of the offering makes it difficult for competitors to meet the same level of personalization or relevance.

Another advantage of focused strategies is the reduced competition within the niche market segment. Firms employing a focused strategy can carve out a space in underserved or overlooked areas of the market, reducing direct rivalry. By serving specific groups more effectively than larger, more generalist competitors, these firms can establish strong market positions without having to constantly fend off well-resourced competitors.

Additionally, focused approaches enable firms to maximize resource efficiency by concentrating on a single market segment. Companies can align their operations, marketing, and product development efforts specifically with the needs of their niche market segment, reducing waste and avoiding the complexity of serving a broad, diverse market.

Companies adopting a focused approach often build significant expertise in their products and services to attract customers to their specialty stores, such as camping shops that offer customers expert advice in maximizing their limited vacation times.

Disadvantages

Focused approaches come with several disadvantages. One major risk is the limited market size. By concentrating on a narrow, niche market segment, firms may struggle to achieve the economies of scale available to competitors with broader market reach. The small size of the target market segment means that growth opportunities are often constrained, limiting the potential for long-term scalability. Demand for specialized goods and services is limited, making each sale critical. For instance, a company that succeeds in a very specific market segment, such as high-end luxury goods, may find it difficult to expand beyond that market segment without losing its specialized appeal.

Another disadvantage is the vulnerability to changes in the niche market. If customer preferences shift or technological advancements alter the landscape, companies employing focused approaches may find it difficult to adapt without fundamentally changing their business models. When a firm's competitive advantage is built on serving a very specific group, any changes in customer demand can significantly impact the firm's success.

Finally, focused approaches are vulnerable to competitors who decide to enter the niche market. Larger firms with more resources might recognize the profitability of the niche market segment and begin targeting it with similar offerings.

Video 8.2: Focused Strategy [03:47]

The video for this lesson explains that focused strategies concentrate on a narrow segment of the total market.

Access this YouTube video by scanning the QR code.



Application

- The second critical decision that firms make when deciding their business level strategy is determining the company's strategic market size.
 - Describe three companies not discussed in the text that follow a broad approach to strategic market size. Explain your rationale.
 - Discuss the advantages and disadvantages of following a broad approach to strategic market size for these companies.
 - Describe three companies not discussed in the text that follow a focused approach to strategic market size. Explain your rationale.
 - Discuss the advantages and disadvantages of following a focused approach to strategic market size for these companies.

Key Takeaways

The second critical decision that firms make when defining their business-level strategy concerns the company's strategic market size. Like the decision about the firm's strategic market position, this decision is also based on the firm's customers. The strategic market size defines whether the firm will target a broad market segment or a focused market segment. If the approach is broad, the strategic market is broad and serves many customer groups, and most customers in an industry buy the product or service. If the approach is focused, the strategic target market is narrow, a niche market segment, and the product or service is not meant for most people in the industry.

Targeting a broad strategic market size enables firms to achieve economies of scale, expand market reach, and build strong brand recognition. A broad approach also brings challenges like operational complexity, diluted focus, and intense competition. Firms pursuing a broad approach must balance efficiency and innovation to serve diverse customer needs while maintaining competitiveness in a large and often contested market.

Focused approaches to strategic market size allow a firm to deeply understand and cater to the specific needs of a niche market segment, fostering strong customer loyalty by offering tailored products or services that meet the unique demands of the target market segment. By concentrating on a narrow market segment, firms that follow a focused approach can reduce direct competition, but the small size of the market segment limits long-term growth opportunities and may constrain economies of scale. Focused approaches are highly vulnerable to changes in customer preferences and can be threatened by larger competitors entering the niche market segment, leveraging their resources and scale to replicate or surpass the focused firm's offerings. Focused approaches allow firms to serve niche market segments with precision and build strong customer loyalty, but they also come with risks, such as limited market size, vulnerability to market shifts, and the threat of competition from larger rivals. Firms pursuing focused approaches must stay vigilant in maintaining their unique value proposition while being prepared to adapt to changes in their niche market segment.

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8.6 Six Business-Level Strategies

So far you have learned that business-level strategy involves two critical decisions. The first addresses a firm's strategic market position and considers whether the firm follows a cost leadership or a differentiation approach. The second addresses a firm's strategic market size and addresses whether a company concentrates on a broad market segment called a broad approach or a narrow market segment called a focused approach.

Now let's consider how these two dimensions dynamically interact to suggest six business-level strategies: broad cost leadership, focused cost leadership, broad differentiation, focused differentiation, best-cost strategy, and blue ocean strategy. Each offers distinct paths to achieving competitive advantage.

Key Takeaways

Strategic market position and strategic market size dynamically interact to suggest six business-level strategies: broad cost leadership, focused cost leadership, broad differentiation, focused differentiation, and two hybrid strategies known as best-cost strategy and blue ocean strategy.

8.7 Broad Cost Leadership

A **broad cost leadership strategy** is a business-level strategy that combines a broad strategic market size and a cost leadership strategic market position. The firm distinguishes itself in the market by responding to consumer preferences for low-cost alternatives and competes primarily by being the lowest-cost producer in its industry. This is the cost leadership element of the company's business-level strategy. The company is also targeting a broad market, meaning most people within that industry buy the product or service.

Firms that pursue a broad cost leadership business-level strategy focus on achieving operational efficiency, leveraging economies of scale, and controlling overhead costs. This strategy is particularly effective in industries where price is the primary driver of customer decisions, such as retail, transportation, or basic consumer goods.

Walmart is an excellent example of a company following a broad cost leadership strategy by streamlining their supply chains and keeping operating costs low to offer lower prices than competitors. Walmart uses its massive supplier network and distribution capabilities to offer low prices to a broad market, securing its leadership in cost-effective retail. Walmart focuses on selling products of an equal or similar quality than its competitors at a lower cost, and most people in the market shop at Walmart. If a customer is purchasing a consumable product like tissue and decides to purchase a name brand product, then it is likely that Walmart has the economies of scale to sell those name brand consumables at a lower cost than most of its competitors. However, if a consumer decides to buy a store brand product, the consumer may consider Walmart's products to be of a lesser quality though still just good enough to purchase. In this case, although the store brand consumable product may not be of an equal or similar quality than its competitors, consumers prioritize cost savings over quality. Walmart's range of products allows it to be an attractive option for many price-sensitive customers.

McDonald's is another example of a company that follows a broad cost leadership strategy. McDonald's uses a standardized menu in many countries and negotiates bulk purchasing agreements, allowing the company to keep costs low while maintaining consistent quality across its global locations. This approach enables McDonald's to offer affordable meals that appeal to a broad customer base, making it a leader in the fast-food industry.

Spotify's free version operates on an ad-supported model that attracts a broad audience with no upfront cost. However, this low-cost strategy depends on having a large user base to generate sufficient ad revenue. Therefore, this Spotify service follows a broad cost leadership business-level strategy. Spotify's dependency on maintaining high volumes creates financial pressure and limits flexibility, as Spotify must continuously cater to and retain a vast user base to sustain profitability on its free tier.

Hulu's low-cost, ad-supported model also follows a broad cost leadership business-level strategy. The ad-supported model allows it to offer affordable streaming options, but it has also restricted its ability to evolve with customer demands by failing to add premium features to their service, such as offline downloads. The broad cost leadership business-level



i'm lovin' it

Figure 8.3: McDonald's

strategy allows them to meet one market and limits their ability to respond to new customer preferences, which in turn affects their competitiveness in the overall marketplace.

Procter & Gamble follows a broad cost leadership business-level strategy by offering a range of affordable household products. This ensures steady revenue streams even as market demands fluctuate.

Company	Example
Walmart	Walmart's broad cost leadership strategy relies on drawing on a huge customer base and maintaining low prices by purchasing goods in massive quantities from suppliers.
McDonald's	McDonald's sells inexpensive fast food to a very broad market. McDonald's Dollar Menu targets price-conscious fast-food customers by providing them with low-cost menu options, offering value-focused meals to attract budget-oriented customers. This strategy has helped McDonald's remain the largest fast-food chain in the world with over forty thousand restaurants in over one hundred countries.
Dunkin' Donuts	Although it's known for doughnuts, Dunkin' Donuts generates more revenue from selling cheap coffee.
Supercuts	Supercuts highlights its long-established cost leadership strategy on its website, stating, "A Supercut is a haircut that has kept people looking their best, while keeping money in their pockets, since 1975."
Little Debbie	Little Debbie snack cakes originated in the early 1930s, when O.D. McKee sold treats for just five cents each. Though prices have risen since then, Little Debbie cakes remain much cheaper than similar products sold by their competitors, Entenmann's and Tastykake.
Planet Fitness	The commercial gym Planet Fitness has become a rapidly growing business thanks to its affordable membership model, appealing to a broad customer base and securing a strong market share in the gym industry.
Netflix	Netflix, with its budget-friendly streaming service, offers a basic plan that can withstand price wars, as higher-priced competitors often avoid direct competition with more efficient, lower-cost options.
Papa Murphy's	Papa Murphy's focuses its affordable "take-and-bake" pizzas on budget-conscious families. Because the pizzas are baked at home, the company can accept food stamps, enabling Papa Murphy's to serve customers who might not typically purchase restaurant-quality pizza.
Costco	Costco provides its members with bulk buying options, with a focus on low-price, high-volume products. By selling huge amounts and requiring a membership fee, Costco can reduce per-unit costs, appealing to customers who are willing to buy in bulk to save money.

Figure 8.4: Broad cost leadership strategy examples

Application

- A broad cost leadership business-level strategy is a business-level strategy that combines a broad strategic market size and a cost leadership strategic market position.
 - Describe three companies not discussed in the text that follow a broad cost leadership business-level strategy. Assess whether this is a strong strategy for companies. Explain your rationale.

Key Takeaways

A broad cost leadership strategy is a business-level strategy that combines a broad strategic market size and a cost leadership strategic market position. The strategy is effective when most people within the market buy the product or service and those customers are price-sensitive customers. A firm that pursues a broad cost leadership strategy targets most consumers in an industry, distinguishes itself in the market by responding to consumer preferences for low-cost alternatives, and competes primarily by being the lowest-cost producer in its industry. The goal is to offer standard products or services at a price lower than competitors, appealing to a broad base of cost-conscious customers.

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8.8 Focused Cost Leadership

Firms that pursue a **focused cost leadership strategy** target a narrow market segment that prefers low-cost products. The firm distinguishes itself in the market by responding to consumer preferences for low-cost alternatives and competes primarily by being the lowest-cost producer in its industry, appealing to cost-conscious customers. This is the cost leadership element of the company's business-level strategy. The company is also following a focused strategy, which means the company is concentrating on a target market segment that is a narrow, niche market and that the product or service is not meant for most people in the industry. The firm's strategic market position is cost leadership, and its strategic market size is focused. Focused cost leadership involves offering products or services at the lowest price within a defined market segment, catering to a particular group of cost-conscious customers.

Focused cost leadership strategy involves a company targeting a specific niche market segment while maintaining a low-cost structure to serve that market. The focus is not on competing broadly across all market segments but on tailoring products or services to meet the specific needs of a defined group of customers. Companies that pursue this strategy aim to be the lowest-cost provider in their niche, offering affordable solutions without the broad operational scope required by larger competitors. By zeroing in on a smaller market segment, firms can better align their resources, capabilities, and core competencies to maximize efficiency and minimize costs while addressing the unique needs of their customers.

Dollar General, for instance, employs a focused cost leadership strategy by targeting rural and small-town customers with low-cost, basic goods. Dollar General's business model is built around keeping operational costs low, including a focus on smaller store footprints and private-label goods, which helps reduce purchasing and distribution costs. By focusing on price-sensitive customers in underserved areas, Dollar General effectively captures a niche market segment that is less competitive than the broader retail market dominated by companies like Walmart. Its ability to offer affordable goods in convenient, smaller locations makes it attractive to customers who prioritize convenience and low prices. Dollar General has been able to thrive in rural, lower-income areas where larger retailers like Walmart have less presence, leveraging its focused cost leadership approach to dominate that market segment.

Another example of a company that follows a focused cost leadership strategy is Ryanair, which has become a dominant player in the European budget airline industry by targeting budget-conscious travelers. Unlike full-service airlines, Ryanair offers extremely low base fares by stripping away all nonessential services and charging extra for things like luggage, seat selection, and food. This no-frills approach is designed specifically for customers who prioritize price over comfort. Ryanair's focused cost leadership strategy includes using secondary airports and maintaining a standardized fleet, both of which contribute to keeping costs down. By catering to a niche market segment of cost-sensitive travelers willing to sacrifice convenience and amenities for lower fares, Ryanair has successfully built a strong presence in the highly competitive airline industry.

The success of focused cost leadership hinges on the company's ability to tightly manage costs while meeting the essential needs of its target market segment. Firms often achieve this by offering fewer product variations, reducing complexity in their supply chains, and simplifying operational processes. For example, Dollar General minimizes store sizes and product variety to keep overhead costs low, passing those savings on to customers through lower prices. Similarly, Ryanair's use of secondary airports not only reduces airport fees but also allows for faster turnaround times, enabling more flights per day. In both cases, the companies have honed in on a specific customer market segment that values affordability above all else, tailoring their business models to meet those expectations.

This strategy is particularly effective when there is a segment of the market that is underserved by broader competitors. In the case of Dollar General, major retailers often overlook smaller, rural markets, allowing the company to step in and dominate those areas with its focused, low-cost approach. Similarly, Ryanair has found a niche in the European market where cost-conscious travelers are looking for the cheapest possible airfare, even if it means sacrificing comfort. By understanding and capitalizing on the specific needs of its niche market, the company has created a strong competitive position within its industry while maintaining low operational costs.

Another example of focused cost leadership is Xiaomi, the Chinese electronics and smartphone company. Xiaomi has grown rapidly by implementing a focused cost leadership strategy in the highly competitive smartphone industry. Unlike major players like Apple or Samsung, Xiaomi minimizes costs by selling its devices primarily through e-commerce, cutting out intermediaries, and maintaining extremely low profit margins on hardware. In addition, the company generates revenue through software, apps, and internet services, allowing it to offer high-quality smartphones at significantly lower prices than its competitors. Xiaomi's ability to deliver affordable yet innovative devices has enabled it to rapidly expand its market share, particularly in developing markets, by appealing to price-sensitive consumers without sacrificing product quality. Less-expensive smartphones from companies such as budget-friendly brands like Xiaomi and Realme can offer smartphones with the same competitive features as flagship models from Apple and Samsung, such as high-refresh-rate screens, decent cameras, and a solid performance for everyday tasks at a fraction of the price. These alternatives attract price-sensitive buyers who want a good smartphone without paying premium prices. Imitation

devices and lookalike smartphones closely resemble popular flagship models and are often sold by street vendors and online marketplaces. This can result in budget-conscious buyers straying away from the original brand, diluting their exclusivity.

Aldi, the German-based grocery retailer, is another example of a company that follows a focused cost leadership strategy. Aldi has made a significant impact in various global markets, including the United States. Aldi's success is rooted in its rigorous cost-cutting measures. The company reduces operational expenses by offering a limited selection of private-label products. Requiring customers to bring their own shopping bags and deposit coins to use shopping carts is standard procedure in global markets, such as the United Kingdom. They are less common in the United States. These efficiency-driven and sustainability-focused practices allow Aldi to keep prices significantly lower than traditional grocery chains while maintaining quality standards that appeal to budget-conscious shoppers. By focusing on operational simplicity and scale, Aldi has effectively maintained a competitive position in the crowded grocery market.

Company	Example
Five Below	Five Below uses a focused cost leadership strategy, appealing to their narrow target market segment of preteens and young adults by keeping everything in their store \$5 or less.
Dollar General	Dollar General targets a niche demographic, primarily lower-income consumers in rural and small-town areas, by offering a limited selection of low-cost products.
Ryanair	Ryanair has become a dominant player in the European budget airline industry by targeting budget-conscious travelers.
Aldi	Aldi, the German-based grocery retailer, has made a significant impact in various global markets, including the United States. Aldi offers their customers the essential groceries but at a much lower price by reducing their operational costs such as limiting product choices, limiting their staff and creating simple store layouts. This allows Aldi's to target cost-conscious consumers who prioritize savings over premium brands.
Claire's	Claire's targets young women with inexpensive jewelry, accessories, and ear piercing.

Figure 8.5: Focused cost leadership strategy examples

Application

- A focused cost leadership business-level strategy is a business-level strategy that combines a focused strategic market size and a cost leadership strategic market position.
 - Describe three companies not discussed in the text that follow a focused cost leadership business-level strategy. Assess whether this is a strong strategy for companies. Explain your rationale.

Key Takeaways

A focused cost leadership strategy is a business-level strategy that combines a narrow strategic market size and a cost leadership strategic market position. This strategy is effective when few consumers within the market buy the product or service and those customers are price sensitive customers. Firms that pursue a focused cost leadership strategy target a niche market segment by responding to con-

sumer preferences for low-cost alternatives, competing primarily by being the lowest-cost producer in its industry. The goal is to offer standard products or services at a price lower than competitors, appealing to cost-conscious customers in a narrow strategic market.

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8.9 Broad Differentiation

Firms that pursue a **broad differentiation strategy** target a broad market and customers who want a quality product. A firm distinguishes itself in the market by responding to consumer preferences, typically for luxury items. A company using such a strategy competes primarily by offering products or services that are perceived as unique or superior by customers. This is the differentiation element of the business-level strategy. If the company is also following a broad strategy, this means it is concentrating on a target market that is broad, meaning most people within that industry buy the product or service. The firm's strategic market position is differentiation, and its strategic market size is broad.

An example of a firm that follows a broad differentiation strategy is Marriott International, which differentiates itself through a wide range of premium accommodations and customer service, catering to both business and leisure travelers worldwide.

One significant advantage of broad differentiation strategies is the ability to attract a large customer base while maintaining higher profit margins. Customers are often willing to pay premium prices for products or services that they perceive as superior, allowing firms to sustain profitability despite higher production or marketing costs. Additionally, strong brand recognition and customer loyalty fostered by differentiation can provide long-term competitive advantages, reducing vulnerability to price-based competi-

tion. For example, BMW is able to command higher prices for its vehicles from a large worldwide consumer base that appreciates the admiration tied to the brand.

Broad differentiation also enables firms to adapt to diverse customer preferences. By offering products or services that appeal to a wide audience but maintain unique attributes, companies can meet the varied demands of their customer base, driving growth and market share. For instance, Toyota's Lexus brand targets luxury car buyers globally with a blend of premium quality, technology, and reliability.

Although broad differentiation can be beneficial, these strategies are accompanied with challenges as well. One major disadvantage is the significant cost of maintaining differentiation while serving a large, diverse market. High investments in research, development, branding, and marketing are often required to sustain a unique position, which can strain a firm's resources.

Firms pursuing broad differentiation are also vulnerable to imitation. Competitors with lower costs may attempt to replicate unique features or quality, eroding the firm's competitive advantage. For example, luxury fashion brands like Gucci often face competition from lower-cost brands or counterfeit producers that mimic their designs and style. These imitators can attract price-sensitive customers, potentially diluting the exclusivity and perceived value of the high-end brand.

Company	Example
Nordstrom	Nordstrom, as well as other department stores, like Macy's, builds a broad differentiation strategy around offering designer merchandise and providing exceptional service to a broad market.
Nike	Nike builds its broad differentiation strategy around its athletic products, including exclusive footwear, apparel, and sports equipment, using its strong household reputation, athletic endorsements, and continuous innovations to consistently appeal to audiences worldwide.
Ralph Lauren	Top-tier designer apparel line Ralph Lauren employs a broad differentiation strategy, offering exclusive items to a broad market.
FedEx	FedEx's former slogan, "When it absolutely, positively has to be there overnight," highlights the commitment to very speedy delivery that differentiates them from competitors such as UPS and the U.S. Postal Service.
Airbnb	Airbnb's strategy is to differentiate themselves by providing unique and diverse lodging experiences internationally, from treehouses to farmhouses, setting them apart from traditional hotel chains. Airbnb's brand focuses on local experiences and owner personalization, which appeals to guests who are looking for something different from the typical hotel.

Figure 8.6: Broad differentiation strategy examples

Application

- A broad differentiation business-level strategy is a business-level strategy that combines a broad strategic market size and a differentiation approach to strategic market position.
 - Describe three companies not discussed in the text that follow a broad differentiation business-level strategy. Assess whether this is a strong strategy for companies. Explain your rationale.

Key Takeaways

A broad differentiation strategy is a business-level strategy that combines a broad strategic market size and a differentiation approach. This strategy is effective when most consumers within the market buy the product or service and those customers want a quality product. Broad differentiation combines the advantages of offering unique, high-quality products or services with the ability to appeal to a large, diverse customer base. This business-level strategy allows firms to command high prices and build brand loyalty, making it a powerful approach in competitive markets. However, broad differentiation requires significant investments in innovation, marketing, and operational efficiency to maintain a distinctive position while serving a wide audience. Companies must carefully balance broad market appeal with their unique value proposition to avoid diluting the brand or losing focus. The success of broad differentiation lies in continually delivering value that resonates across multiple customer segments while protecting the brand from imitation and maintaining its competitive edge.

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8.10 Focused Differentiation

A firm that pursues a **focused differentiation strategy** targets a narrow, niche market segment and offers quality products. The firm distinguishes itself in the market by responding to consumer preferences for luxury items, offering products or services that are perceived as unique or superior by customers. The company concentrates on a niche target market, and the product or service is not meant for most people in the industry. The firm's strategic market position is differentiation, and its strategic market size is

focused. Focused differentiation involves offering unique, differentiated products or services tailored to the specific needs of a niche market segment, allowing the firm to charge premium prices.

The focused differentiation strategy involves a firm targeting a specific niche market and offering products or services that are highly differentiated and tailored to meet the unique needs of that market segment. Focused differentiation concentrates on a particular consumer group with specific preferences or demands. The essence of this strategy is to provide something unique and valuable for which customers in the market will pay a premium. By doing so, firms can build strong customer loyalty and insulate themselves from price-based competition, as customers are drawn to the specialized nature of the product or service rather than any factor relating to price.

One of the primary characteristics of focused differentiation strategies is the ability to offer a product or service that is difficult for competitors to replicate. Companies that pursue this approach spend significant time and resources studying the needs, desires, and pain points of their target customers. By honing in on these unique characteristics, the firm can craft a highly specialized offering that resonates with the segment. For example, Ferrari focuses exclusively on high-performance luxury cars for affluent customers who value exclusivity, design, and engineering excellence. The company's focused differentiation strategy allows it to cater specifically to a small but wealthy market that is less sensitive to price and more concerned with brand prestige and performance.

The success of the focused differentiation strategy often hinges on brand loyalty and customer retention. Because the firm's product or service is so tailored to the specific needs of its niche market segment, customers develop strong brand loyalty and are less likely to switch to competitors. The emotional connection and perceived value of the specialized offering create a barrier to entry for other firms. This allows companies to build long-term relationships with their customers, fostering repeat business and reducing the threat of price competition. By continually innovating and maintaining a close connection with their market segment, focused differentiators can sustain a competitive advantage in the long run. Many individuals stay loyal to Apple due to their seamless connectivity across devices like the iPhone, iPad, Apple Watch, and MacBook. The integration of services, such as iCloud and AirDrop, incentivizes customers to stay with Apple in order for their devices to stay connected. Apple's focus on the creative professional market segment has allowed it to cultivate a highly loyal customer base willing to pay a premium for the brand's high-performance products.

However, the narrow strategic market size of focused differentiation means that firms must remain vigilant in staying aligned with the evolving needs of their quality-conscious customers. Changes in customer preferences or shifts in the market can quickly erode the competitive advantage if the firm fails to adapt. Additionally, the company's growth potential may be more limited compared to firms pursuing broader strategies because the company targets a smaller market segment. Nevertheless, for firms that can effectively cater to a specialized group and offer something truly unique, focused differentiation provides an opportunity to build a strong, loyal customer base and command premium prices, establishing a distinct market position.

One of the most prominent examples of a focused differentiation strategy is Tesla, which has redefined the automotive industry by offering electric vehicles (EVs) that combine luxury, sustainability, and advanced technology. Tesla's vehicles stand out for their long-range electric powertrains, high performance, and innovative software features, including autonomous driving capabilities. Beyond the product itself, Tesla has differentiated its brand by providing over-the-air software updates that continually enhance the functionality and performance of its cars, allowing customers to experience new features long after their initial purchases. Tesla's commitment to innovation, sustainable transportation, and cutting-edge design has created a loyal customer base that is willing to pay a premium for these exclusive benefits. This has positioned Tesla as a leader not only in the EV market but also in the broader technology and luxury spaces. By differentiating itself through innovation and performance, Tesla maintains a loyal customer base that values its products beyond just their functional capabilities.

While Tesla has enjoyed a significant lead in electric vehicle technology, other automakers are rapidly developing their own EV models, forcing Tesla to continuously innovate to maintain its competitive edge. This ongoing investment can put pressure on profitability, particularly if the firm is unable to justify premium pricing indefinitely. While Tesla's initial differentiation was its pioneering electric vehicle technology, other automakers like Ford and Volkswagen have introduced their own electric models, with some offering similar features at more competitive prices. The more these rivals imitate Tesla's differentiation points, the more difficult

it becomes for Tesla to maintain its premium positioning without introducing new innovations. This ongoing investment can put pressure on profitability, particularly if the firm is unable to justify premium pricing indefinitely.

A different but equally strong example of focused differentiation can be found in Palantir, a data analytics company that has set itself apart by offering highly specialized and customizable software solutions for governments and large enterprises. Palantir's differentiation lies in its ability to provide powerful, mission-critical tools that help organizations make sense of massive amounts of data for intelligence, defense, and commercial applications. Palantir's platforms, such as Gotham and Foundry, are renowned for their ability to integrate and analyze vast datasets, offering insights that drive key decision-making processes. What differentiates Palantir from other software companies is its deep collaboration with clients. Its software is not a one-size-fits-all solution but is tailored to the specific needs of each client, whether it be national security, public health, or financial services. This level of customization, combined with Palantir's expertise in handling highly sensitive data, has made it indispensable to clients that require precision, security, and flexibility, allowing the company to charge premium prices for its services and building long-term relationships with its clients. Because Palantir tailors its software to meet the exact needs of its clients, the switching costs for customers are high, and they are less likely to move to another provider, even if a cheaper option becomes available.

Both Tesla and Palantir demonstrate the power of focused differentiation to establish a strong market presence. Tesla's focus on innovative, luxury electric vehicles and Palantir's ability to provide customized, high-stakes data solutions have allowed both companies to build loyal customer bases and command premium pricing. By offering unique value propositions that competitors find difficult to replicate, these firms have carved out durable competitive advantages in their respective industries. Differentiation, when executed effectively, enables companies like Tesla and Palantir to transcend traditional price competition and build deeper connections with their customers based on the specialized benefits they offer.



Figure 8.7: Patagonia

Patagonia is another company that uses a focused differentiation business-level strategy. Patagonia is known for giving their consumers high-quality, durable outdoor clothing and for having a commitment to environmental activism through various environmental programs. This company targets eco-conscious adventurers that are willing to pay extra for sustainable products from a company that cares about the planet.

Success in focused differentiation comes from knowing the customer segment deeply and offering a product that is tailored specifically to their needs and preferences.

They differentiate themselves within the milk industry by promoting their strong environmental responsibility and sustainability as well as by using a marketing approach focused on humor to appeal to eco-conscious consumers and vegans by highlighting the benefits of oat milk over traditional dairy milk.

A focused differentiation strategy works well in industries where customer preferences are highly diverse and specialized products can command higher prices. Companies pursuing focused differentiation may target high-end customers, specific geographic regions, or niche needs within a broader market. Ferrari, for example, focuses on a luxury, high-performance car market, providing exclusive, differentiated vehicles to a narrow audience of high-end consumers. Success in focused differentiation comes from knowing the customer segment deeply and offering a product that is tailored specifically to their needs and preferences.

Oatly, a Swedish food company, specializes in plant-based milk made from oats.



Figure 8.8: Oatly

Company	Example
Anthropologie	Anthropologie follows a focused differentiation strategy by selling distinctive and expensive women's apparel, accessories, and home furnishings.
Bombas	Bombas follows a focused differentiation strategy by selling premium socks with a social mission, as Bombas donates a pair of socks to someone in need for each pair purchased. By combining quality and purpose, Bombas is able to attract wealthy and socially conscious consumers.
Bergdorf Goodman	Top-tier department stores like Bergdorf Goodman, as well as Saks Fifth Avenue and Von Maur, build a focused differentiation strategy around offering designer merchandise and providing exceptional service in limited markets segments.
REI	Recreational Equipment Incorporated (REI) is able to charge high prices for outdoor gear and clothing from strong brands such as North Face and Marmot.
Whole Foods	Whole Foods Market specializes in offering natural and organic products free from hydrogenated fats and artificial colors, flavors, and preservatives. However, this supermarket is often referred to as "Whole Paycheck" due to its high prices, though many shoppers are willing to pay extra for the reassurance of healthier food choices.
Tesla	Tesla offers electric vehicles that combine luxury, sustainability, and advanced technology.
Palantir	Palantir is a data analytics company that has set itself apart by offering highly specialized and customizable software solutions for governments and large enterprises.
Apple	Many individuals stay loyal to Apple due to their seamless connectivity across devices like the iPhone, iPad, Apple Watch, and MacBook. The integration of services, such as iCloud and AirDrop, incentivizes customers to stay with Apple in order for their devices to stay connected.
Peloton	Peloton's strategy to differentiate themselves within the fitness industry involves taking high-end luxury workout equipment and adding a digital platform that offers a sense of community through live and on-demand fitness classes. Peloton's interactive content provides their users with a community feel, offering exclusive instructors that create a fun fitness experience that differs from traditional gyms and workout equipment brands.
Google	Google's Pixel line stands out with the AI feature Magic Eraser that removes unwanted objects from photos and enhanced Night Sight, which improves the quality of low-light photography. These camera capabilities draw in photography enthusiasts who are willing to pay more for these features on their phones.
Patagonia	Patagonia is a company known for giving their consumers high-quality, durable outdoor clothing with a commitment to environmental activism through various environmental programs. This company targets eco-conscious adventurers that are willing to pay extra for sustainable products from a company that cares about the planet.
Cinnabon	While cinnamon rolls are available elsewhere cheaper, Cinnabon's delicious pastries are so irresistible that sweet-toothed customers will happily line up for them. Fittingly, Cinnabon is owned by the parent company called Focus Brands, perhaps reflecting their strategic approach.
Mercedes-Benz	The German automobile company Mercedes-Benz has a strong commitment to advanced technology, stylish design, and safety innovations, which has made the company's vehicles highly valued among affluent buyers.

Figure 8.9: Focused differentiation strategy examples

Application

- A focused differentiation business-level strategy is a business-level strategy that combines a focused strategic market size and a differentiation approach to strategic market position.
 - Describe three companies not discussed in the text that follow a focused differentiation business-level strategy. Assess whether this is a strong strategy for companies. Explain your rationale.

Key Takeaways

A focused differentiation strategy is a business-level strategy that combines a narrow strategic market size and a differentiation approach. Few customers within the market buy the product or service, and those customers who do want a quality product. Firms that pursue focused differentiation strategies distinguish themselves in the market by responding to consumer preferences for luxury items. The companies compete primarily by offering products or services that are perceived as unique or superior by customers in a niche market segment.

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8.11 Best-Cost Strategy

There are two business-level strategies that rely on combining a cost leadership approach and a differentiation approach. The first is a **best-cost strategy**, a hybrid approach that combines elements of both cost leadership and differentiation in an existing market or market segment.

A best-cost strategy allows firms to offer products or services with superior features at lower prices than competitors. This strategy seeks to deliver more value to customers by providing high quality while keeping costs lower than rivals who offer similar levels of quality.

By offering both superior quality and competitive pricing, firms employing this strategy can attract both price-conscious consumers and those who are willing to pay a bit more for added value. This dual appeal allows companies to capture market share from both low-cost competitors and premium brands.

To successfully implement a best-cost strategy, companies must tightly control costs while continuing to invest in features or attributes that enhance the perceived value of their offerings. This requires efficient operations, strong supply chain management, and a focus on innovation. Firms need to leverage technology, economies of scale, and operational efficiency to keep production costs down, allowing them to offer competitive pricing without sacrificing quality.

Strategic Market Position: A Continuum

For firms that implement broad cost leadership, focused cost leadership, broad differentiation, or focused differentiation business-level strategy, an assumption is that the two dimensions that underpin these strategies consist of two primary and opposing choices. As you recall, a firm defining its strategic market position either follows a cost leadership strategy and appeals to cost-conscious customers or it follows a differentiation strategy and appeals consumer preferences for luxury items. When defining a company's strategic market size, a firm either follows a focused approach, targeting a narrow, niche market segment or a broad approach, targeting a broad market.

A best-cost strategy primarily focuses on this first dimension, strategic market position. A best-cost strategy is based on the starting premise that the choice of strategic market position is a continuum of choices, with pure cost leadership at one end and pure differentiation at the other. There are many points along the strategic market position continuum that represent varying degrees of cost leadership and differentiation.

In practice, firms that follow a best-cost strategy aim to balance offering some degree of luxury with offering as low a cost as possible. Firms compete, at least indirectly, with both cost leadership and differentiation rivals. They often aim to acquire market share from rivals using both cost leadership and differentiation strategies.

Although best-cost strategy primarily addresses strategic market position, all firms using this strategy must also choose their strategic market size. A best-cost strategy is based on the assumption that the choice of a strategic market size is also a continuum of choices, with a pure focused approach at one end and a pure broad approach at the other. There are many points along the continuum that represent varying degrees of targeting a narrow niche market segment through a focused approach and targeting a broad market through a broad approach.

For example, IKEA uses a best-cost strategy by offering stylish, well-designed furniture at affordable prices. While customers could find cheaper options at discount furniture stores or more luxurious items at high-end retailers, IKEA's combination of modern design and reasonable pricing allows it to appeal to both markets, giving customers the perception of high value.

Toyota uses a best-cost strategy with its Lexus brand, offering luxury features at lower prices than traditional luxury automakers like Mercedes-Benz or BMW. Toyota achieves this balance by leveraging its efficient manufacturing processes and economies of scale, keeping costs low while maintaining high quality in its Lexus line. Lexus appeals to customers who may not be able to afford more luxury vehicles or who choose not to spend their money on more expensive automobiles from a value perspective but who still want a little luxury at a reasonable price.

Another example of a company that follows a best-cost strategy in the fast-fashion industry is Zara. Zara has successfully employed a best-cost strategy by offering trendy, stylish clothing at relatively affordable prices. Zara's ability to quickly produce fashion-forward designs while maintaining competitive pricing gives it an edge over both lower-cost fast-fashion competitors and more expensive designer brands.

Advantages

A best-cost strategy can achieve a strong competitive advantage. The ability to offer customers more value for their money—high-quality products at reasonable prices—creates a compelling proposition in many markets. Companies that master this strategy can

build a loyal customer base and protect themselves from competitive pressures by offering a unique blend of cost efficiency and quality. The best-cost strategy allows firms to occupy a middle ground between cost leadership and differentiation, giving them flexibility and broad appeal.

Disadvantages

The best-cost strategy can be challenging to execute because it requires excellence in both cost management and differentiation, which are different strategies with different trade-offs. Firms must be able to provide features or qualities that customers value while maintaining low-cost structures. Balancing the cost driver of cost leadership and the value driver of differentiation is difficult in practice.

This best-cost strategy works well in a market where customers want *both* a little luxury and affordability, but it might not be as effective in markets or market segments where customers prioritize *either* luxury or the lowest possible price. The strategy works best in markets where customers want products that offer enhanced features but are not willing to pay premium prices, combining differentiation and affordability. The goal of the best-cost strategy is to strike a balance, offering customers more value for their money without sacrificing profitability.

Company	Example
Southwest Airlines	Southwest Airlines offers low-cost flights to a limited number of vacation destinations, a strategy resembling a cost leadership strategy. Additionally, Southwest provides exceptional customer service and offers a distinctive flying experience by focusing on creating fun. Southwest Airlines successfully employs the hybrid best-cost strategy.
Target	Target offers extremely competitive prices, but the firm also differentiates itself from other discount retailers by carrying products from trendy designers such as Michael Graves, Isaac Mizrahi, Fiorucci, and Universal Thread.
Chipotle	Chipotle Mexican Grill offers a limited menu of low-cost Mexican fare. However, the menu is customizable and uses organic ingredients. Chipotle successfully employs the hybrid best-cost strategy.
IKEA	IKEA uses a best-cost strategy by offering stylish, well-designed furniture at affordable prices. While customers could find cheaper options at discount furniture stores or more luxurious items at high-end retailers, IKEA's combination of modern design and reasonable pricing allows it to appeal to both markets, giving customers the perception of high value.
HelloFresh	HelloFresh, a meal kit delivery service, offers cheap healthy meal plans compared to dining out, while using fresh ingredients and simple recipes. Their direct-to-consumer approach allows their busy consumers to enjoy high-quality meals at home for a much lower cost than ordering takeout or eating out. Hello Fresh successfully uses the hybrid best-cost strategy.
Toyota	Toyota has used a best-cost strategy with its Lexus brand, offering luxury features at lower prices than traditional luxury automakers like Mercedes-Benz or BMW.
Zara	Zara has successfully employed a best-cost strategy by offering trendy, stylish clothing at relatively affordable prices. Zara's ability to quickly produce fashion-forward designs while maintaining competitive pricing gives it an edge over both lower-cost fast-fashion competitors and more expensive designer brands.

Figure 8.10: Best-cost strategy examples

One way to be successful by using a best-cost strategy is by reducing overhead costs while providing innovative quality products. Entrepreneurial enterprises may have an advantage when it comes to balancing reducing overhead and providing creative products and may find a best-cost strategy appealing.

Entrepreneurs in the food industry are an excellent example of this strategy, as seen in figure 8.11.



Figure 8.11: Recent business graduates who are successful entrepreneurs inspire other recent graduates to become entrepreneurs

Company	Example
The Toast Truck	For around \$5, a customer can pick from a variety of gourmet toasts, from avocado toast with chili flakes to ricotta and honey on sourdough. The Toast Truck, a food truck based out of Detroit, can keep their costs low by using their mobile format, allowing customers to enjoy artisanal flavors without the overhead cost of running a full restaurant.
Crave Crepes	Crave Crepes uses a crepe cart to keeps things simple, selling crepes with great toppings such as Nutella and strawberries or ham with Swiss cheese, which are all under \$5. Their cart setup allows for Crave Crepes to keep overhead low while also still being able to deliver fresh and made-to-order crepes.
Bento Heaven	Bento Heaven in Miami specializes in Japanese-style bento boxes that are all under \$8 and packed with options like teriyaki chicken, tofu katsu, and vegetable tempura. By focusing on small and well-curated meals, they can provide variety and affordability to their customers, allowing them to become a go-to spot for many.

Figure 8.12: Pursuing a best-cost strategy by reducing overhead and providing quality products

Video 8.3: Best-Cost Provider Strategy [03:30]

The video for this lesson discusses companies that use best-cost strategies.

Access this YouTube video by scanning the QR code.



Video 8.4: Five Competitive Strategies [02:51]

The video for this lesson discusses five competitive strategies.

Access this YouTube video by scanning the QR code.

**Application**

- A best-cost strategy, a hybrid approach that combines elements of both cost leadership and differentiation in an existing market or market segment. Fewer companies follow a best-cost business-level strategy than the previous four business-level strategies.
 - Describe one company not discussed in the text that follows a best-cost business-level strategy. Assess whether this is a strong strategy for the company. Explain your rationale.

Key Takeaways

The best-cost strategy allows firms to offer high-quality, differentiated products at competitive prices, appealing to both price-conscious consumers and those seeking superior features, which creates a strong value proposition in diverse markets. Successfully executing a best-cost strategy requires tight cost control combined with continuous investment in innovation and quality, as firms must balance cost efficiency with delivering differentiated value to avoid being outcompeted by both low-cost and premium brands. Firms must carefully manage their cost structures while continuing to innovate and invest in the features that set them apart. When executed well, the best-cost strategy can give companies an edge over both low-cost and premium competitors, appealing to customers looking for value without compromise. However, firms must navigate the challenges of maintaining both cost and quality to avoid falling into the trap of being outperformed on both fronts.

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8.12 Blue Ocean Strategy

Some firms find it difficult to strictly adhere to either a cost leadership or differentiation strategy, as market conditions often require a blend of cost control and differentiation. Firms that choose a best-cost strategy combine cost leadership and differentiation in existing markets. Other companies are bold, creating a completely new market using a **blue ocean strategy**, which is also a combination of cost leadership and differentiation but with the distinction of market creation.

Blue ocean strategy is a relatively new strategic approach which has resonated both in the academic community and the corporate world. The core goals of the blue ocean strategy are to create uncontested market space and ideally make competition irrelevant. By doing so, blue ocean strategy breaks the paradigm that business is a zero-sum game in which a company can only increase its business at the expense of its competitors.

In contrast to blue ocean strategy, red ocean leads to competing on the same attributes with the same or similar products and services as the organization's competitors; in this situation, market share gains can only be achieved at the expense of competitors. When all industry players compete in this red ocean, they face intense competition with limited differentiation, using price as one of the means to gain market share. This approach will eventually lead to lower industry profit, a limited industry attractiveness, and eventually a deterioration of profitability for all players in the red ocean.

Business professors Chan Kim and Renée Mauborgne identified the blue ocean strategy. This new paradigm strategically positions a business for success and is characterized by the following elements.

- Creating uncontested markets instead of competing in an existing market space
- Making the competition irrelevant instead of beating them
- Creating new demand instead of capturing more of the existing demand
- Creating value innovation that disproves the value/cost trade-off

Value innovation as one of the core principles of blue ocean strategy, which defies the notion that a business can only select either a differentiation or cost leadership strategy. The blue ocean strategy simultaneously pursues both through the concept of value innovation. Successfully combining differentiation and cost leadership activities through value innovation allows a business to conquer untapped market space, create additional demand, and pursue opportunities for highly profitable growth.

An example of a company that followed a blue ocean strategy to great success is Marvel. Marvel was founded in 1939 as a comic book company, and its customers were children. In the 1960s, Marvel followed a blue ocean strategy by seeking new customers, college students, with superheroes that were humans first and superheroes second, like the Hulk. In the 1980s, Marvel returned to a red ocean strategy by repeating the same strategy with little innovation. Customers were alienated, and the company went bankrupt. In 1999, Peter Cuneo was appointed CEO, and he is credited with taking Marvel from bankruptcy to its purchase by Disney to being valued at over four billion dollars in a decade. In achieving this, Marvel also transformed movie production. Marvel is an excellent example of a blue ocean strategy because it not only opened a new field, it reconstructed the field to open a blue ocean. Marvel was able to create unprecedented value at a low cost, using both differentiation and cost leadership to create a new a market.

There are many advantages to following a blue ocean strategy, such as brand identity and customer loyalty. However, a firm cannot remain in the same blue ocean indefinitely because competitors quickly enter the blue ocean, turning it red. It takes continuous innovation to lead an industry in a blue ocean. As you can see from the case of Marvel, a company can create multiple blue ocean strategies.

While this sounds surely very compelling and like a “no-brainer” for every business leader and strategy expert, the decisive question is where and how an organization can find these “magic” blue oceans. The answer to this success-critical question is the thorough use of value curves.

Value Curves

The value curve is a different concept from the value chain analysis. The value curve is a two-dimensional graph that shows the principal buying factors on the X-axis and the service level on the Y-axis.

The X-axis depicts the competing factors that are the main factors that a customer considers in a buying decision in the specific industry. Typical principal buying factors are price, innovation, reliability, customer service, supply security, global availability, and sustainability of the offered product and service, among others. These principal buying factors are specific to the industry in which the business operates.

The Y-axis depicts the service level offered per principal buying factor, ranked from low to high (for example, on a scale from 0–5 or 0–10).

Using this concept, the organization creates two different value curves. The industry as-is curve depicts the current profile of offerings. Additionally, the company depicts its current value curve for its business.

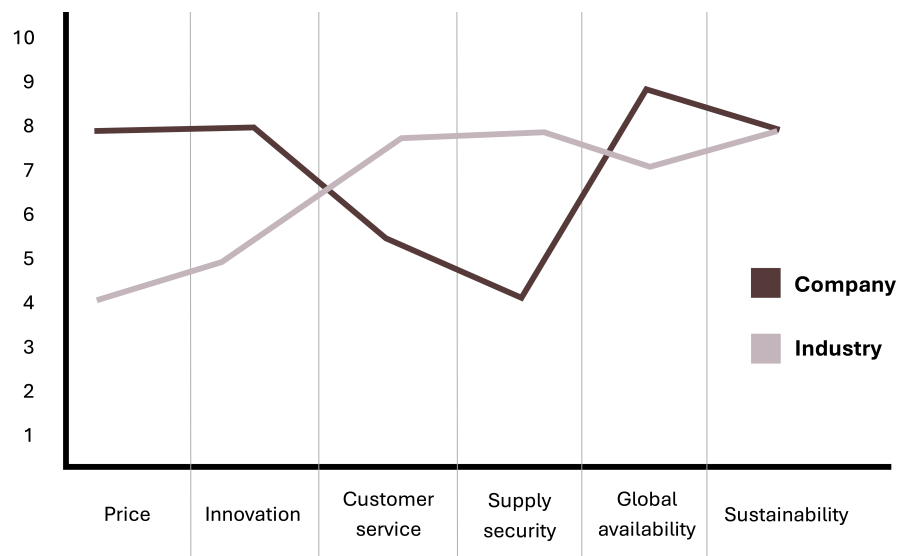


Figure 8.13: Value curve

Lastly, the organization identifies a blue ocean market space by purposefully and intentionally diverting from the as-is industry value curve. The logic of this move is that the organization deliberately does not want to offer the same level of the same principal buying factors, which would lead to the classic red ocean play. Based on the as-is industry curve and the current value curve of the organization, a blue ocean can be identified by raising the service level of certain principal buying factors, reducing the service level, eliminating certain product and service elements, and creating new product and service factors.

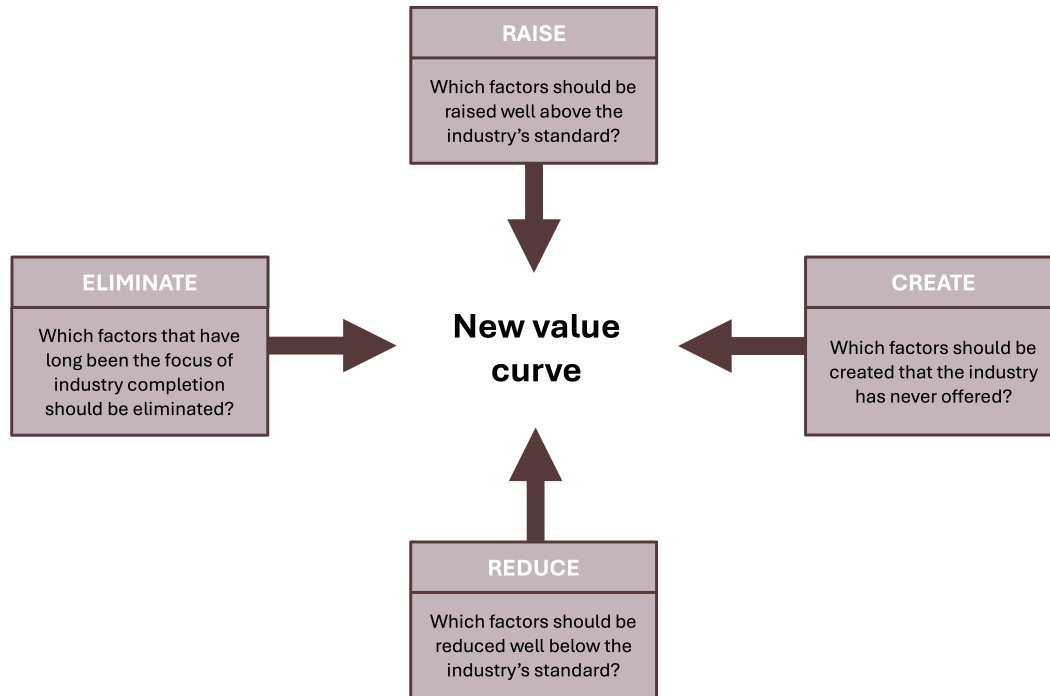


Figure 8.14: Creating a blue ocean value curve

Through this process, the organization purposefully creates a new value curve that deviates from the as-is industry curve. This blue ocean move means that the business is not operating anymore in the same market space, as it has created a differentiated offering that ideally creates a new blue ocean space.

The organization that uses this approach lowers its costs by eliminating or reducing factors that the industry takes for granted and that are the industry's current standard. At the same time, the business also increases perceived consumer benefits by raising and creating factors well above the industry's standard or by offering completely new factors that the industry has never offered. This simultaneous reduction of costs and creation of new benefits supports the value innovation at the core of blue ocean strategy as a combination of differentiation and cost leadership strategies.

Value innovation places equal emphasis on value and innovation. As such, it is a new way of thinking about and executing strategy that results in the creation of a blue ocean. The creation of blue oceans allows driving costs down while simultaneously driving value up for buyers.

The graph in figure 8.16 shows a blue ocean value curve that purposefully deviates from the industry curve.

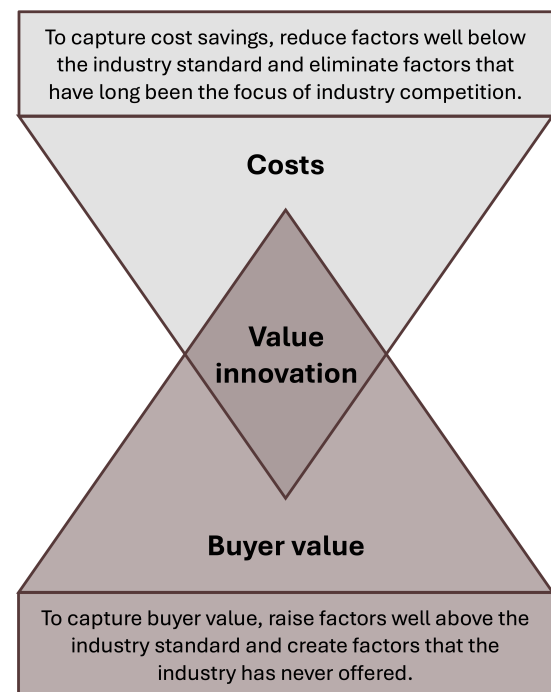


Figure 8.15: Value innovation as the result of lowering costs while increasing customer benefit

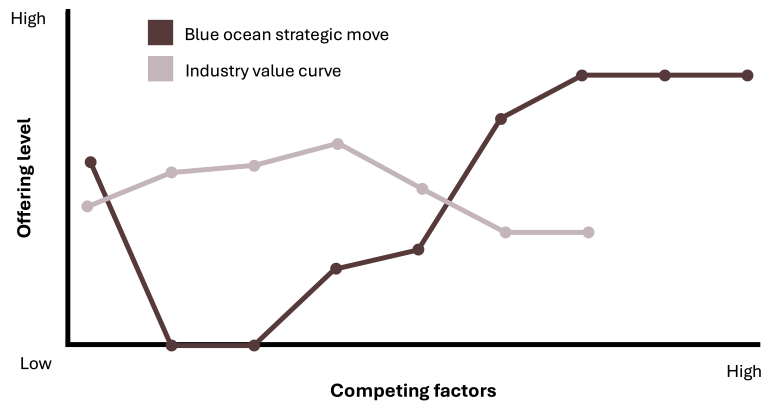


Figure 8.16: Creating a blue ocean value curve that purposefully deviates from the industry value curve

Video 8.5: Blue Ocean Strategy [06:02]

The following video by Renée Mauborgne explains the blue ocean strategy.

Access this YouTube video by scanning the QR code.



Application

- A blue ocean strategy is a combination of cost leadership and differentiation with the distinction of market creation. Even fewer companies follow a blue ocean business-level strategy than the previous business-level strategies.
 - Describe one company not discussed in the text that follows a best-cost business-level strategy. Assess whether this is a strong strategy for the company. Explain your rationale.

Key Takeaways

The blue ocean strategy can be a very powerful strategic approach to drive competitive differentiation and carve out a niche of uniqueness in otherwise crowded and competitive markets. The key to a successful blue ocean strategy is a very profound and in-depth market understanding of what customers truly value and want to pay for and what competitors are currently offering. Value curves for the industry and for the organization using blue ocean strategy are the basis for identifying uncontested market space. Many leading companies involve key customers in designing differentiating value curves by checking which principal buying factors really matter to them and which buying factors they are truly willing to pay for. Using this customer input and the in-depth market understanding, companies

design new blue ocean value curves using the concept of value innovation by lowering and eliminating specific factors (cost leadership element) and by raising or adding new factors (differentiating element). The new blue ocean value curve is then implemented in the new strategy and the new differentiating business model.

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8.13 Stuck in the Middle

Companies that attempt to combine cost leadership and differentiation strategies and fail to balance the tensions inherent in cost leadership and differentiation may end up being **stuck in the middle**, unable to compete on price with low-cost leaders or on quality with premium brands. This is a risk for companies following a best-cost strategy, which focuses on existing markets or market segments. It is also a risk for firms that are attempting to create entirely new markets by following a blue ocean strategy.

For instance, if a firm attempts to cut costs too aggressively, it may erode the value of its differentiated features, causing customers to perceive the product as inferior. Conversely, if the firm invests too heavily in enhancing product features without controlling costs, it may not be able to offer competitive pricing, limiting its appeal to price-sensitive consumers.

When firms are stuck in the middle, they are left without a clear competitive advantage. These firms cannot compete on price with low-cost leaders, nor can they offer unique enough products or services to justify premium pricing.

A recent example of a company caught in this strategic dilemma is Fisker Automotive, an electric vehicle manufacturer. Fisker attempted to position itself as both a luxury electric vehicle producer, competing with Tesla, and as an affordable option for environmentally conscious consumers. However, the company failed to differentiate itself with unique technology or a distinct brand identity. At the same time, it was unable to achieve the cost efficiencies required to compete with lower-priced electric vehicle options offered by larger manufacturers. This misalignment left Fisker without a strong customer base, and the company filed for bankruptcy in 2024 after struggling to find a buyer or secure additional funding to continue operations.

Another company that recently became stuck in the middle is Bed Bath & Beyond, which filed for bankruptcy in 2023. Bed Bath & Beyond was once a dominant player in the home goods market, but over time, the company failed to clearly define its competitive strategy. It was unable to effectively compete with low-cost giants like Walmart and Amazon, who offered similar products at lower prices. At the same time, the company did not differentiate itself enough in terms of customer experience, product offerings, or convenience to maintain its status as a go-to destination for home goods. As online retailers gained market share with more efficient operations and aggressive pricing, Bed Bath & Beyond found itself squeezed between cost leaders and brands that are more innovative or customer-centric, ultimately leading to its collapse.

Being stuck in the middle poses significant risks for companies. Without a clear value proposition, these firms face increasing pressure from all sides. Competitors with well-defined cost leadership or differentiation strategies will be better positioned to attract customers, leaving middle-ground companies vulnerable to shrinking margins, declining sales, and loss of relevance in the market. Both Fisker and Bed Bath & Beyond serve as recent examples of how lacking strategic focus can lead to financial instability and eventually bankruptcy.

Company	Example
Arby's	Arby's signature roast beef sandwiches are neither more affordable than other fast-food options nor are they exceptional in flavor. Arby's has failed to implement either a cost leadership or a differentiation strategy.
Under Armour	Under Armour has been in a tough situation. Positioned between budget-friendly athletic wear brands like Adidas and premium brands like Nike, it struggles to clearly define its market segment. It lacks the aspirational and product quality image of its premium competitors and the affordability of its value brand competitors, which has led to consistent slow growth and missed revenue targets. Under Armour has failed to implement either a cost leadership or a differentiation strategy.
GameStop	Video game retailer GameStop has consistently struggled to stay relevant in the age of digital downloads and competition from online platforms like Amazon and Steam. Unable to compete on price or deliver a unique customer experience, GameStop has faced many store closures and huge revenue declines.
IHOP	The International House of Pancakes, aka IHOP, is known for its breakfast, but it is stuck in between fast-casual spots like Denny's and Waffle House and premium trendy brunch locales that offer more modern and social-media-friendly experiences. IHOP's inability to become an affordable breakfast option with quick service or to provide their customers with aesthetically pleasing dishes for social media has led to many store closures.
Fisker Automotive	Fisker attempted to position itself as both a luxury electric vehicle producer, competing with Tesla, and as an affordable option for environmentally conscious consumers. However, the company failed to differentiate itself with unique technology or a distinct brand identity. At the same time, it was unable to achieve the cost efficiencies required to compete with lower-priced electric vehicle options offered by larger manufacturers.
Bed Bath & Beyond	Bed Bath & Beyond failed to clearly define its competitive strategy. It was unable to effectively compete with low-cost giants like Walmart and Amazon, who offer similar products at lower prices. At the same time, the company did not differentiate itself enough in terms of customer experience, product offerings, or convenience to maintain its status as a go-to destination for home goods.

Figure 8.17: Examples of companies that are "stuck in the middle"

Application

- Describe one company not discussed in the text that has gotten stuck in the middle. Explain your rationale.

Key Takeaways

Companies that fail to clearly commit to either a cost leadership or differentiation strategy risk being squeezed between low-cost competitors and more differentiated brands. This “stuck in the middle” position makes them vulnerable to losing market share, profitability, and relevance, often leading to financial instability, as seen in recent bankruptcies like Fisker and Bed Bath & Beyond.

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8.14 Limitations of Business-Level Strategies

While broad cost leadership, focused cost leadership, broad differentiation, and focused differentiation provide useful frameworks for understanding competitive positioning, they have several limitations. One of the key challenges is that these strategies can be overly simplistic and may not fully capture the complexity of real-world competition. Competitors can easily imitate cost or differentiation advantages, eroding a firm's edge.

The existence of hybrid strategies like best-cost strategy can lead to some firms trying to do too much, getting stuck in the middle of the industry. Additionally, shifting customer preferences, technological advancements, and the fast-paced nature of industries can make these static strategies less effective over time, requiring firms to constantly adapt their approach to remain competitive.

Key Takeaways

The business-level strategies can be overly simplistic and may not fully capture the complexity of real-world competition.

8.15 Analyze Business-Level Strategy

Strategic business unit managers focus on formulating business-level strategies. When you conduct a case analysis, you analyze a firm's business-level strategy. This is step six in the case analysis process.

6. As appropriate to the case, analyze strategies: Corporate-level, business-level, innovation, sustainability and ethics, technology, and multinational strategies.

- a. Use strategic management analytical frameworks to analyze, interpret, and evaluate strategies.
- b. Ensure line of sight and congruence within analysis of each strategy.

8.16 Why Business-Level Strategy Is Important to Business Graduates

Just like corporate-level strategy, business-level strategy has a direct influence on the implementation of functional-level strategy. Business graduates that start as business support unit managers will support business units of large companies, such as business information technology managers. They may be asked to support divisional or strategic business unit managers by providing data analysis from functional business managers, such as managers of marketing, accounting, and human resource management are ideally placed to assist with. As divisional managers choose between broad cost leadership, broad differentiation, focused cost leadership, focused differentiation, and best cost strategies, the access that business support unit managers have to key data and their skills with robust data analysis is essential support for divisional leaders. Even in those more rare instances of a firm that follows a blue ocean strategy, timely data analysis is vital to a successful outcome.

Those of you joining smaller companies will immediately spend more time working closely with divisional or strategic business unit managers responsible for business-level strategy. Business graduates that enter either internal or external consulting roles require a high level of competence with business-level strategy to communicate to divisional or strategic business unit managers how their consulting projects fit into the business-level strategy of the firm. Some of you already are or will become entrepreneurs, and fluency with business-level strategy is essential to establishing and growing a successful firm. It is essential to know how your company competes within its chosen market and market segments.

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8.17 Conclusion

Business-level strategies are essential for firms to create and sustain competitive advantage in their respective markets. Companies must clearly define how they will compete to serve their target customers effectively. Each strategy has its benefits and challenges, requiring careful alignment of resources, capabilities, and core competencies. Firms that fail to commit to a clear strategy risk

becoming stuck in the middle, where they lose out to both low-cost leaders and differentiated competitors. To thrive, companies must remain adaptable, continuously refining their strategies to meet evolving market conditions and customer needs. Firms can pursue one of six business-level strategies: broad cost leadership, focused cost leadership, broad differentiation, focused differentiation, best-cost strategy, or blue ocean strategy. Each offer a distinct path to achieving competitive advantage.

Demonstrate Your Knowledge, Skills, and Competence

Use these questions to test your knowledge of the chapter.

1. Describe business-level strategy. Describe a strategic business unit and the relationship between a strategic business unit and business-level strategy. What questions does business-level strategy answer? How does it relate to a VUCA environment? What is the role of synergy in corporate-level strategy?
2. Explain the difference between corporate-level strategy and business-level strategy.
3. Describe the role customer analysis plays in business-level strategy. What key questions do leaders and managers ask about customers to support business-level strategy?
4. Explain the two dimensions in the business-level strategy framework.
5. Describe in detail cost leadership and differentiation. What are the advantages and disadvantages of each? Give examples.
6. Discuss in detail focused and broad approaches. What are the advantages and disadvantages of each? Give examples.
7. Describe the key features of the six business-level strategies. Give examples.
8. Describe a blue ocean strategy. Explain the idea of value curves and how this relates to blue ocean strategy.
9. Explain being stuck in the middle and why firms should try to avoid this.
10. Describe how competence with business-level strategy is relevant and important to you.

You are now skilled at analyzing a company's business-level strategy. Congratulations!

Figure Descriptions

Figure 8.1: Purple hierarchical organizational chart displaying the structure of a company's management and strategic planning. At the top is a rectangle labeled "Board of directors." Below this, another rectangle labeled "Corporate office (corporate executives)." This level of hierarchy represents corporate-level strategy. Below this, two rectangles are labeled "Division 1 (division 1 manager)" and "Division 2 (division 2 manager)." Below this, there are four SBU boxes (each with one manager). There are two SBU boxes beneath Division 1 and two SBU boxes beneath Division 2. This level of hierarchy represents business-level strategy, innovation strategy, sustainability and ethics strategy, technology strategy, and multinational strategy. Below the SBUs are five "Business support Unit 1" boxes, dedicated to finance, operations, human resources (HRM), IT, and sales and marketing, each managed by their own business support unit manager. This level of hierarchy represents functional-level strategy.

Figure 8.2: First quadrant of an X-Y axis with four purple boxes. The x-axis represents strategic market position (ranging from low cost to unique) and the y-axis represents strategic market size (ranging from narrow market to broad market). Low cost and narrow market is marked focused cost leadership. Unique and broad market is marked broad differentiation. Unique and narrow market is marked focused differentiation. Low cost and broad market is marked broad cost leadership. At the center of these four boxes, there is "Best cost; Blue ocean."

Figure 8.13: Line graph comparing the performance of a company against the industry across six categories: Price, Innovation, Customer Service, Supply Security, Global Availability, and Sustainability. The vertical axis ranges from 1 to 10, representing the performance scores. Two lines are plotted: a dark purple line representing the company and a light purple line for the industry. For price,

the company scores 8 while the industry scores 4. In innovation, the company scores 8, and the industry 5. For customer service, the company scores 5, while the industry scores 8. In supply security, the company scores 4, while the industry scores 8. For global availability, the company scores 9, and the industry 7. Lastly, in sustainability, the company and industry both score 8.

Figure 8.14: Four purple boxes are arranged in a circle and all point to the center that reads “New value curve.” The top box is labeled “RAISE” and asks which factors should be raised above the industry’s standard. The right box is labeled “CREATE” and asks which factors should be created that the industry has never offered. The bottom box is labeled “REDUCE” and asks which factors should be reduced below the industry standard. The left box is labeled “ELIMINATE” and asks which factors that have long been the focus of industry competition should be eliminated.

Figure 8.15: Venn diagram of two purple triangles (one inverted and stacked on top of the other) that meet at their apexes in the middle of the diagram. The top triangle is labeled costs with a description that reads “To capture cost savings, reduce factors well below the industry standard and eliminate factors that have long been the focus of industry competition.” The bottom triangle is labeled buyer value with a description that reads “To capture buyer value, raise factors well above the industry standard and create factors that the industry has never offered. Where costs and buyer value overlap, is value innovation.”

Figure 8.16: Line graph comparing two curves: the blue ocean strategic move (dark purple) and the industry value curve (light purple). The x-axis is labeled competing factors and ranges from low to high, while the y-axis is labeled offering level, and ranges from low to high. The blue ocean strategic move line starts in the middle, falls, begins rising again, and ends higher than where it started. The industry value curve starts in the middle, increases slightly, decreases slightly, and ends slightly lower than where it started.

Figure References

Figure 8.1: Three levels of strategy. Kindred Grey. 2025. CC BY.

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Figure 8.8: Oatly. Tiia Monto. 2018. CC BY-SA 3.0. <https://commons.wikimedia.org/wiki/File:Oatly.jpg>

Figure 8.11: Recent business graduates who are successful entrepreneurs inspire other recent graduates to become entrepreneurs. Tima Miroshnichenko. 2020. [Pexels license](https://www.pexels.com/photo/business-meeting-5686105). <https://www.pexels.com/photo/business-meeting-5686105>

Figure 8.13: Value curve. Kindred Grey. 2025. CC BY.

Figure 8.14: Creating a blue ocean value curve. Kindred Grey. 2025. CC BY-NC-SA. Adapted from <http://dx.doi.org/10.1016/j.sbspro.2015.06.162> (CC BY-NC-SA 4.0)

Figure 8.15: Value innovation as the result of lowering costs while increasing customer benefit. Adapted under fair use from <https://barnabythinks.wordpress.com/2018/12/02/blue-ocean-strategy-kim-mauborgne>

Figure 8.16: Creating a blue ocean value curve that purposefully deviates from the industry value curve. Kindred Grey. 2025. CC BY.

PART V: FORMULATE STRATEGIES THAT ARE EMBEDDED IN BUSINESS-LEVEL STRATEGY: INNOVATION, SUSTAINABILITY AND ETHICS, TECHNOLOGY, AND MULTINATIONAL STRATEGY

In Part IV, you learned about corporate-level strategy and business-level strategy and how to analyze each.

In Part V, you learn about four strategies that are embedded into business-level strategies. These are innovation, sustainability and ethics, technology, and multinational strategy.

9. FORMULATE INNOVATION STRATEGY

Learning Objectives

After engaging with this chapter, you will understand and be able to apply the following concepts to formulating innovation strategies.

1. Innovation strategy
2. Entrepreneurial orientation
3. The importance of innovation
4. The types of innovation
5. Footholds
6. The ways innovation relates to business-level strategies
7. First movers and fast followers
8. Product life cycle
9. Crossing the chasm
10. Cooperative moves
11. Responding to innovation in the market
12. Measuring innovation performance
13. Why technology strategy is important to business graduates

Ultimately, this chapter equips you to analyze innovation strategy.

9.1 Introduction

In this chapter, you first learn what innovation strategy is. Next you learn about entrepreneurial orientation (EO) and its role in innovation. This term is applied to both entrepreneurship and intrapreneurship, as well as to individuals. EO accounts for innovativeness, proactiveness, and risk-taking. This chapter also discusses why innovation is important and the four major types of innovation. These differ along two dimensions. The first considers whether the company is innovating by creating a new market or addressing an opportunity in an existing market. The second dimension of innovation considers whether the innovation uses a new technology or takes advantage of existing technology. Incremental innovation involves entering an existing market with existing technology; disruptive innovation enters an existing market with new technology; architectural innovation enters a new market with existing technology; and radical innovation enters a new market with new technology. After considering the four types of innovation, you learn that first movers are those firms that enter a market first and fast followers enter the market after first movers pave the way. Then you learn how the four types of innovation and first movers and fast followers apply to a product's life cycle (introduction, growth, maturity, and decline).

As this chapter continues, you learn the five stages of a company's product adoption cycle or an industry's technological advancement. These five stages are innovators, early adopters, early majority, late majority, and laggards. You learn the importance of crossing the chasm as a means of sustaining a product's growth in the market. You revisit internal development, strategic alliances, joint ventures, and mergers and acquisitions as means of cooperating with other firms. Next you learn ways of responding to innovation

in the market, including multipoint competition, responding to disruptive innovations, fighting brands, co-location, and co-opetition. Then you learn how to measure a firm's performance through the lens of innovation. Finally, you learn how to analyze innovation strategy.

9.2 Innovation Strategy

Like all strategy formulation, innovation strategy formulation answers the question “Where are we going?” Innovation strategy addresses where a firm is going as it relates specifically to innovation. All firms need to address innovation and innovation strategy.

Innovation strategy is the first strategy you learn that is embedded in business-level strategy at the strategic business unit level of a firm. Strategies that are embedded in business-level strategies address the “Right to win?” question. All companies have the ambition to win in their chosen markets. They want to gain market share, increase revenue and profit, and enter new markets and regions, among other barometers of success. However, strategy is more than a wish list of what a company would ideally want to do and achieve. Strategy is a company-specific roadmap for navigating in its industry, directing how a firm moves from its current state toward the firm's vision.

Like all strategy, innovation strategy focuses on an outside-in perspective. Companies need to carefully monitor their external environments. They need to analyze trends and formulate strategies that are forward-looking. Robust innovation strategy takes into account the volatile, uncertain, complex and ambiguous (VUCA) nature of the firm's external environment, where change and disruption have become the new normal.

A firm's approach to innovation plays a crucial role in shaping its competitive advantage. A strong commitment to innovation, often reflected in a firm's entrepreneurial mindset, drives the development of new products and services while refining existing offerings. This process of continuous improvement not only enhances the company's market position but also expands its reach into new, often untapped, markets.

Key Takeaways

Like all strategy formulation, innovation strategy formulation answers the question of where a firm is going. Innovation strategy addresses where a firm is going as it relates specifically to innovation. All firms need to address innovation and innovation strategy. Innovation strategy is embedded in business-level strategy at the strategic business unit level of a firm. Strategies that are embedded in business-level strategies address the “Right to win?” question. A firm's approach to innovation plays a crucial role in shaping its competitive advantage.

9.3 Entrepreneurial Orientation

An essential part of innovation, **entrepreneurial orientation (EO)** is a fundamental concept in strategic management and entrepreneurship, capturing the essence of how firms innovate, take risks, and proactively engage with the market to seize new opportunities. At its core, EO reflects a firm's willingness to embrace change, challenge the status quo, and explore uncharted territories, which can drive growth and competitive advantage. By embodying a mindset that prioritizes bold strategic moves, agility, and a forward-looking perspective, companies with strong EO are better positioned to navigate uncertainty, respond to shifting market

dynamics, and sustain long-term success. Understanding EO offers valuable insights into how firms can cultivate a culture of entrepreneurship to thrive in today's dynamic business environment.

Entrepreneurial orientation is characterized by three core traits: innovativeness, proactiveness, and risk-taking. Innovativeness represents a company's willingness to experiment with new ideas, products, or processes. Proactiveness refers to a firm's ability to anticipate and act on future opportunities rather than simply reacting to external changes. Risk-taking involves the willingness to invest in uncertain ventures and explore new territories, even when the outcomes are unknown. Although EO has traditionally focused on these three characteristics, two additional traits, competitive aggressiveness and autonomy, have been proposed as part of EO. However, these have sparked debate in academic circles and are excluded from this discussion so that we may focus on the core dimensions of EO that are universally recognized.

Innovativeness

Innovativeness refers to the drive to embrace creativity and experimentation. Some innovations are incremental, building on existing skills to make small improvements, while others are more radical, demanding new skills and potentially rendering old ones obsolete. The goal of innovativeness is to develop new products, services, or processes. Companies that excel in innovation typically outperform those that fail to prioritize it, gaining a competitive edge and enhancing overall performance.

Renowned for its commitment to efficiency, UPS introduced its ORION system, an innovative technology that optimizes delivery routes in real time, saving fuel and reducing delivery times. This type of advancement is particularly valuable for businesses handling time-sensitive goods, such as pharmaceuticals or fresh produce. But how do companies come up with such innovations that address their customers' specific and complex needs?

Companies like Apple and Atlassian offer some insights. Apple frequently sends its design teams into consumer environments to better understand user pain points and needs, resulting in products that anticipate market demand. Atlassian, known for its project management tools, allows employees to dedicate a portion of their work hours to passion projects, leading to the creation of new features like Jira's customizable workflows. These examples highlight how encouraging employee autonomy can fuel innovation, demonstrating how multiple dimensions of entrepreneurial orientation, such as autonomy and innovativeness, can work together to drive breakthrough ideas.



Figure 9.1: UPS

Proactiveness

Proactiveness refers to the ability to anticipate and act on future needs rather than merely responding to events as they unfold. Proactive organizations are opportunity-driven, identifying and capitalizing on emerging trends before competitors.

Take, for example, Tesla's early investment in electric vehicles. Long before the market for EVs was fully established, Tesla anticipated a shift toward sustainable transportation and positioned itself as a leader in the industry.

Similarly, Shopify, recognizing the growing trend of e-commerce, rapidly adapted to the needs of small businesses by offering easy-to-use, scalable solutions before many other platforms could catch up. These companies embody proactiveness by actively seeking

out opportunities in changing technological, environmental, and market conditions, allowing them to stay ahead of the curve and build strong competitive advantages.

Risk-Taking

Risk-taking involves pursuing bold actions rather than opting for conservative or cautious strategies.

A strong example of this can be seen in Netflix's decision to transition from DVD rentals to streaming services, a move that required significant investment and foresight at a time when streaming technology was still in its infancy. This bold shift not only redefined how people consume media but also established Netflix as a global entertainment powerhouse, none of which would be possible if Netflix had not taken the risk of changing its entire business model.

While entrepreneurs and companies are often portrayed as habitual risk-takers, research shows that many do not perceive their actions as inherently risky. Instead, they employ careful planning and forecasting to mitigate uncertainty.

For instance, when Tesla decided to build its Gigafactory, the company faced massive financial and logistical challenges.

However, detailed planning and strategic partnerships helped reduce the uncertainty, enabling Tesla to scale up production and dominate the electric vehicle market. Yet, as with any venture, uncertainty can never be entirely eliminated.

When BP decided to expand its oil exploration operations in the Gulf of Mexico, the company exemplified risk-taking by investing heavily in a venture fraught with political, environmental, and technical challenges. Despite the potential for high returns from gaining access to vast oil reserves, the move exposed BP to unpredictable risks, which ultimately materialized during the Deepwater Horizon disaster, which caused the largest marine oil spill in history. This incident highlighted the inherent dangers of risk-taking, as the pursuit of strategic opportunities can lead to substantial gains but also significant losses.

These examples show that, while risk-taking is essential for growth, successful entrepreneurs and firms should balance bold action with strategic foresight to increase the likelihood of long-term success.



Figure 9.2: Netflix

EO dimension	Definition	Example
Innovativeness	Tendency to engage in and support new ideas, experimentation, and creative processes that lead to the development of new products, services, or processes	Apple's Apple Watch, developed through a culture of innovation and cross-functional experimentation, blending health tracking, communication, and design to redefine wearable technology
Proactiveness	The ability to anticipate and act on future needs rather than merely responding to events as they unfold	Tesla's early investment in electric vehicles. Long before the market for EVs was fully established, Tesla anticipated a shift toward sustainable transportation and positioned itself as a leader in the industry.
Risk-taking	Involves pursuing bold actions rather than opting for conservative or cautious strategies	Netflix's decision to transition from DVD rentals to streaming services, a move that required significant investment and foresight at a time when streaming technology was still in its infancy

Figure 9.3: The three dimensions of entrepreneurial orientation

Intrapreneurship

Entrepreneurship is often synonymous with trailblazers who build empires from scratch—figures like Whitney Wolfe Herd, who revolutionized online dating with Bumble, or Melanie Perkins, who simplified graphic design with Canva. But the spirit of entrepreneurship is not confined to startups or garage-born businesses. In fact, some of the most impactful innovations come from individuals working within large organizations who challenge the status quo, pushing for the development of groundbreaking products or services. These employees may not be founders, but they act with the same determination and creativity to bring their ideas to fruition, often reshaping the company's future in the process.

This form of entrepreneurship within an organization is known as **intrapreneurship**. Unlike traditional entrepreneurship, intrapreneurs innovate from within, navigating the complexities of large organizational structures to drive change.

For instance, 3M's famous invention of Post-it notes didn't come from external R&D but from an employee experimenting with new uses for a weak adhesive. Similarly, Netflix's shift from DVD rentals to streaming content came from internal visionaries who saw the potential long before streaming was a mainstream concept.

Companies that foster intrapreneurship often gain a competitive advantage by leveraging their existing resources, capabilities, and core competencies to develop new products and services without needing to acquire or merge with external firms. Rather than solely seeking growth through acquisitions, firms like Apple and Google have created cultures that encourage employees to think and act entrepreneurially, resulting in innovations like the iPhone and Google Maps, both developed internally.



Figure 9.4: Google Maps

Moreover, thinking entrepreneurially isn't just beneficial for organizations; it's a powerful tool for personal career growth. Employees who adopt an entrepreneurial mindset often excel in navigating corporate landscapes, identifying opportunities others overlook, and positioning themselves as valuable innovators within their firms. Those who think outside the box and take initiative often find that they can climb the corporate ladder faster, all while making meaningful contributions to the company's success.

Intrapreneurs, much like their entrepreneurial counterparts, blend creativity with strategic risk-taking, showing that entrepreneurship isn't confined to new ventures but is also thriving within the walls of some of the world's largest corporations.

EO Applied to Individuals

Entrepreneurial orientation applies not only to organizations but also to individuals. Traits such as risk-taking, innovation, and competitiveness, key characteristics of entrepreneurial companies, are equally important for individuals. Those who embrace creativity, are comfortable with uncertainty, and thrive in competitive environments tend to score higher in EO, which often translates to greater success when starting a business. While EO is frequently associated with high-tech startups, it is equally valuable for more traditional ventures like lawn care services or hair salons. For anyone interested, online tools are available to assess EO and better understand entrepreneurial potential.

Building an Entrepreneurial Orientation

Executives can take deliberate steps to cultivate stronger entrepreneurial orientation across their organizations, just as individuals can develop more entrepreneurial mindsets in their own roles. For executives, it's critical to align organizational systems and policies with the key dimensions of EO. For example, compensation structures should be designed to encourage entrepreneurial behavior. Are employees rewarded for taking calculated risks, even if those risks don't always pay off? Or does the system discourage risk-taking by penalizing failures? Corporate debt levels also play a role in shaping EO, as high levels of debt might stifle innovation

by making the organization more risk averse. Thoughtfully structured debt, however, can provide the financial flexibility needed to support innovation and risk-taking.

Executives can assess their organizations' EOs by examining various performance measures that reflect key dimensions of entrepreneurial behavior. For example, to gauge autonomy, they might track employee satisfaction and turnover rates, as organizations that encourage autonomy often see higher satisfaction and lower turnover. Innovativeness can be evaluated by measuring the number of new products or services introduced as well as the patents secured in a given year, offering tangible evidence of how effectively the company promotes creativity and experimentation.

For individuals, developing a stronger entrepreneurial orientation requires reflecting on personal attitudes and behaviors. Are you taking proactive steps rather than reacting to competitors? Are you offering fresh ideas for products or processes that could drive value for the company?

An individual employee can play a key role in enhancing EO by consistently thinking ahead, proposing new ideas, and making decisions that align with the company's strategic goals. By doing so, they not only support the organization's entrepreneurial culture but also position themselves as valuable contributors to its growth and success.

Application

- On a scale of 1–10, with 1 being low and 10 being high, rate yourself on innovativeness, proactiveness, and risk-taking.
 - Of these three key areas of EO, are there any you would like to challenge yourself to expand?
 - Considering your ratings, how likely are you engage in entrepreneurial activity at some point in your career?
 - Considering your ratings, how likely are you engage in intreprenurial activity at some point in your career?

Key Takeaways

Entrepreneurial orientation, an essential part of innovation, is characterized by three core traits: innovativeness, proactiveness, and risk-taking. Innovativeness refers to the drive to embrace creativity and experimentation. Proactiveness refers to the ability to anticipate and act on future needs rather than merely responding to events as they unfold. Risk-taking involves pursuing bold actions rather than opting for conservative or cautious strategies. Intrapreneurship refers to individuals acting entrepreneurially within a company. Entrepreneurial orientation applies not only to organizations but also to individuals. Executives can take deliberate steps to cultivate a stronger entrepreneurial orientation across their organizations, just as individuals can develop more entrepreneurial mindsets in their own roles.

Innovation is essential for firms to maintain a competitive edge. Companies that continuously innovate are better positioned to capture new markets, improve products, and outpace competitors, while firms that remain stagnant risk losing customers and market share. A strong EO helps firms continuously seek out new opportunities and innovate, which is crucial for staying competitive in dynamic markets.

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9.4 Why Innovate?

Innovation is a critical strategy for maintaining a competitive edge in rapidly evolving industries. Companies that become complacent risk losing market share to more agile competitors who are constantly pushing boundaries. An innovation-driven approach, paired with a strong entrepreneurial orientation, helps companies keep customers engaged and returning for the latest products or services.

Consider the tech industry, where companies like Apple and Samsung consistently release new versions of their smartphones with enhanced features like more powerful processors, better camera quality, or advanced software capabilities. This approach drives consumer demand, encouraging people to upgrade regularly to the latest model. In a similar fashion, streaming platforms like Netflix continuously innovate by adding interactive content and personalized recommendations, keeping users engaged and attracting new subscribers.

The automotive industry also relies heavily on innovation to stay relevant. Each year, manufacturers introduce updated models with improved designs, advanced safety features, and cutting-edge technology like electric powertrains or autonomous driving capabilities. Tesla, for example, has revolutionized the car market with its electric vehicles and over-the-air software updates, making continuous innovation a cornerstone of its success.

Even in fields like pharmaceuticals, innovation is essential. Companies invest heavily in research to develop new treatments for chronic diseases, such as cancer or Alzheimer's, ensuring they remain at the forefront of life-saving medical advancements. Without continuous innovation, companies risk falling behind and losing their competitive positions, regardless of the industry.



Figure 9.5: Tesla

Innovation is often the backbone of strategy for new startups across various industries, particularly in tech and consumer services. For instance, companies in renewable energy or electric mobility may develop groundbreaking battery technologies or new charging infrastructures that solve consumer needs and disrupt existing markets. These innovations are the engines that propel companies forward, allowing them to carve out new spaces in competitive markets.

While innovation is critical, it doesn't negate the need for a clear business-level strategy, whether that takes the form of focused cost leadership, broad cost leadership, focused differentiation, broad differentiation, best cost, or blue ocean. A firm must still define its competitive approach to ensure the success of its innovative offerings. There is a success-critical role for innovation in all business-level strategy.

Startups introducing unique, high-demand products or services often employ a differentiation strategy, setting premium prices due to limited competition. For instance, Tender Food, founded in 2020, specializes in plant-based meat alternatives that closely mimic the taste and texture of traditional meats. By utilizing innovative fiber-spinning technology, Tender Food creates a unique and healthier plant-based meat, such as beef short ribs and chicken breasts, appealing to consumers seeking sustainable and health-conscious options. This distinct technology allows Tender Food to position itself as a leader in the plant-based food industry, justifying premium pricing for its products.

The famous saying “He who hesitates is lost,” credited to the eighteenth-century writer Joseph Addison, holds significant truth in today's fast-moving business landscape. Executives often face overwhelming choices, but hesitation can be costly, especially in environments where rapid decision-making is crucial. Many industries now operate in conditions of hyper-competition, where the speed of competitive moves and countermoves makes it difficult to sustain a lasting competitive advantage. Under these circumstances, it is better to make a timely, reasonable decision than to wait for the perfect one, which might never materialize.

In addition, the value of continuous learning emphasizes the importance of a “take action” mindset. Business success often depends not on executing flawless moves but on learning from a series of strategic decisions and adjusting along the way. Sometimes decisive action can yield advantages, even when the decisions are made with incomplete information. Startups



Figure 9.6: Zoom

like Zoom capitalized on this during the pandemic by quickly scaling their services, seizing the opportunity before competitors had fully adapted to the surge in demand. These companies exemplify how timely decisions, combined with innovation, can lead to significant market gains in fast-paced industries.

Key Takeaways

Innovation is a critical strategy for maintaining a competitive edge in rapidly evolving industries. Companies that become complacent risk losing market share to more agile competitors who are constantly pushing boundaries. An innovation-driven approach, paired with a strong entrepreneurial orientation, helps companies keep customers engaged and returning for the latest products or services. Many industries now operate in conditions of hyper-competition, where the speed of competitive moves makes it difficult to sustain a lasting advantage. Under these circumstances, it is better to make a timely, reasonable decision than to wait for the perfect one, which might never materialize. The value of continuous learning emphasizes the importance of a “take action” mindset.

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9.5 First Movers and Fast Followers

In the competitive landscape, companies must decide how best to approach new market opportunities. Two common strategies are being a first mover or a fast follower. A **first mover** is a company that enters a new market or launches a new product before any competitors, aiming to establish an early advantage. A **fast follower** is a firm that enters the market immediately after the first mover.

First movers are the pioneers who introduce new products or services to the market, aiming to capture customer attention and establish strong market position before competitors emerge. This approach requires significant investment and a willingness to face uncertainty, as these firms must educate the market as to what they are offering and navigate uncharted territory. In contrast, fast followers enter the market after the first movers have paved the way, learning from their experiences and improving upon the original offering. Each strategy comes with its own set of advantages and challenges, and the choice between them depends on a firm's resources, capabilities, core competencies, and risk tolerance.

The concept of first-mover advantage draws parallels from military strategy, where the objective is to strike first and gain a dominant position before competitors can respond. In business, this means entering a new market or launching a new product before others, capturing customer attention and shaping market expectations. However, the decision to be a first mover also carries risks, as early entrants must face skepticism or challenges that later entrants can avoid.

The well-known saying “the early bird gets the worm” suggests that acting early can offer distinct advantages. In business, being the first mover into a market can help a company gain a competitive edge that may be difficult for later entrants to overcome. First-mover advantage occurs when a firm's initial move allows it to dominate the market by establishing strong brand recognition, customer loyalty, or technological leadership.

For example, Apple's early introduction of the user-friendly personal computer in the 1980s built a reputation for creativity and innovation that continues to this day. Kentucky Fried Chicken (KFC) was the first Western fast-food chain to enter China, building strong relationships with local officials, which allowed it to become the top fast-food chain in that market. Genentech, a biotechnology company focused on using DNA to produce medicine, played a pioneering role in biotechnology, which helped it



Figure 9.7: KFC

overcome traditional barriers to entry in the pharmaceutical industry and become highly profitable. In each of these cases, being the first mover gave these firms a distinct advantage that contributed to their long-term success.

Being a first mover is inherently risky, and companies cannot be certain consumers will embrace their offerings. Being first to the market can still yield valuable organizational learning and competitive insights, even if the product itself fails. For instance, Apple's Newton, an early attempt to enter the personal digital assistant market, ultimately failed financially, as did Google's initial foray into digital glasses. However, Apple and other first movers gained crucial knowledge about market demands, technological hurdles, and consumer behavior, which they could leverage in future innovations. Apple, for example, applied insights from the Newton to later products, eventually leading to the groundbreaking success of the iPhone and iPad. By learning from earlier missteps, first movers can refine their approaches, potentially leading to new and successful entries as first movers in other markets. Meanwhile, later entrants benefit from observing both the failures and successes of first movers, enabling them to refine or replicate these innovations more affordably. For example, companies like Sony and Samsung quickly followed Apple's AirPods with their own wireless earbuds, building on Apple's initial market insights and successes to create competing products.

First movers must also commit sufficient resources to following through on their initial advantage. For example, RCA and Westinghouse were early leaders in LCD display technology, but they failed to invest in the development and commercialization of their innovations. Today, they are not significant players in the flat-screen market, which supplies displays for everything from laptops to medical devices. Instead, companies such as Samsung, LG Display, and BOE Technology have emerged as top leaders in LCD display technology, dominating the market with their advanced research, production capabilities, and global distribution networks.

Research offers mixed conclusions about the benefits of being a first mover. Some studies suggest that a first mover typically enjoys an advantage for about a decade, while others argue that the advantages are minimal or short-lived. The key for executives is to assess whether a first move will create a sustainable competitive advantage. First moves that leverage strategic resources, such as patented technologies, are harder for competitors to replicate and thus are more likely to succeed. For example, Pfizer's patent on Viagra gave it a monopoly in the erectile dysfunction market for five years, and even after rivals entered the market, Viagra remains a significant revenue generator for the company, earning about \$1.9 billion annually.

Conversely, first movers that do not rely on strategic resources are more easily imitated. E-Trade Group's introduction of the portable mortgage, which allowed customers to transfer a mortgage when buying a new home, lacked protection from imitation by larger banks. As a result, even if the idea had gained traction, it could have easily been replicated, limiting E-Trade's ability to profit from being the first mover.

Application

- Describe a product that you like that is the result of a company following a first mover strategy. Discuss the advantages the company has by being a first mover.
- Describe a product that you like that is the result of a company following a fast follower strategy. Discuss the advantages the company has by being a fast follower.

Benefits	Risks
First mover	
Early market dominance, establishing strong brand recognition	High investment costs (R&D, marketing, education)
Technological leadership or innovation	Uncertainty and risk of market rejection or failure
Customer loyalty and potential for a long-term competitive edge	Competitors can learn from mistakes and avoid early pitfalls
Ability to shape market expectations and industry standards	Must educate the market and create demand from scratch
First-mover advantage (for example, intellectual property or exclusive contracts)	Early products may fail, resulting in financial loss or missed opportunities (for example, the Apple Newton)
Fast follower	
Lower risk, as they learn from the mistakes and successes of first movers	Lack of market leadership and potentially weaker brand recognition
Can improve upon existing products, offering enhanced features or lower costs	Risk of being perceived as imitative or lacking innovation
Reduced development costs from the adoption of proven technology and models	May face strong competition from the first mover or other followers
Faster market entry with established demand	Less control over market direction and customer perception
Ability to benefit from first-mover insights without bearing the full cost of market creation	Missed opportunity to set industry standards or gain early brand loyalty

Figure 9.8: First mover and fast follower strategies

Key Takeaways

A first mover is a company that enters a new market or launches a new product before any competitors, aiming to establish an early advantage. A fast follower is a firm that enters the market immediately after the first mover. There are benefits and risks to both approaches. The decision to be a first mover should be carefully evaluated based on whether the move offers the potential for a lasting competitive advantage. Without the right resources and strategic planning, first-mover status may offer only a temporary edge.

Being the first to enter a market can offer significant benefits, such as brand dominance and customer loyalty. However, it also comes with risks, including the costs of educating the market and the uncertainty of whether the product will be widely accepted. Later entrants can learn from a first mover's mistakes and refine their own offerings.

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9.6 Innovation Framework: Four Types of Innovation

In this section, you learn an innovation framework that considers four types of innovation that firms can leverage to drive growth and competitive advantage: incremental, disruptive, architectural, and radical innovation. Each type varies based on two key factors: whether it addresses an existing market or creates a new one and whether it utilizes existing technology or introduces new technology. Understanding these distinctions helps companies strategize how to innovate effectively, depending on their goals and market conditions.

Incremental Innovation

Incremental innovation involves enhancing an existing product or service by making improvements based on current technology and targeting the existing market. In the automotive industry, for example, incremental innovations take the form of yearly updates to car models, such as improved fuel efficiency, updated safety features, or minor design tweaks. These changes don't create new markets but instead refine the product using established technologies to offer a better version to existing customers.

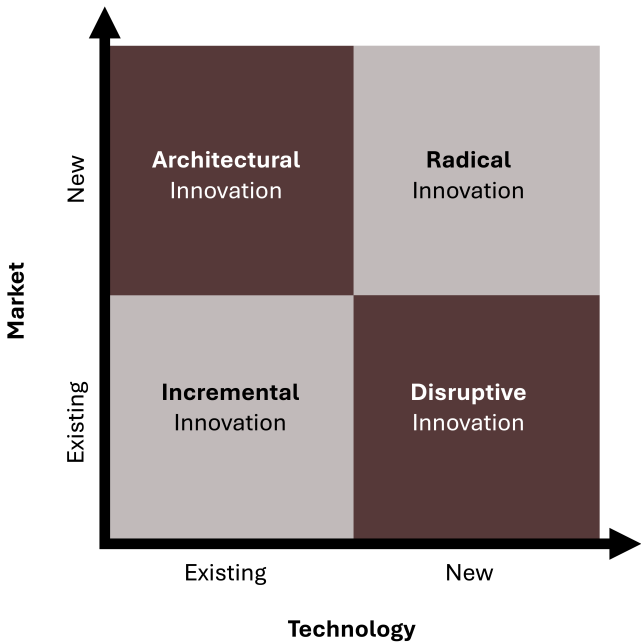


Figure 9.9: Types of innovation

Company	Example
Toyota	Toyota continuously updates its vehicles, such as by adding advanced driver-assistance systems or improving hybrid engine performance.
Samsung	Samsung's Galaxy smartphones are incrementally improved with better screen technology, faster processors, and enhanced camera capabilities.
Coca-Cola	Coca-Cola introduces new variations of its drinks, such as Coca-Cola Zero Sugar and smaller, more convenient packaging sizes.

Figure 9.10: Incremental innovation examples

Disruptive Innovation

According to a 2015 article by Christensen, Raynor, and McDonald, **disruptive innovation** occurs when a product or service initially enters a market by catering to an often underserved segment, often offering a simpler, more affordable solution than existing options. Over time, this innovation improves, eventually displacing established competitors. The key aspect of Christensen's definition is that disruptive innovations begin by targeting overlooked or low-end consumers before challenging mainstream markets.

However, the term *disruptive innovation* has often been misunderstood or misapplied. Many products labeled as disruptive are not. According to Christensen, true disruptive innovations initially underperform in comparison to established products but appeal to customers who value new dimensions, such as simplicity or lower cost.

A classic example is Netflix. When it first launched, Netflix's mail-order DVD rental service catered to a niche of customers who valued convenience over visiting brick-and-mortar video rental stores like Blockbuster. Over time, as internet speeds improved and streaming technology developed, Netflix moved upmarket, disrupting the entire entertainment industry and leading to the downfall of video rental stores.



Figure 9.11: Blockbuster

In contrast, products like Apple's iPad, often cited as disruptive, don't fully align with Christensen's definition. The iPad was a high-end, well-performing product at launch. While it impacted the laptop market, it didn't follow the typical path of targeting low-end or overlooked consumers before dominating the mainstream.

Christensen's perspective emphasizes that disruptive innovations don't succeed by merely being better than existing products; they succeed by reshaping the competitive landscape, starting in less-demanding markets and moving upward. For example, digital cameras began with lower-quality images and slower performance compared to traditional film, appealing mainly to niche market segments. As the technology advanced, they improved in quality and convenience, ultimately surpassing film cameras and transforming the photography industry. This shift led to the decline of film giants like Kodak, who struggled to adapt. True disruptive innovations can challenge and replace incumbents by fundamentally altering how businesses and customers operate within the industry.

Below are several examples of disruptive innovation.

- The rise of tablet computers has affected laptop sales due to their greater portability and multifunctionality. While reading books on traditional computers can be uncomfortable, devices like the iPad, Nook, and Kindle offer a more convenient experience and have become favored by textbook publishers.
- Numerous stores that depended on compact disc (CD) sales closed when downloadable digital media revolutionized the music industry. Prior to this, CDs had replaced vinyl records and cassette tapes because of their better durability and sound quality. Now, music subscription services like Spotify and Apple Music are taking the place of digital downloads. What emerging technology might eventually replace these subscription models?
- Digital cameras transformed the photography industry by providing immediate results and removing the need for film development. More recently, high-quality cameras on smartphones have disrupted the digital camera market.
- The rise of personal computers challenged the supremacy of mainframes, allowing individuals to own computers in their homes.
- LED lights, a more recent technology, are gradually replacing incandescent bulbs by capturing the existing market.

Typically, disruptive innovations start with a small, niche audience of early adopters and gradually gain traction as the product improves. For example, digital cameras were initially slow and produced lower-quality images compared to traditional film, limiting their appeal. However, as the technology advanced, digital cameras gradually won over even the most loyal film users. The iPad serves as another example, but with a different trajectory. Unlike most disruptive innovations, the iPad was an immediate success, quickly gaining widespread popularity across various demographics. Its intuitive design, portability, and versatile functionality allowed it to create a new category of devices (tablets), appealing to consumers, professionals, and educational institutions from the outset.

For companies considering disruptive innovation, patience and resilience are key. Growth may be slow at first, but the ability to navigate the initial period of low adoption is crucial to long-term success. Firms need to ensure they have the resources, capabilities, and core competencies to weather this slow build while improvements are made and a broader customer base develops.

Architectural Innovation

Architectural innovation is about transforming familiar technologies into new formats, often unlocking markets that didn't previously exist. By reimagining the structure or configuration of a product or service, companies can create offerings that appeal to entirely new audiences. A notable example is the smartwatch, which repurposed existing smartphone technology into a wearable device, creating a new consumer category. By integrating product capabilities like fitness tracking, notifications, and health monitoring into a compact, wrist-worn format, companies like Apple and Samsung redefined the potential of wearable tech and broadened the appeal of digital connectivity.

This form of innovation thrives on reshaping existing technologies in creative ways. Companies don't need to invent something entirely new; they just need to rethink how their current technologies can be used in different contexts. By doing so, firms can tap into new markets and meet the needs of consumers who may have been uninterested in the original product. Architectural innovation allows businesses to expand without reinventing the wheel—simply by giving old technologies a fresh, compelling new form.

Below are examples of effective architectural innovation.

- Peloton combines existing technologies such as bicycles, the internet, and communication tools to attract new customers who might not have purchased an exercise bike otherwise.
- Some companies have utilized solar cell technology to create small sources of rechargeable outdoor lighting, attracting a new group of consumers who use these eco-friendly lights to decorate their yards.
- Copiers were once large, costly machines designed for use in large offices. Canon and other companies redesigned these machines to be compact and desktop-friendly, opening up a new market for personal copier/printers.

Radical Innovation

Radical innovation occurs when entirely new technologies are used to create products or services that open up new markets. A prime example is the invention of the airplane, which revolutionized transportation by making long-distance travel feasible in ways that were previously unimaginable. Before air travel, a trip from New York to San Francisco could take weeks by car or train, but the airplane dramatically shortened this time, transforming the way people and goods moved across the world.

Radical innovation isn't just about introducing something new; it's about reshaping the landscape of what's possible. By utilizing groundbreaking technologies, companies can reach new consumers and create markets that didn't previously exist.

Artificial intelligence (AI) is a defining innovation of the current business landscape. Companies that respond effectively to disruptive, new, and emerging technologies, such as AI, are engaging in radical innovation. NVIDIA's CUDA platform opened up the parallel processing power of GPUs to general-purpose computing, enabling GPUs to complete complex AI and deep learning tasks. In healthcare, AI models analyze data to identify early signs of diseases before symptoms appear. AI in finance is used in algorithmic trading to analyze market data, predict market movements, and execute trades at optimal times.

Once a firm successfully launches a radically innovative product or service, they often shift to a strategy of incremental innovation, making continuous improvements to enhance performance and attract even more customers. For example, after the initial development of smartphones, which is an example of radical innovation, companies like Apple and Samsung used incremental innovation to add features like better cameras and faster processors, keeping consumers engaged and boosting sales. Radical innovations create the foundation, but it's the steady stream of enhancements that ensures long-term success.

Below are examples of radical innovation in different industries.

- Pharmaceutical researchers frequently develop groundbreaking products through innovative combinations of chemicals designed to treat medical conditions, which in turn draw new customers. For example, Aricept, a medication co-marketed by Eisai and Pfizer for managing Alzheimer's symptoms, has expanded market opportunities.
- Apple's AirPods represent a radical innovation, as the company created a wireless earpiece capable of receiving Bluetooth signals. Today, it's common to see people wearing AirPods, a shift from the past when wired earphones were more commonly used.
- The magnetic resonance imaging (MRI) machine utilizes electromagnetic forces, rather than X-rays, to capture internal images of the body. This innovation created an entirely new market, with hospitals investing in these machines to expand their diagnostic abilities.

Application

- Incremental innovation involves enhancing an existing product or service by making improvements based on current technology and targeting the existing market.
 - Describe a product that you like that is the result of a company following an incremental innovation strategy. Discuss the advantages the company has by following an incremental innovation strategy. Explain how the product is an existing product in an existing market.
- Disruptive innovation occurs when a product or service initially enters a market by catering to an often underserved segment, typically offering a simpler, more affordable solution than existing options.
 - Describe a product that you like that is the result of a company following a disruptive innovation strategy. Discuss the advantages the company has by following a disruptive innovation strategy. Explain how the product is a new product in an existing market.
- Architectural innovation is about transforming familiar technologies into new formats, often unlocking markets that didn't previously exist.
 - Describe a product that you like that is the result of a company following an architectural innovation strategy. Discuss the advantages the company has by following an architectural innovation strategy. Explain how the product is an existing product in a new market.
- Radical innovation occurs when entirely new technologies are used to create products or services that open new markets.
 - Describe a product that you like that is the result of a company following a radical innovation strategy. Discuss the advantages the company has by following a radical innovation strategy. Explain how the product is a new product in a new market.

Key Takeaways

There are four types of innovation that firms can leverage to drive growth and competitive advantage: incremental, disruptive, architectural, and radical. Each type varies based on two key factors: whether it addresses an existing market or creates a new one and whether it utilizes existing technology or introduces new technology. Incremental innovation involves enhancing an existing product or service by making improvements based on current technology and targeting the existing market. Disruptive innovation occurs when a product or service initially enters a market by catering to an often underserved segment, offering a simpler, more affordable solution than existing options. Over time, this innovation improves, eventually displacing established competitors. The key is that disruptive innovations begin by targeting overlooked or low-end consumers before advancing to challenge mainstream markets. Architectural innovation is about transforming familiar technologies into new formats, often unlocking markets that didn't previously exist. Radical innovation occurs when entirely new technologies are used to create products or services that open up new markets.

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9.7 Footholds

Just as rock climbers rely on footholds for stability and progress when ascending steep cliffs, firms use footholds to secure positions in markets where they are not yet established. In business, a **foothold** refers to a small but strategic entry point that a company deliberately creates in an unfamiliar market. This initial presence allows the firm to gather market insights, test the waters, and prepare for potential expansion. Footholds are factors in architectural and radical innovations, as they are the two types of innovation that involve entering new markets.

For instance, a company may acquire small local firms or open a limited number of stores in a new region as a way of gaining a foothold. This approach allows the company to understand local consumer behavior and competition without committing to large-scale operations right away. Once a foothold is secure, the firm can build from this position, gradually scaling up its presence and influence in the new market.

Below are examples that illustrate the use of footholds.

- When IKEA enters a new country, like Japan, it typically opens only one store initially. This first location serves as a showcase to build the brand's presence, and additional stores are opened once the brand has gained recognition (Hambrick & Fredrickson, 2005).
- Pharmaceutical leader Merck gained a strong position by acquiring SmartCells Inc., a company working on a potential new treatment for diabetes.
- The concept of a foothold is also relevant in warfare, where armies establish new positions in previously unoccupied territories. During World War II, the Allied Forces used Normandy, France, as a strategic base to launch their advance against German forces.

Many companies strategically use footholds to gain small but intentional presences in new markets before making larger commitments. A foothold provides a low-risk way to explore market dynamics and refine offerings without fully diving in (Upton et al., 2012).

Tech companies also use footholds to explore emerging markets. Microsoft often enters new industries by acquiring smaller startups, as it did with its purchase of Mojang, the developer of the popular game Minecraft. This foothold allowed Microsoft to enter the gaming space more robustly, later expanding its Xbox offerings and gaming services. Similarly, Amazon initially secured a foothold in the grocery market by acquiring Whole Foods. This strategic entry allowed Amazon to explore the grocery industry with an established brand while integrating its own e-commerce and logistics expertise. By using these smaller, calculated steps, companies like Microsoft and Amazon can test the waters in new markets before fully scaling their operations.

Application

- Think about your own personal experience in school. When have you made a small but strategic entry point in an unfamiliar area?
- Describe a time when you have gained a foothold. Perhaps it was with a new social group of friends. Maybe you made it happen by playing club sports. Have you gotten a foothold in a new subject, such as strategic management?
 - Discuss the advantages the foothold gave you.

Key Takeaways

A foothold refers to a small but strategic entry point that a company deliberately creates in an unfamiliar market. This initial presence allows the firm to gather market insights, test the waters, and prepare for potential expansion. This applies to architectural and radical innovations, as they are the two types of innovation that involve entering new markets. Radical and disruptive innovations have the potential to completely change industries by introducing new technologies that redefine markets. However, these innovations are typically followed by incremental improvements, which help sustain the product's market relevance and profitability over time. Establishing footholds allows companies to gain small but strategic presences in new markets, minimizing risk while gathering insights before committing to full-scale operations. This approach helps firms test their products or services and adapt before expanding.

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9.8 Innovation and Business-Level Strategy

We often think of innovation as applying to the products that high-tech companies produce, with innovation being a central focus for these companies. High tech companies typically follow a differentiation strategic market position and either a focused or broad strategic market size, choosing a broad differentiation business-level strategy or a focused differentiation strategy. However, those firms are not the only firms that focus on innovation. In fact, all companies need an innovation strategy. Innovation strategy is central to organizations that follow any type of business-level strategy.

Differentiation

For firms that follow a broad or focused differentiation strategy, innovation is typically more focused on product and service innovations. Innovation drives differentiation more externally through customers.

A part of the innovation strategy for firms that follow these strategies is high investments in R&D to fuel continuous product and service innovation. This is a clear choice, as they are operating in a business environment where customers want continuous upgrades to their products and services.

In high-tech industries, customers want new features and new product innovations. In the high-end fashion market segment for example, consumers want the latest fashion innovations. They also expect exceptional service and individualized attention.

Companies following focused or broad differentiation business-level strategies are able to demand higher prices for the latest products and services. They use the higher profit margins on their products and services to ensure a return on their R&D investments. Because of this, they can create new products and continuously introduce new or improved services to sustain their competitive advantage.

These firms focus on being the first to market with a new product or service. Firms that follow a differentiation strategy often aim to be first movers.

While all firms may use different types of innovation at different times, companies that approach strategic market position by targeting differentiation and cost leadership use the four types of innovation differently. Companies following a focused or broad differentiation business-level strategy use each type of innovation—incremental, disruptive, architectural, and radical—to innovate in customer-facing product and service innovation.

Cost Leadership

For firms that follow a cost leadership business-level strategy, either broad or focused, innovation is typically more internally focused on process optimization in support of lean operations that reduce costs.

Firms that follow a broad or focused cost leadership strategy focus on reducing costs in their firm value chains. To optimize operational efficiency and reduce costs, they focus on process innovation in their primary activities, such as in their inbound and outbound logistics and standardizing operations. They may also focus on doing the same in manufacturing, warehousing, and distribution. Because they have smaller profit margins, these companies must focus on enhancing operational excellence.

Firms that follow broad or focused cost leadership business-level strategies often aim to be fast followers. Their low investments in R&D do not generally support a first-mover approach. Industry leading cost leadership companies capitalize on innovations that other first movers have made by being fast followers.

All firms may use different types of innovation at different times. Companies that follow broad or focused cost leadership strategy use incremental, disruptive, architectural, and radical innovation to innovate internally, focusing on process innovation, operational efficiency, and cost reduction.

Application

- Describe how a value chain analysis would assist an analysis of innovation for a company following a cost leadership approach to strategic market position.
- Review [figure 5.9](#) to refresh your memory of a value chain analysis. Explain which primary and support activities offer the most potential for process optimization in support of lean operations that reduce costs. Illustrate your answer with an example of a company and discuss your rationale.

Key Takeaways

For firms that follow either a focused or broad differentiation strategy, innovation is typically more focused on product and service innovations. Innovation drives differentiation more externally through customers. These firms focus on being the first to market with a new product or service. Firms that follow a differentiation strategy often aim to be first movers. For firms that follow cost leadership approaches, either broad or focused, innovation is typically more internally focused on process optimization in support of lean operations that reduce costs. Industry-leading cost leadership companies capitalize on innovations that other first movers have made by being fast followers.

9.9 Product Life Cycle

When a new product is introduced to the market, it typically follows a progression through four distinct stages that represent the product life cycle. These stages are the same for all types of products, from high-tech gadgets like virtual reality headsets to every-

day items like cleaning solutions. Product life cycle stages apply primarily to architectural innovation (a product in a new market that uses an existing technology), radical innovation (a product in a new market that introduces new technology), and disruptive innovation (a product introduced in a new market that uses new technology). The four product life cycle stages are introduction, growth, maturity, and decline.

Introduction

In stage one, the product is launched with hopes of gaining traction in the market. Sales are usually slow at this stage as customer awareness for the product builds.

When the product is new to consumers, companies follow a first mover's approach, observing the first to introduce a product. Stage one of the product life cycle applies primarily to those types of innovation that introduce a product into a new market and/or uses new technology. This includes three types of innovation: architectural innovation, disruptive innovation, and radical innovation.

For example, the sustainable brand Patagonia, known for its eco-friendly outdoor clothing, introduced a line of clothing made from recycled materials, representing architectural innovation. The company entered a market of environmentally-conscious consumers by using existing materials but offering an innovative product that focused on sustainability. This approach helped Patagonia stand out as a leader in the sustainable fashion industry.

Growth

Then in stage two, as the product begins to gain popularity, sales begin to steadily increase. Competitors, including many fast followers, enter the market, though competition remains manageable, allowing room for growth. For both the original product designer and imitators, conducting a Porter's Five Forces analysis at this stage is valuable to assess the threat of new entrants. This analysis helps the original designer understand how to maintain their competitive edge, while imitators can identify opportunities to differentiate or compete on cost. By understanding the dynamics of competition, barriers to entry, and the potential power of suppliers and buyers, both groups can strategically position themselves for sustained success in the growing market.

Maturity

Once a product market has grown rapidly and sales have increased in the growth stage, the product reaches maturity in the market. The early maturity stage is characterized by continued growth and sales. Then market saturation is reached, and sales reach their peak in the later phase of the maturity stage. By the end of the maturity stage, market growth slows as the market becomes saturated. Competition intensifies, and a shakeout occurs, where some competitors exit or merge with others. Conducting a Porter's Five Forces analysis to analyze the threat of substitute products is also valuable at this stage.

Decline

Finally, the product life cycle ends in a stage of decline. Sales start to drop as the product loses relevance or market demand decreases. Fewer competitors remain, and firms begin looking for exit strategies or ways to consolidate. During the decline stage, the product's placement on the Boston Consulting Group matrix can give executives initial information about whether to divest the product line from their portfolio.

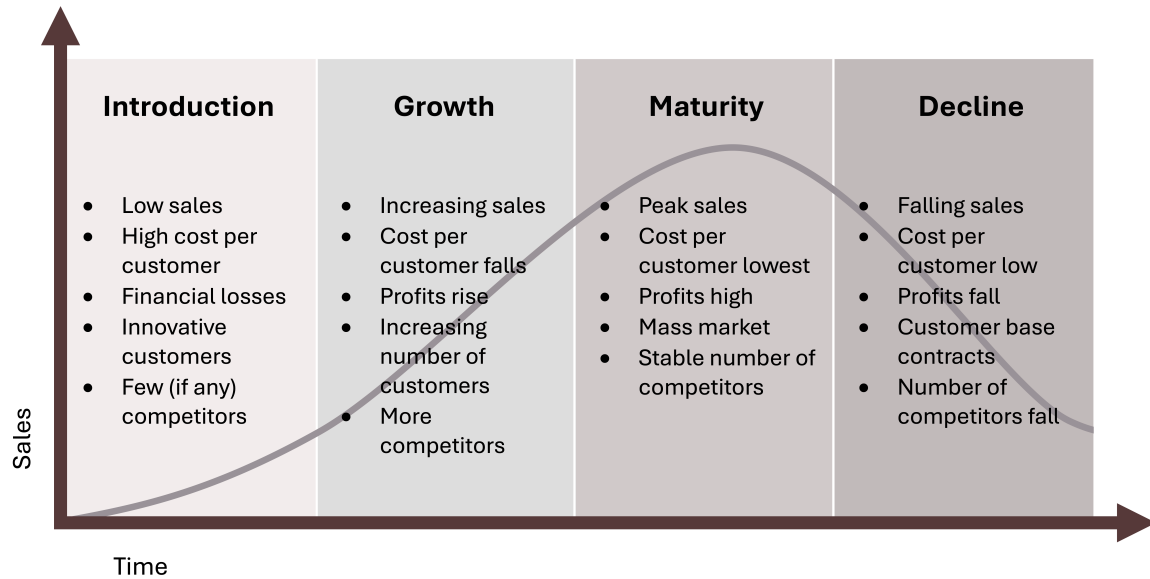


Figure 9.12: Product life cycle

This life cycle can be visualized as a bell curve, with sales starting low during the introduction stage, rising during the growth stage, peaking during the maturity stage, and eventually falling during the decline stage. Notice the bell curve is not symmetrical, as the product life cycle curve for stage one, product introduction, rises much more slowly than stage two, the growth stage. First movers who introduce a new product must be prepared to weather stage one and continue to invest in the product and its production as well as marketing so that they reach stage two, growth, when the life cycle curve is much steeper. During stage one, companies must create capacity in all areas of both the firm and industry value chains to be ready to adequately deal with the growth stage of the product.

Product Life Cycle Extension

To avoid or delay the decline stage of a product's life cycle, companies often relaunch their products by introducing updated or improved versions. This is an example of incremental innovation (introducing products in existing markets using existing technology), and it helps revitalize interest and effectively restarts the product life cycle. For example, Apple frequently updates its iPhone with new features to maintain consumer demand, and car manufacturers like Ford and Toyota regularly release improved models to keep their products competitive. This cycle of innovation helps extend the product's lifespan in the market.

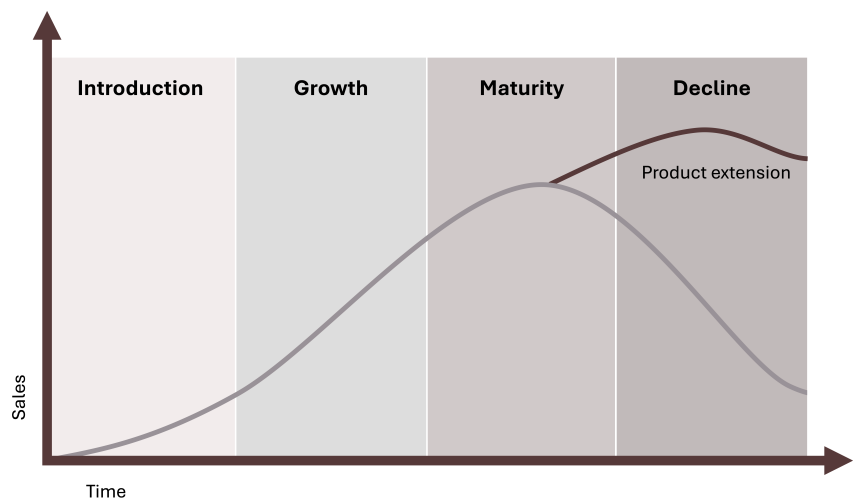


Figure 9.13: Product life cycle extension

Profits During the Product Life Cycle

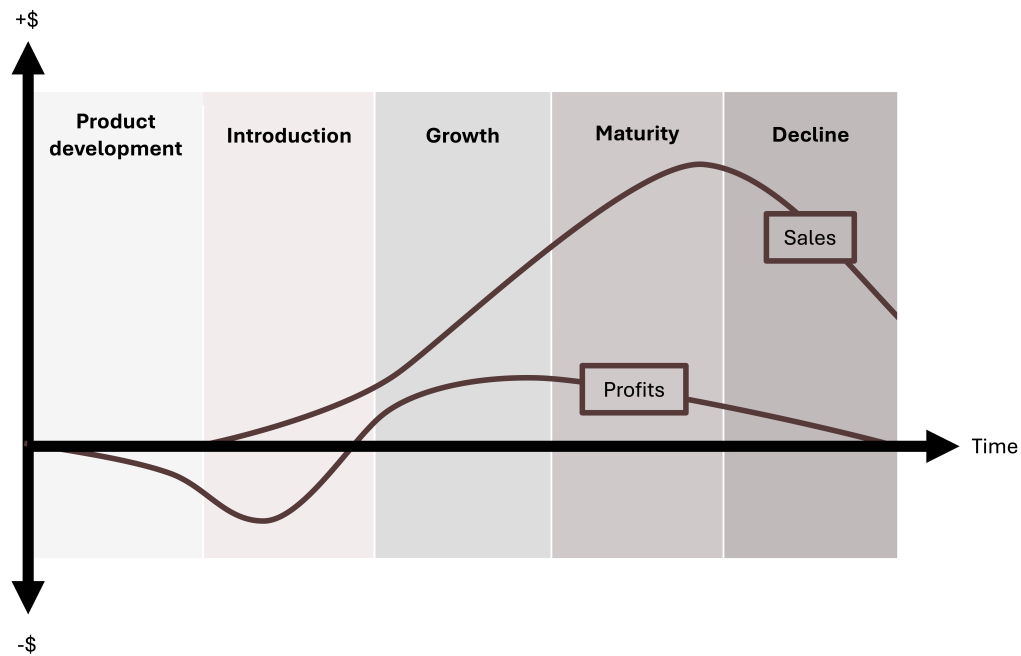


Figure 9.14: Profits during the product life cycle

Profits throughout a product's life cycle typically follow a predictable trajectory. In the early research and development (R&D) phase, a company invests heavily in developing the product, resulting in negative profits as costs outweigh revenue. This trend continues into the introduction stage, where sales are still low and significant marketing expenses are required to build awareness, further delaying profitability.

The turning point occurs in the growth stage, where increasing sales allow the firm to start recouping its initial investment in R&D and marketing. Profits usually peak at the beginning of the maturity stage as sales reach their highest levels. However, as competition intensifies during this stage, companies are often forced to lower prices, which erodes profit margins. By the time the product enters the decline stage, profits shrink significantly, and firms may begin looking for ways to exit or consolidate. This pattern highlights the importance of planning throughout the product life cycle to maximize profitability, especially during the growth and early maturity phases when the potential for returns is highest.

Application

- Think about a product you like and use frequently.
 - Describe the product's life cycle.
 - What stage is the product in now?
 - At what stage did you purchase the product?

Key Takeaways

When a new product is introduced to the market, it typically follows a progression through four distinct stages that represent the product life cycle. These stages are the same for all types of products, from high-tech gadgets like virtual reality headsets to everyday items like cleaning solutions. Product life cycle stages apply primarily to architectural innovation, radical innovation, and disruptive innovation. The four product life cycle stages are introduction, growth, maturity, and decline. To avoid or delay the decline stage of a product's life cycle, companies often relaunch their products by introducing updated or improved versions. This is an example of incremental innovation, and it helps revitalize interest and effectively restarts the product life cycle. Profits throughout a product's life cycle typically follow a predictable trajectory.

9.10 Crossing the Chasm

Now that you have learned about the four stages of a product's life cycle, how that life cycle can be extended, and profits during a product's life cycle, you can now learn a closely related idea—crossing the chasm. Crossing the chasm is a concept related to the stages of consumer adoption of a company's new product or service. It can also apply to industrywide innovations, which are usually technology advancements, such as AI and media streaming services.

The point when a firm's new product or an industry's technological advancement crosses the chasm is the point when the success of a new product is more certain. To illustrate this, we review the five stages of a product's or technology's adoption life cycle and the related concept of crossing the chasm.

The five stages of a product's, service's, or technology's adoption life cycle include innovators, early adopters, early majority, late majority, and laggards. As you can see, the stages of the adoption life cycle correspond to consumer characteristics. These consumer characteristics influence many business aspects of the new product or technology, such as the firm's marketing approach. Crossing the chasm happens between the early adopters and early majority stages.

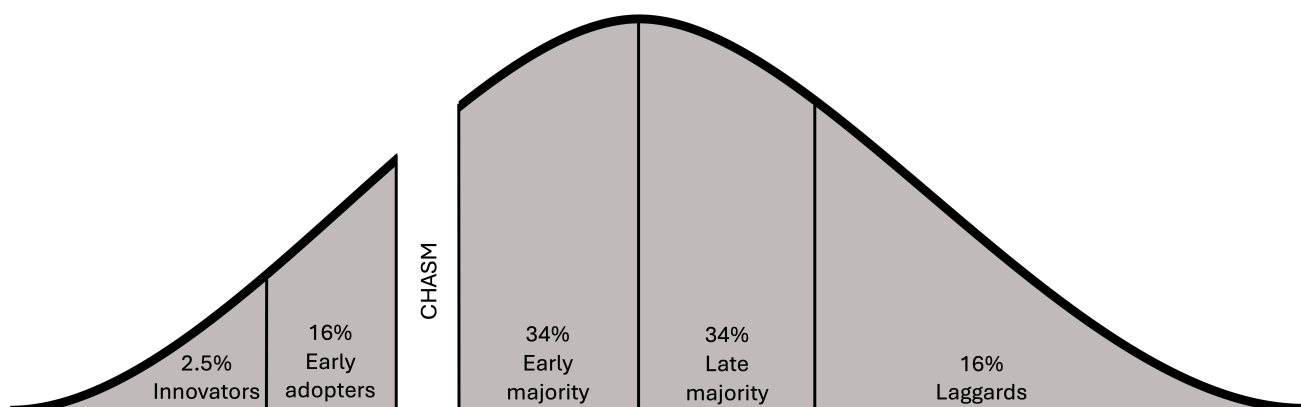


Figure 9.15: The adoption cycle of a company's product or service, or an industry's technological advancement

Innovators

When a new product, service, or technology is introduced, it is typically adopted first by innovators—people eager to experiment with cutting-edge advancements. These are consumers enthusiastic about the new product, service, or technology. They are typically tuned into the product's market and may even be eagerly awaiting the next advancement. They may be motivated by the need or want for the new product addresses by the desire to be one of the first to use the new product, or both. Innovators make up about 2.5 percent of the market potential of a product.

Early Adopters

Early adopters are a slightly larger group and follow closely behind innovators. Early adopters show early interest in trying out the product, service, or technology. Early adopters share some characteristics with innovators. These are consumers that are also enthusiastic about the new product or service. Early adopters make up about 13.5 percent of the market potential of a new technology.

Once innovators and early adopters are onboard with a new product or service, about 16 percent of the product's potential market share is using the new product. This is still a small percentage of the potential for the new product.

Crossing the Chasm

The real challenge for many companies and industries lies in moving beyond these innovators and early adopters and gaining traction with the broader, more mainstream consumer group. This leap to the mainstream is what's referred to as crossing the chasm, and it often requires a different business and marketing approach to succeed. Innovators and early adopters represent about 16 percent of the overall market.

Early Majority

For the product, service, or technology to become a success, companies must strategize on how to reach the early majority, those customers who represent a larger majority of the market potential for the product. These customers are both enthusiastic about the new product and cautious enough to wait to be sure it is likely to catch on before buying it. They may respond to assurances the new technology is here to stay and is worth their investment. The early majority comprises about 34 percent of the potential market.

Failure to convince the early majority to adopt the product typically leads to the product's demise. An example of a product that failed to cross the chasm is Google Glass. While it was highly innovative, offering internet-connected eyeglasses that could display information and take photos, its practical value was unclear. Despite generating interest among early adopters, the product did not resonate with the broader market, leading to its failure.

Electric vehicles represent a current example of an industry wide technology in the process of crossing the chasm to mainstream adoption. In recent years, EV adoption has accelerated significantly, with global EV sales accounting for 14 percent of all new car sales in 2023. However, despite this growth, there are still challenges preventing EVs from fully reaching the early majority. Key factors include concerns about charging infrastructure, range anxiety, and the higher upfront costs compared to traditional gas-powered cars. While automakers like Tesla, Ford, and Rivian have made significant strides in addressing these concerns by expanding charging networks and improving battery efficiency, many consumers remain cautious. For EVs to fully cross the chasm into mainstream adoption, these concerns must be further alleviated through more widespread infrastructure, lower costs, and greater education on the long-term benefits of electric vehicles.

As you can see, once early adopters embrace a product, service, or technology, the adoption life cycle peaks at the top of the bell curve. This now represents 50 percent of the potential market. Half the market remains to be attracted to a firm's product. This is useful information for companies to plan for the next phase in the product life cycle, the late majority.

Late Majority

Consumers in the late majority stage of the adoption cycle of a product, service, or technology are more cautious than early majority adopters. There are many reasons consumers wait to adopt a product, and it is important for a firm to understand their consumer base so that they can tailor their marketing and other business approaches accordingly. The late majority represents 34 percent of the potential market. Once the late majority has joined other consumers in owning the product, the product is used by 84 percent of the potential market.

Laggards

Laggards represent the last group of consumers to come onboard with a new product, service, or technological advancement. Laggards represent the remaining 16 percent of the potential market.

Consumers in all stages of the adoption cycle may belong to their respective groups for multiple reasons ranging from values to affordability. Understanding the specific product adoption cycle of a firm's products or services or of an industry's technological advancement is essential to developing approaches that resonate with each group and ensure full market saturation.

Application

- Think about a company with a line of products, such as Apple or Amazon.
 - Describe products that have crossed the chasm and ones that did not. Explain your rationale.

Key Takeaways

Crossing the chasm is a concept related to the stages of consumers' adoption of new products or services. It can also apply to industrywide innovations. The point when a new product crosses the chasm is the point when its success is more certain. The five stages of a product's adoption life cycle include innovators, early adopters, early majority, late majority, and laggards. The challenge for many companies and industries lies in moving beyond the innovators and early adopters and gaining traction with the broader, more mainstream consumer groups. This leap to the mainstream is what's referred to as crossing the chasm.

9.11 Cooperative Moves

Bill Gates once noted, “Our success has really been based on partnerships from the very beginning.” In today’s business environment, cooperation between firms is often just as critical as competition. While competition drives innovation and improvement, collaboration allows companies to tackle larger challenges, access new markets, and leverage each other’s strengths. Below, we explore four common cooperative strategies that firms use to enhance their market positions and achieve shared success. Beyond competing head-to-head, businesses can unlock significant advantages by working together.

In [Chapter 7](#), we introduced a make-contract-create-acquire continuum to show the ways a firm can diversify. This same framework can be used to cooperate with other firms.

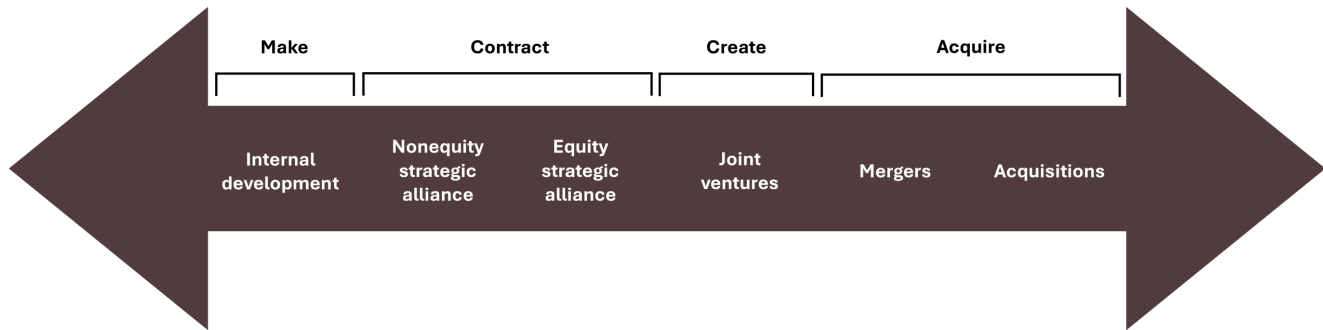


Figure 9.16: Make-contract-create-acquire continuum

Internal Development

Internal development occurs when firms can choose to build new capabilities and core competencies in-house. This strategy is more competitive than cooperative, as it relies on a firm’s own resources, capabilities, core competencies, entrepreneurial orientation (EO), and innovative culture to drive growth. As previously noted, Apple is an excellent example of a company that relies heavily on internal development.

Internal development taps into intrapreneurship, where employees within the organization use their entrepreneurial skills to create new products or services. Although internal development can take longer and require significant investment, it allows a company to retain full control over its innovations and processes.

Strategic Alliances

Strategic alliances occur when firms partner through an agreement to work together on a specific goal while maintaining their independence.

For example, Starbucks and Spotify formed a strategic alliance to blend coffee culture with music streaming. Through their partnership, Starbucks employees and customers gained access to exclusive playlists on Spotify, and Spotify gained increased visibility through Starbucks’ vast network of stores. Both companies maintained their separate operations, but their collaboration enhanced customer experiences and created mutual benefits.

Another example is the partnership between Nike and Apple, which led to the development of the Nike+iPod activity tracker. This strategic alliance blended Nike’s athletic expertise with Apple’s tech innovation, allowing users to track their workouts using iPods integrated with Nike shoes. It was a win-win for both brands. Nike became more tech-forward, and Apple strengthened its presence in the fitness world without the need for either company to merge or create a new business entity.

The pharmaceutical industry often relies on strategic alliances to drive innovation and growth. For example, Merck and PAREXEL International Corporation formed a strategic alliance to collaborate on biotechnology, specifically focusing on developing biosimilars—pharmaceutical drugs that have properties of other, pre-existing drugs. This alliance is crucial for Merck, as the global biosimilars market is expected to experience substantial growth in the coming years (PRWeb, 2011). Through partnerships like this, pharmaceutical companies can pool resources and expertise, accelerating advancements in medical technologies.

Joint Ventures

A **joint venture** is when two or more companies combine to create a separate, shared entity. Each partner has a stake in the new venture, involved in everything from decision-making to profits, creating a collaborative relationship with joint responsibility.

Take the collaboration between Google and Fiat Chrysler as an example. The two companies formed a joint venture to develop self-driving cars. Google brought its advanced technology in autonomous driving, while Fiat Chrysler contributed its expertise in vehicle manufacturing. Together, they created a new frontier in the automotive industry that neither could have tackled alone as effectively. By sharing their strengths, both companies could accelerate innovation in the race for autonomous vehicles.

In another scenario, Sony and Ericsson teamed up to form Sony Ericsson, a joint venture aimed at combining Sony's expertise in consumer electronics with Ericsson's strong background in telecommunications. The goal was to create cutting-edge mobile phones, which was a market both companies wanted to dominate. Although the joint venture eventually dissolved, during its time, it allowed both companies to compete more effectively against major players in the mobile phone industry.

Collaboration through joint ventures or strategic alliances can open doors to opportunities that might be out of reach if a company tried to go it alone. By pooling resources, knowledge, and expertise, firms can move more quickly and efficiently. However, cooperation isn't without risks. Companies may face loss of control, potential leaks of confidential information, or even exploitation by their partners (Ketchen et al., 2004).

In both joint ventures and strategic alliances, businesses find creative ways to collaborate, capitalizing on each other's strengths to achieve more than they could on their own. However, these partnerships require trust, clear goals, and a careful balancing of interests to succeed.

Mergers and Acquisitions

Another common way companies collaborate for mutual benefit is through mergers and acquisitions (M&A). In a **merger**, two companies of roughly equal size combine to form a new, stronger entity. A high-profile example is the merger of T-Mobile and Sprint, which transformed the two smaller wireless providers into a more formidable competitor against industry giants like AT&T and Verizon. Sometimes, the merged companies retain elements of both names, such as the case with Exxon and Mobil merging to form ExxonMobil, while other times, a new name or one firm's name is used moving forward.

Acquisitions, on the other hand, usually involve a larger company purchasing a smaller one. For example, Google acquired FitBit. Although the end result is similar to a merger, acquisitions often result in the larger firm absorbing the smaller one, though in some cases the acquired firm maintains its separate identity. Mergers and acquisitions can combine complementary strengths, eliminate competitors, and enhance market share.

However, M&A activities come with significant risks. According to a *Harvard Business Review* study, between 70 percent and 90 percent of mergers and acquisitions fail (Lakelet Capital, 2019). This failure rate is often attributed to challenges like integrating different corporate cultures, underestimating the total costs of the deal, and technical or operational mismatches between the two companies. In addition, acquisitions are sometimes driven by CEOs eager to boost short-term revenues without fully considering the long-term implications, a situation referred to as an agency problem, which will be discussed in more detail in [Chapter 10](#).

Application

- Think of companies you have studied in your business education.
 - Describe an example of a strategic alliance and an example of a joint venture that were used as a means of cooperating rather than competing. Explain your rationale.

Key Takeaways

In today's business environment, cooperation between firms is often just as critical as competition. While competition drives innovation and improvement, collaboration allows companies to tackle larger challenges, access new markets, and leverage each other's strengths. Internal development occurs when firms can choose to build new capabilities and core competencies in-house. This strategy is more competitive than cooperative, as it relies on a firm's own resources, capabilities, core competencies, entrepreneurial orientation, and innovative culture to drive growth. Strategic alliances occur when firms partner through an agreement to work together on a specific goal while maintaining their independence. A joint venture is when two or more companies combine to create a separate, shared entity. Each partner has a stake in the new venture in all aspects from decision-making to profits, creating a collaborative relationship with joint responsibility. In a merger, two companies of roughly equal size combine to form a new, stronger entity. Acquisitions, on the other hand, usually involve a larger company purchasing a smaller one. While cooperation through alliances, joint ventures, and mergers can provide firms with significant strategic advantages, they also come with risks such as loss of control, cultural clashes, and agency problems. Companies must carefully weigh these risks against potential benefits to succeed in today's competitive landscape. Cooperation between firms through internal development, strategic alliances, or joint ventures allows companies to pool resources and expertise to achieve common goals.

Instead of acquiring external expertise, firms can develop new capabilities in-house. Internal development fosters innovation within the organization and encourages intrapreneurship, allowing the firm to retain control over new products and services while leveraging its entrepreneurial orientation.

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9.12 Responding to Innovation in the Market

In fast-paced industries, executives often contend with constant competitive pressures, such as aggressive marketing, price cuts, and attempts to poach key customers. Quick responses are vital, as delays can give competitors a significant edge. For example, when Samsung launched its Galaxy Fold, Apple took time before introducing a competing foldable phone, allowing Samsung to gain an early foothold in the foldable phone market. Conversely, when Apple introduced the Apple Watch, Samsung swiftly responded with the Galaxy Watch, preventing Apple from monopolizing the emerging wearable tech space. As former General Electric CEO Jack Welch famously noted, success in competition relies less on perfect predictions and more on the ability to react swiftly to evolving market conditions.

Multipoint Competition

When companies compete against the same rival across multiple markets and market segments, this is known as **multipoint competition** (or multimarket competition), which makes decisions about responses more complex. Take the rivalry between cigarette manufacturers R.J. Reynolds (RJR) and Philip Morris, which compete in both U.S. and international markets. When RJR lowered prices in the U.S. to gain customers, Philip Morris responded by cutting prices in the U.S. and ramping up its presence in Eastern Europe, forcing RJR to defend itself on two fronts.

In some cases, rivals recognize that aggressive moves could lead to costly retaliation, resulting in mutual forbearance. For example, Southwest Airlines and United Airlines once found themselves poised to compete more aggressively, but when Southwest's CEO publicly threatened retaliation, United backed off. Both firms benefited from avoiding direct conflict, preserving profits that would have been eroded by unnecessary competition.

Responding to Disruptive Innovations

When a disruptive innovation challenges an industry's established norms, companies have three main ways to respond. First, executives might choose to stick with traditional business models, hoping the disruption doesn't fully displace their offerings. This was the case with Barnes & Noble, which initially underestimated the threat of Amazon's online bookstore. Second, firms can counter-attack by innovating along different dimensions, as Apple did when it responded to low-cost competitors like Dell by adding more features and power to its products. The third option is to match the competitor's move, as Merrill Lynch did when it launched its own online trading platform, recognizing that ignoring the disruption could cost them future customers.

Fighting Brands

When a competitor undercuts a firm by offering lower-priced goods or services of comparable quality, one response is to create a fighting brand. A **fighting brand** is a lower-end product introduced specifically to protect the firm's market share without devaluing its primary brand. In the late 1980s, General Motors (GM) responded to the growing popularity of affordable Japanese cars by creating the Geo brand. GM didn't want to hurt its established brands like Chevrolet and Cadillac, so it sold low-cost cars under the Geo name instead. Interestingly, some Geo models were produced in joint ventures with the same Japanese companies against which GM was trying to compete. By the late 1990s, however, the market shifted toward higher-quality vehicles, and Geo was discontinued.

Some fighting brands are short-lived and fail to achieve their desired objectives. Take the case of GlaxoSmithKline's (GSK) attempt to protect its market share in Europe. When the patent for its popular asthma drug, Seretide, was about to expire, GSK launched Seretide Eco, a lower-cost version aimed at preventing customers from switching to generic alternatives. However, once generics hit the market, Seretide Eco wasn't priced competitively enough, and customers quickly migrated to cheaper options. GSK soon discontinued the brand, marking the effort as a misstep in the fight against generics.

The airline industry offers similar cautionary tales. In response to the growing success of budget carriers like Ryanair and EasyJet, British Airways launched Go in the late 1990s as a low-cost alternative. Despite initial interest, Go struggled to compete with established budget airlines and was sold off in 2002. Similarly, Scandinavian Airlines introduced Snowflake in 2003 to rival low-cost carriers, but the brand was discontinued two years later due to poor performance. These examples highlight the challenges legacy carriers face when trying to succeed in the discount market, where competing on cost often conflicts with their existing differentiation strategies based around, for example, reputation or luxury. As seen here, shifting from a differentiation to a cost leadership strategy, or vice versa, can be especially difficult for established companies, whose resources, capabilities, core competencies, and brand identities are deeply tied to their original market positioning.

However, not all fighting brands face the same fate. Some have proven to be enduring successes. A notable example is Toyota's creation of Scion in the early 2000s. Designed to appeal to younger, budget-conscious consumers without diluting Toyota's premium image, Scion successfully built a niche market segment in the compact car market for over a decade before being discontinued in 2016 when market conditions shifted. Another success story comes from Unilever, which launched Axe as a lower-priced men's grooming product in response to competition from smaller, upstart brands. Axe not only reclaimed market share but also grew into a globally recognized brand in its own right.

These successful examples illustrate how fighting brands, when well-conceived and properly positioned, can effectively protect a company's market share without undercutting its premium offerings. However, as the failures demonstrate, launching a fighting brand requires careful strategy and a deep understanding of market dynamics.



Figure 9.17: The Geo brand was recognized for its affordability and fuel efficiency rather than its design

Co-Location

Co-location refers to the strategy of situating different businesses near one another, creating a collective hub that draws more customers than each would individually. A prime example can be seen in bustling tech hubs like Austin, Texas, where startups and tech giants like Dell, IBM, and Oracle are clustered. The proximity of these firms fosters an ecosystem that attracts talent, investors, and business opportunities, all while benefiting the companies involved.

Similarly, retail outlets like outdoor gear shops, bike stores, and coffee shops tend to pop up near hiking trails or in adventure sports districts, appealing to specific clientele. These clusters thrive because customers appreciate the convenience of having multiple options in one location.

Some companies also leverage co-location by positioning their own brands close together. For example, Hilton might strategically place a Hampton Inn next to a higher-end Hilton Garden Inn, allowing them to capture both budget and premium travelers without losing customers to competitors.

In the fast-casual dining space, Dunkin' often co-locates with Baskin-Robbins in shared storefronts, giving customers the option of coffee or ice cream under one roof. Similarly, Coca-Cola places multiple different vending machines in the same locations, offering soda, juice, and water so that every consumer's thirst is quenched. Co-location doesn't just provide customers with choice; it also helps businesses maximize foot traffic and diversify their offerings within the same space.



Figure 9.18: Co-located brands

Co-Opetition

Although competition and cooperation are usually viewed as opposing forces, the concept of co-opetition reveals a more intricate dynamic in which firms can simultaneously collaborate and compete.

Ray Noorda, founder of Novell, coined the term to describe a blend of rivalry and partnership. For example, tech giants Microsoft and Samsung compete directly in the electronics market, but they have also partnered to integrate Microsoft's software into Samsung devices. This allows both companies to benefit from each other's strengths while still maintaining competition in other areas. Similarly, Google and Apple are competitors in the smartphone market, but they collaborate through partnerships in mapping and app development, working together on projects while competing for consumer attention.

A notable example of co-opetition is the partnership between Ford and Volkswagen. While the two automakers fiercely compete in the global car market, they have joined forces in the development of electric vehicles and autonomous driving technologies. The collaboration allows both companies to reduce research and development costs while pooling their expertise in these cutting-edge fields. At the same time, they continue to compete for market share, with each striving to outsell the other in regions around the world.

In their book *Co-opetition*, Adam Brandenburger and Barry Nalebuff argue that firms often collaborate to “create the pie” and then compete to “divide it up.” In other words, companies typically cooperate in areas removed from direct customer interaction, such as research and development, but become rivals when it comes to sales, marketing, and distribution.

For instance, in the Scandinavian telecom industry, firms have been known to collaborate on infrastructure development but fiercely compete in consumer products and services. Similarly, in the food and beverage industry, companies might work together on sustainability initiatives like waste management or packaging innovation, while competing aggressively in branding and retail strategies.

Application

- Think of companies you have studied in your business education.
 - Describe examples of a multipoint competition, fighting brand, co-location, and co-opetition as a means of responding to innovation in the market. Explain your rationale.

Key Takeaways

In fast-paced industries, executives often contend with constant competitive pressures, such as aggressive marketing, price cuts, and attempts to poach key customers. Quick responses are vital because delays can give competitors a significant edge. When companies compete against the same rival across multiple markets and market segments, known as multipoint competition (or multimarket competition), decisions about responses become more complex. When a disruptive innovation challenges an industry's established norms, companies have three main ways to respond: stick with traditional business models, counterattack by innovating along different dimensions, or match the competitor's move. When a competitor undercuts a firm by offering lower-priced goods or services of comparable quality, one response is to create a fighting brand. Co-location refers to the strategy of situating different businesses near one another, creating a collective hub that draws more customers than each would individually. Co-opetition is a blend of rivalry and partnership. By partnering on specific initiatives, companies can pool resources and expertise, reducing the costs of innovation. This approach helps firms accelerate innovation while remaining competitive in other market segments.

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9.13 Measuring Innovation Performance

Measuring the performance of innovations involves assessing both the success of new initiatives and their impact on overall business outcomes. Various metrics can be employed to capture the effectiveness of innovation strategies and investments.

One common approach is to evaluate the percentage of sales generated from products or services launched within a specific time frame. This metric indicates the contribution of recent innovations to the company's overall revenue. Another useful measure is the

success ratio, which compares the number of successful innovations to the total number of initiatives undertaken. This helps assess the efficiency and effectiveness of the innovation process. Innovation output is sometimes measured as the percentage of product sales which were new to market (Laursen & Salter, 2006).

Revenue growth attributed to new products and services can highlight how much innovation is driving top-line growth. Companies can also track the return on invested capital from innovation-related projects, providing insight into the profitability of innovation efforts relative to the resources invested.

In addition, companies often calculate the net present values of their innovation portfolios. This metric estimates the long-term financial return from innovation projects, helping organizations prioritize and manage their innovation investments for future growth.

These metrics, when combined, offer a comprehensive view of how well innovation efforts are contributing to both short-term performance and long-term strategic objectives.

Measure	Description	Purpose
Percentage of sales from new products/services	Evaluates the percentage of sales generated from products or services launched within a specific time frame.	Indicates the contribution of recent innovations to overall revenue.
Success ratio	Compares the number of successful innovations to the total number of initiatives undertaken.	Assesses the efficiency and effectiveness of the innovation process.
Innovation output	Measures the percentage of product sales that were new to the market.	Tracks how much of the company's sales come from new innovations.
Innovation quality (forward citations)	Measures the number of forward citations to patents, indicating technological impact.	Assesses the technological significance and impact of innovations.
Revenue growth from new products/services	Tracks revenue growth directly attributed to innovations in products or services.	Highlights how much innovation drives top-line growth.
Return on invested capital (ROIC)	Calculates the return on capital invested in innovation-related projects.	Provides insight into the profitability of innovation investments.
Net present value (NPV) of innovation portfolio	Estimates the long-term financial return from innovation projects.	Helps prioritize and manage innovation investments for future growth.

Figure 9.19: Measures of innovation strategy and investment effectiveness

Key Takeaways

Measuring the performance of innovations involves assessing both the success of new initiatives and their impact on overall business outcomes. Various metrics can be employed to capture the effectiveness of innovation strategies and investments.

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9.14 Analyze Innovation Strategy

When you conduct a case analysis, you analyze a firm's innovation strategy. This is step six in the case analysis process.

6. As appropriate to the case, analyze strategies: Corporate-level, business-level, innovation, sustainability and ethics, technology, and multinational strategies

- Use strategic management analytical frameworks to analyze, interpret, and evaluate strategies.
- Ensure line of sight and congruence within analysis of each strategy.

9.15 Why Innovation Strategy Is Important to Business Graduates

Because innovation strategy is formulated at the strategic business unit of a firm and embedded into a company's business-level strategy, graduates starting as business support unit managers in support business units in large companies, such as marketing managers, will see that innovation has a direct influence on the implementation of key functional-level strategy. For example, whether a firm chooses a first mover or fast follower approach directly influences the day-to-day work of business support unit managers. Whether a firm follows an incremental, disruptive, architectural or radical innovation strategy, business executives and divisional or strategic business unit managers may solicit data analysis from functional business managers of business information technology, accounting, and marketing.

Business graduates joining smaller companies will spend even more time working closely with executives responsible for innovation strategy from the start. Business graduates that serve in internal or external consulting roles require a high level of competence with innovation strategy to communicate with business executives how their consulting projects fit into the overall innovation strategy of the firm. For business graduates who already are or will become entrepreneurs, fluency with innovation strategy is essential to establishing and growing a successful firm.

9.16 Conclusion

This chapter delves into the critical role of innovation in shaping a company's strategy and the various ways firms can navigate competitive pressures. By fostering an entrepreneurial mindset, companies can drive innovation, though being a first mover comes with both advantages and risks, as competitors may learn quickly and overtake the pioneer. Alternatively, firms may take a more measured approach, establishing footholds in niche market segments or using a blue ocean strategy to avoid direct competition altogether.

Innovation manifests in four key types: incremental, disruptive, architectural, and radical. Most new products follow a familiar life cycle of introduction, growth, maturity, and decline. However, incremental improvements often allow firms to reintroduce products, renewing their relevance. To achieve mainstream success, companies must help new products “cross the chasm” into wider acceptance. Collaboration also plays a key role, with firms forming joint ventures and strategic alliances or even engaging in co-opetition, where they cooperate and compete simultaneously. In some cases, companies may launch fighting brands to protect market share from low-cost competitors. All of these tactics are part of a broader strategic management process that allows firms to adapt and thrive in dynamic markets.

Demonstrate Your Knowledge, Skills, and Competence

Use these questions to test your knowledge of the chapter:

1. Describe innovation strategy and its relationship to business-level strategy.
2. Explain entrepreneurial orientation (EO) and three core traits that make up EO. Explain intrapreneurship and its relationship to entrepreneurship. Are you more likely to demonstrate your EO through being an entrepreneur or an intrapreneur?
3. Describe why innovation is important for companies. Discuss the risks for companies that fail to innovate.
4. Explain in detail first movers and fast followers and the benefits and risks of each.
5. Describe the innovation framework, including the two key factors that are central to the framework and the resulting four types of innovation.
6. Explain footholds and how these relate to innovation.
7. Explain how firms that use cost leadership and differentiation approach innovation differently. Discuss how a value chain analysis can support cost leadership differentiation.
8. Describe the product life cycle and its four stages. Explain how the product life cycle can be extended. Describe the relationship of profits to the product life cycle. Give an example.
9. Describe what crossing the chasm means. Give an example.
10. Using the make-contract-create-acquire continuum, describe how companies may cooperate.
11. There are multiple ways firms can respond to innovation in the market. Explain these in detail, and give an example of each.
12. Refer to figure 9.19 and ensure you understand each measure and their purpose and can use them in a case analysis. If there are any areas you need to study further, we encourage you to do this now because you use these concepts throughout the course.
13. Describe how competence with innovation strategy is relevant and important to you.

By answering these questions robustly, you have demonstrated your thorough knowledge of innovation strategy. Well done!

Figure Descriptions

Figure 9.9: First quadrant of an X-Y axis with four purple boxes. The x-axis represents technology (either existing or new) and the y-axis represents market (either existing or new). Existing technology and existing market is marked incremental innovation. New technology and new market is marked as radical innovation. New technology and existing market is marked as disruptive innovation. Existing technology and new market is marked as architectural innovation.

Figure 9.12: X-Y plot with time on the x-axis and sales on the y-axis. A curve starts in the bottom left hand corner (labeled introduction) and increases (labeled growth) until it reaches its apex (labeled maturity), then the curve begins to decline (labeled decline). Bullet points to note during the introduction phase: low sales, high cost per customer, financial losses, innovative customers, few (if any) competitors. Growth phase: increasing sales, cost per customer falls, profits rise, increasing number of customers, more competitors. Maturity phase: peak sales, cost per customer lowest, profits high, mass market, stable number of competitors. Decline phase: falling sales, cost per customer is low, profits fall, customer base contracts, number of competitors fall. This graphic is purple.

Figure 9.13: Same plot as described in figure 9.12. Except, in this plot, instead of the line declining, it continues to increase. This is labeled as product extension.

Figure 9.14: Line graph representing the product life cycle with two lines denoting sales and profits over time. The graph is divided into five vertical sections labeled: Product development, Introduction, Growth, Maturity, and Decline. The sales line is the same as described in figure 9.12 (slowly rises in the introduction phase, rising through growth, peaking in maturity, and then declining). The profits line starts below zero during product development, increases into the growth phase, peaks slightly during maturity, and decreases during decline. This graphic is purple.

Figure 9.15: Bell curve diagram with six sections. From left to right, the sections are innovators (2.5%), early adopters (16%), chasm, early majority (34%), late majority (34%), and laggards (16%). This graphic is purple.

Figure 9.16: Horizontal purple arrow pointing in both directions. From left to right, the main sections of the arrow are (1) Make (includes internal development), (2) Contract (includes nonequity strategic alliance and equity strategic alliance), (3) Create (includes joint venture), and (4) Acquire (includes mergers and acquisitions).

Figure References

Figure 9.1: UPS. Trimetwes fan1003. 2024. CC BY-SA 4.0. https://commons.wikimedia.org/wiki/File:Grumman_P800_of_UPS_Portland.jpg

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Figure 9.14: Profits during the product life cycle. Kindred Grey. 2025. CC BY.

Figure 9.15: The adoption cycle of a company's product or service, or an industry's technological advancement. Kindred Grey. 2025. CC BY.

Figure 9.16: Make-contract-create-acquire continuum. Kindred Grey. 2025. CC BY.

Figure 9.17: The Geo brand was recognized for its affordability and fuel efficiency rather than its design. dave_7. 2008. CC BY-SA 2.0. <https://commons.wikimedia.org/wiki/File:PontiacSunburst.jpg>

Figure 9.18: Co-located brands. Hirohisat. 2007. CC BY-SA 3.0. https://commons.wikimedia.org/wiki/File:KFC_and_Baskin_31_Robins.jpg

10. FORMULATE SUSTAINABILITY AND ETHICS STRATEGY

Learning Objectives

After engaging with this chapter, you will understand and be able to apply the following concepts:

1. Sustainability and ethics strategy
2. Disruptive megatrends and how they impact business strategy
3. The drivers of climate change as the defining megatrend and approaches to fight the climate crisis
4. The concept of sustainability and the stakeholder-driven business case for companies to implement business sustainability strategies
5. The pros and cons of companies embracing a social responsibility beyond the profit motive
6. The triple bottom line approach.
7. The concept and content of corporate social responsibility (CSR) strategy
8. Environmental, social, and governance (ESG) strategies as the latest and most relevant concept of sustainability
9. The elements of a robust ethics strategy
10. Contemporary issues of corporate ethics that are shaping the business strategy agenda
11. Why sustainability and ethics strategy is important to business graduates

When you finish Chapter 10, you will be equipped to analyze sustainability and ethics strategy.

10.1 Introduction

This chapter covers sustainability and ethics strategy. This entails you learning about megatrends, including climate change, that drive sustainability and ethics strategy. Then you learn about sustainability strategy in more detail, including its history and evolution. You learn about the continuing impact of the triple bottom line approach. The chapter covers two crucial sustainability strategies: corporate social responsibility (CSR) and today's most current framing of sustainability strategy, the environmental, social, and governance (ESG) approach. Next you learn about ethics strategy and contemporary questions of corporate ethics. Then you learn how to analyze sustainability and ethics strategy. Finally, the chapter concludes with a discussion of why sustainability and ethics strategy is important to business graduates.

10.2 Sustainability and Ethics Strategy

Like all strategy formulation, formulating sustainability and ethics strategy answers the question “Where are we going?” This form of strategy addresses how a firm can use sustainability and business ethics to establish a competitive advantage over its competitors by better meeting evolving customer demands and the expectations of important business stakeholders. All firms need to address sustainability and ethics.

Like innovation, sustainability and ethics is another strategy focus that is formulated at the strategic business unit level of a company and embedded in business level-strategy, answering the strategic question of how specifically a firm is going to win or compete in its chosen markets and market segments.

Like all strategy, sustainability and ethics strategy focuses on an outside-in perspective. Companies need to carefully monitor their external environments. They need to analyze trends and formulate strategies that are forward-looking. Robust sustainability and ethics strategy takes into account the volatile, uncertain, complex, and ambiguous nature of the firm's external environment, where change and disruption have become the new normal.

This chapter analyzes how changes in the external environment of the firm drive strategic responses with companies embracing their corporate social responsibility, developing environmental, social, and governance strategies and treating corporate business ethics as a possible source of winning in the market versus just a legalistic approach to stay compliant.

Key Takeaways

Like all strategy formulation, formulating sustainability and ethics strategy answers the question “Where are we going?” and addresses how a firm can use sustainability and business ethics to establish a competitive advantage. All firms need to address sustainability and ethics strategy. Like innovation, sustainability and ethics is another strategy focus that is formulated at the strategic business unit level of a company and embedded in business-level strategy, answering the strategic question “Right to win?”

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10.3 Megatrends and Climate Change

Positioning a business strategically for success requires a thorough analysis of disruptive **megatrends**, which are deep and profound trends that are global in scope and long term in effect. These must be considered for strategy formulation. Important disruptive megatrends relevant for business rest in technological transformation (for example, AI, cloud and quantum computing, big data, and automation) as well as shifts in economic power to emerging countries, rapid urbanization, global population growth, supply chain disruptions in an increasingly globalized business environment, aging Western populations, young populations in emerging countries, geopolitical tensions, social change, climate change, and resource scarcity.

Figure 10.1 provides an overview of disruptive megatrends that companies need to consider in their strategy development and implementation.

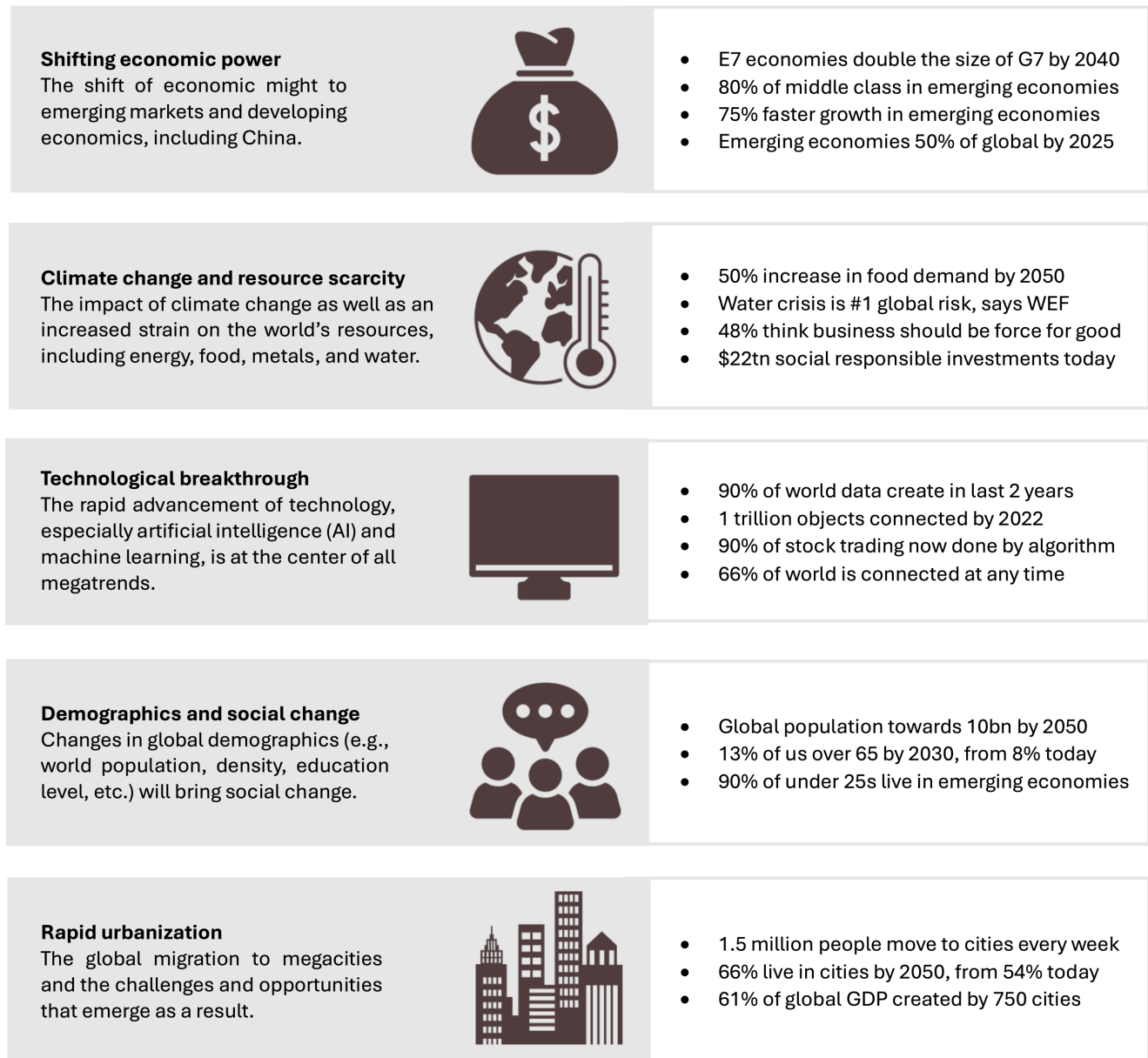


Figure 10.1: Disruptive megatrends will impact strategy formulation and implementation

Climate Change

Addressing climate change is the defining challenge of our time and is one megatrend that threatens to disrupt modern society. **Climate change** is a significant variation of average weather conditions (warmer, wetter, or drier) over several decades. When the earth absorbs the sun's energy, or when atmospheric gases prevent heat released by the earth from radiating into space (the **greenhouse effect**), the planet warms. **Global warming** refers to the increase in the planet's overall average temperature in recent decades. Global warming is part of climate change and is driven by greenhouse gases (GHGs), with carbon dioxide (CO₂) being the main driver of global warming. The burning of fossil fuels like coal, oil, and gas for electricity, heat, and transportation is the main root cause of the huge increase of CO₂ emissions. CO₂ concentration is now at its highest level in 800,000 years, leading to a rapidly increasing global temperature which is causing draughts, rising sea levels, extreme weather events, food shortages, the reduction of biodiversity, lack of fresh water and climate refugees, among other issues. In his opening remarks to COP27 on November 7, 2022, United

Nations (UN) Secretary Antonio Guterres had some very clear, powerful, and concerning messages to the world regarding climate change:

“We are on a highway to climate hell with our foot still on the accelerator.”

“We are in the fight of our lives, and we are losing.”

“Greenhouse gas emissions keep growing, global temperatures keep rising, and our planet is fast approaching tipping points that will make climate chaos irreversible.”

To limit the negative effects of climate change, almost all countries in the world committed to a reduction of CO₂ emissions in the Paris Agreement in 2015. The target of the Paris Agreement is limiting global warming to 1.5 degrees Celsius above preindustrial level. To achieve this, countries committed to a net-zero CO₂ target by 2050.

These commitments have implications for all businesses around the world, leading to strategic questions like:

- What does my industry and market look like in a net-zero world?
- How do I transform and decarbonize my business model?
- How do I identify, mitigate, and address climate risk in my operations?
- How do I climate-proof my operations?
- How do I manage my global supply chain, and how do I cooperate with suppliers around the world who contribute to my firm's greenhouse gas footprint?
- How do I stay legally compliant with current and emerging climate regulations and laws?
- How do I report on the environmental (and social) performance of my firm?

Application

- Refer to figure 10.1. Choose one of the disruptive megatrends that interests you the most.
 - Explain how the disruptive megatrend impacts strategy formulation and implementation.

Key Takeaways

Megatrends are deep and profound trends that are global in scope and long term in effect. Important disruptive megatrends relevant for business involve technological transformation, shifting economic power to emerging countries, rapid urbanization, global population growth, supply chain disruptions, aging Western populations, young populations in emerging countries, geopolitical tensions, social change, climate change, and resource scarcity. Positioning a business strategically for success requires a thorough analysis and integration of disruptive megatrends.

Addressing climate change is the defining challenge of our time and is one megatrend that threatens to disrupt modern society. Climate change is a significant variation of average weather conditions over several decades. When the earth absorbs the sun's energy, or when

atmospheric gases prevent heat released by the earth from radiating into space (the greenhouse effect), the planet warms. Global warming refers to the increase in the planet's overall average temperature in recent decades.

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10.4 Sustainability Strategy

Addressing the issues of climate change, resource scarcity, biodiversity, human rights, social issues, and social justice are covered by the term *sustainability*. **Sustainability** is defined by the UN Commission for Sustainable Development (Brundtland Commission) as meeting the needs of the present generation without compromising the ability of future generations to meet their own needs. **Sustainability strategy** is a company's strategy to reduce adverse environmental and social impacts resulting from business operations while still pursuing profitable growth. Strategies that fall under this umbrella include corporate social responsibility (CSR) strategies and environmental, social, and governance (ESG) strategies. Sustainability is a business imperative and should be at the core of every business's strategy and operations.

Figure 10.2 shows a few examples of firms' sustainability statements.

Company	Sustainability statement
Ford	Vision For The Future: We aim to reach carbon neutrality no later than 2050. This encompasses our entire impact on the planet – from the emissions from our vehicles to the power in our factories, to our suppliers.
McDonald's	Our Planet: We're helping to drive climate action, protecting natural resources, reducing waste, and transitioning to more sustainable packaging and toys.
Oatly	So, you may be wondering why a company needs a to-do list or how long a company's to-do list might be. Hopefully, this explains it or leaves you with your own questions. Anyway, it's our to-do list to take important steps toward our vision for a food system that is better for people and the planet. But it's not just a to-do list! It's our sustainability plan outlining the actions we will take to meet our sustainability ambitions.

Company	Sustainability statement
Tesla	Tesla's mission is to accelerate the world's transition to sustainable energy. Sustainability is integral to Tesla, and it is central to its mission.
Avon	We're open to all. Every member of our team has the right to personal self-expression such as dress, hair, or other forms of body adornment. We believe in inclusive beauty and support self-expression by challenging stereotypes, supporting freedom of expression, and representing a wide range of people.

Figure 10.2: Sustainability statements from companies

Do Companies Have a Social Responsibility beyond Profit?

There is a decades-long controversy over whether business should (or even must) support environmental and social issues or whether they should just focus on generating profits. The strongest supporter of the profit focus is American economist and Nobel Prize Winner in Economic Sciences, Milton Friedman. He stated that “the business of business is doing business.” He believed that there is one and only one social responsibility of business: “To use its resources and engage in activities designed to increase its profits so long as it stays within the rules of the game, which is to say, engages in open and free competition without deception or fraud” (Forder, 2019).

On the other hand, Theodore Levitt, American economist and professor at the Harvard Business School stated, “Although profits are required for business just like eating is required for living, profit is not the purpose of business any more than eating is the purpose of life” (Levitt, 1983).

There is a strong argument to be made that companies do have an ethical and moral obligation to give back to society and support environmental and social issues. With great power, there comes great responsibility. Companies have the resources available to make a positive difference, and it seems to be the right and ethical thing to do.

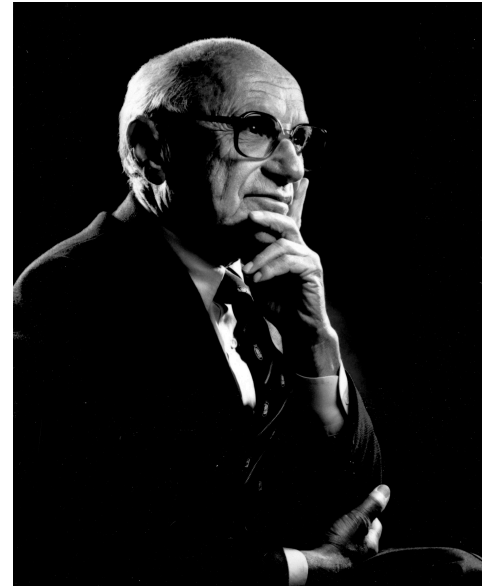


Figure 10.3: Milton Friedman

Business Case for Sustainability Strategy

As you have just seen, there are different perspectives on whether the purpose of business includes a social responsibility beyond just making profits. We now want to go beyond an ethical assessment toward a clear financial business case in favor of sustainable business management. This business case is driven by the expectations of business' main stakeholders: customers, employees, investors, and regulators.

Customers

- Eighty percent of consumers are more likely to buy from a company that stands up for environmental issues (PWC, 2023).
- Ninety percent of Gen-Zs believe companies should act on social issues, and 90 percent of millennials in the U.S. would switch brands to those championing a cause (BCG, 2021).
- Eighty-seven percent of Americans will purchase a product because a company advocated for an issue they care about, whereas 76 percent will refuse to purchase a company's product from a company supporting issues contrary to their beliefs (Cone Communications CSR Study, 2017).

While customers have always supported sustainability to a high degree, the current game changer is the customers' willingness to pay more for sustainable products and solutions, basically voting with their wallets in support of sustainability. Offering sustainable solutions helps companies to win with their customers and in their chosen markets and market segments.

Employees

- Forty percent of millennials state that sustainability was a consideration in their job choice (BCG).
- Over 40 percent of Gen-Zs and millennials would switch jobs over climate concerns (Segal, 2024).
- Eighty-three percent of employees are more likely to work for a company that addresses environmental and social issues in their business (PWC, 2021).
- Eighty-six percent of employees prefer to support or work for companies that care about the same issues they do (PWC, 2021).

Talent attraction, talent retention, and managing an engaged and committed workforce depends on the strength of companies' sustainability strategies.

Investors

- Eighty-eight percent of investors believe companies that prioritize sustainability initiatives represent better opportunities for long-term returns than companies that do not (PWC, 2022).
- Beyond strong financial performance, institutional investors demand a strong environmental and social performance from the companies in which they invest. They see a lack of social commitment and a business model that doesn't transform the company's business toward sustainability as signs of a financial investment risk.
- In the words of Larry Fink, Chairman and CEO of the world's largest asset management firm, BlackRock: "To prosper over time, every company must not only deliver financial performance but also show how it makes a positive contribution to society. Companies must benefit all of their stakeholders."

Access to capital and capital costs depends on a robust sustainability strategy that convinces private and institutional investors that the company is well positioned with a clear purpose and a meaningful management of climate risk in their business model.



Figure 10.4: Larry Fink

Government and Regulators

- Governments and regulators have set the bold ambition for countries to become carbon-neutral by 2050. This is the direct consequence of countries committing to the Paris Agreement. Regulatory approaches to achieve this include regulation on the industry sector level designed to limit and continuously reduce greenhouse gas emissions, the implementation of a carbon tax to make the use of fossil energy more expensive, and tax breaks and financial subsidiaries in support of a business transformation toward a low-carbon business model.
- Regulators introduce carbon pricing and regulations on a sector level to reduce CO₂ emissions. For example, California outlawed the sale of new fossil fuel cars as of 2035.
- There is significant pressure on businesses to comply with quickly evolving new environmental regulation and laws and a clear mandate to decarbonize companies' business models.

A proactive approach to sustainability helps companies to stay compliant and ahead of the curve in terms of legislation and regulation. Instead of just passively reacting to new legislation and regulation, companies can proactively factor new laws and regulations into their business models, excel in reporting and disclosure, and transform their business models ahead of the competition.

Sustainability strategies drive positive performance by saving on costs through lower energy and water consumption, waste reduction, pollution control, improved employee recruitment, retention, and work productivity, improved corporate reputation and brand recognition, and the creation of new revenue-generating opportunities through innovation, new products, and new markets. Sustainability also supports cost savings through risk management in global supply chains, tax credits and subsidies, legal and regulatory compliance, positive community relations, and better access to capital.

Figure 10.5 summarizes the business case for sustainability strategies.

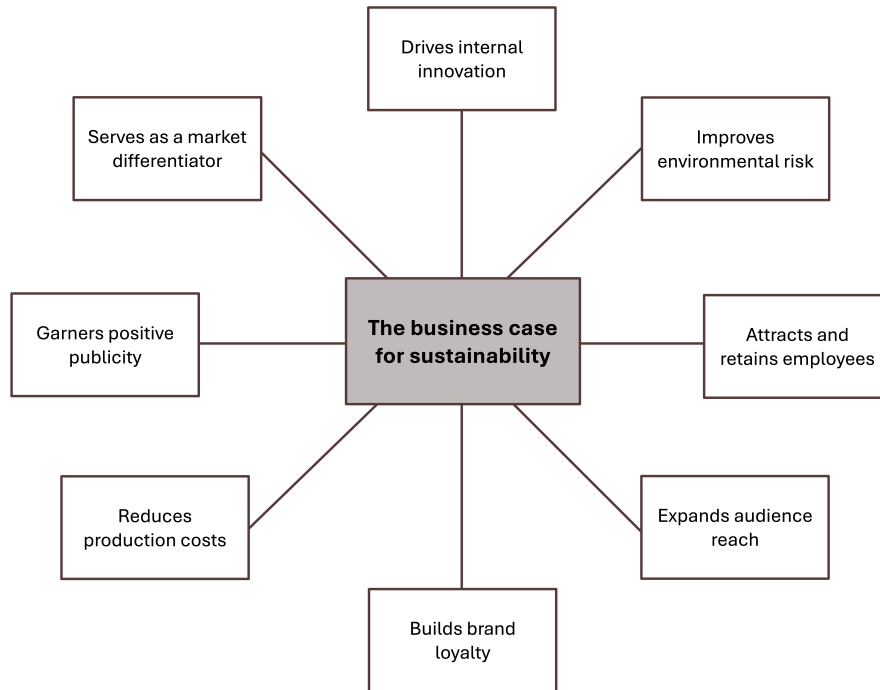


Figure 10.5: The business case for sustainability

This positive financial business case of sustainable business models has also been supported by a large-scale meta-study of the New York University Center for Sustainable Business. The Center examined the relationship between ESG and financial performance in 245 research studies between 2015 and 2020. The results of this study showed that a majority of studies (58 percent) indicated a positive impact of ESG and business sustainability on financial performance, whereas only 8 percent show a negative impact (Whelan, Atz, Van Holt, & Clark, 2021).

Application

- Research the sustainability statements for three companies you admire. Discuss whether each company is following its sustainability commitments and how this impacts profits.

Key Takeaways

Sustainability is defined by the UN Commission for Sustainable Development (Brundtland Commission) as meeting the needs of the present generation without compromising the ability of future generations to meet their own needs. Sustainability strategy is a company's strategy to reduce adverse environmental and social impacts resulting from business operations while still pursuing profitable growth. Strategies that fall under the umbrella of sustainable strategies include corporate social responsibility (CSR) strategies and environmental, social, and governance (ESG) strategies. Businesses need to balance economic, social, environmental, and legal and regulatory obligations in order to satisfy stakeholder desires and therefore must assume broad responsibilities that include complying with social norms and expectations. There is a clear financial business case in support of sustainability strategy driven by customers, employees, investors, and regulatory agencies.

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10.5 Triple Bottom Line

Closely related to the positive financial business case of sustainable business is the triple bottom line concept. Business leader Sir Richard Branson once said, “Doing good is good for business.” This reflects a growing mindset in modern companies where social and environmental responsibility go hand in hand with profitability. This is often reflected in a firm's purpose and values. It is also a focus of corporate social responsibility and environmental, social, and governance strategy.

Instead of asserting that doing positive things for the environment and society comes at the expense of profit, the triple bottom line states that a good environmental and social performance will support the financial performance of companies. There is no tradeoff between profit and people and the environment; in fact, there is a positive correlation. Companies use sustainability strategies to enhance financial performance, and sustainability becomes a driver of competitive differentiation.

The triple bottom line framework emphasizes a broader view that focuses on the three Ps: people, planet, and profits. These may also be referred to as social/societal, environmental, economic/financial. The triple bottom line ensures that organizations consider not only financial success but also their impact on society (people) and the environment (planet). Although the concept originated in the 1980s, it gained significant traction in the late 1990s as businesses began recognizing that sustainable and ethical practices lead to long-term success. Almost all companies have embraced this approach, prioritizing environmental sustainability and social responsibility alongside their financial goals.



Figure 10.6: Richard Branson

The logic in support of the business case for sustainable business management and the triple bottom line approach can be summarized by the following statements:

- Doing well by doing good
- Making “doing the right thing” profitable
- Creating a better world through better business

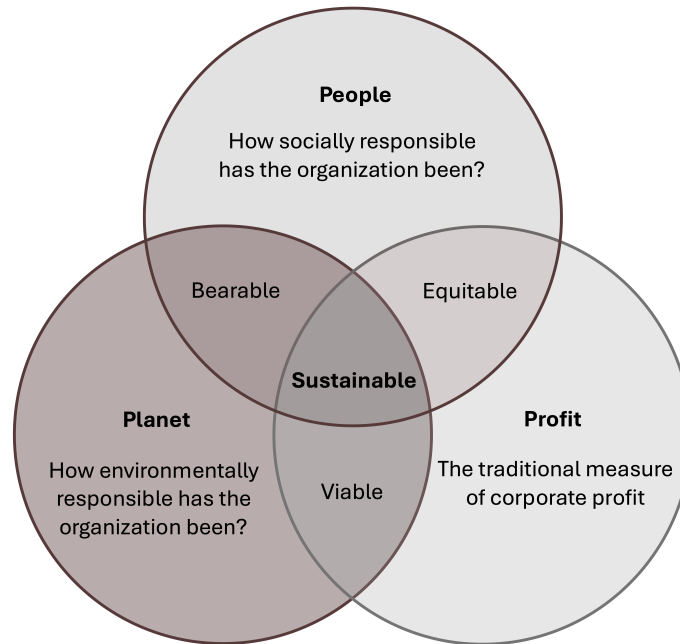


Figure 10.7: The triple bottom line emphasizes the three Ps: people (social concerns), planet (environmental concerns), and profits (economic concerns)

Deloitte demonstrates its commitment to the planet and people through an integrated approach to sustainability and social impact. The company's environmental pledge, embedded in its strategy, includes ambitious goals to achieve net-zero emissions by 2030 and drive climate-positive initiatives across industries. Deloitte doesn't stop at environmental leadership; it also prioritizes the people aspect of the triple bottom line by focusing on creating equitable opportunities within the communities it serves.

Through programs like its WorldClass initiative, Deloitte aims to empower 100 million individuals worldwide by 2030 through education and skills development, especially in underserved populations. Balancing these commitments with strong financial performance, Deloitte demonstrates how large organizations can be profitable while remaining socially responsible and environmentally conscious. Deloitte encourages its employees to learn skills that benefit both the firm and individuals through its Graduate School Assistance Program. The program helps to send high-performing consultants to top graduate schools. In doing so, Deloitte hopes to encourage top talent to choose employment with the firm. The program provides a reward for the high-achieving employees who it wishes to retain. This is evidence of Deloitte's commitment to the people pillar of the triple bottom line.

Deloitte.

Figure 10.8: Deloitte

Key Takeaways

The triple bottom line framework emphasizes a broader view that focuses on the three P's: people, planet, and profits. There is no trade-off between profit and people and the environment; instead there is a positive correlation. Companies use sustainability strategy to enhance financial performance, and sustainability becomes a driver of competitive differentiation.

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10.6 Corporate Social Responsibility: A Sustainability Strategy

Corporate social responsibility (CSR) is the idea that a business has a responsibility to the society in which it operates. CSR is an approach where a company operates in ways that enhance society and the environment while pursuing its profit goal. CSR can promote a positive reputation with stakeholders and a positive brand image for the company. With the parallel pursuit of environmental, social, and economic objectives, CSR shows many parallels with the triple bottom line approach (profit, people, planet). One of the main drivers and advantages of CSR is that it acknowledges and embraces the fact that business operates in a multi-stakeholder context.

Corporate social responsibility strategy is a sustainability strategy that focuses on the tenants of the CSR approach. Assuming corporate responsibility not only for a company's financial results but also considering various stakeholders and their environmental and social interests strengthens a business's social license to operate. It enhances relationships and drives support of various primary and secondary stakeholders whose support a company needs to stay successful in the long term.

Beyond allowing a company to thrive in a multi-stakeholder society, CSR encourages long-term thinking, drives innovation and cost savings, enhances brand differentiation, and furthers customer and employee engagement. Beyond customers and employees, investors and governmental regulators are additional important stakeholders. CSR improves business reputation and standing, provides access to investment and funding opportunities, and generates positive publicity and support by the general public and media, also known as the “court of public opinion.”

Let's take Levi Strauss & Co. as an example of what companies do in support of their CSR strategies. Levi's explains how it supports society and the environment through these specific activities:

- We had the courage to reject racial segregation: Our first desegregated sewing factory opened in Blackstone, Virginia in 1960.
- We championed corporate integrity through transparency: Our Terms of Engagement were instituted worldwide in 1991, ensuring worker protection at every point of the supply chain.
- We encouraged empathy in the face of fear: Our leaders and employees came together in 1982 to educate the public on issues facing the LGBTQ+ community.
- We're making things better & thinking sustainability first.
- We're collaborating with suppliers on programs that improve the lives of apparel workers.
- We're committed to saving arts education (Levi's, n.d.).



Figure 10.9: Levi's corporate headquarters

You can easily see how Levi's targets various stakeholders, how it wants to improve social matters (improving the lives of apparel workers) and environmental matters (prioritizing sustainability). You can also easily see how consumers may identify with these activities and reward Levi's with their business, which would then drive Levi's financial performance as a result of brand loyalty and higher willingness to pay by consumers.

Other typical activities of a socially responsible company include making products that are safe, obeying laws and regulations in all aspects of business, promoting honest and ethical employee behavior, committing to a safe workplace for all employees, avoiding misleading or deceptive advertising and marketing practices, giving money to charitable causes, responding quickly to customer problems, and avoiding polluting the environment, among many other methods.

Specific company examples of robust CSR activities include:

- LEGO's pledge to reduce its carbon impact: LEGO is the first and only toy company to be named a World Wildlife Fund Climate Savers Partner (lego.com).
- Salesforce's 1-1-1 philanthropic model: Beyond being a leader in the technology space, cloud-based software giant Salesforce is a trailblazer in corporate philanthropy. Since its outset, the company has championed its 1-1-1 philanthropic model, which involves giving one percent of product, one percent of equity, and one percent of employees' time to communities and the non-profit sector (salesforce.com).
- Ben & Jerry's social mission: At Ben & Jerry's, positively impacting society is just as important as producing premium ice cream. As part of its overarching commitment to leading with progressive values, the ice cream maker established the Ben & Jerry's

Foundation in 1985, an organization dedicated to supporting grassroots movements that drive social change (benjerry.com).

- Starbucks's commitment to ethical sourcing: Starbucks launched its first corporate social responsibility report in 2002 with the goal of becoming as well known for its CSR initiatives as for its products. One of the ways the brand has fulfilled this goal is through ethical sourcing. In 2015, Starbucks verified that 99 percent of its coffee supply chain is ethically sourced, and it seeks to boost that figure to 100 percent through continued efforts and partnerships with local coffee farmers and organizations (starbucks.com).

The different corporate responsibilities that business has are illustrated in the CSR pyramid in figure 10.10.

If you were to visualize CSR strategy as a hierarchy of different social responsibilities, the foundation would be composed of legal and regulatory compliance. All companies need to obey laws and regulations as the minimum social responsibility. While this sounds banal and obvious, the copious amount of ethics scandals shows that this is not always the case. Some companies may be able to disobey laws and regulations, pay a fine, and go on to recover their market share. On the other hand, lawsuits can bankrupt a business. Either way, customers want to do business with companies that obey all applicable laws and regulations.

The second level in the hierarchy of social responsibility of corporations is an economic and financial responsibility to the firm's owners, shareholders, and other stakeholders. Without being financially healthy and without continuously generating profits, a company is not viable, disappearing from the market. A company cannot create social good without being profitable.

The third level of social responsibility is being ethical. This goes beyond legal and regulatory compliance and is driven by robust voluntary corporate ethics programs, ethical culture, ethical leadership, and robust corporate governance.

The fourth level of the CSR pyramid is the social responsibility of being a good corporate citizen. This encompasses the firm's social responsibility to give back to society through strategic philanthropy and to give back to the local and global communities with which the firm interacts. This level balances the firm's financial performance with its environmental and social impact in the framework of a holistic approach to business that considers the needs of all stakeholders, not just shareholders.

CSR evolved over time and is now characterized by an integrated and transforming approach to CSR strategy. The strategic intent of CSR is value creation and social change rather than just legal and regulatory compliance. CSR is not just outsourced to a team or specialists in the organization; CSR is owned and driven by strategic leaders and managers with the support of business unit managers. It embraces a multi-stakeholder approach with partnership alliances, and it provides a high level of transparency through a full disclosure of CSR performance in specific CSR reports that the organization publishes on a regular basis. CSR went from something extra or even a greenwashing endeavor to a fully integrated strategy that is part of an organization's culture, policies, operations, and strategy.



Figure 10.10: Different corporate responsibilities

Video 10.1: Business Ethics: Corporate Social Responsibility [02:57]

The video for this lesson further explains corporate social responsibility.

Access this YouTube video by scanning the QR code.

**Video 10.2: Insight: Ideas for Change—Michael Porter—Creating Shared Value [14:10]**

The video for this lesson focuses on the differences between CSR and creating shared values (CSV).

Access this YouTube video by scanning the QR code.

**Key Takeaways**

Corporate social responsibility (CSR) is the idea that a business has a responsibility to the society in which it operates. CSR is an approach where a company operates in ways that enhance society and the environment while pursuing its profit goal. CSR strategy as a hierarchy of different social responsibilities, including legal and regulatory responsibility, economic and financial responsibility, ethical responsibility, and corporate responsibility.

The social contract between society and business has changed. Companies are expected to assume much broader responsibilities in support of positive societal and environmental outcomes than ever before. As a result, companies are repositioning their business purposes in support of making a positive difference in the world instead of being motivated by profit alone. Stakeholders support companies that assume broader social responsibilities, which drives the positive correlation between doing something good for the planet and for people while increasing profits at the same time. Corporate social responsibility starts with the foundation of companies being compliant with all applicable laws and regulations while also acting economically and financially responsible to the firm's owners, shareholders, and other stakeholders. Beyond that, companies are expected to be ethical, give back to society, and be good corporate citizens. Subsequently, strategic management is unsuccessful if it is performed in an ethical vacuum. An authentic and genuine commitment to CSR is rewarded by stakeholders and makes CSR a driver of value creation in the form of competitive differentiation that is business driven and stakeholder supported.

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10.7 Environmental, Social, and Governance (ESG): A Sustainability Strategy

An organization's sustainability practices are typically analyzed against environmental, social, and governance (ESG) metrics. Sustainability has environmental, social, and economic perspectives. In addressing sustainability challenges, almost all companies develop **environmental, social, and governance strategy**.

Although CSR strategy still holds relevance and importance, ESG has emerged as the leading concept for achieving or maintaining a sustainable and ethical organization. ESG has become a success-critical strategy element. ESG focuses on a company's environmental performance, its support of social topics, such as social justice and human rights, and its corporate governance. Sometimes ESG is called "CSR with teeth" because ESG is more heavily regulated than CSR. There are far-reaching ESG disclosure and reporting requirements for companies that are not found under the CSR model. In the European Union, the Corporate Sustainability Reporting Directive (CSRD) requires around 50,000 companies to report and disclose their environmental, social, and governance performances through audit-grade reporting. There is also a high level of transparency with ESG reports, and ESG ratings must meet formal transparency standards.

Stakeholders such as institutional investors place high importance on a company's ESG performance. According to a PWC study:

- Eighty-three percent of consumers think companies should be actively shaping ESG best practices.
- Ninety-one percent of business leaders believe their company has a responsibility to act on ESG issues.
- Eighty-six percent of employees prefer to work for a company that cares about the same issues they do.
- More than 50 percent of all investments will be ESG-driven in the near future.

The large majority of investors believe that strong ESG practices can lead to better long-term returns (Deloitte Survey, 2023; Morgan Stanley Survey, 2024). Achievement of sustainability goals was the most cited business priority, identified by 75 percent of organizations as one of their five most important initiatives, well ahead of second-place digital transformation Initiatives at 56 percent (Honeywell study, 2023).



Figure 10.11: ESG

ESG strategy is a driver for value creation. The ESG-driven sustainable business transformation is collaborative, with various stakeholders like suppliers included along the value chain. A company defines its ESG strategy in support of its mission, purpose, vision, and values.

ESG is embedded in business-level strategy and contains the following strategic pillars.

- **Environmental pillar:** Addresses resource, land, and water use. Promotes a reduction of carbon emissions, pollution, and waste, the decarbonization of a firm's business model, and biodiversity. Is aligned with the circular economy.
- **Social pillar:** Addresses labor management. Promotes the health and safety of employees, human capital development and talent management, supply chain labor standards for workers in the global value chain, social justice, consumer rights, product safety, privacy and data security, and the rights of communities affected by the business.
- **Governance pillar:** Promotes corporate business ethics, codes of conduct, advisory board oversight, tax transparency, anti-corruption and anti-bribery policies, and executive pay.

Environmental Pillar

The decarbonization of a company's business model is the most critical element in fighting climate change and often the main element of the ESG environmental pillar. Companies need to define their journeys to become carbon-neutral by 2050 at the latest. As a consequence, companies are currently transparently assessing and measuring their emissions as the baseline for defining specific programs to reduce carbon emissions along their complete value chains. This is covered under corporate decarbonization strategy, which is a part of an overall sustainability strategy and includes measures like energy efficiency projects, the use of renewable energy, electrification, the use of life cycle assessments (LCA) to reduce the environmental impact of products, and partnerships with suppliers.

Another important and strategy-changing environmental element of ESG is the transformation to a circular economy. This contrasts with the current linear economy and linear business model, which follow a take-make-waste approach where resources are used to make products that are being consumed and then wasted.

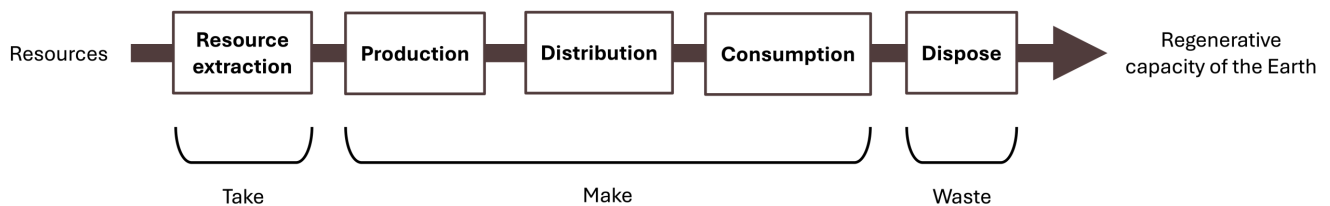


Figure 10.12: Linear economy

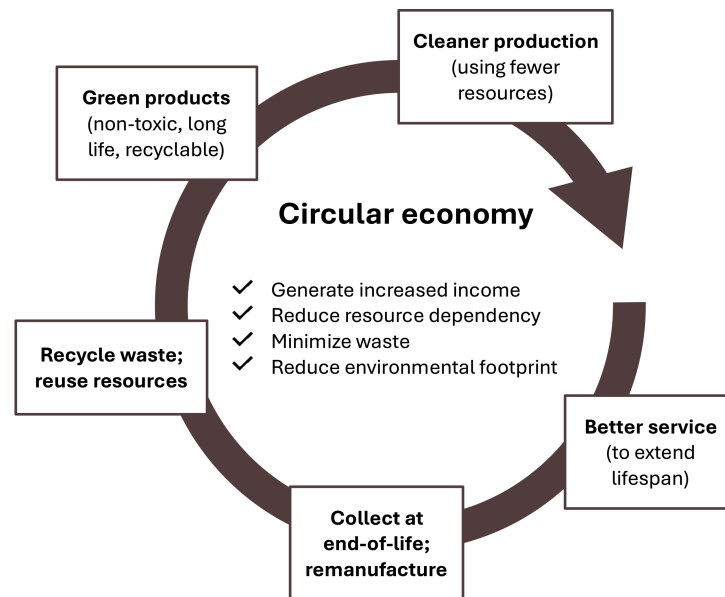


Figure 10.13: Circular economy

Other important elements of the environmental pillar are the reduction of pollution and waste, responsible management of water, support of biodiversity, reduction of land use, opportunities in green building, renewable energy, and investment in green technology.

Social Pillar

The next pillar of ESG is the social pillar, which is related to the company's impact on social issues and human rights. The social pillar focuses on the firm's positive impact on different stakeholders.

The first stakeholder group is the firm's own employees. The firm should create safe working conditions, provide appropriate compensation and development opportunities, support the continuous upskilling of its workforce, allow unionization, and have robust anti-discrimination and equal opportunity policies in place.

One success-critical element of the social pillar is the continued talent development of the firm's workforce in the era of AI. AI, automation, and robotics are changing the way we live and the way we work. There are estimates that forecast that up to 40 percent of current jobs will disappear by 2030. Many employees will also work in jobs and positions in the future that don't even exist today. Job families will rise and decline in the context of the transformation of industries and business models. This often requires fundamentally different and new skill sets for employees and new ways to organize work. Hence, the continued upskilling and reskilling of a company's workforce is one of the success-critical elements of the social pillar.

Another important topic for a firm's own workforce is the topic of "new work." This concept encompasses all changes to work design initiated by the COVID-19 pandemic. Employees worked from home, and many continue to expect some kind of balance between in-office work and working from home. At the same time, many companies have requested employees to return full time to their offices. New hybrid work models are important challenges and critical success factors regarding a firm's own workforce under the social pillar of ESG. Figure 10.14 shows some of the topics that are currently discussed with a high priority.

- 1 Flexible and remote work remains employee priority.
- 2 Rebuild the employee experience and manage connectivity in a hybrid work model.
- 3 Reimagine the physical space and design new footprint and office space for a hybrid work model.
- 4 Measure productivity in a remote setting. Redefine metrics to assess productivity and rules of engagement.
- 5 Manage work-life boundaries and fundamental human needs. Support mental and physical well-being.

Figure 10.14: Organizations reimagining “new work” in a hybrid work model

The second stakeholder group in the social pillar is workers in the firm's global value chain. This element of ESG drives a significant paradigm change in business. The social responsibility of companies does not end at their factory gates or at borders. Firms are responsible for labor standards of workers in their global value chains. This means that companies assume responsibility for the working conditions, safety standards, work hours, and payment of workers who work for their suppliers abroad. This is a significant paradigm change that is accompanied by management and reporting challenges. Supply chain standards in global value chains need to be managed thoroughly, and companies must manage responsible sourcing practices with all of their suppliers, including auditing the human rights of their suppliers' workers.

The third stakeholder group are communities affected by the firm's business operations. The firm needs to respect the rights of local communities affected by the company's operations and must provide remedies for any adverse impact of their operations.

The last stakeholder group are the firm's consumers and end users who have the right to safe products, the absence of misleading marketing information, and especially important in the era of big data, privacy rights (for example, data protection and cybersecurity).

Patagonia, Inc., is an American retailer of outdoor recreation clothing, equipment, and food. It was founded by Yvon Chouinard in 1973 and is based in Ventura, California. Patagonia's revenue is estimated at \$1.5 billion, and the company has shown strong growth and robust success over time. However, the driver of this success is not just its high-quality products. The main differentiator and the source of Patagonia's competitive advantage is its sustainable business model and its focus on its environmental, social, and governance performance, which is the core of ESG and CSR strategy. This is rewarded by key stakeholders like customers, who respond with brand loyalty and a higher willingness to pay for Patagonia's sustainable products.



Figure 10.15: The Patagonia story: making business sustainability the strategic right to win and the main source of competitive differentiation

The company has three pillars—environmental programs, social programs, and business conduct—that follow the ESG structure. Patagonia explicitly addresses climate change in declaring “The climate crisis is our business.” Patagonia is radically reducing its carbon emissions and is transforming how they make products, using materials that cause less harm to the environment. Patagonia’s commitment goes beyond its own company and includes a goal to make a positive impact along the full global value chain, from suppliers to customers, which is one of the best practices for a robust ESG strategy.

Since 1985, Patagonia has pledged 1 percent of sales to the preservation and restoration of the natural environment. The firm awarded over \$140 million in cash and in-kind donations to domestic and international grassroots environmental groups making a difference in their local communities. This is an example of strategic philanthropy, which is part of the CSR pyramid and part of the social ESG pillar.



Figure 10.16: Patagonia's "Don't buy what you don't need" advertisement

Patagonia is a certified B Corp. Becoming a B Corp is another trend in sustainable business strategy. In business, a B Corporation is a for-profit corporation certified by B Lab, a global nonprofit organization. The certification is granted based on an assessment of a firm's social and environmental performance.

Lastly, Patagonia is committed to the reuse and recycling of its products. Patagonia is letting go of virgin materials in support of post-consumer recycling, which refers to any finished product that has been used and then diverted from landfills at the end of its life. Patagonia ran an iconic marketing campaign in the form of a full-page advertisement in *The New York Times* discouraging customers from purchasing one of their jackets.

Patagonia stated in this advertisement that producing the jacket generated waste in an amount equivalent to two-thirds of the jacket's weight. This included thirty-six gallons of water, which is the equivalent to fulfilling the daily needs of forty-five people, and twenty pounds of carbon dioxide emissions, which is twenty-four times the weight of the jacket. The advertisement ended with the plea: "Don't buy what you don't need." This is an excellent example of Patagonia, like many other firms, moving from a linear to a circular economy to protect the planet's scarce resources. A linear economy takes, makes, uses, and then wastes resources. Embracing the principles of the circular economy is an important element of the environmental pillar of ESG strategy. This replaces the linear economy with elements of reusing materials, repairing products, prolonging the product life cycle, refurbishing and remanufacturing, and recycling.

Governance Pillar

Corporate governance is the system of rules, practices, and processes by which a company is directed, managed, and controlled. The system guides a company's relationships with its shareholders and stakeholders. Establishing and implementing these rules and practices involves balancing the interests of a company's many stakeholders. Creating and implementing transparent rules and controls can guide leadership in aligning the interests of shareholders, directors, management, community members, and employees. Good corporate governance can benefit various stakeholders as well as the operations and reputation of a company. Bad corporate governance can destroy a company's operations and ultimate profitability.

In large companies, a company's board of directors is responsible for the direction and execution of the company's corporate governance. The company's shareholders appoint the directors to make sure that the organization has an appropriate governance structure in place.

An effective board plays a key role in various areas that are critical to an organization. Here are some of their roles:

- Appointment of corporate officers, including the CEO
- Executive compensation
- Setting company goals and approval of financial objectives
- Strategic leadership and oversight, including advising on strategic issues
- Ensuring internal controls are adequate
- Representation of shareholders and other stakeholders who have an interest in the long-term performance of the firm
- Ensuring legal compliance
- Business ethics and conduct, including anti-corruption and anti-bribery policies and tax transparency
- Providing external perspective, best practices from other industries, resources, and networking and strategic partnership opportunities, as board members are often senior executives in other companies

One of the most important roles and responsibilities of the board of directors is the representation of shareholder interest in the company. Corporate governance addresses the separation of ownership and control. Shareholders are the owners of the company, but it is not possible for individual shareholders who lack a large percentage of overall shares to have meaningful and reasonable oversight of how the company is managed by the CEO and other company officers. Hence, dispersed shareholders need a voice to speak for them and their interest—the board of directors.

A specific issue that requires robust corporate governance is conflict of interest. A company employee could possibly choose personal gain over duties to shareholders and could possibly abuse the position in the company for personal gain. This can happen when a person could receive personal benefit from decisions being made by a company employee in their official capacity. For example, a procurement manager has been tasked with identifying the best supplier to provide maintenance services for the company's car fleet. One of the possible suppliers is owned by his brother-in-law, who would be happy to gain this significant business. However, the company operated by him does not provide the best offer in terms of quality and price for the organization that buys the maintenance services. The company's procurement manager may have two conflicting interests. In his capacity as a professional procurement manager, he needs and wants to give the business to the most suitable supplier, which is not his brother-in-law's business. On the other hand, he would love to help his brother-in-law, his sister, and their family to do well and gain the business. Obviously, the decision to give the business to the procurement manager's brother-in-law is not in the interest of shareholders. Corporate governance needs to address conflict of interest issue and provide some clear policies and guidance.

Another example is a CEO who pursues the acquisition of a competitor and who is willing to spend too much money on the acquisition. The reasons for the CEO's willingness to overpay for the acquisition may be personal interest in gaining power and reputation, leading a larger company, and possibly receiving higher compensation for leading the larger company. This would be a conflict of interest in regards to what is best for shareholders compared to the CEO's own personal ambitions.

The disconnect between the interests of the employees, manager, and CEO in the above examples and the interests of the owners (the shareholders), are described as the principal-agent problem or agency problem. The principal-agent problem is a conflict in priorities between a principal, here the shareholders, and the agent authorized to act on their behalf, company employees and especially leadership. An agent may act in a way that is contrary to the best interests of the principal.

The role of corporate governance is to identify and address possible conflicts of interest and possible principal-agent problems. This could be achieved by providing clear guidance on how possible conflicts of interest need to be handled in the company's code of conduct.

Generally, the basic principles of good corporate governance are as follows.

- **Accountability:** The board must explain the purpose of a company's activities and the results of its conduct. Both board and company leadership are accountable for the assessment of a company's capacity, potential, and performance. It must communicate issues of importance to shareholders.
- **Transparency:** The board should provide timely, accurate, and clear information to all stakeholders.
- **Fairness:** The board of directors must treat shareholders, employees, vendors, and communities fairly and with equal consideration.
- **Responsibility:** The board is responsible for the oversight of corporate matters and management activities. It must be aware of and support the successful ongoing performance of the company. Part of its responsibility is to recruit and hire a CEO. It must act in the best interests of a company and its investors.
- **Risk management:** The board and management must determine risks of all kinds to shareholders and other stakeholders. It must provide guidance on how best to control and mitigate risks. It must act on those recommendations to manage risks and inform all relevant parties about the existence and status of risks.

The benefits of good corporate governance include building trust with investors, the community, and public officials. Good corporate governance helps an organization to operate more efficiently, and it promotes the long-term financial viability of the organization. It helps organizations to respond to stakeholder concerns swiftly and effectively. It improves access to capital, improves a company's reputation and reduces the risk of business ethics violations. Finally, good corporate governance safeguards against mismanagement and the potential for financial loss.

Bad corporate governance can have the opposite effect, eroding relationships and trust with both internal and external stakeholders. This can damage a company's reputation, create legal, regulatory, or ethical scandals, reduce both employee and customer retention, cause stock prices to fall, and ultimately eat away at a company's profitability.

Corporate governance, particularly the role of boards of directors, has long been critiqued for its relative ineffectiveness in safeguarding ethical business conduct and ensuring long-term value creation. Boards are meant to provide oversight, ensure accountability, and represent shareholders' interests, yet several inherent weaknesses often limit their effectiveness.

One primary critique is the problem of insufficient independence between board and firm. Many boards are composed of directors with close personal or professional ties to the CEO or other executives, leading to conflicts of interest and a lack of genuine oversight. This dynamic can result in management decisions being "rubber-stamped" rather than challenged, especially on ethical or controversial issues. Another criticism is the lack of broad perspective in expertise, perspective, and background among board members, which can narrow the scope of strategic discussions and blind boards to emerging risks, particularly around social, environmental, and ethical concerns.

Additionally, the infrequency of meetings and the often-superficial nature of board deliberations can prevent directors from fully understanding complex business operations and risks.

Ethical failures often stem from boards prioritizing short-term financial performance over long-term sustainability and ethical considerations, pressured by shareholder expectations or executive incentives tied to stock performance. This can lead to a focus on profit at the expense of social responsibility, environmental stewardship, or sound governance, undermining the board's fiduciary duty to broader stakeholder groups.

Some of the most recent trends and hot topics in corporate governance are:

- Board composition with a broad background
- Executive compensation
- Making ESG an imperative
- Dealing with more conscientious consumers, with millennials and Gen-Z leading the change

- Ensuring boards are a strategic asset
- A focus on future-proofing companies in the face of disruptive change
- Companies implementing new technologies like AI in a responsible way using robust and meaningful data governance policies

CEO compensation and excessive retirement packages and severance agreements are issues in corporate America, where they are sometimes called “golden handshakes.” CEO-to-worker compensation has reached a multiple of around 350 in the U.S., a huge increase from a ratio of around forty until the 1980s and much higher than ratios in other countries and regions of the world. Obviously, it is not possible to determine a perfect ratio and the appropriate compensation for senior executives, which is a very complex, multifactor decision. The notion of self-serving executives is a criticism raised by stakeholders in the U.S. CEO compensation is the result of supply and demand, and executive leaders bring unique competencies and experience into the equation. However, excessive ratios have seen a lot of scrutiny in the governance pillar for assessing a company's ESG performance.

Video 10.3: Role of the Board in Creating an Ethical Corporate Culture [06:48]

The video for this lesson describes the role of the board in creating an ethical corporate culture.

Access this YouTube video by scanning the QR code.



Application

- Choose your favorite company or your preferred future employer. Visit the company's website, and explore the company's ESG strategy.
 - What are the specific initiatives and actions that the company takes in support of environmental and social issues?
 - How does the company measure its performance?
 - Which metrics and KPIs are being used?
 - How does the company report on its ESG activities and ESG performance?

Key Takeaways

An organization's sustainability practices are typically analyzed against environmental, social, and governance (ESG) metrics. Sustainability has an environmental, social, and economic scope. In response to addressing sustainability challenges, almost all companies develop ESG strategy.

A company must embed sustainability into the fabric of its business, corporate culture, and corporate strategy. A robust ESG strategy is the core of a company's sustainability strategy, which enables new business models to support sustainability goals, increases operational efficiencies, complies with regulatory requirements, exposes innovation opportunities, and improves the customer experience.

while creating competitive advantage. Success-critical areas of ESG include the design of transparent and resilient global supply chains that embed ethical and sustainable practices and that support a circular supply chain. Firms must embark on transparent and high-quality legal and regulatory reporting that meets the demands of regulators and investors for financial-grade disclosure of ESG metrics. Firms engage with various stakeholders in the context of inclusive stakeholder management. Lastly and maybe most importantly, firms decarbonize their production and operations to manage the transition to clean energy and to map out a clearly defined path to net-zero business operations.

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10.8 Ethics Strategy

One positive outcome of corporate scandals has been an increased focus on business ethics by firms. Business ethics covers the moral principles, policies, and values that govern the way companies and individuals engage in business activity. It is a form of applied professional ethics that examines ethical principles and problems that can arise in a business environment. Business ethics applies to all aspects of business conduct and is relevant to the conduct of individuals and entire organizations. At the minimum, companies need to stay compliant with all applicable laws and regulations to avoid lawsuits and fines, and they must also avoid violating regulation that will limit the business's freedom to act. Strategy development should always occur through acceptable practices in the industry and in light of the firm's own code of ethics and compliance.

Corporate scandals:

- Bernie Madoff's Ponzi scheme: Madoff was a former chairman of the NASDAQ stock exchange and ran an investment firm that promised consistently high returns. Instead of using real investment profits, he paid earlier investors with money from newer investors, which created the illusion of success. His scheme lasted from the '90s until its collapse in 2008, when the financial market downturn led to many clients withdrawing their money, exposing his fraud. Madoff's scheme is considered the largest

financial fraud in history.

- Volkswagen's Dieselgate: In 2015, Volkswagen was caught in a scandal for installing illegal software and defeat devices in millions of diesel cars worldwide to cheat on their emissions tests. The software allowed the cars to pass emissions tests by temporarily lowering nitrogen oxide emissions to comply with regulations during testing. However, during regular driving, the cars emitted pollutants forty times greater than allowed, far exceeding legal limits. As a result, Volkswagen faced massive amounts of recalls, numerous legal actions, and fines, costing the company billions of dollars as well as severely damaging its reputation.
- Purdue Pharma and the U.S. opioid crisis: A pharmaceutical company founded in 1892 played a significant role in the U.S. opioid crisis by aggressively marketing OxyContin as a safe painkiller with a low addiction risk, despite a lack of evidence. Purdue's misleading claims resulted in widespread overprescription, which led to many patients becoming dependent on the drug. As these addiction rates skyrocketed, OxyContin became extensively misused, meaning that Purdue Pharma played a huge role in the catastrophic opioid epidemic. The company then had to face numerous lawsuits, having to settle for over 4.5 billion dollars in 2021 and eventually filing for bankruptcy. The opioid crisis led to the overdose death of hundreds of thousands of victims.
- Boeing 737 Super Max airliner with two crashes: The Boeing 737 MAX was involved in two fatal crashes that resulted in 346 people losing their lives. These unfortunate crashes resulted from the malfunction in their Maneuvering Characteristics Augmentation System, which caused the planes' noses to be tilted down due to faulty sensor data. Investigations into the two flights exposed Boeing's design flaws and its lack of pilot training and regulatory management by the Federal Aviation Administration. The 737 MAX fleet had to be grounded, and Boeing was met with countless lawsuits and reputational damage. The Boeing 737 MAX was able to be redeployed after software fixes and regulatory changes.
- Two million fake Wells Fargo accounts: This scandal was centered on Wells Fargo employees developing over two million unauthorized bank and credit card accounts without consent from customers, driven by extreme sales pressure to meet unrealistic quotas set by Wells Fargo Management. Customers were billed fees for these accounts, negatively affecting their credit scores and their wallets. Wells Fargo was ordered to pay \$185 million and was subject to abundant lawsuits and investigations. Several Wells Fargo executives resigned, and the company was required to reform its unethical sales practices and corporate culture.
- Theranos case: Elizabeth Holmes founded Theranos in 2003, claiming its technology could change blood testing forever by only requiring a couple drops of blood. The company raised over \$700 million, reaching a \$9 billion valuation. However, in 2015, investigations showed that Theranos's device, Edison, was unreliable and that the company was really using commercial machines for their tests. This led to lawsuits, federal charges, and the downfall of Theranos. In 2022, Holmes was convicted of defrauding investors.

As firms move from “doing right” to “doing good” and endorse ESG and CSR strategies, then employees, managers, customers, and other stakeholders take pride and satisfaction in the impact their company has on improving society. Further, as contemporary societal expectations have shifted toward companies embracing a responsibility beyond the profit motive, firms have witnessed new opportunities to turn corporate values and ethical decision-making into a competitive advantage within their marketplace.

Today, corporate business ethics goes beyond compliance and is not solely a reactive approach. Business ethics is part of an organization's core values and corporate culture. Ethics is part of an organization's foundation, incorporated into the organization's business-level strategy and embedded in its daily decision-making. Failure to balance stakeholder interests can result in failure to maximize shareholders' wealth. A robust corporate ethics strategy becomes a source of competitive differentiation and a source of sustainable competitive advantage.

Video 10.4: The ethics of business. Where and why it can go wrong [10:55]

This video explains the ethics of business and where and why it can go wrong.

Access this YouTube video by scanning the QR code.

**Video 10.5: What is business ethics? [04:08]**

The video for this lesson explains personal business ethics.

Access this YouTube video by scanning the QR code.

**Video 10.6: What is Ethics? What is Business Ethics? [04:35]**

This second video for the lesson focuses on business ethics.

Access this YouTube video by scanning the QR code.

**Application**

- Think about your own personal ethics. Describe the ways that “doing right” and “doing good” are different for you.

Key Takeaways

Business ethics covers the moral principles, policies, and values that govern the way companies and individuals engage in business activity. It is a form of applied professional ethics that examines ethical principles and problems that can arise in a business environment.

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10.9 Contemporary Questions of Corporate Ethics

Businesses need to embrace a robust system of **data governance** to manage data responsibly.

For new technologies, there is clearly a regulation lag. Regulators and lawmakers struggle to grasp the ethical implications of new technologies, leading to a lack of regulation in this time of accelerating technology penetration.

At the same time, there is also an ethical lag that occurs when the speed of technological change far exceeds that of ethical development.

Consequently, ethical technological leadership is critical for businesses, which includes an appropriate level of self-regulation. The current business ethics “hot topic” is making responsible and ethical decisions as to what ethical principles will be programmed into AI and applied to machine learning. While there is no perfect solution, companies need to develop robust technology strategies and data governance strategies embedded in their ethics and CSR/ESG strategies.

Business Ethics in a Multi-Stakeholder Society and Shareholder Activism

Companies operate in an era of hyper-transparency and intensifying political and social disruptions. There are growing expectations from various stakeholders to support a more inclusive economy and sustainable environment. The U.S. has clearly moved away from a business social contract where the shareholder is the most important stakeholder and guiding star for business. We have moved away from a shareholder economy to an inclusive stakeholder economy. As a result, companies are reevaluating their purpose in society. Business assumes broader responsibilities in relation to society and serves a wider range of human values than ever before. Engagement with multiple stakeholders and the strategic management of public issues becomes critical not only for financial success but often for the survival of companies.

Another contemporary issue is the emergence and evolution of shareholder activism. Now, even smaller shareholders use their rights to position topics on the agendas of CEOs and boards of directors that go beyond financial topics. Social and environmental issues are aggressively pursued, and companies need appropriate strategies to interact with activist shareholders.

One example of shareholder activism illustrates the power that even smaller shareholders hold. Rio Tinto is world's second largest metals and mining corporation. In May 2020, Rio Tinto detonated explosives at Juukan Gorge in Western Australia to expand an iron ore mine. The destruction included two significant Aboriginal rock shelters that contained evidence of human occupation for forty-six thousand years. As a result of opposition from activist shareholders, Rio Tinto's Chief Executive, Jean-Sébastien Jacques, had to quit his position over this destruction of a sacred aboriginal site in Western Australia despite the fact that the destruction was done with ministerial consent under Western Australia's cultural heritage protection laws.

Business Ethics in a Globalized World

Most U.S. multinational corporations operate in one of two ways internationally: sourcing from suppliers abroad or selling products and services abroad. Being a global player adds several additional business ethics topics to the ethics agendas of companies. The fundamental question for global players is which ethical norms should guide their business ethics policies when they are operating in two (or more) different countries with different laws, different values, and different cultural norms.

In support of a global business ethics strategy, there is a clear global code of conduct in which companies must find an appropriate middle ground between home and host country stakeholder expectations. For example, local laws set the minimum standard, such as ensuring that a living wage is paid to employees abroad and that the working conditions are conducive to the work being done. As stated in the ESG strategy, it is consensus now and the expectation of many stakeholders that U.S. companies have a responsibility to monitor and maintain the working conditions in the factories of their suppliers abroad. The rights of workers in the global value chain are a strong focus. These rights are related to issues of slave-free labor, appropriate and safe working conditions, equal opportunities, nondiscrimination, a living wage, and other work-related rights.

Beyond employees in the value chain, companies also need to manage their impact on affected communities and the impact of business operations on local economies. They must protect social and cultural rights and the civil and political rights of local populations, especially as they relate to the impact on indigenous people.

Finally, the rights of consumers and end users need to be protected regarding information, personal safety, social inclusion, and the protection of personal data.

Video 10.7: What are the ethical issues facing business today? [02:25]

The video for this lesson explores the ethical issues that businesses face today.

Access this YouTube video by scanning the QR code.



Key Takeaways

With emerging technologies like AI, big data, and automation, business ethics is rapidly changing. Companies need an active approach and need to assume ethical responsibility for the use of new technologies, with a focus on good data governance and transparency. Businesses need a robust system of data governance to manage data responsibly. Operating in a globalized business world, human rights issues and social issues need to be addressed beyond the borders of the U.S. and the factory gates of U.S. companies. Contributing to fighting climate change becomes an opportunity in support of stakeholder loyalty and competitive differentiation but also an ethical obligation. Companies have the resources, the know-how, and the power to make a positive difference. With great power comes great responsibility.

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10.10 Analyze Sustainability and Ethics Strategy

When you conduct a case analysis, you analyze a firm's sustainability and ethics strategy. This is step six in the case analysis process.

6. As appropriate to the case, analyze strategies: Corporate-level, business-level, innovation, sustainability and ethics, technology, and multinational strategies.

- a. Use strategic management analytical frameworks to analyze, interpret, and evaluate strategies.
- b. Ensure line of sight and congruence within analysis of each strategy.

10.11 Why Sustainability and Ethics Strategy Is Important to Business Graduates

Sustainability and ethics is a rather new area that is already a competency highly valued by employers. The majority of CEOs address risks and opportunities of climate change in their business models. As a consequence, two-thirds of CEOs are looking to upskill or reskill their workforce in the topic of sustainability, according to a 2023 global PwC survey of 4,700 CEOs. Sustainability does not only impact the scope of skills expected in successful managers in all business and functional areas of a firm, it also has become a hiring criterion. Seventy-one percent of business leaders intend to implement sustainability experience as a hiring criterion, according to a 2023 IBM survey of more than three thousand business leaders. Having a sound understanding of business sustainability gives you a head start in the application process and the corporate world, where sustainability expertise is becoming the backdrop for managers in all areas of business. Lastly, sensitizing you to the importance of business ethics keeps you out of trouble and helps you to embrace a moral compass aligned with business ethics to drive sustainable success in your career.

10.12 Conclusion

Businesses are operating in an increasingly volatile, global, and multi-stakeholder environment that is driven by continuous change and disruption. To strategically position the business for success, organizations account for disruptive megatrends related to climate change, social justice, and technology that drive the strategic agendas of organizations.

Every organization's strategic canvas must include consideration of sustainability (and its resulting CSR and ESG strategies) as well as business ethics strategy. Codes of conduct and various other business ethics practices improve companies' accountability to the communities and society they serve. Globally, business activities have lowered poverty rates, but ethical issues remain. Balancing competing interests on many issues (such as offshoring, pollution, sustainability, and economic inequality) are a high priority. Responsible AI and data governance strategies provide guidelines for how companies act ethically in the era of accelerating technology advancement.

The role of boards of directors in the corporate governance of organizations has become more important than ever, especially in large publicly traded corporations. Wise boards work to manage the agency problem that creates a conflict of interest between top managers, such as the CEO, and other groups with stakes in the firm.

Demonstrate Your Knowledge, Skills, and Competence

Use these questions to test your knowledge of the chapter:

1. Describe megatrends and the major categories of megatrends, giving an example of each. Discuss the impact of megatrends of strategy formulation and implementation.
2. Discuss climate change, the greenhouse effect, and global warming. Explain the relationship of these concepts.
3. Describe sustainability strategy and its relationship to business-level strategy.
4. Explain the business case for sustainability.
5. Describe the triple bottom line.
6. Discuss corporate social responsibility (CSR) and how this is a sustainability strategy.
7. Describe environmental, social, and governance (ESG) strategy and how this is a sustainability strategy.

8. Discuss the relationships between the triple bottom line, CSR, and ESG.
9. Describe ethics strategy and its relationship to business-level strategy.
10. Discuss key contemporary questions of corporate ethics.
11. Describe how competence with sustainability and ethics strategy is relevant and important to you.

You have just demonstrated your knowledge of sustainability and ethics strategy. Congratulations!

Figure Descriptions

Figure 10.1: Shifting economic power: The shift of economic might to emerging markets and developing economies, including China. (1) E7 economies double the size of G7 by 2040. (2) 80% of middle class in emerging economies. (3) 75% faster growth in emerging economies. (4) Emerging economies 50% of global by 2025. Climate change and resource scarcity: The impact of climate change as well as an increased strain on the world's resources, including energy, food, metals, and water. (1) 50% increase in food demand by 2050. (2) Water crisis is #1 global risk, says WEF. (3) 48% think business should be force for good. (4) \$22tn social responsible investments today. Technological breakthrough: The rapid advancement of technology, especially artificial intelligence (AI) and machine learning, is at the center of all megatrends. (1) 90% of world data create in last 2 years. (2) 1 trillion objects connected by 2022. (3) 90% of stock trading now done by algorithm. (4) 66% of world is connected at any time. Demographics and social change: Changes in global demographics (i.e., world population, density, education level, etc.) will bring social change. (1) Global population towards 10bn by 2050. (2) 13% of us over 65 by 2030, from 8% today. (3) 90% of under 25s live in emerging economies. Rapid urbanization: The global migration to megacities, and the challenges and opportunities that emerge as a result. (1) 1.5 million people move to cities every week. (2) 66% live in cities by 2050, from 54% today. (3) 61% of global GDP created by 750 cities. This graphic is purple.

Figure 10.5: The business case for sustainability: drives internal innovation, improves environmental risk, attracts and retains employees, expands audience reach, builds brand loyalty, reduces production costs, garners positive publicity, and serves as a market differentiator. This graphic is purple.

Figure 10.7: Venn diagram of three overlapping purple circles. The top circle is labeled "People" and asks, "How socially responsible has the organization been?" The bottom left circle is labeled "Planet" with the question, "How environmentally responsible has the organization been?" The bottom right circle is labeled "Profit" stating, "The traditional measure of corporate profit." The overlapping areas between "People" and "Planet" are labeled "Bearable," between "People" and "Profit" is labeled "Equitable," and between "Planet" and "Profit" is labeled "Viable." The central overlapping area where all three circles intersect is labeled "Sustainable."

Figure 10.10: A purple pyramid divided into four horizontal levels, each representing a type of responsibility. From top to bottom, the levels are labeled: "Corporate responsibility," "Ethical responsibility," "Economic and financial responsibility," and "Legal and regulatory responsibility."

Figure 10.11: Environmental: carbon footprint reduction, climate change strategy, waste reduction, energy usage/efficiency. Social: fair living wages, equal job opportunity, health and safety, responsible suppliers, respecting labor laws. Governance: risk management, compliance, ethical business practices, accounting transparency. This graphic is purple.

Figure 10.12: Linear diagram with a purple arrow moving from left to right. From left to right: (1) resources, (2) take (including resource extraction), (3) make (including production, distribution, and consumption), (4) waste (including dispose), and (5) regenerative capacity of the Earth.

Figure 10.13: A circular purple arrow pointing clockwise with "Circular economy" written in the center. Bullet point list for circular economy includes: generate increased income, reduce resource dependency, minimize waste, reduce environmental footprint. On

the circular arrow there are five boxes: (1) better service (to extend lifespan), (2) collect at end-of-life and remanufacture, (3) recycle waste and reuse resources, (4) green products (non-toxic, long-life, recyclable), and (5) cleaner production (using fewer resources).

Figure 10.14: Five high priority topics for hybrid work. (1) Flexible and remote work remains employee priority. (2) Rebuild the employee experience and manage connectivity in a hybrid work model. (3) Reimagine the physical space and design new footprint and office space for a hybrid work model. (4) Measure productivity in a remote setting; redefine metrics to assess productivity and rules of engagement. (5) Manage work-life boundaries and fundamental human needs. Support mental and physical well-being. This graphic is purple.

Figure References

Figure 10.1: Disruptive megatrends will impact strategy formulation and implementation. Kindred Grey. 2025. CC BY. Adapted under fair use from <https://www.peterfisk.com/2019/12/mega-trends-with-mega-impacts-embracing-the-forces-of-change-to-seize-the-best-future-opportunities>. Includes the following icons from the Noun Project ([Noun Project license](#)): Money (New River, 2025, <https://thenounproject.com/icon/money-7572620>), climate change (Lewen Design, 2024, <https://thenounproject.com/icon/climate-change-6816602>), computer (Siti Zaenab, 2024, <https://thenounproject.com/icon/computer-7554842>), social (Adrien Coquet, 2024, <https://thenounproject.com/icon/social-7479108>), and city (mohkamil, 2018, <https://thenounproject.com/icon/city-1744061>)

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Figure 10.6: Richard Branson. Jeff Foust. 2010. CC BY 2.0. <https://flic.kr/p/8MgXvG>

Figure 10.7: The triple bottom line emphasizes the three Ps: people (social concerns), planet (environmental concerns), and profits (economic concerns). Kindred Grey. 2025. CC BY.

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Figure 10.9: Levi's corporate headquarters. Maxence. 2016. CC BY 2.0. [https://commons.wikimedia.org/wiki/File:Levi_Strauss_and_co_\(29045329720\).jpg](https://commons.wikimedia.org/wiki/File:Levi_Strauss_and_co_(29045329720).jpg)

Figure 10.10: Different corporate responsibilities. Kindred Grey. 2025. CC BY.

Figure 10.11: ESG. Kindred Grey. 2025. CC BY. Includes the following icons from the Noun Project ([Noun Project license](#)): Leaf (Dwi Budiyo, 2025, <https://thenounproject.com/icon/leaf-7559318>), people (Wilson Joseph, 2024, <https://thenounproject.com/icon/people-6641820>), and scroll (ardi muctar, 2024, <https://thenounproject.com/icon/scroll-7279286>)

Figure 10.12: Linear economy. Kindred Grey. 2025. CC BY.

Figure 10.13: Circular economy. Kindred Grey. 2025. CC BY.

Figure 10.14: Organizations reimagining “new work” in a hybrid work model. Kindred Grey. 2025. CC BY.

Figure 10.15: The Patagonia story: making business sustainability the strategic right to win and the main source of competitive differentiation. Dave Dugdale. 2010. CC BY-SA 2.0. <https://flic.kr/p/8ygy9M>

Figure 10.16: Patagonia's “Don't buy what you don't need” advertisement. Used under fair use from <https://medium.com/@the-learningcurve/dont-buy-this-jacket-fc3bece754aa>

11. FORMULATE TECHNOLOGY STRATEGY

Learning Objectives

After engaging with this chapter, you will understand and be able to apply the following concepts to developing and implementing strategy.

1. Disruptive technologies, Industry 4.0, and the Fourth Industrial Revolution
2. Overview of new and emerging technologies and their impact on strategy
3. The role of technology in strategic planning
4. Frameworks for technology-driven strategic innovation
5. Technology as a strategic resource and a driver for gaining a sustainable competitive advantage
6. Alignment of technology strategy with business strategy
7. Leading-edge technology strategy elements
8. Why technology strategy is important to business graduates

By this chapter's conclusion, you will be equipped to analyze technology strategy.

11.1 Introduction

This chapter examines technology strategy. In the discussion, you learn what navigating technological disruption entails, including the role of digital transformation and its impact as a megatrend on business and strategy as well as the role of Industry 4.0, the Fourth Industrial Revolution. Next you learn the importance of new and emerging technologies and their strategic implications. This includes big data and data analytics, artificial intelligence and machine learning, cloud computing, Internet of Things, blockchain technology, and quantum computing. Then you learn a framework that considers technology as a strategy or an enabler of strategy. You learn that there are a few relevant intersections of technology and strategy, where technology can create value and drive competitive differentiation. These areas of value and differentiation include data governance and the responsible use of AI, implementation of Industry 4.0, technology-enabled new business models and enhanced customer experiences, technology as a strategic resource, digital transformation, architecture, and the creation of an agile organization. Finally, you learn how to analyze technology strategy.

11.2 Technology Strategy

Like all strategy formulation, formulating technology strategy answers the question “Where are we going?” All firms need to address the role of technology and technology strategy.

Like innovation and sustainability and ethics, technology is another strategic focus that is formulated at the strategic business unit level of a company and embedded in business-level strategy. As such, technology strategy also answers the “right to win” question of how specifically a firm is going to win or compete in its chosen markets and market segments.

Like all strategy, technology strategy focuses on an outside-in perspective. Companies carefully monitor their external environments and analyze trends and formulate strategies that are forward-looking. Robust technology strategy considers the volatile, uncertain, complex, and ambiguous nature of the firm's external environment.

This chapter analyzes how changes in the external environments of firms drive strategic responses and how companies formulate technology strategy to create and sustain a competitive advantage.

Technology strategy uses digital technology to improve an organization's processes, operations, products, and services. Technology strategy frames the “rewiring” of an organization, with the goal of creating value by continuously deploying technology at scale.

Key Takeaways

Like all strategy formulation, formulating technology strategy answers the question “Where are we going?” Like innovation and sustainability and ethics, technology is another strategy focus that is formulated at the strategic business unit level of a company and is embedded in business-level strategy. Technology strategy focuses on the use of digital technology to improve an organization's processes, operations, products, and services.

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11.3 Navigate Technological Disruption

The previous chapter focused on sustainability and ethics strategy, providing a framework for how disruptive megatrends impact strategy (in the form of new ESG strategy, for example).

This chapter introduces a second disruptive megatrend with significant impact on strategy, digital transformation, which involves new and emerging technologies that impact both strategy formulation and strategy implementation. **Digital transformation** is the process of using existing or new digital technologies to address evolving market conditions and customer expectations.

We are living in the era of technological disruption, and we are in the middle of the Fourth Industrial Revolution. This rapidly evolving landscape of technology changes the way we work and the way we live. It also has significant implications on businesses, their strategic positioning, and their ways of looking for technology-driven and technology-enabled opportunities of competitive differentiation. Digital transformation changes how companies make strategic decisions and how companies operate and deliver value. Digital transformation also drives strategic shifts that every firm needs to embed in its business-level strategy. Hence, developing strategy in the age of technology requires a deep understanding of technological trends and their strategic impacts in a technology-driven environment.

Figure 11.1 shows disruptive technologies.

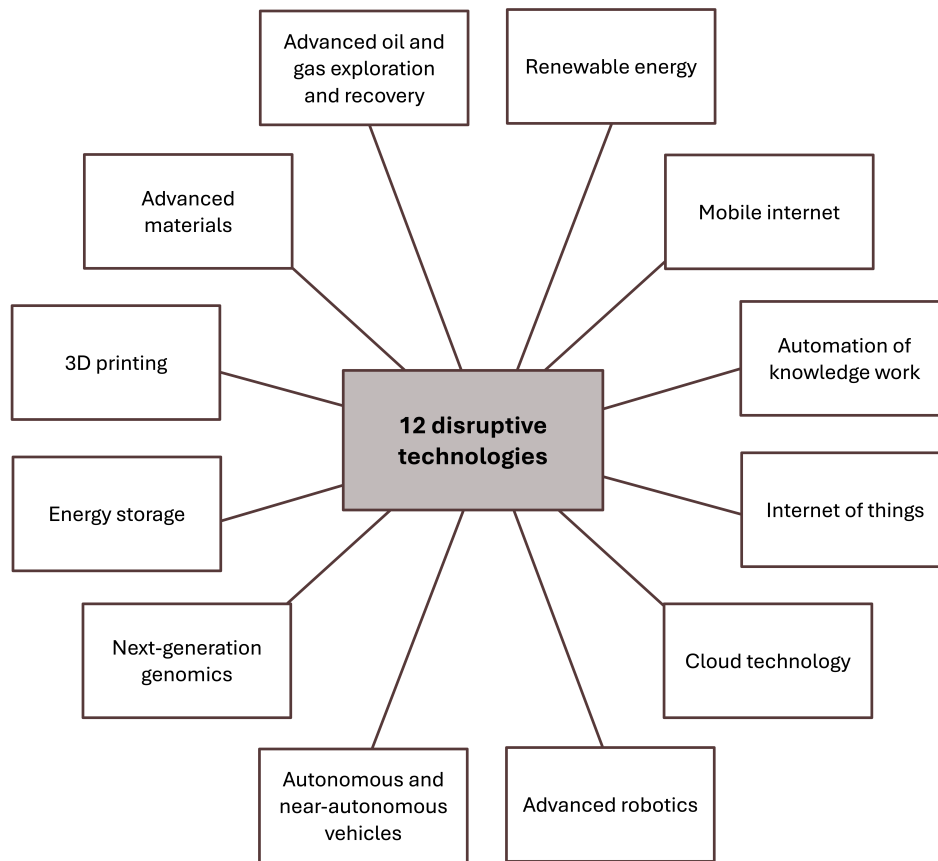


Figure 11.1: Disruptive technologies

According to Boston Consulting Group's Transformation Benchmarking Survey, digitization and digital transformation are the main drivers of companies evolving to survive the Fourth Industrial Revolution. This transformation needs to be driven by strategic considerations and must be a part of the technology strategy embedded into the business-level strategy of a firm.

Some data points and examples that illustrate the acceleration of technology development:

- In terms of new technologies, it took the telephone fifty years to reach fifty million users, the ATM eighteen years, the cell phone twelve years, and the internet seven years. It took Pokemon Go just nineteen days to reach fifty million users.
- During the First Industrial Revolution, it took four hundred years for human knowledge to double. IBM states that we are currently seeing a doubling of knowledge every twelve hours. We are living in the information age, and new technologies like the Internet of Things drive the trend of rapidly increasing knowledge, but they're also becoming obsolete quicker than ever before.
- You all use AI every day, driverless cars are already operating on U.S. streets, and technology companies are powering the econ-

- omy, creating more than 50 percent of total market value growth across all sectors since 2015 (Bain & Company).
- Ninety percent of the world's data has been created in the last two years. In 2022, more than one trillion objects were connected, and more than 90 percent of stock trading is now done by algorithms.
- In a PwC study of 4,700 CEOs, 56 percent stated that technological change is the main factor that drives change in the way their companies create, deliver, and capture value.
- When you apply for the job you will have after graduating from university, it will most likely be AI, not a personal recruitment specialist, that decides whether your application advances beyond the screening round in the application process.

These examples show that technology is a true game changer and that companies need to factor in a robust and holistic technology strategy. Disruptive innovation is much more common than ever before.

Another concept that emphasizes the strategic implications of technological disruption is the fact that we are living in the era of the Fourth Industrial Revolution. The First Industrial Revolution happened in the eighteenth century with the development of mechanical production equipment that replaced human labor, leading to enormous increases in productivity. This was followed by the Second Industrial Revolution with mass production and then the third, driven by the internet. The Fourth Industrial Revolution does not replace the “hand” (manual labor) with machines as the first did, but it replaces the “head” with smart machines, which is truly revolutionary and disruptive. The impact of this Fourth Industrial Revolution goes beyond economic impacts like productivity increases and mass production, also showing a significant social impact. Business is now embracing the concept of Industry 4.0, leveraging the rapid technological advancement that blurs the separation between the physical, digital, and biological worlds. **Industry 4.0** drives fundamental shifts in the global production and supply chain networks using smart technologies, automation, robotics, AI, machine learning, and embedded connectivity.

Figure 11.2 shows the evolution from Industry 1.0 (or the First Industrial Revolution) to Industry 4.0 (the Fourth Industrial Revolution).

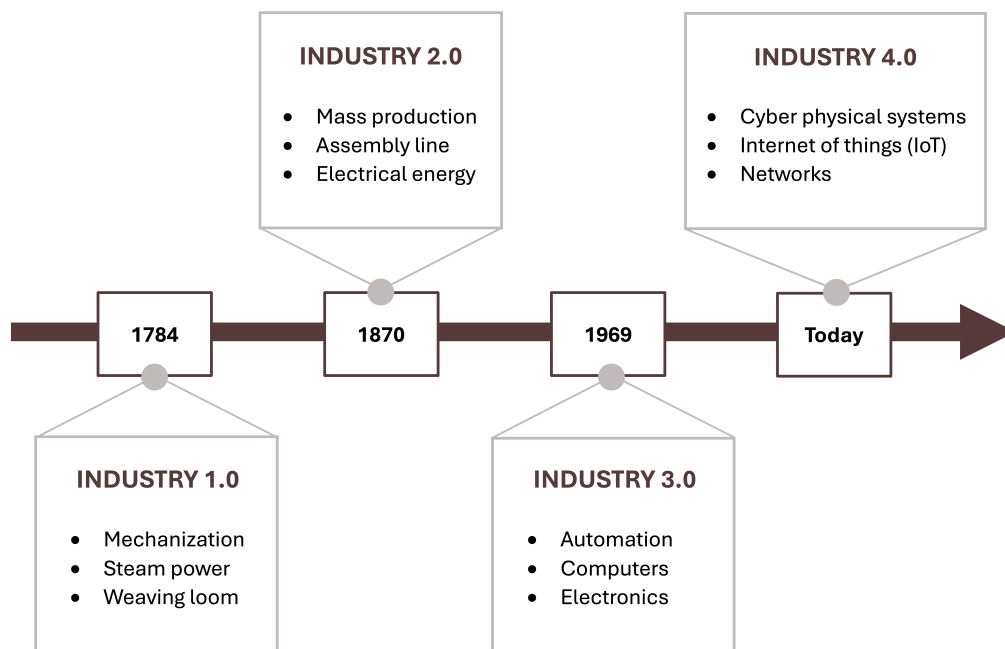


Figure 11.2: Evolution from Industry 1.0 to Industry 4.0

A practical example of a company navigating Industry 4.0 is BASF, the world's largest chemical company. While the chemical industry is an old and traditional industry, BASF uses Industry 4.0 concepts to change the way that the company operates. BASF implemented what it calls “smart manufacturing,” stating, “We are increasing the effectiveness of our plants and the efficiency of our

production processes through the use of digital technologies and data. With mobile devices, we have access to relevant information for our daily work. The tight integration of production and business processes allows us to make better and fast decisions” (basf.com). BASF uses augmented reality and the Internet of Things (discussed in detail in [section 11.4](#)) to make the maintenance and repair of their physical assets quicker and more productive.

The BASF example illustrates that new and emerging technologies are the game changer in Industry 4.0, showing significant impact on strategy development and strategy implementation.

Figure 11.3 provides an overview of disruptive Industry 4.0 technologies that drive the digital transformation and that need to be factored into the strategy process.

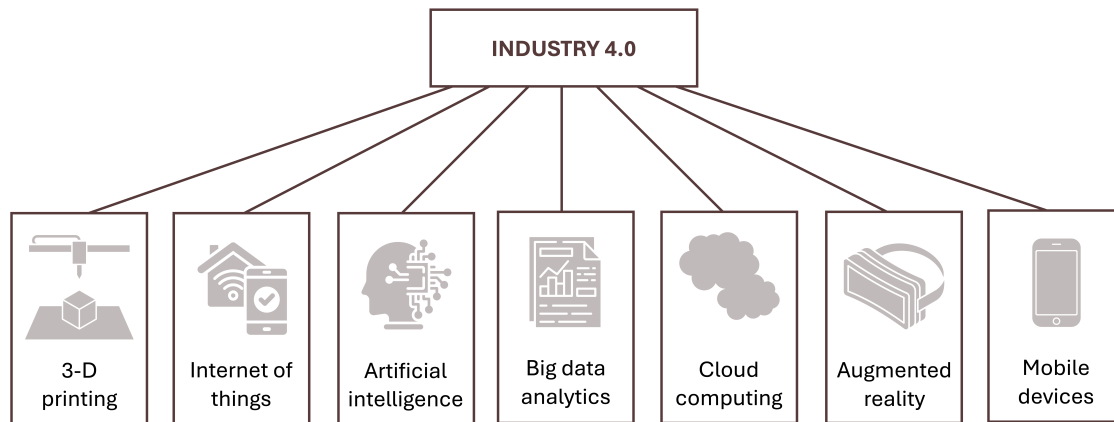


Figure 11.3: Disruptive Industry 4.0 technologies

The remainder of this chapter explores the critical intersection of technology and strategic management, examining how emerging technologies reshape business landscapes, competitive dynamics, and organizational capabilities.

Application

- Discuss three of the disruptive Industry 4.0 technologies in detail.
 - Describe your personal experience with these disruptive technologies.

Key Takeaways

A disruptive megatrend with significant impact on strategy is digital transformation, which involves new and emerging technologies that impact both strategy formulation and strategy implementation. We are living in the era of the Fourth Industrial Revolution. The First Industrial Revolution happened in the eighteenth century with the development of mechanical production equipment that replaced human labor and that led to enormous increases in productivity. This was followed by the Second Industrial Revolution with mass pro-

duction and then the third driven by the internet. The Fourth Industrial Revolution introduces smart machines that can drive industry like never before, which is truly revolutionary and disruptive.

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11.4 New and Emerging Technologies and Their Strategic Implications

New and emerging technologies are shaping strategy. The following technologies are game changers in the ongoing digital transformation, and they have a significant impact on strategy. Their impact on business and the strategy process needs to be understood, and the insight and opportunities made possible by technology need to be integrated and leveraged into a firm's technology strategy, which is embedded in its business-level strategy.

Big Data and Data Analytics

Business has an abundance of data available that can be used and leveraged for strategic decision-making, including critical strategic topics like market analysis, customer insights, and competitive intelligence. In the current digital age of data-driven decision-making, the data has a high strategic importance. Data is a strategic asset that provides insights into customer preferences, market trends, and operational efficiency. By collecting and analyzing vast amounts of data, companies can make informed, evidence-based strategic decisions, optimize their processes, personalize customer experiences, and forecast future trends, thus shaping their competitive advantage.

For example, many companies use data from rewards apps to analyze their customer preferences to tailor their promotions and recommendations to their individual users. In return, the apps offer value to customers, such as the convenience of quick and remote ordering. Data analytics allows these firms to gain a better understanding of customer behavior and preferences. A few examples of this include Starbucks, Waffle House, Taco Bell, and Kroger.

Artificial Intelligence and Machine Learning

While AI is not necessarily a new technology (computational linguistics started in the 1950s), its full game-changing impact on business has fully developed in recent years. AI, including generative AI, is used to automate processes, enhance decision-making, and provide predictive insights into the strategy process. It is used and leveraged throughout the entire strategy process. These uses include identifying complex market patterns and trends, strategically understanding past performance, forecasting future outcomes, using scenario planning for strategy formulation and implementation, and formulating and evaluating strategic alternatives. Advanced algorithms enhance strategic scenario analysis and optimize resource allocation. For example, Shell uses scenario planning to prepare for various future energy landscapes, ensuring that its business model provides adaptable strategic responses to a rapidly evolving external business environment.

Amazon uses artificial intelligence in its strategic management process to maintain its position as a leader in e-commerce and logistics. The company uses AI-driven algorithms to analyze vast amounts of customer behavior data, identifying complex market patterns and trends, such as changes in purchasing habits during economic shifts. Predictive analytics help Amazon forecast future demand for products in order to ensure inventory optimization and resource allocation.



Figure 11.4: Amazon

Together with AI, vastly large data sets, known as big data, can be used strategically to scan the external environment, identify emerging technology, create a technology roadmap, and detect weak signals. It can be used to anticipate demand patterns and consumer behavior, provide recommendations for optimal strategic decision-making, and support strategic planning in a dynamic VUCA environment.

Kroger has been exploring ways in which AI can be used to improve customer experience. In a *Forbes* interview, Kroger Chief Data & Technology Officer Todd James explains, “We are using AI-enabled dynamic batching to reduce Pickup lead time while enhancing the store associate experience. Through the power of machine learning and AI, we are developing new ways to elevate the Pickup experience for customers.”

Cloud Computing

Cloud computing enables on-demand access to computing resources, reduced infrastructure costs, and the flexible scaling of cloud solutions. This supports strategy by enabling faster responses to customer needs, collaboration and knowledge sharing, enhanced innovation, and faster execution of strategic initiatives.

For example, Netflix uses cloud computing in order to flexibly scale its streaming services. When a new season of a very popular show is released, the platform scales up its server capacity to handle increased viewer traffic in real time, ensuring uninterrupted service.

Internet of Things (IoT)

The Internet of Things (IoT) is a network of physical objects that can connect and share data with other devices and systems over the internet. IoT devices are also known as smart objects and can include common household items like fixtures and kitchen appliances. According to Statista, the number of Internet of Things devices worldwide is forecasted to almost double from 15.9 billion in 2023 to more than 32.1 billion IoT devices in 2030. The Internet of Things is one of the drivers for the abundance of data that businesses can use in their strategy formulation. In strategy, the Internet of Things is used to improve operations, enhance the customer experience, and improve service offerings. IoT-enabled businesses can use real-time data to make informed decisions, respond to market shifts, and anticipate challenges.

For example, Siemens uses the Internet of Things in its factories to improve productivity and operational efficiency. John Deere uses the Internet of Things to integrate their sensors on their agricultural equipment, allowing farmers to collect and analyze real-time data on soil moisture, weather, and crop health. This data allows farmers to make data-driven decisions improving their yields and overall operational efficiency.

Blockchain Technology

The blockchain offers a decentralized and secure way to record transactions. Its implications for strategy include enhanced transparency, reduced fraud, and the possibility of new business models.

IBM uses blockchain in supply chain management to create secure transaction mechanisms and to improve transparency and traceability. Another example is international shipping and logistics giant, Maersk. Maersk uses blockchain in global shipping to create an end-to-end transparent supply chain tracking system with higher levels of visibility, a reduced administrative overhead, and an enhanced compliance tracking across complex global logistics networks.



Figure 11.5: Kroger is an example of a company using AI to improve customer experience

Blockchain technology also allows for supply chain transparency. IBM uses blockchain to enable their supply chain partners to share trusted data through permissioned blockchain solutions. This approach provides end-to-end visibility that allows businesses and consumers to verify product authenticity and responsible sourcing, in return gaining trust from customers across the supply chain.

Quantum Computing

Quantum computing promises unprecedented computational power. The applications for quantum computing are primarily centered around speed. Quantum computing allows for the processing of vast amounts of datasets and complex calculations at extremely high speeds that are unattainable by normal computers. While this is not yet a market-ready technology, businesses need to monitor its development closely and possibly use first-mover advantages in this area as a possible source of a sustainable competitive advantage.

Quantum computing also allows for advantages in securing sensitive government communications and protecting financial transactions and personal data.

Application

- Discuss one of the new and emerging technologies in detail.
 - Describe your personal experience with this new and emerging technology.
 - Explain how you predict the new and emerging technology will impact business in the short and long run.

Key Takeaways

New and emerging technologies are shaping strategy, including big data and data analytics, artificial intelligence and machine learning, cloud computing, Internet of Things (IoT), blockchain technology, and quantum computing.

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11.5 Framework: Technology as a Strategy or an Enabler of Strategy

Technology can be either a strategy or an enabler of strategy.

Technology strategies co-evolve along with the emergence of new technology systems. New technology systems such as printed electronics and fiber optics, are rapidly emerging at the interfaces of unrelated technology areas. Therefore, new technology systems, result from the convergence of these distinct yet now intersecting technology systems. When formulating a robust and value-adding technology strategy, firms need to integrate new and existing technologies into a coherent strategy. Firms are dealing with unrelated knowledge rooted in different technologies and must decide how systemic (complete technology system) or focused (single component of the technology system) their engagement in technology development in the converging technology system is going to be. Companies also must decide strategically the extent to which to develop specialized or design knowledge. From a systems perspective, technology strategy can be considered from the perspective of the scope (focused vs. systemic engagement with the technology system) and type of technological knowledge (specialized or design knowledge) (Wambsganss, et al., 2023).

A firm's technology strategy must directly support and enable the firm's broader strategic objectives. Technology needs to create value and drive competitive differentiation, and technology strategy needs to address this. Technological investments in a firm's resources, capabilities, and core competencies need to align with the firm's mission, purpose, vision, and values, and the investments must directly enhance the firm's technology strategy. In this sense, technology strategy is a success-critical strategy.

As an enabler of strategy, the more extensive the adoption of new digital technology, the larger the change in strategy (Van Zeebroeck, Kretschmer, & Bughin, 2023).

When firms approach technology as an enabler of strategy, technology is not the primary focus of strategy. In this case, technology is neither the starting point nor the solution for a firm's strategy. Taking the approach of technology as an enabler of other strate-

gies, a firm first must define strategic opportunities and threats that arise from its external environment; then it defines the strategic strengths and weaknesses that result from internal resources, capabilities, and competencies. Then the firm needs to analyze how new and emerging technologies can position the company to take advantage of its opportunities and mitigate its threats by enhancing its strengths and bolstering its weaknesses.

As an enabler of strategy, technology needs to be closely aligned with strategy, and the firm's approach to technology must be derived from the firm's other strategies and embedded in them, directly supporting the firm's broader strategic objectives. Technology needs to create value and drive competitive differentiation while aligning with the firm's mission and other strategies. Here, technology is a success-critical strategy enabler but not the starting point of strategy.

While there is no “one size fits all” approach to integrating technology into a firm's other strategies, the following are a few relevant intersections where technology and strategy interface and where technology can create value and drive competitive differentiation.

Data Governance and Responsible Use of AI

While the use of technology provides unprecedented business opportunities, every company also must address the risks and threats that accompany the use of new technologies. The abundance of available data about customers can cause issues related to privacy rights. Data breaches in an increasingly digital world pose a significant risk both to customers and the firm. Cybersecurity is not just a technical concern but a strategic business concern because of the threats to brand reputation and financial stability when data is breached. A robust cybersecurity strategy helps organizations build trust with customers and other stakeholders, protect critical assets, and ensure compliance with all applicable laws and regulations.

It is also important that companies establish robust data governance strategies and policies. Transparent AI development and use are critical. As AI becomes more advanced and integrated into various business processes, it raises ethical concerns around fairness, accountability, transparency, and privacy. Responsible AI development and deployment should prioritize the principles of fairness (avoiding bias), accountability (ensuring explainability), and privacy (protecting user data). Companies must implement ethical technology governance and comprehensive data governance with compliance mechanisms that consider the social implications of technological implementation in business. It is also important that companies implement risk management strategies for technologies that they use.

Boston Consulting Group identifies the following responsible AI principles that companies need to embrace and cover in their AI and technology strategy:

- Accountability
- Fairness and equity
- Data and privacy governance
- Social and environmental impact
- Safety, security, and robustness
- Transparency and explainability

Implementation of Industry 4.0

The implementation of Industry 4.0 principles presents tremendous strategic opportunities for companies. Using Industry 4.0 technologies can drive operational efficiency and increase productivity. Embedding sophisticated sensors in machinery to monitor the health of production assets enables preventive maintenance and significantly reduces operational downtime (predictive maintenance). Automation and robotics reduce labor costs and increase productivity. For firms, it is critical to understand the implications of automation and robotics. According to the U.S. Bureau of Labor statistics and consulting firm McKinsey, up to 40 percent of current jobs will disappear by 2030. Companies need to understand the transformation of industries and business models, declining

and growing job families, and the new skill sets and new ways to organize work that are necessary. Against common belief, automation and robotics are not issues that only affect unskilled work. There are well-qualified job categories that are impacted by the potential to automate work.

Technology-Enabled New Business Models and Enhanced Customer Experience

Technologies enable disruptive and enhanced business models. For example, technology is at the core of how Uber disrupted the taxi market and how Airbnb disrupted the hotel market. E-commerce and platform-based business solutions provide new approaches to meeting and exceeding customer needs. Microsoft's shift to cloud computing with Azure has transformed its business model and revenue streams significantly. The same is true for Amazon Web Services (AWS), which currently generate more net profit than the traditional Amazon e-commerce business.

Amazon also uses AI to enhance its recommendation algorithms, improving customer satisfaction and increasing sales. Hence, there are a variety of opportunities for using technology like AI to enhance customer experience and customer engagement in support of gaining a sustainable competitive advantage.

Another example of using new technologies to enhance customer experience is Netflix's use of data analytics to monitor viewer preferences and optimize content production. In the finance industry, Goldman Sachs uses sophisticated algorithmic AI approaches and machine learning for their risk assessment, automated trading strategies, and personalized investment recommendations.

Technology as a Strategic Resource

As you now know, strategy is the quest to create a sustainable competitive advantage. Any firm that can use technology as a means of competitive differentiation has a strategic resource that they may capitalize upon to build strategic capabilities and turn them into core competencies that meet all criteria of a VRIO analysis (valuable, rare, inimitable, and organized to capture value). Firms that use technology to gain technological differentiation, technology-enabled innovation, and product development are especially well positioned for success.

Digital Transformation Framework and Architecture

As you now know, it is critical that a firm has resources, capabilities, and core competencies that can provide a sustainable competitive advantage. The technologies reviewed here are potential candidates for these strategic resources. Every company needs to invest in digital transformation to enable the use of technology as a competitive advantage. This digital transformation investment includes talent and capability development with the upskilling and reskilling of employees, treating knowledge workers as a strategic resource, and investing in the technological infrastructure. Creating AI and technology literacy throughout the whole organization through workforce development becomes a strategic differentiator, making human resources a critical factor. The firm needs to develop a comprehensive roadmap for digital capabilities and create a flexible corporate infrastructure that supports rapid technological adaptation and the ability to design and scale technology in support of profitable growth.

Creating an Agile Organization

In times of continuous technological disruptions, traditional organizational structures with hierarchical levels and functional and organizational silos are no longer appropriate. Companies must design organizational structures and key processes in support of technological and strategic business agility. This allows organizations to respond swiftly to a quickly evolving and changing environment that is characterized by disruptive and continuous change. Companies need to build agile paradigms into their strategies and organizational capabilities. This includes the ability to continuously adapt strategy. The former approach of developing strat-

egy and then just focusing on implementation for the next five to ten years is no longer a successful approach to strategy. It is a strategic imperative for successful organizations to employ continuous strategy adoption mechanisms backed up by real-time performance management.

Application

- Research a company that focuses on technology.
 - Describe the company's technology strategy.
- Research a company that uses technology to accomplish its mission.
 - Describe how the company uses technology as an enabler of other strategy.
- Discuss the differences between technology as a strategy and as an enabler of strategy.

Key Takeaways

Technology can be either a strategy or an enabler of strategy. As a strategy, one focus is on how technology strategies co-evolve along with the emergence of new technology systems. As an enabler of strategy, the more extensive the adoption of new digital technology, the larger the change in strategy. A few relevant intersections where technology and strategy interface and where technology can create value and drive competitive differentiation include data governance and the responsible use of AI, implementation of Industry 4.0, technology-enabled new business models and enhanced customer experience, technology as a strategic resource, digital transformation framework and architecture, and the creation of an agile organization.

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11.6 Analyze Technology Strategy

When you conduct a case analysis, you analyze a firm's technology strategy. This is step six in the case analysis process.

6. As appropriate to the case, analyze strategies: Corporate-level, business-level, innovation, sustainability and ethics, technology, and multinational strategies.

- a. Use strategic management analytical frameworks to analyze, interpret, and evaluate strategies.
- b. Ensure line of sight and congruence within analysis of each strategy.

11.7 Why Technology Strategy Is Important to Business Graduates

As you now see, technology strategy may be both a strategy and an enabler of strategy. As a recent business graduate starting as a business support unit manager in support business units in a large company (such as an accounting manager), you are directly impacted by all uses of technology. You may also be asked to support strategic business managers in formulating technology strategy (such as data governance, the responsible use of AI, or how to use Industry 4.0 technologies to drive operational efficiency and increase productivity).

Business graduates that enter either internal or external consulting roles require a high level of competence with technology strategy to communicate with business executives how their consulting projects fit into the overall technology strategy of the firm. For example, you may be asked to consult on how to create a more agile organizational culture to capitalize quickly on new and emerging technologies. For business graduates who are or will become entrepreneurs, fluency with technology strategy is essential to establishing and growing a successful firm. How will you invest in digital transformation to enable the use of technology as a competitive advantage?

11.8 Conclusion

In the current era of technological disruption and digital transformation, technology and strategy are closely linked and interconnected. Technology is crucial in building competitive, agile, and resilient organizations. It is integral to strategic success by allowing companies to leverage data analytics and compete more effectively. Technology is shaping business strategy by driving competitive differentiation, enabling innovative and disruptive business models, opening new markets, improving efficiency and productivity, and fundamentally changing the way businesses operate. It is important to align technology with core business objectives, focusing on customer needs, fostering innovation, and ensuring security. With the strategic opportunities that new technologies present, companies also need to address possible risks through robust data governance, cybersecurity strategies, and policies regarding the responsible use of AI. Emerging technologies such as quantum computing will continue to shape strategy. Companies must continuously balance and evaluate opportunities and risks, making it essential for companies to stay vigilant, adaptable, and forward-looking in their strategic approach to technology as a driver of long-term success.

Demonstrate Your Knowledge, Skills, and Competence

Use these questions to test your knowledge of the chapter:

1. Describe technology strategy and its relationship to business-level strategy.
2. Discuss disruptive technologies, and give examples.
3. Describe Industry 1.0 to 4.0, and discuss the current impact of Industry 4.0 on business.
4. Discuss new and emerging technologies and their strategic implications.
5. Discuss how technology can be either a strategy or an enabler of strategy.
6. Describe how competence with technology strategy is relevant and important to you.

By answering these questions robustly, you have demonstrated your thorough knowledge technology strategy. Well done!

Figure Descriptions

[Figure 11.1](#): Twelve disruptive technologies: (1) renewable energy, (2) mobile internet, (3) automation of knowledge work, (4) internet of things, (5) cloud technology, (6) advanced robotics, (7) autonomous and near-autonomous vehicles, (8) next-generation genomics, (9) energy storage, (10) 3D printing, (11) advanced materials, (12) advanced oil and gas exploration and recovery. This graphic is purple.

[Figure 11.2](#): Industry 1.0 (1784): mechanization, steam power, weaving loom. Industry 2.0 (1870): mass production, assembly line, electrical energy. Industry 3.0 (1969): automation, computers, electronics. Industry 4.0 (today): cyber physical systems, internet of things, networks. This graphic is purple.

[Figure 11.3](#): Industry 4.0 includes 3D printing, internet of things, artificial intelligence, big data analytics, cloud computing, augmented reality, and mobile devices. This graphic is purple.

Figure References

Figure 11.1: Disruptive technologies. Kindred Grey. 2025. CC BY.

Figure 11.2: Evolution from Industry 1.0 to Industry 4.0. Kindred Grey. 2025. CC BY.

Figure 11.3: Disruptive Industry 4.0 technologies. Kindred Grey. 2025. CC BY. Includes the following icons from the Noun Project ([Noun Project license](#)): Virtual reality (krisna arga muria, 2024, <https://thenounproject.com/icon/virtual-reality-7432738>), AI (Ketileng Design, 2024, <https://thenounproject.com/icon/ai-7464800>), data (Najwa Himma, 2024, <https://thenounproject.com/icon/data-7553891>), cloud (Ecem Afacan, 2015, <https://thenounproject.com/icon/cloud-165891>), internet of things (MUHAMMAT SUKIRMAN, 2024, <https://thenounproject.com/icon/internet-of-things-7552002>), cell phone (Dong Gyu Yang, 2024, <https://thenounproject.com/icon/cell-phone-6835678>), and 3D printing (miftakhudin, 2024, <https://thenounproject.com/icon/3d-printing-7223752>)

Figure 11.4: Amazon. AMAZON. 2020. Public domain. https://commons.wikimedia.org/wiki/File:Amazon_PNG6.png

Figure 11.5: Kroger is an example of a company using AI to improve customer experience. Ambrosia LaFluer. 2019. CC BY 2.0. https://commons.wikimedia.org/wiki/File:Kroger_Pharmacy_-_Shepherdsville,_KY_%2850980791912%29.jpg

12. FORMULATE MULTINATIONAL STRATEGY

Learning Objectives

After engaging with this chapter, you will understand and be able to apply the following concepts.

1. The motivations for going global
2. The risks of going global
3. Theories of multinational business
4. The CAGE distance framework
5. The integration responsiveness framework
6. Methods of entry available to firms that seek to compete in international markets
7. Why multinational strategy is important to business graduates

You will be equipped to analyze a firm's

1. Opportunities and threats in different global markets using the CAGE distance framework analysis instrument
2. Corporate multinational strategy using the integration-responsiveness framework

12.1 Introduction

You have learned about the innovation, sustainability and ethics, and technology strategies embedded in business-level strategy at the strategic business unit level of a firm. Successful companies address each of these areas.

In this chapter, you learn about the next embedded strategy: multinational strategy. This involves a review of the history of global commerce. You learn the motivations and risks associated with choosing a multinational strategy. Next you learn key theories of multinational business. Then you learn a framework for analyzing the attractiveness of foreign markets, the CAGE distance framework, which assesses foreign markets along four dimensions: cultural, administrative, geographical, and economic. The chapter explains how to use the CAGE distance framework analysis instrument to analyze the attractiveness of proposed foreign markets.

Next you learn a framework for types of multinational strategy, the integration-responsiveness framework. This framework analyzes multinational strategy along two dimensions, whether the strategy is responsive to global integration pressures and whether the strategy is responsive to local pressures. An international strategy combines a low responsiveness to global integration pressures with a low responsiveness to local preferences. A multidomestic strategy combines a low responsiveness to global integration pressures with a high responsiveness to local preferences. A global strategy combines a high responsiveness to global integration pressures with a low responsiveness to local preferences. A transnational strategy combines a high responsiveness to global integration pressures with a high responsiveness to local pressures.

Then you learn about a firm's choices when entering foreign markets, as well as issues and strategies related to exporting, licensing and franchising, joint ventures, strategic alliances, wholly owned subsidiaries, and foreign direct investment. Finally, you learn how to analyze multinational strategy when you conduct a case analysis.

12.2 Multinational Strategy

Like all strategy formulation, multinational strategy answers the question “Where are we going?” Multinational strategy addresses where a firm is going as it relates specifically to its commerce in foreign markets.

Like innovation, sustainability and ethics, and technology strategy, multinational strategy is formulated at the strategic business unit level of a company and embedded in business-level strategy. It addresses how a firm is going to win or compete in its chosen markets and market segments.

A **multinational corporation (MNC)** is a firm that has operations in more than one country. Not all companies compete internationally. Multinational corporations formulate multinational strategy. **Multinational strategy** focuses on the ways multinational corporations compete in global markets.

Like all strategy, multinational strategy focuses on an outside-in perspective. Companies carefully monitor their external environments, analyze trends, and formulate strategies that are forward-looking. Robust multinational strategy considers the volatile, uncertain, complex, and ambiguous nature of the firm's external environment.

Multinational strategy is a critical component of a company's strategy. Multinational strategy focuses on expanding operations beyond domestic markets to drive profitable growth and manage risks effectively. This approach involves strategic decision-making about how best to enter and compete in foreign markets, whether and to what degree to adapt products or services to local consumer preferences and cost pressures, and how to manage multinational risks and secure competitive advantage on a global scale. By pursuing multinational strategy, companies can tap into larger consumer bases; distribute risk across diverse industries, markets, market segments, and businesses; enhance operational efficiencies; and leverage global resources, capabilities, and core competencies. As part of a broader business-level strategy, multinational expansion enables firms to achieve scale, optimize resource allocation, and capitalize on new growth opportunities, all while bolstering their resilience in an increasingly interconnected marketplace.

Application

- Research three multinational corporations in three different market sectors.
 - Describe their product lines.

Key Takeaways

Multinational strategy addresses where a firm is going as it relates specifically to its commerce in foreign markets. Like innovation, sustainability and ethics, and technology strategy, multinational strategy is another strategy focus that is formulated at the strategic business unit level of a company and embedded in business-level strategy. A multinational corporation (MNC) is a firm that has operations in more than one country. Not all companies compete internationally. Multinational corporations formulate multinational strategy. Multinational strategy focuses on the ways multinational corporations compete in global markets.

12.3 The History of Global Commerce

The evolution of multinational strategy has followed significant historical events that shaped global commerce. The Silk Road facilitated early trade between Asia and Europe. Prior to European contact, many indigenous nations, such as First Nations in the Americas, had elaborate federations and complex trade agreements (Blackhawk, 2023). Colonialization has rightly come under serious critical scrutiny for its impacts on indigenous populations. European colonial expansions of the sixteenth and seventeenth centuries laid the groundwork for modern multinational trade. In the twentieth century, multilateral institutions like the World Trade Organization (WTO) and economic blocs such as the European Union played pivotal roles in reducing trade barriers and promoting cross-border trade. Trade agreements, such as the North America Trade Agreement, support trade between countries, while trade tariffs, such as those between the U.S. and China, can discourage or limit commerce across borders.

Today, technological advancements, improved communication, and the rise of free trade agreements have created a more interconnected global economy, offering companies diverse opportunities for strategic multinational expansion and the ability for some companies to be “born global” at their founding. Globalization provides companies with unprecedented strategic opportunities, including access to new industries, markets, market segments, and businesses. Multinational firms gain economies of scale and the advantage of being able to source talent globally.

However, globalization also poses challenges that require careful planning. Multinational businesses must manage cultural differences, mitigate political risks, and handle the complexities of global supply chains. The COVID-19 pandemic exposed the vulnerabilities of international supply chains, but it also underscored the importance of agility and innovation in multinational strategy, which must be able to adapt quickly to changing circumstances.

One example of successful international strategy is the German mobility startup Tier Mobility. Originally focused on micromobility solutions in its home market, Tier expanded its operations across Europe, capitalizing on the increasing demand for sustainable urban transport solutions. By 2023, Tier had expanded into new cities such as Oslo and Rome, offering electric scooters and bicycles. Tier’s multinational strategy involved building strong relationships with local municipalities and tailoring its offerings to fit specific urban needs, including adapting to different regulatory environments. This tailored approach helped Tier successfully navigate the complexities of international expansion, grow its brand, and enhance city partnerships for sustainable transportation solutions.

Another recent example is the case of Swedish oat milk producer Oatly. Oatly strategically expanded from Europe into North America, recognizing a shift in consumer preferences toward plant-based dairy alternatives. The company’s multinational strategy is built on its ability to convey a clear message about sustainability, climate change, and healthy lifestyle choices. By focusing on these attributes and partnering with notable coffee chains such as Starbucks, Oatly expanded its market presence in the United States and Canada. By 2023, Oatly had not only increased its market share but had also successfully navigated distribution challenges by

setting up local manufacturing facilities and minimizing the logistical issues and tariffs that often arise with international shipments.

These examples illustrate the importance of understanding local market dynamics, aligning products with consumer trends, and forming strategic partnerships as part of an effective multinational strategy. Success lies in being agile and building robust relationships, which are key factors for any company aiming to thrive on the international stage.

Key Takeaways

The evolution of multinational strategy has followed significant historical events that shaped global commerce, beginning with the Silk Road that facilitated early trade between Asia and Europe and the elaborate federations and complex trade agreements of many indigenous nations prior to European contact. Today's trade agreements support trade between countries, and trade tariffs can discourage or limit commerce across borders.

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12.4 Motivations and Risks when Choosing a Multinational Strategy

Companies that choose a multinational strategy share common motivations and also share similar risks.

Motivations for Choosing a Multinational Strategy

Companies pursuing international expansion are often driven by multiple motivations, each tied to enhancing competitiveness, increasing profitability, and positioning themselves strategically within the global market. However, going global comes with its share of complexities and challenges. This section delves into both the motivations behind international expansion and the drawbacks companies face when they decide to operate globally.

Market Seeking

One of the foremost motivations for international expansion is market seeking. Companies often look to expand into new geographic areas to find additional customers, especially when their domestic market is either saturated or shows limited growth potential. By tapping into larger or faster-growing international markets, businesses can significantly increase their revenue streams. For instance, French electric vehicle manufacturer Hopium expanded into the North American market in 2023 to capture the growing demand for electric vehicles in the United States, spurred by favorable government policies and shifting consumer preferences toward green technologies. By gaining a foothold in a lucrative and evolving market, companies like Hopium aim to build stronger brands and secure their shares of new revenue opportunities.

An important driver of finding more robust growth opportunities abroad is the emergence of middle classes in developing countries. Strong population growth in developing countries and emerging middle classes provide untapped growth opportunities that haven't been present in the past, when only a small percentage of the population had enough buying power to purchase consumer products from U.S. global players. For example, in the past, the majority of Indian consumers used bar soap to wash their hair and laundry. Now, hundreds of millions of consumers in India's emerging middle class have the buying power to buy hair shampoo and laundry detergent, which represents huge market opportunities for companies like the U.S. consumer giant Procter & Gamble or Dutch/British consumer giant Unilever. Emerging countries like China, Brazil, India, and Russia have now become growth engines for U.S. companies, and the former BRIC countries (Brazil, Russia, India, China) have now become BRIC+ with the addition of countries like Egypt, Ethiopia, Iran, and the United Arab Emirates.

Resource Seeking

Another major driver for international expansion is resource seeking, which involves accessing cheaper or higher-quality inputs for production. Businesses, particularly those in manufacturing or industries dependent on natural resources, expand internationally to secure better access to raw materials or labor. Finnish renewable energy company Neste, for example, moved into the Asia-Pacific region in 2022 to secure sustainable feedstocks for renewable diesel production. By situating closer to essential resource bases, Neste aimed to reduce logistical costs and ensure a consistent supply, providing a competitive edge in the renewable energy market.

Efficiency Seeking

Efficiency seeking is also a core motivation for internationalization, where companies expand to improve their operational efficiency and profitability. This typically involves leveraging economies of scale or shifting certain operations to regions where costs are lower.

Asset Seeking

Strategic asset seeking is another important motivator, driving companies to pursue international expansion to acquire knowledge, technology, or unique resources, capabilities, and core competencies that are critical for growth. This often involves forming partnerships or acquiring firms with advanced technological assets or market expertise. South Korean conglomerate SK Group, for example, expanded into the U.S. market by acquiring stakes in American battery technology firms, positioning itself favorably within the growing electric vehicle industry. By accessing cutting-edge battery technology through strategic partnerships, SK Group aimed to secure its place at the forefront of a rapidly changing market.

While international expansion offers opportunities for market growth, access to resources, operational efficiencies, and strategic assets, it also involves significant risks that require careful planning and strategic management to avoid and mitigate.

Risks of Choosing a Multinational Strategy

Companies must weigh the potential benefits of choosing a multinational strategy against the potential challenges, such as complex regulations, economic instability, supply chain vulnerabilities, cultural differences, and the need for brand consistency. A successful multinational strategy involves not only leveraging the motivations that drive expansion but also anticipating the challenges that come with entering diverse global markets.

Expanding internationally brings a variety of risks that companies must understand and mitigate to ensure success. While international markets offer opportunities for growth, cost savings, and strategic positioning, they also expose businesses to diverse and often unpredictable risks. Some of the risks that accompany international business operations include political risk, economic risk, operational risk, cultural risk, legal and regulatory risk, competitive risk, financial risk, and reputational risks.

Political Risk

One of the most prominent international risks is political risk, which arises from the uncertainty of government actions in foreign countries. Political risk can include sudden changes in government policies, the nationalization of industries, civil unrest, or unexpected changes in trade regulations. These factors can significantly affect a company's ability to operate effectively. For instance, in 2022, dozens of Western companies faced difficulties in Russia due to increased government scrutiny and economic sanctions, leading some to halt operations or exit the market entirely. Such political dynamics can disrupt operations and create unexpected costs, making it critical for companies to assess the political climate before investing heavily in a foreign market.

Economic Risk

Economic risk is another significant consideration for companies operating internationally. Exchange rate fluctuations can have a major impact on profitability, especially when earnings from foreign operations need to be repatriated. Sudden currency devaluations can erode profit margins, while currency appreciation in a company's home country can make its exports less competitive. The recent volatility in the Turkish lira, for instance, has had a profound impact on foreign businesses operating in Türkiye, leading to increased costs and challenges in managing price stability. Additionally, inflation rates, interest rates, and overall economic stability in the target market can affect consumer purchasing power and the overall business environment.

Operational Risk

Operational risk also plays a significant role in international expansion. These risks include logistical challenges, supply chain vulnerabilities, and difficulties in maintaining consistent quality standards across borders. Global supply chains are vulnerable to various disruptions, such as natural disasters, strikes, or changes in trade agreements. The COVID-19 pandemic exemplified the impact of such disruptions, with companies experiencing significant delays and increased costs as global supply chains were interrupted.

Companies need to build resilient supply chains by diversifying suppliers and creating contingency plans to mitigate these operational risks. Firms must also acknowledge that managing and coordinating international businesses in various countries increases costs and the complexity of a business.

Cultural Risk

Cultural risk is another aspect that can directly affect the success of an international strategy. Differences in consumer behavior, language, business practices, and societal values require careful consideration. Failure to understand these cultural dynamics can lead to marketing blunders, poor customer engagement, or even reputational damage. For instance, some fast-food companies have faced backlash in certain regions when their advertising or product offerings did not align with local cultural norms and expectations, such as promoting beef products in predominantly vegetarian countries or using advertising themes that conflict with local values. Another example is Walmart's failed market entry into the German retail market. Walmart almost lost a billion dollars as a result of not fully understanding very different German consumer shopping habits. These missteps highlight the importance of tailoring products and messaging to resonate with diverse cultural contexts, ensuring a more successful international strategy. Successfully mitigating cultural risks requires in-depth market research, cultural sensitivity training, and often local talent who can provide valuable insights into consumer preferences and behaviors.

Legal and Regulatory Risk

Legal and regulatory risk also poses a challenge when operating in multiple jurisdictions. Each country has its own set of laws and regulations related to labor, environmental standards, taxation, and data privacy, which can be complex and costly to navigate. Companies need to comply with these laws and regulations to avoid fines, legal disputes, and reputational harm. For instance, the European Union's General Data Protection Regulation (GDPR) has strict requirements regarding the collection, use, and storage of consumer data, impacting how companies do business in Europe. Legal compliance is a matter of not only adhering to laws but also ensuring that operations align with evolving regulatory landscapes across different markets. Another risk is the difficulty of protecting intellectual property in some countries, especially when the company enters a partnership, like a joint venture, with local partners. Lastly, tariffs and other trade barriers may change, leading to a loss of profit and market access.

Competitive Risk

Competitive risk arises from the uncertainty of entering new markets where existing players may have a substantial advantage. Local competitors often have a deeper understanding of the market, established customer relationships, and more agile responses to changes in the local environment. This can create challenges for new entrants who are still learning to navigate the complexities of a foreign market. For instance, many Western e-commerce companies have struggled to compete in China, where local giants like Alibaba and JD.com dominate the market through their local brand image, extensive logistics networks, and consumer loyalty programs.

Financial Risk

Financial risk is another crucial factor to consider, especially when dealing with markets that have limited access to financing or higher capital costs. Businesses may face challenges in accessing affordable funding to support their international operations, or they may encounter higher interest rates, making investments more costly. Moreover, inconsistent cash flows due to delayed payments from international customers can pose liquidity challenges. Companies expanding into emerging markets must particularly assess the financial stability of the market and the availability of credit to ensure they can effectively fund their operations.

Reputational Risk

Lastly, reputational risk can arise from operating in multiple regions, where different standards and expectations may lead to perceptions of unfair practices. International businesses are increasingly scrutinized for their impact on the environment, working conditions, and the ethics of their business practices. A misstep in any of these areas can lead to significant backlash and harm to a company's global reputation. For example, clothing brands have faced criticism for poor working conditions in overseas factories, leading to protests, boycotts, and long-term damage to their brand images. As a response to this risk, many companies implement robust environmental, social, and governance strategies that are covered in greater detail in [section 10.7](#).

The risks of operating internationally are interrelated. For example, Nestle has faced economic, cultural, and reputational risks from claims of selling substandard products in low-income countries like India due to rising costs in their supply chain. Nestle has also been slow to respond to consumer preferences for more sustainable packaging. They are now addressing their packaging and receiving a positive consumer response.

Application

- Consider one of the three multinational corporations you researched above.
 - Discuss how market seeking, resource seeking, efficiency seeking, and asset seeking may have been motivators for the MNC to enter global markets.
 - Describe the ways political, economic, operational, cultural, legal and regulatory, competitive, financial, and reputational risks may have been affected the MNC when entering global markets.

Key Takeaways

Seeking new markets, resources, efficiencies, and assets are among the motivations for companies to pursue multinational expansion. All are aimed at enhancing competitiveness, increasing profitability, and positioning the firm strategically within the global market. However, going global comes with its share of complexities and challenges. Some of the risks that accompany international business operations include political risks, economic risks, operational risks, cultural risks, legal and regulatory risks, competitive risks, financial risks, and reputational risks. Successful international expansion involves not just seizing opportunities but also anticipating and addressing the potential risks that come with operating in diverse and dynamic environments.

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12.5 Theories of Multinational Business

Theories exploring multinational business provide essential insights into why companies expand across borders, how they select foreign markets, and the strategies they employ for success. These theories help shape the decisions that businesses make as they navigate the complexities of international markets.

Comparative Advantage Theory

Comparative advantage theory (Ricardo, 2004a; Ricardo, 2004b) is one of the oldest and most fundamental theories that explains international trade and business. The theory posits that countries should specialize in the production of goods where they have a lower **opportunity cost** relative to other nations. This specialization allows countries to benefit from trade by producing what they

make most efficiently and trading for what they are less efficient at making. This theory has formed the basis of modern trade policies, explaining why nations and businesses trade in goods and services that maximize their efficiency and productivity. For companies, understanding comparative advantage is crucial when deciding which products or services to produce domestically and which to outsource or import, thereby allowing them to optimize costs and competitiveness. For example, Brazil specializes in coffee due to its climate and the U.S. in machinery due to its advanced technologies. By trading, both benefit in terms of efficiency and cost savings.

OLI Paradigm

The OLI paradigm, also known as the eclectic paradigm (Dunning, 1977), is a comprehensive framework that explains why firms choose to engage in foreign direct investment (FDI) rather than licensing or exporting. OLI stands for ownership, location, and internalization. Ownership advantages refer to unique resources, capabilities, and core competencies that a company possesses, such as technology, brand reputation, or proprietary knowledge, which give it a competitive edge in foreign markets. A firm's resources, capabilities, and core competencies are analyzed using a VRIO framework, a tool that helps evaluate the "ownership" element of the OLI paradigm. Location advantages pertain to the attractiveness of a foreign market, which may include lower labor costs, favorable regulations, or access to natural resources. Internalization advantages focus on the benefits of maintaining control over operations rather than licensing out technology or the brand. The OLI paradigm thus offers a holistic perspective on why firms decide to establish a physical presence in foreign markets, helping guide decisions on selecting the most appropriate multinational strategy.

Uppsala Model

The Uppsala model of internationalization (Johanson & Vahlne, 2017) provides a gradual, staged approach to multinational expansion. Developed by Swedish researchers, this model suggests that companies begin by entering markets that are culturally and geographically close to their home countries, thereby reducing the uncertainties and risks associated with foreign markets. As firms gain experience and learn from their initial ventures, they expand into markets that are more distant and dissimilar. The Uppsala model emphasizes learning and experiential knowledge, suggesting that firms develop their multinational strategy incrementally, based on the level of knowledge they accumulate over time. It explains the cautious approach often seen in international business, where companies prefer to move step-by-step, increasing their market commitment progressively as they become more confident in their understanding of foreign environments. The CAGE framework discussed in [section 12.6](#) is a useful tool that assesses the cultural (C) and geographical (G) distance between the home country and target foreign markets; it also assesses the administrative (A) and the economic (E) distance.

Porter's Diamond Model of National Competitive Advantage

Porter's Diamond Model of National Competitive Advantage (O'Connell, Clancy, & van Egeraat, 1999; Porter, 1991; van den Bosch, van Prooijen, & Porter, 1992) provides an explanation for why certain industries within specific countries are more internationally competitive than others. Michael Porter identified four key factors that provide a competitive advantage for one national economy or business over another. These factors interact to create favorable environments that support the development of competitive industries in international markets. These same factors also influence whether a firm chooses a cost leadership or differentiation business-level strategy. This demonstrates the interconnectedness of business-level strategies and the strategies embedded into them.

The focus of Porter's Diamond Model is on the industry. The ability of the firms in an industry to be successful in global business is shaped by four factors: (1) factors of production, (2) consumer demand, (3) strategy, structure, and rivalry, and (4) related and supporting industries.

Factors of Production

Factors of production refers to the nature of the resources that firms need to create goods and services in an industry in their home country. Examples include labor, capital markets, and land. Businesses with good access to factors of production are more likely to be successful, and they face challenges when they lack this access. Understanding the factors of production an industry needs and has access to in the home country allows a company to assess the factors of production in foreign markets and make strategic decisions about potential global markets to consider for expansion. For example, India has a large, educated workforce with a high level of English proficiency. When a company understands that the industry needs a workforce like that in India, expanding into India may be a smart option.

Factors of production, such as labor, land, capital, and infrastructure, play a critical role in shaping a company's multinational strategy. The availability and quality of these resources in a target country also influences whether a company pursues a cost leadership or differentiation strategy, which is part of its business-level strategy. Determining a firm's strategic market position is based on the characteristics of the target market and market segments. For example, if a country offers low-cost labor, a multinational strategy that focuses on cost leadership strategy may align with target markets or market segments seeking affordability, as companies may be able to remain profitable while paying locally competitive wages. Conversely, if a country has a highly skilled workforce and advanced infrastructure, companies may choose a multinational strategy that focuses on differentiation strategy to create unique products or services that appeal to consumers willing to pay a premium for innovation and quality. Additionally, access to natural resources, supportive governmental laws, regulations and policies, or efficient logistics networks can influence how companies position themselves to meet specific market demands, shaping their competitive approach in each international setting.

Consumer Demand

Consumer demand refers to the nature of domestic customers. Industries in home countries that have demanding consumers produce higher-quality products domestically and are better positioned to compete internationally. For example, Japanese customers demand high-quality, aesthetically pleasing, and reliable vehicles. Japanese automakers produce automobiles in Japan that meet these high customer demands, and this increases their success in foreign markets. Unlike Japanese customers, French customers of automobiles have low demands, and as a result, the reputation of French automobiles is low, and they do not sell well in foreign markets.

Consumer demand is another critical aspect in determining multinational strategy. Companies must understand the nature of consumer demand in each international market to tailor their offerings effectively. For example, emerging markets with large populations and growing middle-class populations often present opportunities for a multinational strategy that includes a cost leadership strategy focused on affordability. On the other hand, sophisticated and demanding consumers can drive companies to innovate and develop high-quality products, pushing them toward a differentiation strategy. Understanding local demand conditions is essential for companies to align their products and services with consumer expectations and gain competitive edge in international markets.

Strategy, Structure, and Rivalry

Together, strategy, structure, and rivalry refer to how challenging it is to survive domestic competition. When an industry in a home country has intense rivalry, competition drives quality up and creates a domestic industry of competing high-quality products. Producing high-quality products domestically increases the likelihood the industry will be successful in international markets.

Strategy, structure, and rivalry also play a crucial role in determining how businesses compete internationally. In highly competitive markets, companies need to develop distinctive strategic approaches to succeed. When entering markets with intense local competition, companies may have to adopt innovative practices or find unique ways to differentiate themselves to appeal to consumers. Conversely, in markets with limited local rivalry, firms might find opportunities to achieve cost leadership more easily due to

reduced pressure on price competition. The strategic decisions that firms make regarding market positioning, investments, and value propositions are often influenced by the competitive dynamics of each international market.

Related and Supporting Industries

It is common for an industry to rely on related and supporting industries to make products and services for use in its own business. For example, Italians are known for high quality leather goods. Access to an extensive and high-quality leather production industry is essential to the high-end leather goods industry. Being reliant on an industry with few or low-quality products puts an industry at risk. An extensive supporting industry gives an industry more choices when events influence the supporting industry, and it increases competition within the supporting industry to ensure high-quality goods.

The presence of related and supporting industries also influences a company's business-level strategy in international contexts. When a country has strong supporting industries, such as suppliers, distributors, or specialized service providers, companies can leverage these relationships to enhance efficiency or product quality. This interconnectedness often results in more innovation and efficiency, providing companies with competitive advantages. For example, the automotive industry in Germany benefits significantly from a strong network of supporting industries, including engineering firms, component manufacturers, and R&D institutions. Companies that expand into such environments can use the advanced capabilities of these related industries to support their differentiation strategies by offering superior products or processes. In contrast, when related industries are underdeveloped, companies may opt for a simpler cost leadership strategy due to limited support for advanced innovation or premium offerings.

To be successful at the business level, companies expanding internationally must consider how these factors of production; demand conditions; firm strategy, structure, and rivalry; and related and supporting industries shape the opportunities and constraints of each market. By aligning their business-level strategy with these foundational elements, companies can better position themselves to meet local market needs, capitalize on competitive advantages, and achieve sustainable success in international operations.

Porter's Diamond Model helps explain why some nations have clusters of highly competitive industries, such as Germany's automotive sector or Silicon Valley's tech industry in the United States, providing insights into the strategic advantages companies may gain from operating within these clusters. These elements directly influence how companies craft and implement their strategies to achieve competitive advantage in foreign markets.

Together, these theories (among many others) offer a framework for understanding the motivations behind international business and provide a roadmap for companies seeking to expand across borders. By understanding and applying these theories, companies can make informed decisions about market selection, entry strategies, and how to compete effectively in the global landscape. Each theory offers a unique perspective that helps businesses navigate the opportunities and challenges of operating internationally, whether through focusing on efficiency, leveraging unique capabilities, learning through gradual expansion, or capitalizing on national competitive advantages.

Key Takeaways

Theories of international business offer essential insights into why companies expand globally, how they select markets, and which strategies they adopt. Key frameworks include comparative advantage, which highlights specialization for efficiency; the OLI paradigm, which guides firms in leveraging unique assets through foreign direct investment; the Uppsala model, emphasizing gradual expansion to manage risk; and Porter's Diamond Model, which explains national industry competitiveness and requires a careful assessment of factors such as production resources, demand conditions, competitive dynamics, and supporting industries. Each element influences

whether a company pursues cost leadership or differentiation strategy in foreign markets. High-quality labor and infrastructure often lead to differentiation strategies, while cost leadership may suit markets with low-cost labor. Demand conditions shape strategy based on local consumer preferences, and the presence of strong supporting industries can enhance efficiency and innovation. By aligning their business strategies with these factors, companies can tailor their competitive approaches to succeed in varied international environments. Together, these theories provide a strategic foundation for navigating the complexities of international markets, helping businesses make informed decisions about where and how to compete effectively.

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12.6 CAGE Distance Framework

The CAGE distance framework (Chemawat, 2001) is a tool for companies evaluating international opportunities and understanding the challenges involved in entering new global markets. Developed by Pankaj Chemawat, it helps a company analyze the cultural, administrative, geographic, and economic distances between its home country and target foreign markets. This requires a thorough understanding of the home country as well the target countries, calling for extensive research.

These dimensions represent potential barriers to international expansion that can impact product acceptance, operational efficiency, and overall market success. By assessing these factors, companies can make informed decisions about which markets to enter, how to adapt their strategies, and what entry modes are most appropriate.

As you now know, the Porter's Diamond Model of National Competitive Advantage focuses on the industry. The CAGE distance framework focuses on countries.

Cultural Distance

Cultural distance refers to differences in language, values, social norms, and consumer behavior between countries. Cultural differences can impact how products and services are perceived, the effectiveness of marketing messages, and the way businesses interact with customers and stakeholders. For instance, advertising campaigns that resonate in one country may not be suitable in another due to differing values and traditions. A strong understanding of cultural preferences allows companies to tailor their approaches to meet the expectations of each market, ensuring that their branding and customer interactions are culturally sensitive and effective.

Administrative Distance

Administrative distance involves differences in laws, regulations, governance, and political institutions that can create challenges for businesses entering foreign markets. This can include variations in legal systems, trade policies, tariffs, and regulatory requirements. Trade and tariff policies can both help and hinder the growth of MNCs. When there are changes in these policies, business and financial markets are disrupted. Companies may consider onshoring businesses or business operations that have been offshored. Immigration policies and enforcement can also have an influence on businesses and the economy, potentially disrupting labor markets.

Administrative differences significantly impact the ease of doing business, as firms must comply with distinct legal and bureaucratic procedures. For example, highly regulated markets may present barriers such as licensing requirements or ownership restrictions that complicate expansion plans. Companies must navigate these administrative differences effectively and adjust their strategies to comply with local laws and regulations while fostering positive relationships with local authorities.

Geographic Distance

Geographic distance considers not only the physical distance between the home country and the target market but also factors such as transportation infrastructure, time zones, and accessibility. Geographic distance can affect logistics, supply chain management, and the overall cost of moving goods and services across borders. Companies expanding into distant markets often face increased transportation costs, longer lead times, and challenges in managing the flow of goods and services. To succeed in geographically distant markets, businesses need robust supply chain strategies that can handle the complexities associated with longer shipping routes and potential logistical disruptions.

Economic Distance

Economic distance focuses on differences in income levels, consumer purchasing power, infrastructure, and overall economic development between countries. Economic distance influences how companies price their products, determine market positioning, and adapt their offerings to meet the needs of target markets. In countries with lower purchasing power, businesses may need to adjust their offerings to include more affordable options or features tailored to better match local needs. Differences in economic infrastructure, such as the availability of financial services or digital connectivity, can also impact a company's ability to operate effectively. A deep understanding of economic distance helps companies identify which segments of the market to target and how to position their products accordingly.

You now understand how portfolio planning and the BGC matrix can be used in corporate-level strategy. MNCs use portfolio planning to make investment and divestment decisions across their portfolios of operations. For example, an MNC may decide to reinvest profits from one country into another country.

Use the CAGE distance framework analysis instrument to analyze the cultural, administrative, geographical, and economic distance between the home country and target foreign markets.

CAGE distance framework analysis instrument

[Download an editable version](#) or [view this resource in Appendix 7](#).

The resource below provides a detailed analysis of the United States as home country and Bangladesh, Ghana, and Brazil as target foreign markets using the CAGE distance framework analysis instrument.

[Download an editable version](#) or [view this resource in Appendix 7](#).

Application

- Use the CAGE distance analysis framework to assess two target foreign markets for potential global expansion. Use the detailed cage analysis for Bangladesh, Ghana, and Brazil as a guide. Choose two different countries to assess.

Key Takeaways

The CAGE distance framework offers a way for businesses to assess potential barriers to international expansion and determine which markets are most viable for entry. By analyzing cultural, administrative, geographic, and economic distances, companies can better understand the risks and challenges associated with each market, enabling them to make informed strategic decisions. This analysis is particularly useful in helping companies determine the level of adaptation required for their offerings and in selecting the most suitable entry modes for each market. The CAGE distance framework analysis instrument analyzes the cultural, administrative, geographical, and economic distance between the home country and target foreign markets.

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12.7 Integration-Responsiveness Framework

Now that a firm has analyzed the opportunities and threats associated with different global markets using a tool such as the CAGE distance framework, it can use this analysis as it continues to formulate its multinational strategy. Careful consideration is necessary, as companies face diverse and conflicting environmental pressures when expanding into foreign markets.

Multinational corporations make two critical strategic decisions when formulating a multinational strategy. The first decision concerns whether the strategy is globally integrated. The second decision concerns whether the strategy is locally responsive. These two strategic decisions are captured in the integration-responsiveness framework shown in figure 12.1.

The first strategic decision addresses whether and to what degree the strategy is responsive to global integration pressures. Global integration pressures include the need to reduce costs through large-scale investments and the presence of global competitors in the firm's target markets. Global integration pressures require firms to manage their business activities on a global basis.

The second strategic decision is whether and to what extent the strategy is responsive to local pressures. Local pressures include diverse governmental structures and differences in customer needs and preferences across countries. Local pressures compel firms to conduct their business activities on a country-by-country basis.

Combining the decisions made along these two dimensions—responsiveness to global integration pressures and responsiveness to local pressures—results in four multinational strategies: international, multidomestic, global, and transnational. An international strategy combines a low responsiveness to global integration pressures with a low responsiveness to local preferences; a multidomestic strategy combines a low responsiveness to global integration pressures with a high responsiveness to local preferences; a global strategy combines a high responsiveness to global integration pressures with a low responsiveness to local preferences; and a transnational strategy combines a high responsiveness to global integration pressures with a high responsiveness to local pressures.

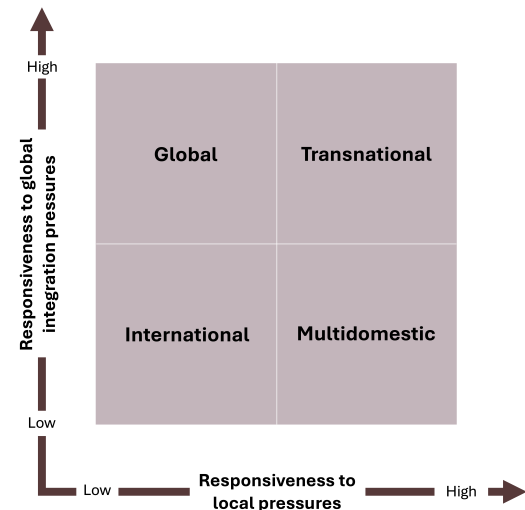


Figure 12.1: Integration-responsiveness framework

International Strategy

An international strategy combines a low responsiveness to global integration pressures with a low responsiveness to local preferences. An international strategy involves expanding into foreign markets with minimal adaptation, relying on products and resources, capabilities, and core competencies developed in the home market to enter new regions with lower risk and investment. An international strategy focuses on leveraging existing resources to reach similar customer segments across borders. This approach is suited for industries where demand for local variation is low, allowing companies to maintain centralized control and achieve cost efficiencies. For example, luxury brands like Rolex use an international strategy by offering a consistent product line and brand experience worldwide, appealing to a global audience with uniform preferences. Red Bull is another brand that follows an international strategy. An Austrian brand, Red Bull is the leading energy drink, with more than \$2 billion in sales every year.



Figure 12.2: Red Bull

Multidomestic Strategy

A **multidomestic strategy** combines a low responsiveness to global integration pressures with a high responsiveness to local preferences. A multidomestic strategy focuses on high local responsiveness by tailoring products, services, and business operations to meet the needs and preferences of each individual market. For example, food and beverage companies like Nestlé employ a multidomestic strategy to adapt their product offerings to local preferences, such as varying flavors and formulations based on regional tastes. Companies that adopt a multidomestic strategy treat each country as a unique market, often allowing local subsidiaries a great deal of autonomy to make decisions that align with the specific consumer expectations of that country. This strategy is particularly suitable for industries where local tastes, cultural preferences, and regulations vary significantly from one market to another. A multidomestic approach allows companies to better serve local customers by adapting their offerings; however, it may lead to higher costs due to the lack of standardized processes and economies of scale. A multidomestic strategy enables companies to closely align with local preferences, though it typically results in higher operational costs due to extensive customization.

Global Strategy

A **global strategy** combines a high responsiveness to global integration pressures with a low responsiveness to local preferences. A global strategy emphasizes high efficiency and the standardization of products and services across all markets. Companies employing this strategy produce and market their offerings in a highly uniform manner, seeking economies of scale and the benefits of a consistent brand image across all countries. By centralizing key functions like research and development, marketing, and production, companies can achieve cost advantages through efficiency and large-scale operations. A global strategy works best for industries where consumer needs and preferences are relatively homogeneous across different countries and where there is a significant cost advantage to producing standardized products. A global strategy achieves cost efficiencies through standardization but may overlook local consumer nuances. For example, technology companies like Apple use a global strategy by offering the same core products worldwide with little variation, ensuring consistency in quality and design while benefiting from the cost efficiencies of mass production.

Transnational Strategy

A **transnational strategy** combines a high responsiveness to global integration pressures with a high responsiveness to local pressures. A transnational strategy focuses on achieving both high local responsiveness and high global integration, representing a balance between the multidomestic and global strategies. Unlike purely multidomestic strategies that prioritize local adaptation or purely global strategies that emphasize standardization, the transnational strategy seeks to combine the best of both. Companies using this approach aim to standardize core operations, such as production, supply chain management, and R&D, to achieve cost efficiencies, while also allowing significant flexibility to adapt products, services, and marketing to local market needs. This dual focus requires careful coordination across diverse locations, enabling the company to respond to specific cultural and consumer preferences without sacrificing operational efficiencies. Although complex to implement, the transnational strategy can offer a competitive advantage by leveraging economies of scale alongside tailored market engagement, as exemplified by Unilever, which standardizes production but customizes product offerings and branding to suit regional tastes. Unfortunately for some, this approach requires a complex organizational structure and substantial coordination to effectively manage both global and local demands, making it challenging to implement successfully. For example, McDonald's has thirty-six thousand locations in more than one hundred different countries, with menu items and prices that change based on the local market.

Each of these multinational strategies offers distinct advantages and challenges depending on the industry, market conditions, and overall business goals. Ultimately, the choice of multinational strategy is influenced by factors such as the degree of variation in consumer needs across markets, the intensity of competition, the nature of the industry, and the company's resources and abilities. Successful multinational companies often align their chosen strategies with their overall competitive advantages, tailoring their approaches to achieve the best balance between global integration and local responsiveness to meet their strategic goals.

Application

- Discuss an example of a product line of a MNC that illustrates each of the four types of multinational strategy: international, multidomestic, global, and transnational. Explain in detail how each is high or low regarding global integration and local responsiveness.

Key Takeaways

Multinational corporations make two critical strategic decisions when formulating a multinational strategy. The first strategic decision concerns responsiveness to global integration pressures, like the need to reduce costs through large-scale investments and the presence of global competitors in the firm's target markets. Global integration pressures require firms to manage their business activities on a global basis. The second strategic decision concerns responsiveness to local pressures, like diverse government regulations and differences in customer needs and preferences across countries. Local pressures compel firms to conduct their business activities on a country-by-country basis. Combining the decisions made along these two dimensions results in four multinational strategies: international (low global responsiveness, low local responsiveness), multidomestic (low global responsiveness, high local responsiveness), global (high global responsiveness, low local responsiveness), and transnational (high global responsiveness, high local responsiveness).

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12.8 Choice of Entry Mode

Choosing the appropriate entry mode is a crucial decision for firms expanding internationally, as it directly influences the level of control, risk, required investment, and overall potential for success. Entry modes vary in terms of risk and commitment, ranging from low-risk, low-investment options to high-risk, high-commitment strategies. Firms with limited resources or a low tolerance for risk may favor modes that require minimal capital and offer lower exposure, such as exporting, while those seeking greater control and long-term presence may opt for more committed approaches, like wholly owned subsidiaries. Common international entry modes, ordered from lowest to highest commitment, include exporting, licensing and franchising, joint ventures, strategic alliances, wholly owned subsidiaries, and foreign direct investment, each offering unique benefits and challenges depending on a firm's strategic goals and market characteristics.

Exporting

Exporting is often the first step for many companies seeking to enter international markets. It involves producing goods domestically and shipping them to foreign markets for sale, allowing companies to expand without investing heavily in foreign facilities. Exporting offers a low-risk way to test the viability of foreign markets and allows companies to retain control over production processes. However, exporting can also lead to increased logistics costs and may expose companies to tariff and nontariff barriers in their target countries. Exporting is suitable for companies with limited international experience or for those wanting to test the waters before making more substantial investments abroad.

Licensing and Franchising

Licensing and franchising are popular entry modes for companies that want to leverage the capabilities of local partners without establishing a direct physical presence. **Licensing** involves granting a foreign entity the rights to use the company's intellectual property, such as technology, patents, or trademarks, in exchange for a fee or royalty. This entry mode allows companies to expand with minimal investment and risk, as the licensee bears the cost of setting up operations in the target market. Similarly, **franchising** allows companies to license their business models, brands, and operational systems to foreign franchisees, who manage and operate the business locally. Franchising is commonly used by service-oriented firms, particularly in the hospitality and food service industries, such as McDonald's and Marriott. While licensing and franchising help companies grow quickly, they often involve a loss of control over the quality of products and services, which can affect brand consistency across different markets.

Joint Venture

A **joint venture** is an entry mode where a company partners with a local firm to establish a new entity in the foreign market. This approach provides both parties with shared ownership, combining the local knowledge and market access of the domestic partner with the foreign firm's expertise and technology. Joint ventures are particularly advantageous in countries with regulatory requirements that mandate local ownership or where navigating cultural and political environments is challenging for foreign firms. A notable advantage of joint ventures is the ability to reduce risk by sharing costs and to benefit from the established relationships of the local partner. However, managing joint ventures can be challenging due to potential conflicts of interest, differences in strategic objectives, and challenges in decision-making.

Strategic Alliances

Strategic alliances represent another entry mode that involves partnering with a foreign firm without forming a separate legal entity. Strategic alliances are often less formal than joint ventures and can include collaborations on specific projects, co-marketing agreements, or joint product development. These alliances allow companies to gain quick access to new markets, share expertise, and distribute costs and risks. For instance, tech companies often form alliances to collaborate on R&D initiatives, allowing both parties to benefit from shared technological advancements. However, strategic alliances may suffer from a lack of clearly defined control, and the success of the partnership often depends on the mutual trust and commitment of both parties.

Wholly Owned Subsidiaries

Wholly owned subsidiaries involve full ownership and control of foreign operations and can be established through either greenfield investments or acquisitions. In a **greenfield investment**, a company builds its operations from scratch in the foreign market, allowing for complete customization and control of the new facility. Alternatively, a firm may acquire an existing local company to gain immediate market access, existing customers, and operational capabilities. Wholly owned subsidiaries provide the highest level of control over international operations, allowing companies to fully integrate their culture, processes, and standards across borders. However, they are also the most resource-intensive and carry significant risk due to the large capital investment required. This entry mode is suitable for firms that prioritize control over their foreign operations and are willing to invest heavily in expanding their international footprints.

Foreign Direct Investment

Foreign direct investment (FDI) is a critical aspect of multinational business strategy, involving the establishment of significant ownership in foreign markets. FDI allows companies to maintain a high level of control over their operations abroad, facilitating deeper market integration and the ability to adapt business strategies to local environments effectively. Unlike other entry modes, such as exporting or licensing, FDI requires a substantial commitment of resources and carries higher risks, including exposure to political, economic, and operational uncertainties. The benefits of FDI include greater access to local knowledge, increased control over production and distribution, and the potential for long-term growth in key international markets. FDI is an essential consideration for companies seeking to establish a robust presence in foreign territories and to leverage local advantages while building a sustainable competitive position.

Application

- Think of the companies you have studied in your business education. Feel free to conduct research if you need to.
 - Discuss one example of a company that has used each of the entry modes to multinational business: exporting, licensing and franchising, joint venture, strategic alliance, wholly owned subsidiaries, foreign direct investment.

Key Takeaways

The choice of entry mode depends on various factors, including the nature of the industry, market potential, risk tolerance, resource availability, and the level of control desired by the firm. Companies must carefully evaluate these factors to determine the entry mode that aligns best with their strategic objectives while balancing risks and investment costs. Each entry mode offers distinct advantages and drawbacks, and choosing the right approach is critical for successful international expansion and long-term growth.

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12.9 Analyze Multinational Strategy

When you conduct a case analysis, you analyze a firm's multinational strategy. This is step six in the case analysis process.

6. As appropriate to the case, analyze strategies: Corporate-level, business-level, innovation, sustainability and ethics, technology, and multinational strategies.

- a. Use strategic management analytical frameworks to analyze, interpret, and evaluate strategies.
- b. Ensure line of sight and congruence within analysis of each strategy.

12.10 Why Multinational Strategy Is Important to Business Graduates

For business graduates starting as business support unit managers in support business units in large multinational companies (such as marketing managers), multinational strategy has a direct influence on the implementation of functional-level strategy. How the company will decide to what degree the company is responsive to global integration pressures and whether and to what extent the firm is responsive to local pressures has a direct impact on business support unit managers. Whether a company formulates an international, multidomestic, global, or transnational strategy, business executives and divisional or strategic business unit managers in large multinational businesses need data and data analysis the business support unit managers have direct access to.

Business graduates that enter either internal or external consulting roles require a high level of competence with multinational strategy to communicate with business executives in multinational firms how their consulting projects fit into the overall multinational strategy of the firm. When business graduates that serve as either internal or external consultants to companies that are currently not engaging in international business, competency with multinational strategy is important so they can work with company executives that may be consider taking their firms global. Many large consulting firms are multinational. For business graduates who are or will become entrepreneurs, fluency with multinational strategy is essential to establishing and growing a successful firm if the goal is international expansion.

12.11 Conclusion

Expanding into international markets is a complex but rewarding endeavor that requires careful consideration of strategic motivations, market conditions, and the potential barriers that could impact success. By employing a comprehensive approach that includes evaluating motivations for expansion and by selecting the most appropriate entry modes, companies can maximize their chances of thriving globally. Theories such as the OLI paradigm and frameworks like the CAGE distance framework and the integration responsiveness framework provide valuable insights to help firms assess which strategies and markets are best aligned with their objectives. Ultimately, successful international expansion requires balancing the need for local responsiveness with the pursuit of global efficiencies, navigating risks effectively, and making informed choices about where and how to enter new markets.

Demonstrate Your Knowledge, Skills, and Competence

Use these questions to test your knowledge of the chapter:

1. Describe multinational strategy and its relationship to business-level strategy. Do all firms formulate and implement multinational strategy?
2. Discuss the history of global commerce.
3. Discuss the motivations and risks associated with multinational strategy.
4. Discuss the key elements of eight theories of multinational business. Which ones appeal to you the most and why? How can these theories inform multinational strategy?
5. Discuss the CAGE distance framework and its four dimensions. Give examples of each dimension. How is the CAGE distance framework used in formulating multinational strategy?
6. Discuss the integration-responsiveness framework. Explain the two critical strategic decisions that strategic leaders and managers make when formulating a multinational strategy and how these relates to four multinational strategies.
7. There are multiple entry modes when considering global expansion. Discuss each of these, and give examples.
8. Describe how competence with multinational strategy is relevant and important to you.

Now you are competent with multinational strategy. Your hard work has paid off! Only one more chapter to go!

Figure Descriptions

[Figure 12.1](#): First quadrant of an X-Y axis with four purple boxes. The x-axis represents responsiveness to local pressures and the y-axis represents responsiveness to global integration pressures. Both axes range from low to high. Low responsiveness to local pressures and low responsiveness to global integration pressures is labeled international. High responsiveness to local pressures and high responsiveness to global integration pressures is labeled transnational. High responsiveness to local pressures and low responsiveness to global integration pressures is labeled multidomestic. Low responsiveness to local pressures and high responsiveness to global integration pressures is labeled global.

Figure References

Figure 12.1: Integration-responsiveness framework. Kindred Grey. 2025. CC BY.

Figure 12.2: Red Bull. Cefalophore. 2024. Public domain. https://commons.wikimedia.org/wiki/File:8.4_floz_can_of_Red_Bull_Energy_Drink.jpg

PART VI: IMPLEMENT STRATEGY

As you are about to engage with the topics in the final part of this book, let's take a brief look at what you have learned about strategic management.

In Part I, you learned what strategic management entails, both as a field of study and as an area of business practice. You also learned how to conduct a case analysis. Part II detailed how to analyze a firm's organizational performance and its external and internal environments. Then in Part III, you learned how to synthesize the analysis you have conducted and how to determine a firm's strategic issue. Part IV focused on how strategic management leaders formulate corporate-level strategy and business-level strategy. In this part, you also learned how to analyze corporate-level strategy and business-level strategy when you conduct a case analysis. Then in Part V, you learned how strategic management leaders formulate four strategies that are embedded in business-level strategy: innovation strategy, sustainability and ethics strategy, technology strategy, and multinational strategy. You also learned how to analyze each of these when you conduct a case analysis.

Now in the final chapter, you learn how strategic management leaders implement strategy.

13. IMPLEMENT STRATEGY

Learning Objectives

After engaging with this chapter, you will understand and be able to apply the following concepts.

1. What implementing strategy entails
2. Why many companies fail to fully achieve the strategic objectives defined in their strategy
3. What the success-critical topics and best practices are for translating a robust strategy into operative financial results
4. How to analyze a strategy-implementation gap
5. How to formulate strategic goals
6. The importance of allocating resources to strategy implementation
7. The importance of broadly communicating and cascading strategy
8. The role of organizational design in executing strategy
9. The role of organizational control systems in executing strategy
10. The role of leadership in the process of strategy implementation
11. How to combine soft and hard implementation factors and hardwire strategy
12. The importance of aligning corporate culture with implementing strategy
13. Why a systematic change management approach is important in the implementation of a new strategy
14. Why strategy implementation is important to business graduates

You will be equipped to

1. Formulate strategic goals
2. Analyze a strategy-implementation gap

13.1 Introduction

In this chapter, you learn what implementing strategy entails. Then you analyze a strategy-implementation gap. Next you learn how to formulate strategic goals. Then you learn the importance of allocating resources to strategy implementation and broadly communicating and cascading strategy. Next you learn how to implement strategy through organizational design and organizational control systems. Then you learn how to combine soft and hard implementation factors and hardwire strategy. Next you learn how to align strategy and corporate culture and how to implement strategy through systematic change management. Finally, you learn why strategy implementation is important to business graduates.

By now, you know that there are three stages to the strategic management process: strategic analysis, strategy formulation, and strategy implementation. You are deeply familiar with strategic analysis (“Where are we?”) and strategy formulation (“Where are we going?”). Strategy implementation is the process of executing every strategy a company has formulated, answering the question “How are we going to get there?” Every strategy that a company has formulated needs to be successfully implemented and should follow some common best practices.

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13.2 Analyze Strategy-Implementation Gap

“However beautiful the strategy, you should occasionally look at the results.”

—Sir Winston Churchill (former Prime Minister of the United Kingdom)

“Strategy is important, but implementation is key.”

—Jack Welch (former Chairman and CEO of General Electric)

“The most brilliant strategy won't lead to success unless it's implemented effectively.”

—Bill Gates (co-founder of Microsoft)

These quotes provide good insight into what many companies face after formulating their strategy: a subpar implementation of the strategy. There are many reasons for a suboptimal or failed strategy implementation. One reason may be an unanticipated and rapidly changing external environment. For example, geopolitical environments can change quickly and impact strategy implementation, with wars, tariffs, and regional disputes greatly impacting strategy implementation.

Another reason why businesses may struggle with successful strategy implementation may be the difference in the pace that an organization moves at the top and throughout the rest of the firm. Depending on organizational size, management style, organizational design, and company culture, some businesses may move slowly in response to change. Some C-suites may move much more quickly compared to the rest of their organizations. The resulting gap between a few fast-moving senior executives and the more inert rest of the organization leads to frustration on both sides.

Still another reason that strategies may not realize their hoped-for results may be an underinvestment of sufficient resources to effectively implement a well-formulated strategy. Once a strategy is formulated, it is essential to

invest in its implementation. As you are about to learn, strategy formulation requires a thought out implementation plan.

Imagine that company executives have invested significant resources into formulating a great strategy. Then the company executives communicate the strategy to employees with a PowerPoint presentation in a townhall meeting. Now imagine that these executives do not invest sufficiently in a robust strategy implementation plan. What do you think the likelihood of success is going to be?

One study found that, on average, companies only realize around 63 percent of their planned performance improvements targeted through their strategy (Makins & Steele, 2005). This is a concerning and sobering statistic considering that a strategy should be the source of a sustainable competitive advantage that helps the company to win in its chosen markets. Seemingly, many companies fail to translate a great strategy into operative performance improvements. They strategize beautifully but inadequately implement.

On the surface, failed strategy implementation leads to subpar financial performance and a lot of work and money wasted. On a deeper level, the failure leads to a negative learning effect in the organization, instilling the idea that new strategies announced

with a big media fanfare do not really change the way the organization works. As a result, employees may just keep their heads down instead of fully embracing new strategies. Change fatigue sets in, and the organization continues to operate in the old way instead of making changes in support of the new strategy.

For example, one senior executive in the chemical industry stated that he prefers 80 percent of a strategy implemented 100 percent rather than a perfect strategy only implemented 80 percent. So, what causes this implementation gap? What can be done to avoid prevalent implementation issues? How can an organization drive true performance improvements via a new strategy and avoid the strategy-to-performance gap?

The formulation of a new strategy does not happen in a vacuum. All companies, except brand-new startups, have an existing strategy that needs to be factored into the formulation of the new strategy. The new strategy is often not entirely dissimilar to a firm's business model and go-to market approach; rather, it is an adjustment, fine tuning, and course correction in light of things that worked well or that do not work well with a firm's current strategy. Hence, understanding whether the current strategy is working and how it is successfully implemented becomes important input in the formulation of a new strategy.

The decisive questions regarding the current strategy are whether it delivered the top-line growth, bottom-line growth, and the market evaluation that the strategy promised. If the promises of the current strategy have been met, the success factors for driving successful strategy implementation should be factored into the development of the new strategy.

However, current strategies often fail to fully deliver on the promises made in strategy formulation. Current performance is not at the promised level, and there is a gap between where the firm should be according to the current strategy and where it is in terms of sales, net profit, cash flow, market share, international presence, innovation success, share price, earnings per share, and other metrics.

Consider figure 13.1. There are multiple gaps to analyze, including the strategic gap, implementation gap, and the performance gap.

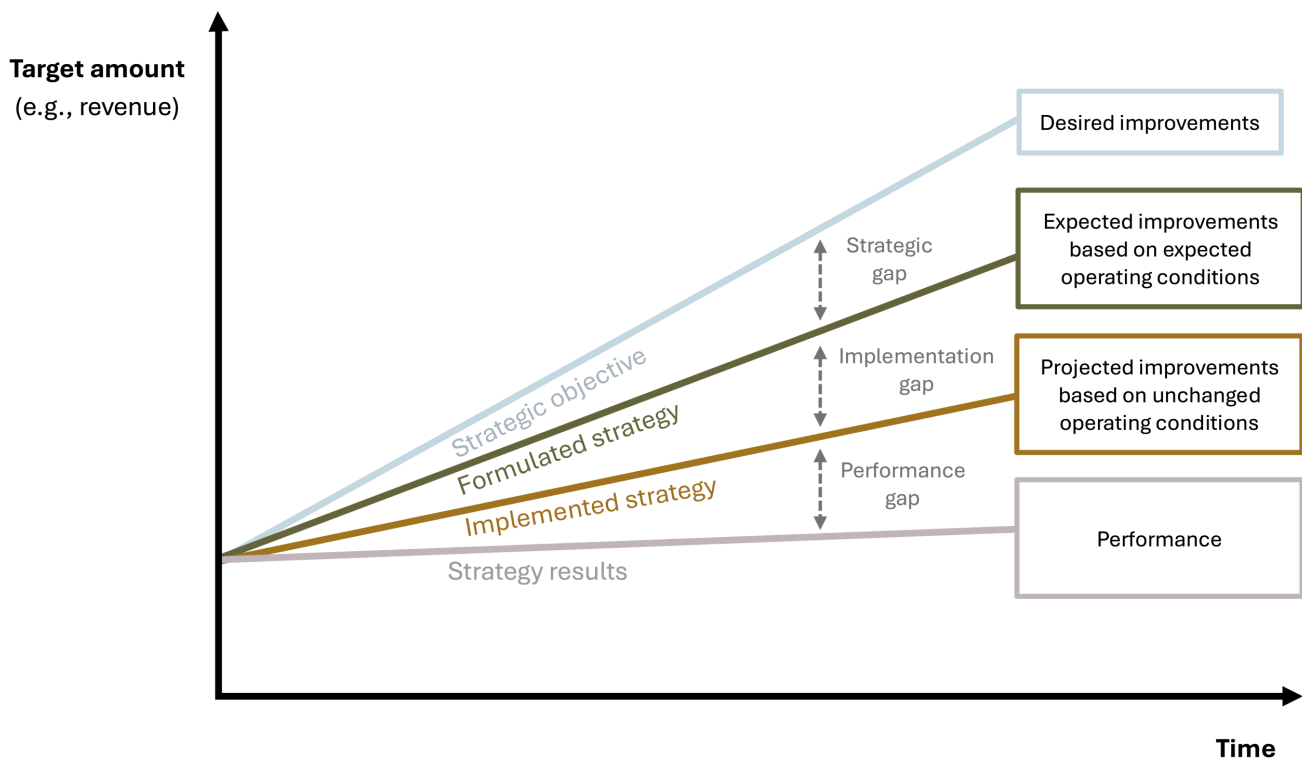


Figure 13.1: Gap analysis

The **strategic gap** is the difference between a firm's strategic objective, what it would like to accomplish, and its formulated strategy, which is based on the improvements the firm expects to realize given the expected operating conditions. A **strategic gap analysis** analyzes the strategic gap and its causes. What a firm would like to accomplish must be tempered with a realistic assessment of what it may expect to accomplish given current conditions. This is important because a company needs to understand what may constrain its desired results. The firm may be able to address the current conditions to maximize more of its strategic objective or at the least monitor the constraining conditions for opportunities when those conditions change.

The **implementation gap** is the difference between the formulated strategy, which considers the improvements the firm expected given the expected operating conditions when the strategy was formulated and the implemented strategy, which is based on projected improvements if the current operating conditions remain the same. **Implementation gap analysis** analyzes this gap and its causes. It is useful to understand how the operating conditions have changed in the time between strategy formulation and strategy implementation. It also is useful to understand the improvements that will likely continue from the current strategy if the current operating conditions remain unchanged. This indicates the likelihood of the currently implemented strategy's continued success under the current conditions and suggests whether it is time to consider revising the current strategy.

The **performance gap** is the difference between the implemented strategy, which considers projected improvements if the current operating conditions remain the same, and organizational performance under the strategy. A firm needs to understand the difference between what it projected it would accomplish with its strategy and what it accomplished. **Performance gap analysis** looks at the gap between where the firm should be according to the current strategy and where it is. Hence, the performance gap analysis is the process that companies use to compare their current strategy performance with their desired, expected performance. A performance gap analysis is used to determine whether a company is meeting expectations and using its resources effectively. After understanding the gap in success-critical strategic metrics and KPIs, the firm conducts a thorough root cause analysis to understand why the strategy was not as successful as it was intended. The lessons learned and the identification of specific root causes that impeded full strategy implementation are then factored into the development of the new strategy to prevent similar challenges from materializing again.

After the strategic, implementation, and performance gaps have been analyzed, root causes are analyzed and then an improvement plan that addresses the root causes is formulated and implemented. For the root cause analysis, it is important that the firm analyzes more than the symptoms of the gap, such as a gap in revenue growth or market share growth. Instead, the company needs to dig deeper into the real root causes that need to be addressed. The **root cause analysis (RCA)** is a structured process for identifying the underlying causes of a problem and developing solutions to prevent it from happening again. RCA assumes that it is much more effective to systematically prevent and solve underlying issues rather than just treating symptoms when necessary and putting out fires or repeating the same mistakes in the formulation and implementation of the new strategy.

Application

- Consider the scenario above where company executives invested significant resources into formulating a strategy, which they then presented in a PowerPoint to the employees. Maybe you have already experienced a similar scenario, perhaps in a job, where an organization announces a big change and then does very little to ensure its successful implementation.
 - What was your experience in this situation? Was it successful? What would have made it more successful?

Analyze Root Causes

As a prerequisite for improving strategy delivery and bringing an organization closer to its stated vision, the formulated strategy needs to be robust. It needs to be specific and state clear strategic objectives that are substantive and truly differentiating. The strategy needs to address a specific and clear right to win for the organization. This means that the strategy needs to be unique, with a specific source of winning in the market and a clear source of competitive differentiation. While this sounds obvious, many strategies are rather broad or just state ambitious targets in the form of a wish list. If you can replace the logo on the strategy documents with the logo of a competitor and the strategy still makes sense, the strategy is neither unique nor truly differentiating. Hence, some strategy implementation processes are doomed to fail because of a subpar strategy that simply is not specific and unique enough to drive superior performance.

Beyond this foundational flaw, there are various factors that lead to possible strategy-to-performance gap. As depicted in figure 13.2, there are a variety of issues that block the translation of a great strategy into improved operative performance (Makins & Steele, 2005), including both hard factors like a lack of resources and soft factors like poor communication of the strategy. If the strategy is not translated to specific and measurable objectives, there is a high risk that the organization does not commit appropriately to necessary change, action, and performance improvements.

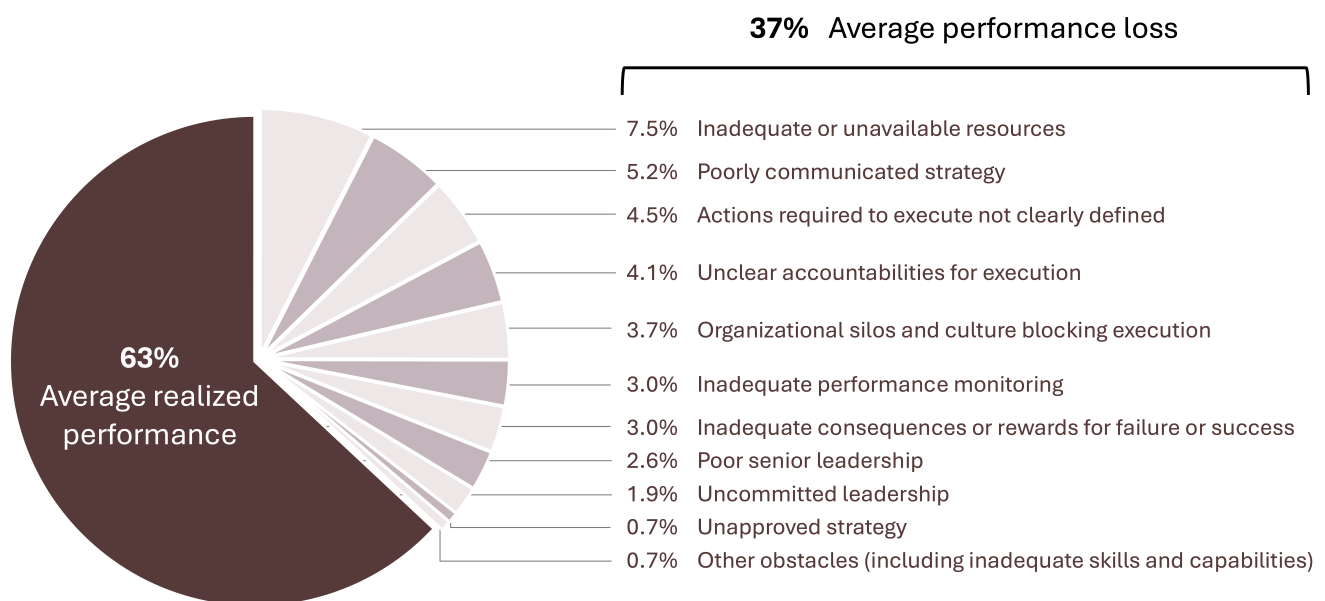


Figure 13.2: Reasons for failed strategy implementation

Clustering the different root causes into bigger blocks, there are six barriers to strategy implementation to avoid.

1. Vision barrier: Only 5 percent of the workforce understands the strategy.
2. Leadership barrier: Executive teams and leaders do not spend enough time discussing and implementing strategy.
3. People barrier: Only 25 percent of managers have incentives linked to strategy.
4. Resource barrier: 60 percent of organizations do not link budgets to strategy, leaving the strategy implementation underfunded.
5. Skill barrier: Only 40 percent of organizations provide sufficient new skills and competencies to implement the new strategy. Insufficient development of employee skills and competencies hinders the ability to realize the strategic “where to play” and “how to win” directives.
6. System barrier: 45 percent of organizations do not have a formal strategy implementation process in place. There are no appropriate processes, structures, and rules in place to build organizational capabilities to implement the new strategy.

Application

- Put yourself in the shoes of a leader whose strategy implementation failed.
 - What might have been the reasons for this?
 - Which roles do employees and middle managers play in the successful rollout of strategy?

Key Takeaways

Executives and managers in the corporate world have much more expertise in developing strategy than implementing strategy fully and effectively. This leads to significant performance gaps and shortfalls between what a new strategy promises and what it delivers. Improving strategy implementation is success-critical in the whole strategy process.

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13.3 Formulate Strategic Goals

Clear strategic goals are part of any good strategy. To achieve the firm's broader aspirations stated in its mission, purpose, vision, and values and to successfully implement strategy, companies need to set specific, actionable objectives. These objectives guide the firm's strategic action plans and employees in their day-to-day work and help align their efforts with the organization's overall strategy. The organization needs to translate strategy into strategic goals. These strategic goals are usually:

- Financial goals like revenue, net profit, share price, cash flow, and net working capital.
- Customer and market goals like market share, customer acquisition, customer retention, and strength of the firm's brand.
- Internal goals like efficiency of operations, innovation processes, the value-adding use of technology, cost management, and the optimization of other success-critical processes.
- Other goals like mergers & acquisitions, corporate culture, talent management, and globalization of business.

It is important to quantify these strategic goals using metrics and key performance indicators (KPIs) that are linked to financial success. Following the approach of “what you measure is what you manage,” a clear set of metrics and KPIs guides strategy implementation. The most effective goals follow the SMART framework, which stands for specific, measurable, attainable, realistic, and time-bound. SMART goals make it easier for employees to stay focused and accountable, increasing the likelihood of success. Robust and actionable strategic goals ideally meet the criteria of SMART goals.

- Are the goals specific?
- Are the goals measurable?
- Are the goals attainable?
- Are the goals realistic?
- Are the goals time-bound?

The period following the achievement of a major goal is often overlooked, yet it is a critical moment for strategic decision-making. This is when an organization must choose whether to maintain its current success or pursue new challenges.

An example can be seen in Apple's shift after successfully launching the iPhone. The iPhone revolutionized the tech industry and brought Apple unparalleled success, but the company didn't rest on its laurels. After achieving dominance in the smartphone market, Apple launched the Apple Watch and AirPods, both of which became key contributors to its revenue. The company also expanded its services sector with offerings like Apple Music, iCloud, and Apple TV+, ensuring continued growth and innovation.

This approach highlights a key principle: organizations that continually set new goals remain competitive and dynamic. Apple's move beyond its original success into new products and services allowed it to remain at the forefront of the tech industry. In contrast, companies that fail to embrace new goals risk stagnation, as demonstrated by industries that rest on past achievements instead of looking to the future. To avoid getting lost in the complexity of too many goals and metrics, it is advisable that firms focus on the few success-critical objectives that require management attention.

After a company-specific and strategy-specific set of meaningful and robust strategic goals have been formulated and communicated, the firm defines specific plans to achieve its strategic goals over the time horizon of the new strategy. Since strategy implementation is always a multi-year process, companies usually define the final strategic objectives as the outcome of successful strategy implementation and also the result of intermediate goals and milestones on the way to reaching the final goals. These strategic milestones act as checkpoints that mark significant achievements or turning points in a firm's strategy implementation process.

Strategic action plans (STRAPs) will drive the operative implementation of the strategy. Strategic action plans define specifically what a company must do in all parts and at all levels of the organization to bring the strategy to life, reach defined milestones, and eventually achieve the final strategic goals. STRAPs and strategic objectives provide a specific compass and guiding star for the whole organization, and they define clear expectations in terms of actions and behaviors.

Ultimately, successful strategy needs to be reflected in tangible improvements in the organization's financial performance. Beyond the quantitative financial metrics, it is also important to include qualitative measures. This **balanced scorecard**, detailed in [Chapter 3](#), is an excellent way to measure and monitor strategy implementation.

Application

- Think about three goals you have. They may relate to your studies, career, health, social life, or any area you like.
 - Assess whether they are specific, measurable, attainable, realistic, and time bound.
 - How could you strengthen your goals by making them more SMART?

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13.4 Allocate Resources to Strategy Implementation

When the strategic direction is clear and after quantitative and qualitative objectives have been defined, the organization needs to allocate sufficient resources to strategy implementation in support of the defined objectives. Usually, a strategy calls for doing things differently, often with the target of profitable growth. Doing things differently and realizing top-line and bottom-line growth requires dedicated budgetary resources.

Strategy implementation needs to be clearly linked to budget, specific resource plans, and a project management approach. Top leadership needs to create a strategy-supporting structure, staff the organization with the needed expertise, and develop and strengthen strategy-supporting resources and capabilities.

Doing things differently requires different skills and competencies for employees responsible for strategy implementation. It is important that employees are supported in acquiring these skills through training and development programs that are fully aligned with the new strategies.

For example, if a company's strategy states that the firm's right to win is their customer-centric innovation approach, then the company needs to strengthen employees' skills to identify business opportunities and unmet customer needs that drive innovation. The organization needs to equip employees with customer interaction and relationship-building skills, possibly hire new employees with specific skill sets or use temporary external resources like consultants to drive successful strategy implementation. Additionally, the organization needs to develop a clear strategy implementation plan and may want to allocate appropriate resources to project teams that drive and manage strategy implementation.

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13.5 Broadly Communicate and Cascade Strategy

Only employees who fully understand their organization's strategy can embrace and implement the strategy. Organizations often communicate new strategies in townhall meetings and emails from the desks of CEOs. However, a surprisingly high percentage of employees do not know or understand their companies' strategies.

According to a *Forbes* study, up to 80 percent of employees have no clear line of sight between their tasks and corporate goals, up to 70 percent of employees could not correctly identify their corporate strategy, and 45 percent of middle managers could not name one of their company's top five strategic priorities. Any organization that does not involve and does not take their employees with them on the strategy implementation journey is not positioned to realize the promised performance improvements.

While leaders may communicate strategy, in many cases it is not heard or understood by employees. Consequently, employees are not able to embrace the strategy, cannot connect their own work with the strategy, and are poorly equipped to support the strategy. An effective communication approach for strategy includes the following success factors.

- A good strategy and a good solution are not enough. Effective strategy communication needs to win employees' hearts and minds.
- Strategy communication needs to include a clear reason and business case for the new strategy. It needs to unambiguously outline the reasons for change, and it needs to provide an emotionally compelling vision for a better future.
- Employees do not get out of bed to improve the firm's net profit margin or other financial metrics. Strategy communication needs to make an emotional case for change and provide a “what's in it for me” connection to employees. Linking strategy to a compelling company purpose that instills employees with a sense of pride and with making a positive difference can be a powerful vehicle to successfully implementing a strategy.
- Use storytelling and symbolic action, which makes strategy messages stick much better than just PowerPoint slides, data, and written communication.
- Customize strategy messages to different employee audiences according to professions and reporting lines.
- As much as possible, make communication two-way, personal, consistent, and inspirational.
- Use a variety of managers to communicate the strategy. Including middle management, top talent, change agents, and informal leaders helps to cascade the strategy throughout the whole organization. Involving key employees early and making them part of the strategy rollout increases their buy-in and support for the new strategy.

Leadership plays a key role in strategy communication and rollout. Leaders are very visible in an organization, and their behaviors are closely observed by employees. Beyond verbal communication, leaders on all levels need to model the new behaviors they want to see in the organization. They need to lead by example, and they need to link new behaviors to the new strategy. They must become the ambassadors of the new strategy, showcasing new skills and competencies in support of the new strategy. They must also publicly recognize and reward these behaviors in others and celebrate examples of successful strategy implementation.

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13.6 Implement Strategy through Organizational Design

The guiding principle for organizational design is that structure follows strategy. There is not an inherently better or worse organizational design. The best organizational design is the one that best supports the organization's mission, purpose, vision, values, and strategy. Organizational designs can have a functional structure, a multidivisional structure, a matrix structure, or a boundaryless structure.

Functional Structure

In a functional structure, the firm organizes its business activities according to functional areas of the business, such as accounting and information systems, business information technology and cybersecurity, finance, insurance and business law, human resource management, innovation and technology, marketing, and operations.

Organizing business activities by functional business areas, a functional structure offers advantages like reduced conflict and costs, maximized efficiency, and expert creation. A disadvantage of a functional structure is that it is slow to respond to change.

Young and small businesses often organize business activities using a functional structure. Functional organizational structures are best for stable environments and are often the choice of large firms operating with a cost leadership strategy as part of their focused or broad cost leadership strategy.

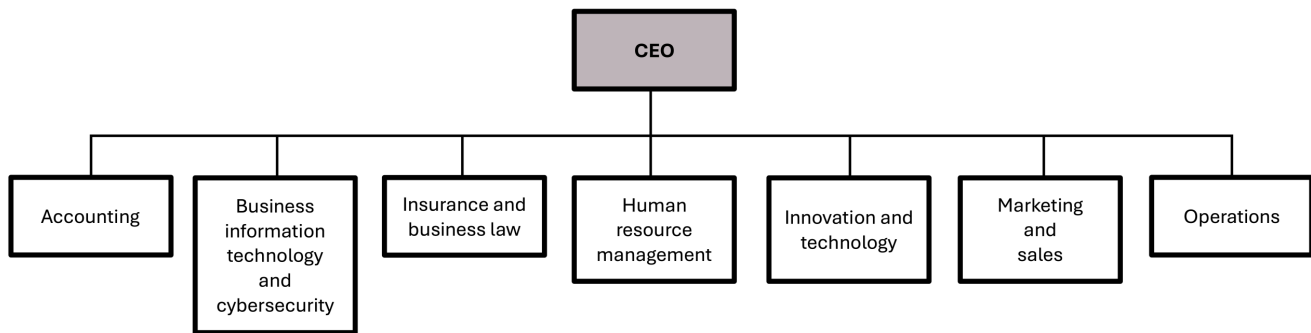


Figure 13.3: Functional organizational structure

Multidivisional Structure

In a multidivisional structure, the company organizes its business activities based on product areas and/or geographic regions. A multidivisional structure has the advantage of being more responsive to customer needs and reacting more quickly to change in the environment. A disadvantage of a multidivisional structure is that it is more costly to operate than a functional structure because each unit that focuses on a product or region duplicate each functional activity, such as human resource management and marketing.

As a young, small company grows, it may change its organizational structure to a multidivisional structure. Large firms also may use a multidivisional structure.

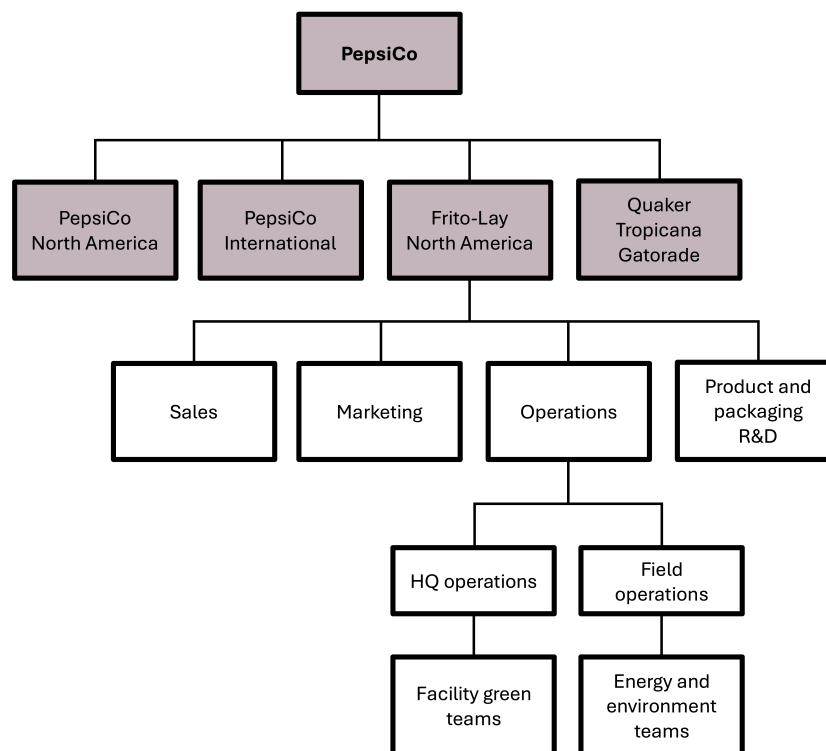


Figure 13.4: Multidivisional organizational structure

Matrix Structure

A matrix structure is hybrid organizational structure that has features of both functional and multidivisional structures.

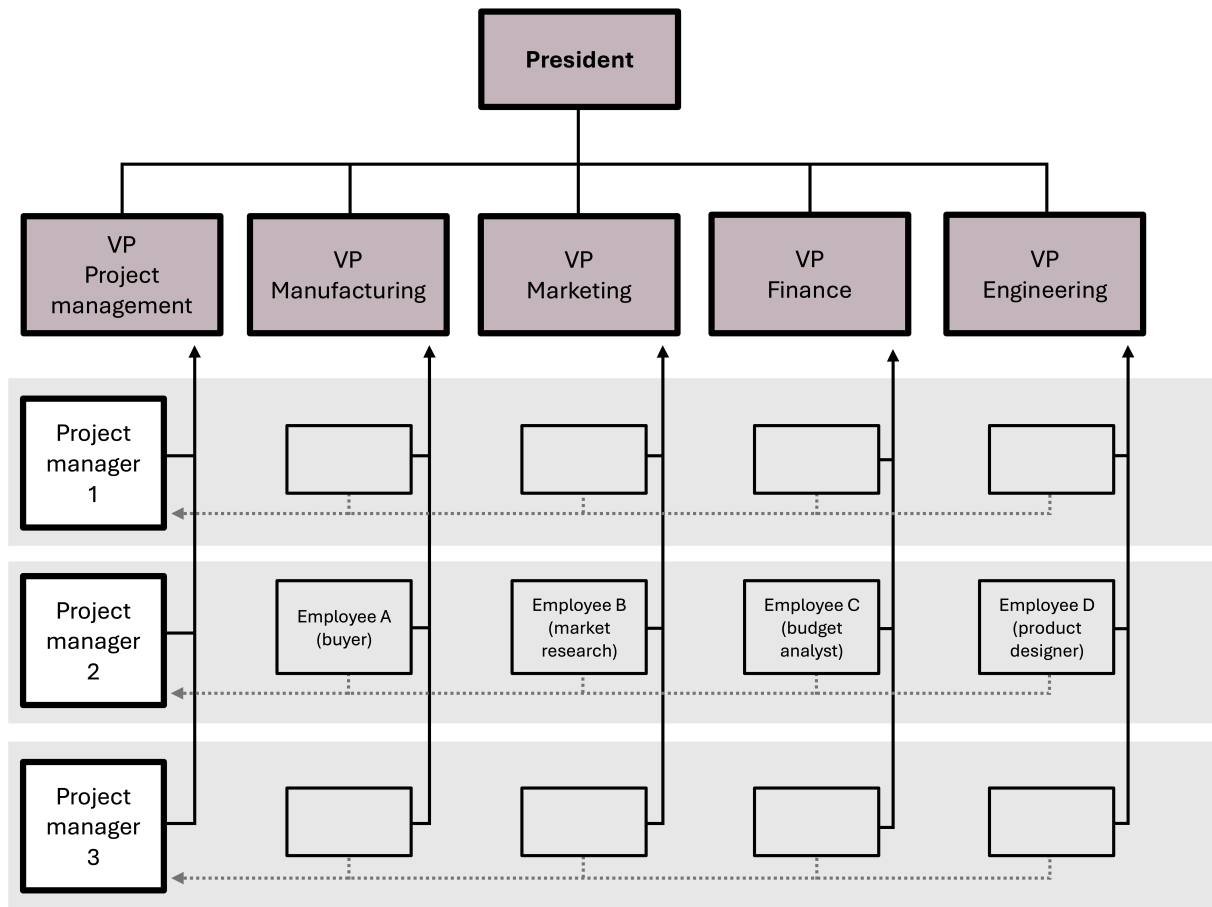


Figure 13.5: Matrix organizational structure

Complex organizations or firms that engage in projects of limited duration may use a matrix structure in which employees can be put on multiple teams based on their functional areas and current projects, maximizing creativity, idea flow, teamwork, and collaboration. A matrix structure also allows for some degree of standardized policies and procedures by maintaining functional areas, such as finance.

Because a matrix organizational structure supports creativity and collaboration, it nurtures new leaders. Because employees report to two managers, one in their functional area and one leading their current project, it is essential that these leaders communicate well and offer congruent guidance to the employees. This can be a disadvantage of the matrix organizational structure if this congruence of guidance is weak or falls apart.

A matrix structure is most common in large companies that engage in creative and collaborative project-based work.

Boundaryless Structure

A boundaryless organizational structure is flat, with decentralized decision-making and many cross-functional teams. This structure works well in knowledge industries such as IT, where responsiveness to changing environmental and competitive forces must be quick.

Advantages of a boundaryless organizational structure include its quick responsiveness and its ability to share knowledge widely and foster innovation. A disadvantage of a boundaryless organizational structure is the lack of clear lines of accountability.

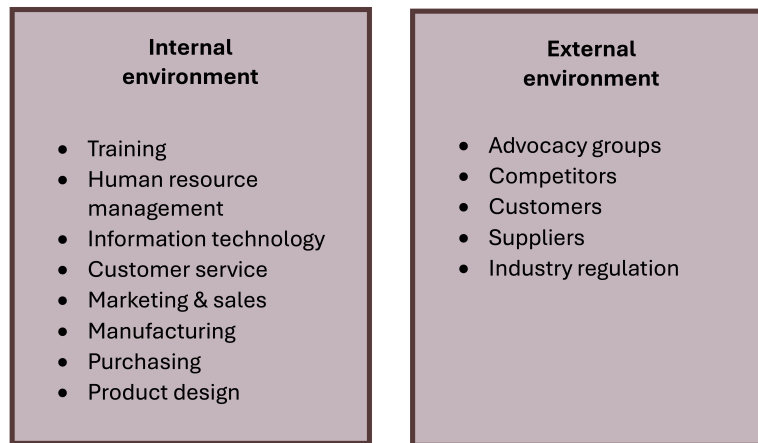


Figure 13.6: Boundaryless organizational structure

While mature organizations normally do not fundamentally change their organizational structures (except for a business restructuring), the right choice of organizational design is critical for smaller and startup companies. As a smaller organization grows, it is also possible that the company may change organizational structures, for example, from a functional to a multidivisional structure.

Other important organizational elements of strategy implementation include an overarching and unifying company purpose, the definition of clear roles and responsibilities of organizational units, clearly defined interfaces between the units, an appropriate span of control, and STRAPs that prevent silo thinking and a lack of cooperation in the different units.

Some organizations use the RASCI matrix to define clear roles and responsibilities and avoid a poor interface between different strategic business units, business support functions, and other organizational units.

The **RASCI matrix** is a responsibility assignment matrix that describes the participation of various roles in completing tasks or deliverables for a project or business process. The RASCI acronym stands for responsible, accountable, supportive, consulted, and informed. The matrix assigns specific roles and responsibilities to stakeholders involved in the management process and strategy implementation. It states in a transparent way who is ultimately responsible for a task, who is accountable, who needs to be involved for support, who needs to be consulted, and who needs to be informed.

Determining the right **span of control** is another important element of organizational design. The term refers to the number of direct reports for which a supervisor is responsible. A span of control that is too high creates management challenges because it is hard to oversee too many direct reports in performance management and talent development. A span of control that is too narrow creates too many supervisors with direct report relationships. This increases organizational complexity and is inefficient.

A trend in organizations is **delayering**, which is the reduction of hierarchical levels in a company. Removing layers of management increases organizational efficiency and responsiveness because there are fewer levels between the organization's leadership and the customers and other external stakeholders, which makes a business more flexible, responsive, and agile.

Application

- Think of the current job you have or a job you have had in the past.
 - What was the organizational design of the organization? Was this the best organizational design for the company? What were its pros and cons? What control systems did it use?

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13.7 Implement Strategy through Organizational Control Systems

Part of strategy implementation is the effective design and use of organizational control systems, which are sets of processes and mechanisms used to monitor and evaluate an organization's performance against set standards, allowing management to identify deviations from strategy and take corrective actions. Organizational control systems play a critical role in successful strategy implementation by ensuring the organization stays on track to achieve its goals. Organizational control systems track performance and identify adjustments that need to be made.

Output Control

Output control uses measurable results to track and monitor strategy implementation. This approach focuses on breaking down strategy into strategic objectives that are formulated as SMART objectives. Output control starts with the definition of targets for performance; it then measures the performance against these targets.

In the case of strategy implementation, these targets and objectives are the strategic targets formulated in the firm's strategy. The primary aim is to ensure that the organization meets its goals, improves efficiency, and maximizes profitability. Establishing specific, measurable, achievable, relevant, and time-bound strategic objectives drives accountability and allows for transparent tracking of strategy implementation progress.

Typical strategic objectives include revenue, net profit, profit margins, market share, newly launched innovations, mergers and acquisitions, entrance into new countries, improved brand recognition, and customer satisfaction, to name just a few. These SMART strategic objectives are used to continuously evaluate strategy implementation performance. Performance data is compared against set standards. This comparison helps in identifying gaps, understanding deviations, recognizing areas for improvement, and initiating corrective action.

The benefits of output control include transparent goal alignment that ensures that all parts of the organization are aligned toward common goals. It also drives accountability and creates a sense of responsibility for implementing strategy among employees and management. Lastly, output control improves efficiency and resource allocation, and it enhances decision-making in the strategy implementation process by using data-driven insights that aid in making informed business decisions.

Behavioral Control

As a system, behavioral control regulates activities rather than outcomes. It's about creating an environment where employees' actions consistently reflect the company's values and objectives. The firm actively monitors and influences employee actions and behaviors to achieve desired results through managerial oversight, detailed job descriptions, company policies, training and development, guidelines, and performance expectations.

Supervisors and company leaders play important roles in directing employees. They lead by example, role-modeling behaviors they want to see in the organizations and regulating how employees conduct themselves at work.

Another important element and driver of behavioral control is the corporate culture of an organization, which also has a significant impact on employee behavior. Corporate culture is a set of shared values, expectations, and norms that guides employee behavior. There needs to be strong alignment between corporate culture, strategic analysis, strategy formulation, and strategy implementation.

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13.8 Hardwiring Strategy in the Organization and Combining Soft and Hard Implementation Factors

Strategy implementation needs to be “hardwired” into an organization. To achieve this, key processes may need to be redesigned and the organizational structure may need to be adjusted. Different measures of employee performance and reward structures may need to be developed to drive new actions and behaviors on organizational and individual levels. The **McKinsey 7-S model** provides a good overview of possible areas impacted by strategy implementation. The model, shown in figure 13.7, also highlights the importance of fully aligning the seven factors and their interconnectedness to achieve full success in strategy implementation.

The seven factors are structure, strategy, systems, skills, style, staff, and shared values. At the center of the model is shared value, which considers the firm's core principles that support this strategy.

The remaining elements of the model are divided into hard Ss and soft Ss. Hard Ss are strategy, structure, and systems. As you are familiar, strategy focuses on strategic analysis, strategy formulation, and implementation.

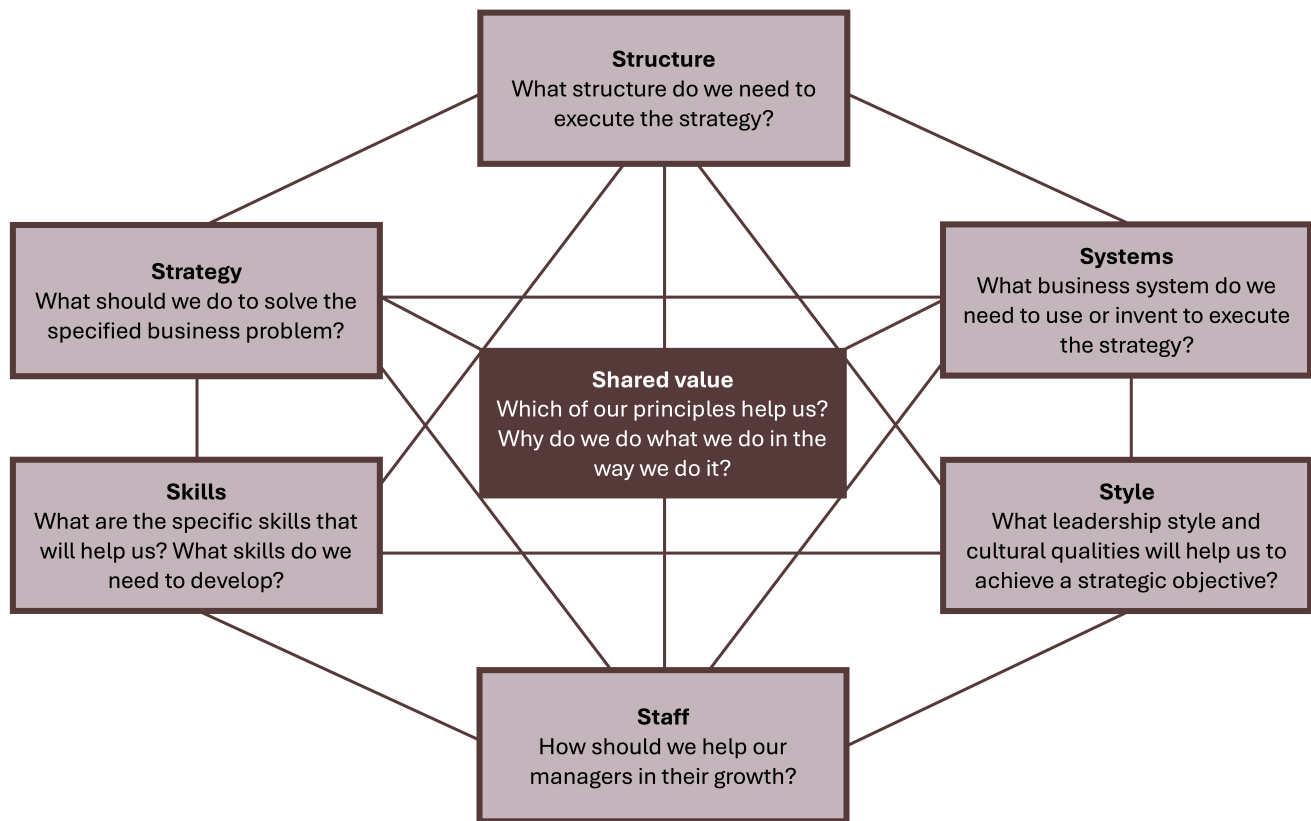


Figure 13.7: McKinsey 7-S framework

Structure focuses on the organizational structure that best supports a firm's strategy implementation. For organizational structure, the paradigm is that "structure follows strategy." For example, young and small businesses often use a functional structure. Because functional organizational structures are best for stable environments, they are also a good choice of large firms operating with a focused or broad cost leadership business-level strategy. For firms in **knowledge industries** that are based on intensive use of technology and human capital, the organizational structure should emphasize cross-functional cooperation, and they should avoid organizational silos that often impede successful strategy implementation due to specific interests of business units that put their own interests above the holistic implementation of a new strategy. Thanks to shortening strategy cycles and more externally induced change than in the past, organizational structures that allow for high levels of flexibility and agility and that are market and customer-centric are more effective at implementing strategy than traditional structures that are rigid and siloed. Organizational silos often impede successful strategy implementation because business units may be incentivized to put their own interests above the implementation of new strategy.

The third hard S, systems, refers to the systems a business needs to use or create for strategy implementation. Performance management is critical for successful strategy implementation, as are compensation and rewards systems. For example, knowing what motivates employees is essential. Many employees are happy and motivated upon getting a salary increase, a positive performance evaluation, a high bonus payment, praise, an opportunity to contribute to meaningful and high-impact work, and a sense of belonging in an organization with similar values. Systems that offer these rewards have a high impact on shaping employee behavior. It is important to reward employees for skills, competencies, and behaviors that support strategy implementation and to possibly sanction behaviors that contradict the new strategy.

For example, a company with a customer-centric innovation model should reward employees who spend quality time with important customers, who identify customers' unmet needs, and who have specific ideas for innovative solutions for these customers.

Including skills and behaviors like this in performance reviews and rewarding successful employees drives strategy implementation because it aligns organizational objectives with individual objectives.

The Soft Ss of the McKinsey framework are skills, staff, and style. Skills focuses on identifying the skills employees need in order to implement strategy, some of which may need to be developed. Staff refers to supporting managers in their growth, and style emphasizes leadership style and corporate culture that supports strategy implementation.

Successful strategy implementation is also dependent on the alignment of business support function strategies—for example, human resource management, procurement, production, supply chain, finance—with the unit's business-level strategy. These functions need to develop or adjust their functional strategies so that they are fully derived from and in support of the overall corporate-level strategy, business-level strategy, and the strategies embedded into business-level strategies.

For the customer-centric, innovation-driven company, here are some ways that business-support functions can drive strategy implementation:

- Human Resources: Hires, trains, and develops employees with specific skill sets to sell innovation to customers.
- Procurement: Partners with strategic suppliers that can support the company's innovation strategy. Selection criteria for suppliers are focused on strategic alignment, inclusion in innovation process, and reliable supply rather than just focusing on lowest price.
- Finance: Develops financial metrics and balanced scorecard that reflects the innovation-driven business model. Focus on ROI on R&D, such as percentage of sales with products newer than five years (percentage of sales of new launches), percentage of SG&A of sales to measure infrastructure investment in R&D, marketing, etc.

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13.9 Aligning Strategy Implementation and Corporate Culture

According to management guru Peter Drucker, even the best strategy fails if it contradicts the organization's culture. For example, if a highly hierarchical, bureaucratic, and internally focused company wanted to implement a customer-centric innovation model, this strategy would most likely fail. To this point, employees have adhered to long-standing values that do not support agile, entrepreneurial, and customer-centric thinking. Being customer-centric and agile is just not in the company DNA.

“Culture eats strategy for breakfast.”

—Peter Drucker (management consultant)

Among other things, corporate culture focuses on “the way things are done around here.” Corporate culture defines the rules of the game and the values, beliefs, assumptions, and norms that govern how members behave. This has implications for both successful and unsuccessful strategy implementation. If the strategy calls for new behaviors that are not supported by the corporate culture in the organizational DNA, strategy implementation fails and the culture lives on.

There are some important points to keep in mind when embedding strategy implementation into organizational culture.

- Strategy drives focus and direction, while culture is the emotional, organic habitat in which a company's strategy lives or dies.
- Strategy is just the headline on the company's story. Culture needs a clearly understood common language to embrace and tell the story that includes mission, purpose, vision, values, and clear expectations.
- Strategy is about intent and ingenuity, and culture determines desire, engagement, and implementation.
- Strategy lays down the rules for playing the game, and culture fuels the spirit for how the game will be played.
- Strategy is imperative for strategy differentiation, but a vibrant culture delivers the strategic advantage.
- When culture embraces strategy, implementation is scalable, repeatable, and sustainable.

Before a strategy is even formulated, it is critical to understand the organization's culture as a starting point and the context in which the strategy is brought to life. While culture can be changed over time, it is important to work with the current culture. Ignoring or fighting the current culture leads to resistance and a high probability of failed strategy implementation. It is better to honor the strengths of the existing culture and to change culture as appropriate over time.

There is no perfect culture, but the right culture is the one that supports an organization in reaching its specific vision and implementing its strategy in a given organizational and market context. The right corporate culture supports the organization's strategy and services the organization's mission, purpose, vision, and values. An organization needs to be intentional about its culture and ensure it is aligned with strategy.

While there is no perfect culture, an adaptive culture provides a great context for successful strategy implementation. Harvard Business School professor and author John Kotter identifies adaptive cultures as having these characteristics:

- Ensures information flows are unobstructed from all areas and across silos
- Encourages smart risks
- Cares deeply about customers, shareholders, and employees
- Strongly values people and processes that can create useful change
- Encourages leadership from more people
- Encourages culture through actions, such as rewarding testing and learning, including the voices of all stakeholders in evaluating success, and allowing for more dispersed decision-making.

Strategy and culture need to match. If they are not aligned, culture always trumps strategy.

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13.10 Strategy Implementation through Systematic Change Management

New strategy normally calls for doing things differently, whether that entails a new business model, globalization, new markets and/or new products, restructuring, strategic partnerships and M&A activities, or new ways to respond to new competitors and new customer needs. In an increasingly global and dynamic market environment, strategy life cycles are shorter. This means that change is the new normal and that strategy needs to respond swiftly to changed market conditions, regulation, and other drivers for a new or adjusted strategy.

Living in the age of disruption, continuous and accelerated change is often met with employee resistance and change fatigue, which becomes a serious barrier to successful strategy implementation. Employees may not see the value of all the change. They may have the tendency to value the known and prefer their comfort zones, and they may not easily embrace change just because there is a new strategy. Often strategy implementation is enthusiastically driven by top management but reaches a sudden halt when mid-management does not buy in and when the new strategy meets passive or even active employee resistance.

Seventy percent of all change initiatives fail, which is an alarming statistic for anyone implementing new strategies. However, there are several systematic approaches available that significantly increase the probability of successful change and strategy implementation. This is where strategy implementation meets systematic **change management**, which guides an organization in assessing change readiness and implementing change.

Kotter's 8-step model for successful organizational change is a great approach for implementing strategy successfully. Different employees travel at different speeds on their own individual change journeys, and there needs to be a clear answer to the employee question of “What's in it for me?” Kotter's model has been updated over time but remains a widely used framework for effective change management.

Kotter's 8-step change model includes three phases and eight steps.

- Phase 1: Create the climate for change
 - Step 1 Create urgency
 - Step 2 Form a powerful coalition
 - Step 3 Create a vision for change
- Phase 2: Engage and enable the organization
 - Step 4 Communicate the vision
 - Step 5 Empower action
 - Step 6 Create quick wins
- Phase 3: Implement and sustain the change
 - Step 7 Build on the change
 - Step 8 Make it stick

Following a systematic approach to change management like Kotter's model significantly increases the probability of successful strategy implementation. The model begins by creating a sense of urgency for the new strategy. A powerful guiding coalition in support of the new strategy is needed to gain the hierarchical momentum and critical mass needed to make the new strategy a reality. Beyond communicating facts, it is important to reach employees' hearts and minds. Leadership needs to develop an emotionally compelling story that resonates with employees from different hierarchical levels so that employees understand why the strategy is good for the organization and employees. Employees need to be convinced that the new strategy leads to greener pastures on the other side of the strategy implementation process.

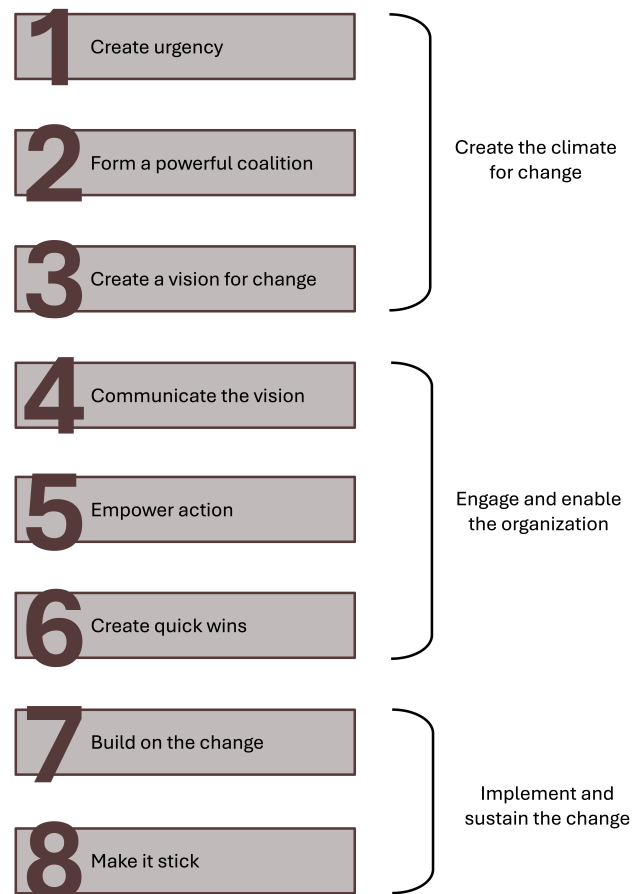


Figure 13.8: Using Kotter's change management model to implement strategy

After that, the new strategy needs to be communicated and implemented. Planning and celebrating quick wins delivered by the strategy convinces employees and stakeholders that the new strategy works, and this drives continued support for the implementation process.

Finally, it is important that new behaviors and new processes laid out in the new strategy become a habit and part of the new corporate culture. The change induced by the new strategy needs to be sustained, and leaders need to reinforce the new strategy to make it stick in the organization.

Application

- Put yourself in the shoes of an employee who is expected to implement a new strategy in your functional or business support unit.
 - What information, communication, and support do you expect from your direct supervisor and your company leadership for you to be willing to fully embrace and implement the new strategy?

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13.11 Why Strategy Implementation Is Important to Business Graduates

Sooner than you think, many of you will become part of a strategy formulation team. This could be on the level of corporate strategy for a smaller firm, on the level of functional strategy (like IT, finance, procurement, HR, etc.), or on the level of a division or strategic business unit. Companies are increasingly involving managers from all levels of the organization, which means that you can easily be a member of a strategy formulation or strategy implementation team. Additionally, your career success depends on your ability to understand and implement corporate-level strategy, business-level strategy (and its embedded strategies), and functional-level strategy in your position on a daily basis. You need to embrace strategy, implement strategy, and bring it to life through its implementation. You need to translate strategy to operative actions that add value to the company to drive superior performance. Knowing best practices of strategy formulation and implementation guides your ability to stand out as a manager who links strategy to specific action in your organizational unit, which is a core competency valued and rewarded by the business leaders to which you report.

13.12 Conclusion

It is easy to dedicate a lot of time and energy to strategy formulation while underestimating the barriers to successful strategy implementation. The real work of strategy implementation starts after a meaningful, differentiating, and robust strategy has been formulated. To avoid becoming one of the companies that do not fully reap the benefits of a new strategy, the good practices shown in the table below should be implemented.

Implementation driver	Best practices
Strategy is executable.	Clear right to win and a specific roadmap to gain competitive advantage
Strategy is well communicated.	Communicate a compelling vision with a clear sense of “what’s in it for me” that cascades down through the whole organization.
Strategy is translated into specific strategic goals and action plans.	Strategy is broken down into specific initiatives and action plans to drive execution on an operational level. Establish clear links between what is being asked and why.
Strategy is supported by required resources.	Allocate necessary financial and people resources to fund and drive the envisioned growth outlined in strategy. Derive functional strategies and strategic action plans derived from business-level strategy.
Strategy is linked to corporate budgets and financial performance.	Link strategy to the P&L and balance sheet to translate strategy into tangible performance improvements.
Strategy is owned and driven by leadership.	Leadership role-models new behaviors in support of new strategy and involves and engages all layers of the organization.
Functional strategies are aligned with business-level strategy.	Functional strategies are derived from and in support of overall business-level strategy.
Strategy and culture are aligned.	Strategy implementation works within the current culture and has measures in place to adjust culture in support of new strategy.
Strategy is managed as a change project.	Use systematic change model to manage resistance and change fatigue.
Strategy execution is transparently monitored and measured.	Strategy is measured and monitored quantitatively and qualitatively through a set of relevant metrics, KPIs, and balanced scorecard.

Figure 13.9: Best practices for strategy formulation

Demonstrate Your Knowledge, Skills, and Competence

Use these questions to test your knowledge of the chapter:

1. Explain strategic gap and strategic gap analysis; implementation gap and implementation gap analysis; and performance gap and performance gap analysis. Discuss the role of root cause analysis in conducting gap analyses.
2. Explain the role of strategic goals in strategy implementation. Explain SMART goals, and give an example.
3. Explain the value of allocating sufficient resources to strategy implementation and the risks if this is not accomplished well.
4. Explain the value of broadly communicating and cascading strategy and the risks if this is not accomplished well.
5. Discuss how organizational design supports strategy implementation. Describe the four main types of organizational design, and give an example. Describe the RASCI matrix, span of control, and layering, including their roles in organizational design.
6. Describe organizational control systems and their role in implementing strategy. Give an example of each.
7. Discuss the McKinsey 7-S model and how this gives firms a structure for hardwiring strategy implementation.
8. Explain why strategy implementation needs to be aligned with an organization's culture and the risks if it is not aligned.
9. Discuss Kotter's 8-step change model and how this can support positive change management when implementing strategy.
10. Describe how competence with strategy implementation is relevant and important to you.

You have demonstrated your competence with strategy implementation. Excellent work! You have now fully demonstrated your knowledge, skills, and competence in strategic management. Very well done!

Figure Descriptions

[Figure 13.1](#): Line graph with four straight, increasing lines. x-axis represents time. y-axis represents target amount (e.g., revenue). From top to bottom (largest slope the smallest slope): strategic objective (blue), formulated strategy (green), implemented strategy (orange), strategy results (gray). Strategic objective represents desired improvements. Formulated strategy represents expected improvements based on expected operating conditions. Implemented strategy represents projected improvements based on unchanged operating conditions. Strategy results represents performance. The gap between strategic objective and formulated strategy is labeled strategic gap. The gap between formulated strategy and implemented strategy is labeled implementation gap. The gap between implemented strategy and strategy results is labeled performance gap.

[Figure 13.2](#): Pie chart showing 63% average realized performance and 37% average performance loss with 11 factors listed for the loss. 7.5% inadequate or unavailable resources. 5.2% poorly communicated strategy. 4.5% actions required to execute not clearly defined. 4.1% unclear accountabilities for execution. 3.7% organizational silos and culture blocking execution. 3.0% inadequate performance monitoring. 3.0% inadequate consequences or rewards for failure or success. 3.6% poor senior leadership. 1.9% uncommitted leadership. 0.7% unapproved strategy. 0.7% other obstacles (including inadequate skills and capabilities). This graphic is purple.

[Figure 13.3](#): Organizational chart with CEO and seven departments listed beneath that position: accounting, business IT and cyber security, insurance and business law, human resource management, innovation and technology, marketing and sales, and operations. This graphic is purple.

[Figure 13.4](#): Organizational chart for PepsiCo. At the top is a single box labeled “PepsiCo.” Below, four branches extend to individual boxes labeled “PepsiCo North America,” “PepsiCo International,” “Frito-Lay North America,” and “Quaker Tropicana Gatorade.” Beneath Frito-Lay North America, there are four boxes: sales, marketing, operations, and product and packaging R&D. Beneath Operations, there are two boxes: HQ operations and field operations. Beneath HQ operations there is one box: facility green teams. Beneath field operations there is one box: energy and environment teams. This graphic is purple.

[Figure 13.5](#): Organizational chart. At the top is a box labeled “President” with lines extending downward to five boxes in the second row, which represent vice presidents of different departments: project management, manufacturing, marketing, finance, and engineering. There are three project managers that report to the VP of project management. There are three employees that report to the VPs for each of the other four categories. These employees also report to the project managers. This graphic is purple.

[Figure 13.6](#): Internal environment: training, human resource management, information technology, customer service, marketing and sales, manufacturing, purchasing, and product design. External environment: advocacy groups, competitors, customers, suppliers, and industry regulation. This graphic is purple.

[Figure 13.7](#): Diagram of six interconnected concepts that center around a “Shared value” box. The six concepts are structure, systems, style, staff, skills, and strategy. Shared value: Which of our principles help us? Why do we do what we do in the way we do it? Structure: What structure do we need to execute the strategy? Systems: What business system do we need to use or invent to execute the strategy? Style: What leadership style and cultural qualities will help us to achieve a strategic objective? Staff: How should we help our managers in their growth? Skills: What are the specific skills that will help us? What skills do we need to develop? Strategy: What should we do to solve the specified business problem? Structure: What structure so we need to execute the strategy? This graphic is purple.

[Figure 13.8](#): (1) create urgency, (2) form a powerful coalition, (3) create a vision for change, (4) communicate the vision, (5) empower action, (6) create quick wins, (7) build on the change, (8) make it stick. Steps 1-3 create the climate for change. Steps 4-6 engage and enable the organization. Steps 7-8 implement and sustain the change. This graphic is purple.

Figure References

Figure 13.1: Gap analysis. Kindred Grey. 2025. CC BY. Adapted under fair use from <https://www.ionos.com/startupguide/grow-your-business/gap-analysis>

Figure 13.2: Reasons for failed strategy implementation. Kindred Grey. 2025. CC BY. Adapted under fair use from <https://hbr.org/2005/07/turning-great-strategy-into-great-performance>

Figure 13.3: Functional organizational structure. Kindred Grey. 2025. CC BY.

Figure 13.4: Multidivisional organizational structure. Kindred Grey. 2025. CC BY.

Figure 13.5: Matrix organizational structure. Kindred Grey. 2025. CC BY.

Figure 13.6: Boundaryless organizational structure. Kindred Grey. 2025. CC BY.

Figure 13.7: McKinsey 7-S framework. Kindred Grey. 2025. CC BY.

Figure 13.8: Using Kotter's change management model to implement strategy. Kindred Grey. 2025. CC BY.

APPENDIX 1: ORGANIZATIONAL PERFORMANCE ANALYSIS INSTRUMENT

Use the organizational performance analysis instrument to analyze a firm's (1) mission, purpose, vision, and values, (2) financial position, (3) market position, (4) other quantitative data, and (5) balanced scorecard. You might not analyze all of these in every case analysis, so use the instrument to support the analysis you conduct. The goal is for the instrument to support your analysis, not to complete every element of the instrument.

Mission, Purpose, Vision, and Values

Analyze mission, purpose, vision, and values.

1. Identify whether the information involving mission, purpose, vision, and values is present.
 - a. A mission statement explains why an organization exists, its role in society, and answers the core question "Who are we?"
 - b. A firm's purpose statement articulates its reason for existence beyond just profit-making.
 - c. A vision statement is forward-looking or aspirational statement that captures what a company or organization wants to achieve in the long run.
 - d. Value statements define the core principles that companies stand by and expect their employees to uphold.
2. Place the analysis in the instrument below.

Interpret mission, purpose, vision, and values.

1. Are the mission, purpose, vision, and values effective?
2. Is there a clear line of sight and congruence between and among the mission, purpose, vision, and values?
3. Place the interpretation in the instrument below.

Make recommendations regarding the mission, purpose, vision, and values.

1. If the mission, purpose, vision, and values are not effective or do not have a clear line of sight and congruence between and among them, what actions do you recommend the company take regarding its mission, purpose, vision, and values?
2. Place your recommendations in the instrument below.

Financial Position

Analyze the firm's financial position.

1. Identify the financial measures you use to analyze the firm's financial position.
2. Place the analysis in the instrument below.

Interpret the firm's financial position.

1. What relationships exist in the financial analysis?
2. How does a measure support, explain, or contradict another measure?
3. What bigger picture/forecast does the total analysis give that an individual measure does not?

Evaluate the firm's financial position.

1. How does the information in the analysis and interpretation impact the company?
2. How is the information in the analysis and interpretation relevant to the company?
3. In what ways is the information in the analysis and interpretation important to the company?
4. What are the company's current, potential, or needed assets, organizational capacity, and managerial ability that may support or mitigate the areas of highest impact, relevance, and importance for the firm?
5. Place the evaluation in the instrument below.

Make recommendations regarding the firm's financial position.

1. Based on your analysis, interpretation, and evaluation of the firm's financial position, what actions do you recommend the company take regarding its financial position?
2. Place your recommendations in the instrument below.

Market Position

Analyze the firm's market position.

1. Identify the measures you used to analyze the firm's market position.
2. Place the analysis in the instrument below.

Interpret the firm's market position.

1. What relationships exist in the market analysis?
2. How does a measure support, explain, or contradict another measure?
3. What bigger picture/forecast does the total analysis give that an individual measure does not?

Evaluate the firm's market position.

1. How does the information in the analysis and interpretation impact the company?
2. How is the information in the analysis and interpretation relevant to the company?
3. In what ways is the information in the analysis and interpretation important to the company?
4. What are the company's current, potential, or needed assets, organizational capacity, and managerial ability that may support or mitigate the areas of highest impact, relevance, and importance for the firm?
5. Place the evaluation in the instrument below.

Make recommendations regarding the firm's market position.

1. Based on your analysis, interpretation, and evaluation of the firm's market position, what actions do you recommend the company take regarding its market position?
2. Place your recommendations in the instrument below.

Other Quantitative Measures

Analyze other quantitative measures.

1. Identify the data and measures you used to analyze other quantitative measures.
2. Place the analysis in the instrument below.

Interpret the other quantitative measures.

1. What relationships exist in the other quantitative measures?
2. How does a measure support, explain, or contradict another measure?
3. What bigger picture/forecast does the total analysis give that an individual measure does not?

Evaluate the other quantitative measures.

1. How does the information in the analysis and interpretation impact the company?
2. How is the information in the analysis and interpretation relevant to the company?
3. In what ways is the information in the analysis and interpretation important to the company?
4. What are the company's current, potential, or needed assets, organizational capacity, and managerial ability that may support or mitigate the areas of highest impact, relevance, and importance for the firm?
5. Place the evaluation in the instrument below.

Make recommendations regarding the other quantitative measures.

1. Based on your analysis, interpretation, and evaluation of the firm's measures, what actions do you recommend the company take?
2. Place your recommendations regarding the other quantitative measures in the instrument below.

Balanced Scorecard

Analyze the firm's balanced scorecard.

1. If there is additional information in the balanced scorecard about the firm's financial measures, place this in your analysis of a firm's financial position above. This keeps all the financial analysis together.
2. Analyze the firm's customer measures.
 - a. Customer measures assess how well a company attracts, satisfies, and retains customers. Customer measures include new customer acquisition rates, customer satisfaction scores, and repeat customer percentages.
3. Analyze the firm's internal business process measures.
 - a. Internal business process measures assess organizational efficiency. Internal business process measures include production times, delivery efficiency, and new product development speed.
4. Analyze the firm's learning and growth measures.
 - a. Learning and growth measures assess how an organization can continue to innovate and create future value. Learning and growth measures focus on employee development, innovation capabilities, and adaptation to changing market conditions.
5. Place the analysis in the instrument below.

Interpret the balanced scorecard.

1. What relationships exist in the balanced scorecard?
2. How does a measure support, explain, or contradict another measure?
3. What bigger picture/forecast does the total analysis give that an individual measure does not?
4. Is there clear line of sight and congruence between and among customer, internal business process, and learning and growth measures?

Evaluate the balanced scorecard.

1. How does the information in the analysis and interpretation impact the company?
2. How is the information in the analysis and interpretation relevant to the company?
3. In what ways is the information in the analysis and interpretation important to the company?
4. What are the company's current, potential, or needed assets, organizational capacity, and managerial ability that may support or mitigate the areas of highest impact, relevance, and importance for the firm?
5. Place the evaluation in the instrument below.

Make recommendations regarding the balanced scorecard.

1. Based on your analysis, interpretation, and evaluation of the firm's balanced scorecard, what actions do you recommend the company take?
2. Place your recommendations regarding the balanced scorecard in the instrument below.

Analysis Instrument

Organizational performance

Mission, purpose, vision, and values

Analyze mission, purpose, vision, and values.

Mission:

Purpose:

Vision:

Values:

Interpret mission, purpose, vision, and values.

Interpretation:

Evaluate mission, purpose, vision, and values.

Evaluation:

Make recommendations regarding mission, purpose, vision, and values.

Recommendations:

Financial position

Analyze financial position.

Analysis:

Interpret financial position.

Interpretation:

Evaluate financial position.

Evaluation:

Make recommendations regarding financial position.

Recommendations:

Market position

Analyze market position.

Analysis:

Interpret market position.

Interpretation:

Evaluate market position.

Evaluation:

Make recommendations regarding market position.

Recommendations:

Other quantitative measures

Analyze other quantitative measures.

Analysis:

Organizational performance**Interpret other quantitative measures.**

Interpretation:

Evaluate other quantitative measures.

Evaluation:

Make recommendations regarding other quantitative measures.

Recommendations:

Balanced scorecard**Analyze balanced scorecard.**

Customer measures:

Internal business process measures:

Learning and growth measures:

Interpret balanced scorecard.

Interpretation:

Evaluate balanced scorecard.

Evaluation:

Make recommendations regarding balanced scorecard.

Recommendations:

[Download an editable version of the analysis instrument here.](#)

APPENDIX 2: PESTEL ANALYSIS INSTRUMENT

Identify the industry, market, and market segment.

1. Identify the industry, market, and market segment under analysis.
2. Place this in the instrument.

Analyze data about the general environment.

Analysis is the process and result of examining all the data available for the case and identifying and classifying all the data for each category in a strategic management tool.

1. Methodically and thoroughly examine all the data available from the case about the general environment in relation to each PESTEL factor: political, economic, sociocultural, technological, environmental, and legal.
2. Identify and classify all the data for the general environment that relates to each PESTEL factor.
 - a. The data needs to be specific to the case. (For example: "Governmental regulation of the [industry name] between [date 1 and date 2] results in [the specific impact].")
 - b. The data cannot be too broad. (For example: "Governmental regulation impacts profit" is too broad.)
3. Place the analysis in the instrument below in the section titled "Analysis."

Interpret the analysis.

Interpretation is the process and result of examining the analysis to identify and explain relationships in the analysis and underlying root causes of the situation. Interpretation is not found in the case or company research. Interpretation applies critical thinking to the analysis conducted so far. Answer only those questions that add value to the overall process of working with the PESTEL to analyze the general environment. Interpretation begins to narrow the focus.

1. Examine the analysis of each PESTEL factor: political, economic, sociocultural, technological, environmental, and legal.
2. Identify and explain whether, how, and in what ways the information in the analysis is related.
 - a. How does the analysis in each section of the PESTEL tool relate to each other?
 - i. How do the different political factors relate?
 - ii. How do the different economic factors relate?
 - iii. How do the different sociocultural factors relate?
 - iv. How do the different technological factors relate?
 - v. How do the different environmental factors relate?
 - vi. How do the different legal factors relate?
 - b. How does one factor in the analysis with the PESTEL tool relate to another factor in the analysis? For example, how do the political factors relate to the legal factors? How do the technological and sociocultural factors relate to the environmental factors?
3. Identify and explain underlying root cause(s) of the situation.
 - a. What may be causing the information identified in the analysis?
4. Place the interpretation in the instrument below in the section titled "Interpretation."

Evaluate the analysis and interpretation.

Evaluation is the process and result of examining the analysis and interpretation to identify and explain the meaning of the information to the company; this is achieved by considering the information's impact, relevance, and importance to the company and by identifying the company's current, potential, or needed assets, organizational capacity, and managerial ability that may support or mitigate the areas of highest impact, importance, and relevance for the firm. Like interpretation, evaluation is not found in the case or company research. Evaluation involves applying critical thinking to the analysis and interpretation conducted so far. Answer only those questions that add value to the overall process of working with the PESTEL to analyze the general environment. Evaluation continues to narrow the focus.

1. Examine the analysis and interpretation.
2. Identify and explain whether, how, and in what ways the information in the analysis and interpretation part of the PESTEL analysis instrument impacts the industry and company.
3. Identify and explain whether, how, and in what ways the information in the analysis and interpretation part of the PESTEL analysis instrument is relevant to the industry and the company.
4. Determine in what ways the information in the analysis and interpretation important to the industry and the company.
 - a. Action to take (if helpful): Rank the analysis and interpretation PESTEL analysis instrument according to strength of importance, such as strong, moderate, or weak.
5. Determine the company's current, potential, or needed assets, organizational capacity, and managerial ability that may support or mitigate the areas of highest impact, relevance, and importance for the industry and the firm.
6. Place the evaluation in the instrument below in the section titled "Evaluation."

Recommend action to the firm.

1. Make recommendations to the company to leverage opportunities in the general environment.
2. Make recommendations to the company to mitigate to threats in the general environment.
3. Place the recommendations in the instrument below in the section titled "Recommendations."

Analysis Instrument

PESTEL

Identify the industry, market, and market segment.

The industry is:

The market is:

The market segment is:

Analysis

Political	Economic	Sociocultural	Technological	Environmental	Legal

Interpretation

Answer only those questions that add value to the overall process of working with the PESTEL to analyze the general environment.

1. Identify and explain whether, how, and in what ways the information in the analysis is related.
 - a. How does the analysis in each section of the PESTEL tool relate to the others?
 - i. How do the different political factors relate?
 - ii. How do the different economic factors relate?
 - iii. How do the different sociocultural factors relate?
 - iv. How do the different technological factors relate?
 - v. How do the different environmental factors relate?
 - vi. How do the different legal factors relate?
 - b. How does a factor in the analysis of the PESTEL tool relate to another factor in the analysis of the tool? For example:
 - i. How do the political factors relate to the legal factors?
 - ii. How do the technological and sociocultural factors relate to the environmental factors?
2. Identify and explain underlying root cause(s) of the situation.
 - c. What may be causing the information identified in the analysis?

Interpretation:

Evaluation

Answer only those questions that add value to the overall process of working with the PESTEL to analyze the general environment.

1. How does the information in the analysis and interpretation impact the industry and the company?
2. How is the information in the analysis and interpretation relevant to the industry and the company?
3. How is the information in the analysis and interpretation important to the industry and the company?
4. What are the company's current, potential, or needed assets, organizational capacity, and managerial ability that may support or mitigate the areas of highest impact, relevance, and importance for the industry and the firm?

Evaluation:

Recommendations

1. What do you recommend to the company to leverage opportunities in the general environment?
2. What do you recommend to the company to mitigate threats in the general environment?

Recommendation:

[Download an editable version of the analysis instrument here.](#)

APPENDIX 3: PORTER'S FIVE FORCES ANALYSIS INSTRUMENT

Identify the industry.

1. Identify the industry under analysis.
2. Place this in the instrument.

Analyze data about the industry environment.

Analysis is the process and result of examining all the data available for the firm and identifying and classifying all the data for each category in a strategic management framework.

1. Identify data in the case or from company research that corresponds to each force in the Porter's Five Forces analysis: bargaining power of suppliers, bargaining power of buyers, threat of substitute products, threat of new entrants, and rivalry among existing competitors.
 - a. The data needs to be specific to the case.
 - i. For example: "The threat of [specific supplier] is high because [specific reason it is high]."
 - b. The data needs to avoid being too broad.
 - i. At this stage, avoid "The threat of suppliers is high." You will analyze the strength of each force next.
2. Place the data corresponding to each force in the Porter's Five Forces framework in the instrument below in the subsection titled "Identify Forces" in the "Analysis" section.
3. Rank the strength of each force: strong, moderate, or weak.
 - a. Enter the strength of each force in the instrument below in the subsection titled "Rank Strength" in the "Analysis" section.

Interpret the analysis.

Interpretation is the process and result of examining the analysis to identify and explain relationships in the analysis and underlying root causes of the situation. Interpretation is not found in the case or company research. Interpretation applies critical thinking to the analysis conducted so far. Answer only those questions that add value to the overall process of working with the Porter's Five Forces framework to analyze the industry environment. Interpretation begins to narrow the focus.

1. Identify and explain whether, how, and in what ways the information in the analysis is related.
 - a. How does the analysis within each force of the Porter's Five Forces framework relate to each other?
 - i. How do the different levels of threats of new entrants relate?
 - ii. How do the different levels of threats of substitute products relate?
 - iii. How do the different levels of bargaining power of suppliers relate?
 - iv. How do the different levels of bargaining power of buyers relate?
 - v. What are the patterns and relationships in the rivalries that exist between competitors?
 - b. How does one force in the analysis in the Porter's Five Forces framework relate to another force in the analysis in the Porter's Five Forces framework?
 - i. For example: How do the threat of new entrants and the threat of substitute products relate?
 - ii. For example: How do the bargaining power of suppliers and buyers relate?
 - c. What elements in the Porter's Five Forces analysis were expected?
 - d. What elements in the Porter's Five Forces analysis were unexpected?
 - e. Are there incongruencies between the elements of the analysis in the Porter's Five Forces analysis?

2. Identify and explain underlying root cause(s) of the situation.
 - a. What may be causing the information identified in the analysis?
3. Place the interpretation in the instrument below in the section titled "Interpretation."

Evaluate the analysis and interpretation.

Evaluation is the process and result of examining the analysis and interpretation to identify and explain the meaning of the information to the company by considering its impact, relevance, and importance to the company and by identifying the company's current, potential, or needed assets, organizational capacity, and managerial ability that may support or mitigate the areas of highest impact, importance, and relevance for the firm. Like interpretation, evaluation is not found in the case or company research. Evaluation involves applying critical thinking to the analysis and interpretation conducted so far. Answer only those questions that add value to the overall process of working with the Porter's Five Forces framework to analyze the industry environment. Evaluation continues to narrow the focus.

1. How does the information in the analysis and interpretation impact the company?
2. How is the information in the analysis and interpretation relevant to the company?
3. In what ways is the information in the analysis and interpretation important to the company?
4. What are the company's current, potential, or needed assets, organizational capacity, and managerial ability that may support or mitigate the areas of highest impact, relevance, and importance for the firm?
5. Place the evaluation in the instrument below in the section titled "Evaluation."

Recommend action to the firm.

1. What do you recommend to the company to leverage opportunities in the industry environment?
2. What do you recommend to the company to mitigate threats in the industry environment?
3. Place the recommendation(s) in the table below in the section titled "Recommendations."

Analysis Instrument

Porter's Five Forces

Identify the industry.

The industry is:

Analysis

Forces	Identify forces			Rank strength (strong/moderate/weak)
Bargaining power of suppliers				
Bargaining power of buyers				
Threat of substitute products				
Threat of new entrants				
Rivalry among existing competitors				

Interpretation

Answer only those questions from the "Interpret the Analysis" section above that add value to the overall process of working with the Porter's Five Forces framework to analyze the industry environment.

Interpretation:

Porter's Five Forces**Evaluation**

Answer only those questions from the "Evaluate the Analysis and Interpretation" section above that add value to the overall process of working with the Porter's Five forces framework to analyze the industry environment.

Evaluation:

Recommendations

Answer the two questions above in the instructions under the section titled "Recommend Action to the Firm."

Recommendations:

Porter's Five Forces analysis instrument

[Download an editable version of the analysis instrument here.](#)

APPENDIX 4: STRATEGIC GROUP MAPPING ANALYSIS INSTRUMENT

Identify the industry, market, and market segment.

1. Identify the industry, market, and market segment under analysis.
2. Place this in the instrument.

Analyze data about the strategic group.

Analysis is the process and result of examining all the data available for the case and identifying and classifying all the data for each category in a strategic management framework.

Create a strategic map.

1. Identify the most important dimensions that characterize the strategic groups. These are company commitments that are both difficult and costly to reverse, including but not limited to research and development investment, the use of technology and technology innovation, product differentiation, distribution channels, and even customer service. This varies by industry.
2. From this list of the most important dimensions that characterize the strategic groups, choose two dimensions.
3. Map these two dimensions. Use the x-axis (horizontal) for one dimension, with low on the left and high on the right. Use the y-axis (vertical) for the other dimension, with low at the bottom and high at the top. Price and product line are dimensions that are commonly paired on x- and y-axes.
4. Graph the firms in the strategic group considering these two dimensions using bubbles.
5. Indicate the market share of each firm through the size and shape of its bubble.
6. The map in the instrument below is for illustrative purposes. Choose the two dimensions, and add the number and size of company bubbles as indicated by the analysis.

Interpret the analysis.

Interpretation is the process and result of examining the analysis to identify and explain relationships in the analysis and underlying root causes of the situation. Interpretation is not found in the case or company research. Interpretation applies critical thinking to the analysis conducted so far. Answer only those questions that add value to the overall process of working with the strategic group framework to analyze the strategic group. Interpretation begins to narrow the focus.

1. Examine the analysis in the strategic group map.
2. Identify and explain whether, how, and in what ways the information in the analysis is related.
3. Identify and explain underlying root cause(s) of the situation.
 - a. What may be causing the information identified in the analysis?
4. Place the interpretation in the instrument below in the section titled "Interpretation."

Evaluate the analysis and interpretation.

Evaluation is the process and result of examining the analysis and interpretation to identify and explain the meaning of the information to the company by considering its impact, relevance, and importance to the company and by identifying the company's current, potential, or needed assets, organizational capacity, and managerial ability that may support or mitigate the areas of highest

impact, importance, and relevance for the firm. Like interpretation, evaluation is not found in the case or company research. Evaluation involves applying critical thinking to the analysis and interpretation conducted so far. Answer only those questions that add value to the overall process of working with the strategic group framework to analyze the strategic group. Evaluation continues to narrow the focus.

1. Examine the analysis and interpretation.
2. Identify and explain how the information in the analysis and interpretation impacts the company.
3. Identify and explain how the information in the analysis and interpretation is relevant to the company.
4. Determine in what ways the information in the analysis and interpretation is important to the company.
5. Determine the company's current, potential, or needed assets, organizational capacity, and managerial ability that may support or mitigate the areas of highest impact, relevance, and importance for the firm.
6. Place the evaluation in the instrument below in the section titled "Evaluation."

Recommend action to the firm.

1. Make recommendations to the company to leverage opportunities in the strategic group.
2. Make recommendations to the company to mitigate threats in the strategic group.
3. Place the recommendations in the table below in the section titled "Recommendations."

Analysis Instrument

Strategic group mapping

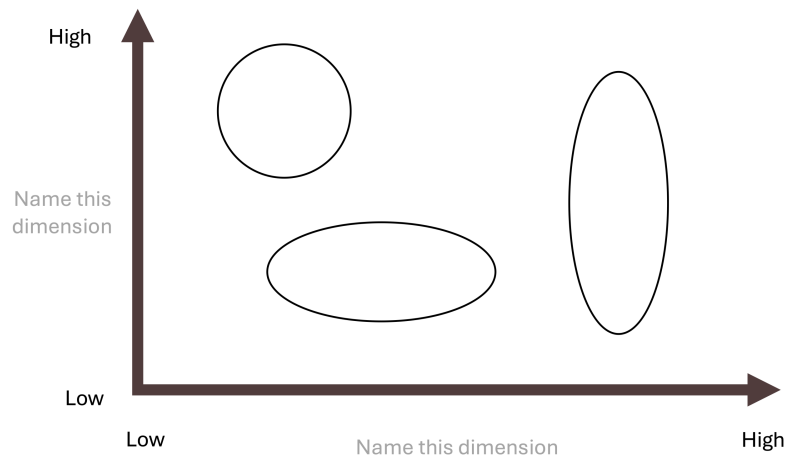
Identify the industry, market, and market segment.

The industry is:

The market is:

The market segment is:

Analysis



Interpretation

Answer only those questions in the “Interpret the Analysis” section above that add value to the overall process of working with the strategic group to analyze the competitive environment.

Interpretation:

Evaluation

Answer only those questions in the “Evaluate the Analysis and Interpretation” section above that add value to the overall process of working with the strategic group to analyze the competitive environment.

Evaluation:

Recommendations

1. What do you recommend to the company to leverage opportunities in the industry environment?
2. What do you recommend to the company to mitigate threats in the industry environment?

Recommendations:

[Download an editable version of the analysis instrument here.](#)

APPENDIX 5: VRIO ANALYSIS INSTRUMENT

Identify the industry, market, and market segment.

1. Identify the industry, market, and market segment under analysis.
2. Place this in the instrument.

Analyze data about the internal environment of the firm.

Analysis is the process and result of examining all the data available for the case and identifying and classifying all the data for each category in a strategic management framework.

1. Methodically and thoroughly examine all the data available from the case about the internal environment.
2. Identify resources, capabilities, and core competencies of the company.
3. Place them in the instrument below in the lefthand column titled “Resource, capability, or core competency.”
4. Analyze whether each resource, capability, or core competency is valuable, rare, costly to imitate, and organized to capture value.
 - a. Complete the table from left to right for each resource, capability, or core competency listed.
 - b. Remember that the VRIO framework is a flowchart.
 - c. Stop your assessment when the resource, capability, or core competency is not valuable, not rare, or not costly to imitate. Once you have answered “no,” move on to the next.
 - d. Place your analysis for each resource, capability, or core competency in the instrument below.
5. When you have completed the analysis of whether each resource, capability, or competency is valuable, rare, costly to imitate, and organized to capture value, determine the competitive implication for the firm.
 - a. Competitive disadvantage (Not valuable → STOP)
 - b. Competitive parity (Valuable → Not rare → STOP)
 - c. Temporary competitive advantage (Valuable → Rare → Not costly to imitate → STOP)
 - d. Unused competitive advantage (Valuable → Rare → Costly to imitate → Not organized to capture value → STOP)
 - e. Sustainable competitive advantage (Valuable → Rare → Costly → Organized to capture value)
6. Place the correct level of competitive advantage in the final column on the right titled “Competitive implication.”

Interpret the analysis.

Interpretation is the process and result of examining the analysis to identify and explain relationships in the analysis and underlying root causes of the situation. Interpretation is not found in the case or company research. Interpretation applies critical thinking to the analysis conducted so far. Answer only those questions that add value to the overall process of working with the VRIO to analyze the internal environment of the firm. Interpretation begins to narrow the focus.

1. Examine the analysis of resources, capabilities, and core competencies.
2. Identify and explain whether, how, and in what ways the information in the analysis is related.
3. Identify and explain underlying root cause(s) of the situation.
 - a. What may be causing the information identified in the analysis?
4. Place the interpretation in the instrument below in the section titled “Interpretation.”

Evaluate the analysis and interpretation.

Evaluation is the process and result of examining the analysis and interpretation to identify and explain the meaning of the information to the company by considering its impact, relevance, and importance to the company and by identifying the company's current, potential, or needed assets, organizational capacity, and managerial ability that may support or mitigate the areas of highest impact, importance, and relevance for the firm. Like interpretation, evaluation is not found in the case or company research. Evaluation applies critical thinking to the analysis and interpretation conducted so far. Answer only those questions that add value to the overall process of working with the VRIO to analyze the internal environment of the firm. Evaluation continues to narrow the focus.

1. Examine the analysis and interpretation.
2. Identify and explain whether, how, and in what ways the information in the analysis and interpretation impacts the company.
3. Identify and explain whether, how, and in what ways the information in the analysis and interpretation is relevant to the company.
4. Determine in what ways the information in the analysis and interpretation is important to the company.
5. Determine the company's current, potential, or needed assets, organizational capacity, and managerial ability that may support or mitigate the areas of highest impact, relevance, and importance for the firm.
6. Place the interpretation in the instrument below in the section titled "Interpretation."

Recommend action to the firm.

1. Make recommendations to the company to leverage strengths identified in the VRIO analysis.
2. Make recommendations to the company to build its strategy around resources, capabilities, or core competencies that provide a sustainable competitive advantage.
3. Place the recommendations in the instrument below in the section titled "Recommendations."

Analysis Instrument

VRIO

Identify the industry, market, and market segment.

The industry is:

The market is:

The market segment is:

Analysis

Resource, capability, or core competency	Valuable	Rare	Costly to imitate	Organized to capture value	Competitive implication

Interpretation

1. How is the information in the analysis related?
2. What may be causing the information identified in the analysis?

Interpretation:

Evaluation

Answer only those questions that add value to the overall process of working with the VRIO framework to analyze the internal environment of a firm.

1. How does the information in the analysis and interpretation impact the company?
2. How is the information in the analysis and interpretation relevant to the company?
3. In what ways is the information in the analysis and interpretation important to the company?
4. What are the company's current, potential, or needed assets, organizational capacity, and managerial ability that may support or mitigate the areas of highest impact, relevance, and importance for the firm?

Evaluation:

Recommendations

1. What do you recommend to the company to leverage strengths identified in the VRIO analysis?
2. What do you recommend to the company to build its strategy around resources, capabilities, or core competencies that provide a sustainable competitive advantage?

Recommendations:

[Download an editable version of the analysis instrument here.](#)

APPENDIX 6: VALUE CHAIN ANALYSIS INSTRUMENT

Identify the industry, market, and market segment.

1. Identify the industry, market, and market segment under analysis.
2. Place this in the instrument.

Analyze data about the internal environment of the firm.

Analysis is the process and result of examining all the data available for the case and identifying and classifying all the data for each category in a strategic management framework.

1. Methodically and thoroughly examine all the data available from the case about the internal environment.
2. Identify firm-specific primary and support activities that make the firm unique and that have the potential to provide a competitive advantage or competitive disadvantage.
3. Place them in the instrument below in the lefthand column titled "Value chain activities."
4. Analyze whether each firm-specific activity is a strength that may provide a competitive advantage or a weakness that may lead to a competitive disadvantage.
5. For each activity, analyze and state the reasons why it is a strength or weakness for the firm. Please note that it is possible that there are different specific activities within one area of a primary or support activity that can be a strength and a weakness. For example, within the procurement activity, a strong buying power can be a strength for a firm, whereas the use of technology in procurement or partnerships with key suppliers may be a weakness. An example for the human resource management activity could be that the firm is great at attracting new talent, which is a key strength; however, the firm may perform poorly at retaining diverse talent, which would be a weakness. Hence, it is important to analyze specific elements of the business function/activity to come to a value-adding assessment of the firm's strengths and weaknesses.
6. Place the analysis in the instrument below in the columns titled "Strengths" and "Weaknesses."

Interpret the analysis.

Interpretation is the process and result of examining the analysis to identify and explain relationships in the analysis and underlying root causes of the situation. Interpretation is not found in the company research. Interpretation applies critical thinking to the analysis conducted so far. Answer only those questions that add value to the overall process of working with the value chain analysis tool to analyze the internal environment of the firm. Interpretation begins to narrow the focus.

1. Examine the analysis of each firm-specific primary and support activity.
2. Identify and explain whether, how, and in what ways the information in the analysis is related.
3. Identify and explain underlying root causes of the situation.
 - a. What may be causing the information identified in the analysis?
4. Place the interpretation in the instrument below in the section titled "Interpretation."

Evaluate the analysis and interpretation.

Evaluation is the process and result of examining the analysis and interpretation to identify and explain the meaning of the information to the company by considering its impact, relevance, and importance to the company and by identifying the company's current, potential, or needed assets, organizational capacity, and managerial ability that may support or mitigate the areas of highest

impact, importance, and relevance for the firm. Like interpretation, evaluation is not found in the company research. Evaluation applies critical thinking to the analysis and interpretation conducted so far. Answer only those questions that add value to the overall process of working with the value chain analysis to analyze the internal environment of the firm. Evaluation continues to narrow the focus.

1. Examine the analysis and interpretation.
2. Identify and explain whether, how, and in what ways the information in the analysis and interpretation impacts the company.
3. Identify and explain whether, how, and in what ways the information in the analysis and interpretation is relevant to the company.
4. Determine in what ways the information in the analysis and interpretation is important to the company.
5. Determine the company's current, potential, or needed assets, organizational capacity, and managerial ability that may support or mitigate the areas of highest impact, relevance, and importance for the firm.
6. Place the interpretation in the instrument below in the section titled "Interpretation."

Recommend action to the firm.

1. Make recommendations to the company to leverage strengths in the value chain to drive competitive differentiation and to win in the market.
2. Make recommendations to the company to address weaknesses in the value chain that negatively impact the firm's ability to win in the market.
3. Make recommendations to the company to take costs out of value chain activities to improve its cost structure.
4. Make recommendations to the company to increase the value contribution to customers in different value chain activities in support of competitive differentiation as well as meeting and exceeding customer expectations.
5. Make recommendations to the company to shift resources from non-key value chain activities to key value chain activities that are critical for the buying decisions of the firm's customers.
6. Make recommendations to the company to outsource value chain activities that are not key to the firm and that can be better provided by specialized third-party providers.
7. Place the recommendations in the instrument below in the section titled "Recommendations."

Analysis Instrument

Value chain		
Identify the industry, market, and market segment.		
The industry is: The market is: The market segment is:		
Value chain activities	Strengths	Weaknesses
Primary activities		
Inbound logistics - Sustainable global supply chains - Efficient warehousing - Robust and reliable logistics - Just-in-time delivery - Efficient inventory management		
Operations - Lean processes - Reliable, safe, and efficient manufacturing - Robust quality control - Economies of scale - Positive experience curve effects		
Outbound logistics - Reliable and cost-effective delivery - Appropriate locations and network of warehouses - Customer-centric design of supply chain and logistics		
Marketing and sales - Excellence in pricing and margin management - Effective communication policies (including use of social media, search engine optimization advertising, direct sales, etc.) - Professional sales channel strategy and distribution management - Omnichannel strategy (if appropriate) - Robust product portfolio management		
Service - Customer-centric customer service - Quick response time - Use of data analytics - Two-way communication with customers		
Secondary activities		
Firm infrastructure - Corporate functions like finance, IT, legal, business development, etc. add value to the business - Business functions in firm infrastructure are at best-practice level - Appropriate corporate governance - The firm's headquarters adds value to the strategic business units and business divisions		
Human resource management - Ability to attract and retain talent - Diverse workforce and inclusive corporate culture - Strong performance culture - Compensation and benefits systems in support of talent and corporate strategy - Data-driven approach with use of HRIS (human resource information systems)		

Value chain

Technology, research, & development and innovation management

- Strong innovation culture
- Customer-centric approach to innovation ideation process
- Clearly defined innovation process
- Open innovation with the input of external partners like suppliers, customers, and universities
- Transparent measuring of the return on investment through meaningful KPI and metrics and an innovation scorecard
- Efficient management of IP to protect the outcome of the firm's innovation output
- Strength of innovation pipeline

Procurement

- Use of purchasing power of the firm
- Leverage opportunities for global sourcing
- Value-adding strategic partnerships with key suppliers
- Diversity and sustainable sourcing as part of ESG strategies (see Chapter 10)
- Design sourcing with reliable, high-quality supply at low prices

Interpretation

Answer only those questions that add value to the overall process of working with the value chain analysis instrument to analyze the internal environment of a firm.

1. How is the information in the analysis related?
2. What may be causing the information identified in the analysis?

Interpretation:

Evaluation

Answer only those questions that add value to the overall process of working with the value chain analysis instrument to analyze the internal environment of a firm.

1. How does the information in the analysis and interpretation impact the company?
2. How is the information in the analysis and interpretation relevant to the company?
3. In what ways is the information in the analysis and interpretation important to the company?
4. What are the company's current, potential, or needed assets, organizational capacity, and managerial ability that may support or mitigate the areas of highest impact, relevance, and importance for the firm?

Evaluation:

Recommendations

1. What do you recommend to the company to leverage strengths in the value chain to drive competitive differentiation and to win in the market?
2. What do you recommend to the company to address weaknesses in the value chain that negatively impact the firm's ability to win in the market?
3. What do you recommend to the company to take costs out of value chain activities to improve its cost structure?
4. What do you recommend to the company to increase the value contribution to customers in different value chain activities in support of competitive differentiation as well as meeting and exceeding customer expectations?
5. What do you recommend to the company to shift resources from non-key value chain activities to key value chain activities that are critical for the buying decisions of the firm's customers?
6. What do you recommend to the company to outsource value chain activities that are not key to the firm and that can be better provided by specialized third-party providers?

Recommendations:

[Download an editable version of the analysis instrument here.](#)

APPENDIX 7: CAGE DISTANCE FRAMEWORK ANALYSIS INSTRUMENT

Analysis Instrument

CAGE dimension	Describe distance	Quantify distance (high/medium/low)	Describe distance	Quantify distance (high/medium/low)	Describe distance	Quantify distance (high/medium/low)
	Country 1:		Country 2:		Country 3:	
Cultural distance						
Administrative distance						
Geographic distance						
Economic distance						
Recommendations						

CAGE distance framework analysis instrument

[Download an editable version of the analysis instrument here.](#)

Example

CAGE dimension	Describe distance	Quantify distance (high/medium/low)	Describe distance	Quantify distance (high/medium/low)	Describe distance	Quantify distance (high/medium/low)
	Country 1: Bangladesh		Country 2: Ghana		Country 3: Brazil	
Cultural distance	Language: The official language is Bengali. While English is used in business and education, language barriers can still exist due to accents and regional dialects. Religion: Bangladesh is predominantly Muslim (about 90%), whereas the U.S. has a Christian majority. Religious differences can influence business practices and consumer behavior. Societal norms: Bangladesh has a collectivist culture, emphasizing group goals over individual desires. The U.S., conversely, values individualism. Power distance: Bangladesh has a higher acceptance of hierarchical structures, which can affect organizational dynamics and negotiations.	High	Language: English is the official language, minimizing language barriers. Religion: Ghana is predominantly Christian (over 70%), like the U.S., which can ease cultural integration. Societal norms: Ghanaian culture leans toward collectivism, valuing community and family ties. Communication styles: Indirect communication is common, which may differ from the direct approach typical in the U.S.	Medium	Language: Portuguese is the official language. While English proficiency is increasing, language barriers can still exist. Religion: Brazil is predominantly Christian (mostly Catholic), like the U.S., aiding cultural affinity. Societal norms: Brazilian culture balances individualism and collectivism, with strong emphasis on relationships and networks. Business etiquette: Personal relationships are crucial in business dealings, and negotiations may take longer.	Medium
Administrative distance	Political system: Bangladesh is a parliamentary democracy but has faced political instability. The U.S. is a stable federal presidential republic. Legal framework: The Bangladeshi legal system is less developed, with challenges in contract enforcement and intellectual property protection. Corruption and bureaucracy: Higher levels of corruption and bureaucratic red tape can hinder business operations.	High	Political system: Ghana is a stable presidential democracy with a history of peaceful transitions of power. Legal system: Ghana's system is based on English common law, which aligns somewhat with the U.S. legal framework. Regulatory environment: Efforts have been made to reduce corruption, but bureaucratic hurdles still exist. Trade agreements: Ghana is part of the Economic Community of West African States (ECOWAS), which may affect trade dynamics.	Medium	Political system: Brazil features a federal presidential republic, like the U.S., but has faced political scandals and instability. Legal system: Its legal system is based on civil law, which differs from the U.S. common law system, potentially affecting legal proceedings. Regulatory environment: Brazil is notorious for complex tax systems and bureaucratic procedures. Trade policies: Its membership in MERCOSUR means it has its own trade regulations and tariffs.	Medium

CAGE dimension	Describe distance	Quantify distance (high/medium/low)	Describe distance	Quantify distance (high/medium/low)	Describe distance	Quantify distance (high/medium/low)
Geographic distance	Physical distance: Approximately 12,500 km (7,770 mi) separate the U.S. and Bangladesh, leading to longer shipping times and higher transportation costs. Time zone difference: Bangladesh is 10-11 hours ahead of Eastern Standard Time, complicating real-time communication. Infrastructure: Underdeveloped transportation and communication infrastructure can pose logistical challenges. Climate and environmental factors: Bangladesh is prone to natural disasters like floods and cyclones, which can disrupt business activities.	High	Physical distance: It is located approximately 8,500 km (5,280 mi) from the U.S., affecting logistics and transportation costs. Time zone difference: Ghana is five hours ahead of Eastern Standard Time. Infrastructure: Developing infrastructure has shown improvements in ports and roads, but gaps remain. Climate: The tropical climate has potential for seasonal disruptions.	High	Physical distance: Brazil is closer to the U.S. than the other two countries, approximately 7,000 km (4,350 mi). Time zone overlap: Time zones partially overlap with the U.S., facilitating communication. Infrastructure: Brazil offers more developed infrastructure, including ports, roads, and telecommunications. Climate: The climate is diverse like the U.S., ranging from tropical to temperate zones.	Low
Economic distance	Economic development: Bangladesh is a lower-middle-income country with a GDP per capita significantly lower than the U.S. Market size and growth: With a large population exceeding 160 million, it offers a sizable market but with lower purchasing power. Industrial focus: The economy relies heavily on the textile and garment industry. Labor costs: Lower labor costs present opportunities for cost-effective manufacturing.	High	Economic development: Ghana is a lower-middle-income country with growing GDP but lower per capita income than the U.S. Market potential: The emerging market features a growing middle class and increasing consumer demand. Natural resources: It is rich in minerals, oil, and agricultural products. Labor market: Ghana offers a young workforce with relatively low labor costs.	High	Economic development: Upper-middle-income country with a sizable economy but lower GDP per capita than the U.S. Market size: Large population of over 210 million, with significant consumer market potential. Industry diversity: The diverse economy includes strong agriculture, manufacturing, and service sectors. Labor market: Brazil's labor costs are higher compared to Bangladesh and Ghana but still competitive.	Medium
Recommendations	Bangladesh presents the greatest distances in all categories. While the large population and low labor costs are attractive for manufacturing, the significant cultural, administrative, and geographic distances, along with infrastructural challenges, make it a more complex market for U.S. businesses to navigate.		Ghana poses moderate challenges. The shared language and political stability reduce some barriers, but economic and infrastructural limitations require careful consideration.		Brazil presents the least distance across all dimensions, making it the most accessible market among the three for U.S. businesses. The cultural similarities, closer geographic proximity, and larger, more developed economy offer favorable conditions for market entry.	

[Download an editable version of the example analysis instrument here.](#)

GLOSSARY

50-50 joint venture

A 50-50 joint venture is when two parent companies establish a new shared entity, a child company, and each parent company owns 50 percent of the child company.

acquisition

An acquisition is the process in which one company purchases and takes control of another company, integrating its assets, operations, and management into the acquiring business.

administrative law

Administrative law is made by U.S. federal executive governmental agencies and forms the basis of federal regulations, many of which impact businesses.

analysis

Analysis is the process and result of examining all the data available for the firm and identifying and classifying all the data for each category in a strategic management tool.

analytical framework

An analytical framework provides a structured format for analyzing data.

architectural innovation

Architectural innovation involves the reconfiguration of existing technologies into new forms and the creation of products that open up entirely new markets.

average accounts receivable

The average amount of money owed to a company by its customers over a period, calculated by averaging the beginning and ending accounts receivable balances.

Example: If a company's beginning accounts receivables \$30,000 and its ending accounts receivable is \$50,000, the average accounts receivable would be $(\$30,000 + \$50,000)/2 = \$40,000$.

average inventory

The typical amount of inventory a company holds over a period, calculated by averaging the beginning and ending inventories for that period.

Example: If a company's beginning inventory is \$50,000 and its ending inventory is \$70,000, the average inventory would be $(\$50,000 + \$70,000)/2 = \$60,000$.

backward vertical integration

Backward vertical integration occurs when a firm moves back along the industry value chain and enters a supplier's business.

balanced scorecard

Balanced scorecard is a management system that evaluates a company using four measures: financial measures, customer measures, internal business processes measures, and employee learning and growth measures.

best-cost strategy

Best-cost strategy is a hybrid business-level strategy that combines elements of both cost leadership and differentiation in an existing market or market segment.

blue ocean strategy

A blue ocean business-level strategy is a combination of cost leadership and differentiation with the goal of market creation. The core element of the blue ocean strategy is to create uncontested market space and ideally make competition irrelevant.

broad approach to strategic market size

Broad approaches to strategic market size target large markets.

broad cost leadership strategy

A broad cost leadership strategy is a business-level strategy that combines a broad strategic market size and a cost leadership strategic market position. Most people within the market buy the product or service, and those customers are price-sensitive customers.

broad differentiation strategy

A broad differentiation strategy is a business-level strategy that combines a broad strategic market size and a differentiation strategic market position. Most consumers within the market buy the product or service, and those customers want a quality product.

business

A business is a single company within an industry or an organization in the private sector that is engaged in commerce and aims to make a profit.

business ethics strategies

Business ethics strategies are strategies embedded into business-level strategies at the strategic business unit level that include a company's approach to increasing ethical behavior and focus the firm on remaining legally compliant.

business functions

Business functions include essential areas of business, such as accounting, business information technology, business law, finance, human resource management, marketing and sales, supply chain management, operations, and procurement.

business integration

Business integration is the process of combining different components of a business into a unified and cohesive operation.

business portfolio

A business portfolio consists of all the products and services a firm sells, all the business it conducts, and all the market segments, markets, and industries in which it participates.

business support units

Business support units focus on specific business functions, such as accounting, business information technology, business law, finance, human resource management, marketing and sales, supply chain management, operations, and procurement.

business-level strategy

Business-level strategy focuses on how to compete within an organization's chosen market and market segments to create and sustain competitive advantage. Business-level strategy addresses a firm's strategic market position (whether it chooses a cost leadership or differentiation approach) and its strategic market size (whether it competes in a focused market segment or a broad market).

capabilities

Capabilities refer to the organizational and managerial abilities to orchestrate a diverse set of resources and deploy them strategically, driving competitive differentiation and adding value to customers.

case analysis

Case analysis is an umbrella term that means applying strategic management concepts and theories alongside analytical frameworks and tools to analyze, interpret, and evaluate company information through a written scenario that uses real or hypothetical data about a company, by researching a company, or by working directly with a company through a consultancy project.

cases

Cases are written scenarios about companies that present real business issues faced by firms. Cases may also be written scenarios about hypothetical companies that use realistic but hypothetical data about the organizations.

change management

A systematic management process for guiding an organization through change, which involves assessing its change readiness as well as planning, implementing, and sustaining change.

climate change

Long-term shifts in temperatures and weather patterns. These shifts may be natural, but since the 1800s, human activities have been the main driver of climate change, primarily due to the burning of fossil fuels (like coal, oil, and gas), which produces greenhouse gases that act as heat-trapping gases.

company

Organization in the private sector that is engaged in commerce and aims to make a profit.

competitive advantage

Competitive advantage refers to the unique characteristics and capabilities of a firm that allow it to outperform its competitors in economic value creation.

competitive environment

The competitive environment of a firm consists of companies that pursue similar strategies in the same industry.

competitor

A competitor is a business within the same industry that offers similar products or services and competes for customers.

concepts

Concepts are ideas. A collection of concepts is referred to as a theory.

congruence

Congruence means there is a one-to-one relationship between two or more things. In case analysis, it refers to one-to-one reconciliation between steps in the case analysis process or across an entire strategic analysis.

core competencies

Core competencies are unique strengths, embedded deep within a firm, that allow the firm to differentiate its products and services from those of its rivals, creating higher value for the customer or offering products and services of comparable value at lower cost.

corporate governance

Corporate governance refers to the system of rules, practices, and processes by which a company is directed, managed, and controlled.

corporate social responsibility

Corporate social responsibility is the idea that a business has a responsibility to the society in which it operates.

corporate-level strategy

Corporate-level strategy is a companywide strategy that focuses on creating and maintaining a firm's competitive advantage by creating synergy within and between multiple industries, markets, market segments, and businesses across multiple industry value chains and in different geographical locations.

cost leadership

Cost leadership is a strategic market position that focuses on consumer preferences for low-cost alternatives. A company deploying this position competes primarily by being the lowest-cost producer or provider in its chosen market. The goal is to offer products or services that are of an equal or similar value to competitors' products or services at lower prices than competitors.

cost of goods sold (COGS)

The cost of goods sold represents the direct costs of producing goods sold by a company, including materials and labor directly involved in production.

Example 1: For a bakery, COGS includes the cost of flour, sugar, and wages for the bakers.

Example 2: If a company manufactures bicycles, its COGS would include expenses for materials, labor, and manufacturing over-head used to produce the bicycles sold.

current assets

Current assets are expected to be converted into cash or used within one year, such as cash in a company's bank account.

current liabilities

Obligations or debts a company must pay within one year, such as accounts payable, which represents money owed to suppliers.

customer measures

Customer measures on a balanced scorecard evaluate how well a company attracts, satisfies, and retains customers. Customer measures include new customer acquisition rates, customer satisfaction scores, and repeat customer percentages.

data

Data is the information in the case being reviewed, in the company being researched, or in the company receiving consulting services.

data governance

Data governance encompasses the policies, processes, roles, metrics, and standards that ensure data is used ethically, effectively, and efficiently.

delaying

Delaying is the reduction of hierarchical levels in a company.

deliberate strategy

A deliberate strategy is the strategy a firm implements as a planned response to alter, but not completely change, an intended strategy in the face of dynamic conditions.

differentiation

Differentiation is a strategic market position that focuses on consumer preferences for high-quality products. The company competes primarily by offering products that are notably unique from others in its chosen market in terms of quality.

digital transformation

Digital transformation uses existing or new digital technologies to address evolving market conditions and customer expectations.

disruptive innovation

Disruptive innovation occurs when a smaller company with limited resources challenges an established incumbent firm by entering an existing market with a new technology at a lower tier and gradually moving up.

diversification

Diversification refers to how a company simultaneously deals with different products and services in different multiple industries, markets, market segments, and businesses.

divestment

Divestment is selling an unprofitable business or product line.

dominant business firm

A dominant business firm derives between 70 percent and 95 percent of its revenues from one business.

dynamic capability

Dynamic capability refers to an organization's ability to use its existing resources continually in creating new core competencies and enhancing, upgrading, and improving existing capabilities to satisfy customers and beat competition.

earnings per share

Earnings per share is a metric that reflects how much profit is attributable to each share of stock, which is crucial for assessing a company's value from an investor's perspective.

economies of scale

Economies of scale are created when the costs of offering goods and services decrease as firms sell more, distributing expenses across a greater number of items.

efficiency ratio

Efficiency ratios assess how well an organization or individual manages resources. High efficiency means getting more out of assets, while low efficiency indicates waste or poor resource management.

emergent strategy

An emergent strategy is a completely new and unplanned strategy that is formulated in response to unexpected circumstances, which most often originate from a firm's external environment. An emergent strategy is completely different than the intended strategy and requires a change of strategic direction.

entrepreneurial orientation (EO)

Entrepreneurial orientation is a firm's strategic posture, characterized by innovation, proactiveness, and risk-taking.

environmental, social, and governance (ESG)

A business model and strategy that simultaneously emphasizes financial performance and environmental, social, and governance performance. Investors use ESG frameworks to assess a company's sustainability efforts and societal impact.

equity strategic alliance

An equity strategic alliance is created when one company contracts with another company to purchase a certain equity percentage of the other company.

evaluation

Evaluation is the process and result of examining the analysis and interpretation to identify and explain the meaning of the information to the company by considering its impact, relevance, and importance to the company and by identifying the company's current, potential, or needed assets, organizational capacity, and managerial ability that may support or mitigate the areas of highest impact, relevance, and importance for the firm.

exporting

Exporting occurs when a company produces goods and sells them in foreign markets.

external environment

The external environment includes everything outside a company that influences its ability to create and sustain a competitive advantage.

fast follower

A fast follower is a firm that enters the market immediately after the first mover.

fighting brand

A lower-end product introduced specifically to protect a firm's market share without devaluing its primary brand.

firm

Organization in the private sector that is engaged in commerce and aims to make a profit.

first mover

A first mover is a company that enters a new market or launches a new product before any competitors, aiming to establish an early advantage.

focused approach to strategic market size

Focused approaches to strategic market size target specific, niche market segments.

focused cost leadership

A focused cost leadership strategy is a business-level strategy that combines a narrow strategic market size and a cost leadership strategic market position. Few consumers within the market buy the product or service, and those customers are price-sensitive customers.

focused differentiation

A focused differentiation strategy is a business-level strategy that combines a narrow strategic market size and a differentiation strategic market position. Few customers within the market buy the product or service, and those customers want a quality product.

foothold

A foothold is a small entry point that a company creates in an unfamiliar market.

foreign direct investment (FDI)

FDI refers to a company investing in a business in another country.

forward vertical integration

Forward vertical integration occurs when a company moves further forward along the supply chain or industry value chain and enters a buyer's business.

franchising

Franchising is an entry mode in which a company (the franchisor) grants a foreign partner (the franchisee) the right to use its proprietary business assets (e.g., products, brand, knowledge) in exchange for fees and ongoing royalties.

functional-level strategy

Functional-level strategy focuses on implementing strategy in business support units.

general environment

The general environment is the broadest level of a firm's external environment and includes societal events and trends that impact all firms in an industry. Sometimes the general environment may be referred to as the macro environment.

geographical scope

Geographical scope refers to the region or location in which firms provide their products and services.

global strategy

A global strategy combines a high responsiveness to global integration pressures with a low responsiveness to local preferences. Global strategy occurs when a company standardizes its products, services, and operations across all international markets to achieve efficiency and consistency.

global warming

Global warming is a broad term used to refer to the increase in the planet's overall average temperature in recent decades. Global warming is part of climate change and is driven by greenhouse gases (GHGs), particularly carbon dioxide (CO₂).

greenfield investment

When a company builds its operations from scratch in the foreign market, allowing for complete customization and control of the new facility.

greenhouse effect

The greenhouse effect occurs when the earth absorbs the sun's energy or when atmospheric gases prevent heat released by the earth from radiating into space.

gross profit

Gross profit refers to the revenue remaining after subtracting the cost of goods sold (COGS). It shows how much a company earns from its core operations before other expenses.

Example: If a company earns \$100,000 in sales and its COGS is \$60,000, the gross profit is \$40,000.

holding company

A holding company is a company whose primary business is holding a controlling interest in the securities of other companies. A holding company usually does not produce goods or services itself, instead owning stock of other companies to form a corporate group.

horizontal integration

Horizontal integration is a business expansion strategy that focuses on relationships with another company in the same business line.

implementation gap

Implementation gap is the difference between the formulated and implemented strategy.

implementation gap analysis

Implementation gap analysis analyzes the difference between the formulated and implemented strategy.

incremental innovation

Incremental innovations make improvements on existing product or service and target the existing market.

industry

Industry is a group of organizations, businesses, companies, or firms that offer similar products and services and compete in the marketplace for profit.

Industry 4.0

Industry 4.0 refers to the current trend of digital transformation in industrial application, enabling real-time decision-making and enhancing productivity, flexibility, and agility to revolutionize the way companies manufacture, improve, and distribute their products. It is the next phase in the digitization of the manufacturing sector, driven by disruptive trends including the rise of data and connectivity, analytics, human-machine interaction, and automation and robotics.

industry environment

The industry environment of a firm consists of the forces that exert influence and pressure over the entire industry in which a firm functions.

industry value chain

An industry value chain is a model that considers the ways a firm adds value to each step or node in the production process.

industry value chain analysis

An industry value chain analysis examines the production stages, from raw material procurement to the delivery of the final product, with emphasis on value creation.

innovation strategies

Innovation strategies are strategies that are embedded into business-level strategies at the strategic business unit level that focus a firm's approach to innovation so that it can create and sustain a competitive advantage.

innovativeness

Innovativeness is the tendency to engage in and support new ideas, experimentation, and creative processes that lead to the development of new products, services, or processes.

intellectual property (IP)

Intellectual property concerns the legal rights that individuals or organizations have over their intellectual creations, granting them control and protection from unauthorized use by others.

intended strategy

An intended strategy is the strategy that an organization plans to implement. It is one strategy in Mintzberg and Waters's (1985) model that considers intended, deliberate, emergent, realized, and unrealized strategies.

internal business process measures

Internal business process measures are an element of the balanced scorecard that measure organizational efficiency. Internal business process measures include production times, delivery efficiency, and new product development speed.

internal development

Internal development describes the process by which a firm expands its resources, capabilities, core competencies, products, or services by leveraging internal resources and expertise.

internal environment

The internal environment includes everything inside a company that influences its ability to create and sustain a competitive advantage.

international strategy

An international strategy combines a low responsiveness to global integration pressures with a low responsiveness to local preferences. An international strategy involves expanding into foreign markets with minimal adaptation, relying on products and capabilities developed in the home market to enter new regions with lower risk and investment.

interpretation

Interpretation is the process and result of examining analysis through critical thinking to identify and explain relationships in the analysis and underlying root causes of the situation. Interpretation is not found in the case or company research.

intrapreneurship

Intrapreneurship is the practice of fostering entrepreneurial initiatives within an existing organization.

isolating mechanisms

Barriers to imitation that prevent competitors from replicating the resource, capability, or core competency that provides a sustainable competitive advantage.

joint venture

A joint venture is established when two parent companies establish a new shared entity, a child company.

knowledge industries

Knowledge industries are firms that are based on intensive use of technology and human capital.

learning and growth measures

Learning and growth measures are an element of the balanced scorecard that measure how an organization can continue to innovate and create future value. Learning and growth measures focus on employee development, innovation capabilities, and adapting to changing market conditions.

leverage measures

Leverage measures evaluate the level of debt in relation to equity. These ratios show how much of a company's or individual's assets are financed by debt, providing insight into financial stability and risk.

licensing

Licensing is an entry mode in which a company allows a foreign company to purchase the rights to produce, sell, or use its products in exchange for royalties or a fee.

line of sight

Line of sight means there is a direct and clear logic connecting two or more concepts or ideas.

liquidity measures

Liquidity measures help assess if an organization or individual can meet short-term obligations. For example, can a company or a person pay off immediate debts with readily available cash?

major areas of strategic concern

Major areas of strategic concern are the most urgent areas that a firm needs to address immediately to ensure its success now and in the future.

majority-owned joint venture

A majority-owned joint venture is formed when two parent companies establish a new shared entity, a child company, and one company owns more than 50 percent of the new company.

market

A market refers to the overall pool of potential customers for a product or service within a specific industry.

market segment

A market segment is a distinct group within a market that is identified by shared characteristics like demographics, needs, or behaviors.

market value

Market value measures indicate the overall value of a company as perceived by investors in the market. These metrics help assess the company's worth based on its stock price and shares outstanding.

McKinsey 7-S model

The McKinsey 7-S model is a framework to align structure, strategy, systems, skills, style, staff, and shared values in the process of strategy formulation and implementation.

megatrend

A megatrend is a deep and profound trend that is global in scope and long term in effect.

merger

A merger occurs when two or more companies of similar size voluntarily join forces and create a new business.

mission statement

A mission statement explains why an organization exists.

multidomestic strategy

A multidomestic strategy combines a low responsiveness to global integration pressures with a high responsiveness to local preferences. Multidomestic strategy involves adaptation of products, services, and operations to align closely with the unique demands of each local market, prioritizing responsiveness over global standardization.

multinational corporation (MNC)

A multinational corporation is a firm that has operations in more than one country.

multinational strategies

Multinational strategies are strategies that are embedded into business-level strategies at the strategic business unit level that address different ways to position the company in multinational markets. These include international, multidomestic, global, and transnational strategies.

multipoint competition (or multimarket competition)

Multipoint competition refers to when firms compete against each other in multiple geographic or product markets simultaneously.

net credit sales

Net credit sales are the total sales a company makes on credit, minus any returns, allowances, or discounts.

Example: If a company has \$100,000 in credit sales and allows \$5,000 returns and discounts, the net credit sales would be \$95,000.

net profit

Net profit is the amount of income remaining after all expenses, taxes, and costs have been subtracted from total revenue. It represents the company's final profit.

Example: If a company's total revenue is \$100,000 and total expenses are \$80,000, the net profit is \$20,000.

net revenue

Net revenue is the total revenue after subtracting returns, allowances, and discounts. It represents the actual income from sales.

Example: If a company's total revenue is \$50,000, but it gave \$5,000 in discounts, the net revenue would be \$45,000.

nonequity strategic alliances

A nonequity strategic alliance is created when two or more companies enter a contractual relationship to pool their resources and capabilities together.

opportunity cost

Opportunity cost refers to the loss of potential gain from alternative options that were not pursued.

For example: Idle cash balances represent an opportunity cost in terms of lost interest.

organization

Organization is the broadest term used to describe a specific entity and applies to entities in all sectors: private (for-profit), governmental (public), and not-for-profit (including nonprofit, nongovernmental organizations [NGOs], and voluntary organizations). Organizations in the private sector are also referred to as businesses, companies, and firms.

performance benchmarks

Performance benchmarks are standards or reference points used to evaluate an organization's metrics by comparing them to historical data, industry standards, or the performance of competitors.

performance gap

Performance gap is the difference between the implemented strategy and organizational performance under the strategy.

performance gap analysis

A performance gap analysis analyzes the performance gap and its causes. Performance gap analysis looks at the gap between where the firm should be according to the current strategy and where it is. Hence, the performance gap analysis is the process that companies use to compare their current strategy performance with their desired, expected performance.

performance measures

Performance measures are metrics used to track an organization's progress, such as profits, stock prices, or sales figures.

PESTEL

The PESTEL framework is the strategic management framework that is used to analyze the general environment of a company. The acronym PESTEL stands for political, economic, sociocultural, technological, environmental, and legal.

presidential executive order

A presidential executive order is issued by the President of the United States and gives directives that may impact businesses.

private placement

A private placement is a sale of stock shares or bonds to preselected investors and institutions rather than on a public exchange.

proactiveness

Proactiveness is a firm's tendency to anticipate and act on future opportunities, needs, and market changes ahead of competitors.

profitability ratio

Profitability ratios focus on the ability to generate profit. These measures show how well an organization or individual is able to grow their income over time, which is essential for sustainable success.

purpose statement

A firm's purpose statement articulates its reason for existence beyond just profit-making.

radical innovation

Radical innovation is the development of new technologies or products that create new markets, often leading to significant shifts in consumer or competitor behavior.

RASCI matrix

The RASCI matrix model describes the participation by various roles in completing tasks or deliverables for a project or business process. The RASCI acronym stands for responsible, accountable, supportive, consulted, and informed.

realized strategy

A realized strategy is the strategy that an organization follows over time. Realized strategies include a firm's planned intended strategy as amended to take into account any changes that arise in a dynamic environment as reflected in a company's deliberate strategy. Realized strategies also include an emergent strategy if an unanticipated and completely new opportunity has arisen and the firm has been nimble and quick enough to capitalize on it.

related diversification

Related diversification is expanding into new and similar markets, market segments, and businesses in a new industry that has similarities to a firm's current industry or industries.

resources

Resources are the tangible and intangible assets owned by a company.

retrenchment

Retrenchment is a reduction in size and product offerings intended to continue to make profits. It is also referred to as downsizing or rightsizing, which often require laying off employees.

return on investment

Return on investment describes how effectively a company generates profit relative to the cost of investments, which ties directly to profitability.

risk-taking

Risk-taking is a firm's willingness to engage in bold actions that involve significant uncertainty, such as investing in new ventures, entering unfamiliar markets, or committing resources to unproven projects. It reflects a readiness to take calculated risks for potential high returns.

root cause analysis

Root cause analysis is a structured process for identifying the underlying causes of a problem and developing solutions to prevent it from happening again.

share price

Share price is the current market price of a single share of a company's stock, determined by supply and demand in the stock market.

shareholder equity

Shareholder equity represents the ownership interest of shareholders in a company, calculated as the difference between a company's total assets and total liabilities.

Example: If a company has \$1 million in assets and \$600,000 in liabilities, its shareholder equity would be \$400,000.

shares outstanding

Shares outstanding refers to the total number of a company's shares currently held by all its shareholders.

single business firm

A single business firm is a firm that derives 95 percent or more of its revenues from one business.

span of control

The span of control represents the number of direct reports for which a supervisor is responsible.

spinoff

A spinoff involves selling part of a company, such as a division or strategic business unit.

stock price

Stock price reflects how investors perceive a company's worth, making it a fundamental metric for market value.

strategic alliance

A strategic alliance is a mutually beneficial contractual relationships between two independent organizations.

strategic alternative

A strategic alternative is an action that addresses and has the potential to resolve every aspect of a strategic issue.

strategic analysis

Strategic analysis is the process of applying strategic management concepts and theories as well as analytical frameworks and tools to conduct a thorough 360-degree analysis of a firm, enabling strategy managers to make evidenced-based decisions about strategy formulation and strategy implementation in all areas of the company's operations.

strategic business unit

A strategic business unit is a fully functional unit of a business that has its own vision and direction and is part of a larger organizational unit like a division. A strategic business unit focuses on one business-level strategy.

strategic gap

Strategic gap is the difference between a firm's strategic objective—what it would like to accomplish—and its formulated strategy, which is based on the improvements the firm expects to realize given the operating conditions.

strategic gap analysis

Strategic gap analysis inspects the difference between a firm's strategic objective (what they would like to accomplish) and its formulated strategy (which is based on the improvements the firm expects to realize given the expected operating conditions).

strategic group

A strategic group consists of companies that pursue similar strategies in the same industry.

strategic group mapping

Strategic group mapping is the strategic management framework used to analyze industry competitors that have similar characteristics to each other and differ in important ways from the companies in other strategic groups.

strategic issue

A firm's strategic issue is the most important, urgent, broad, long-term matter that the company is facing. Strategic issues require significant organizational talent and resources to resolve. Addressing a strategic issue moves a firm toward its mission, purpose, and vision; therefore, the issue should be congruent with its values, and goals. A strategic issue focuses on the present and specific organizational context, addressing what is happening with this firm, at this time, in this place, and under these circumstances.

strategic leadership

Strategic leadership includes the responsibility, talent, capacity, power, and actions to steer an organization strategically through a dynamic market to create and sustain a competitive advantage and to become and remain an industry leader.

strategic management

Strategic management is the dynamic and ongoing endeavor that follows a structured process to methodically and thoroughly analyze the environment, industry, and firm as well as to formulate and implement strategy.

strategic management frameworks

Strategic management frameworks provide a structured format to analyze company data as it relates to a major area of strategic management. These analytical frameworks may also be referred to as strategic management tools.

strategy

Strategy is a collection of organizational plans and processes that focus on creating and sustaining superior firm performance relative to a company's competitors, which creates a sustainable competitive advantage. Strategies are broad and long-range, with few specifics. They do not typically address actions.

strategy formulation

Strategy formulation is the process of designing strategies throughout all levels and areas of an organization. Successful strategy formulation relies on evidenced-based decisions that are grounded in strategic analysis.

strategy implementation

Strategy implementation is the process of executing the strategies that a company has formulated.

stuck in the middle

Companies that attempt to combine cost leadership and differentiation approaches but fail to balance the tensions inherent between the two approaches may end up being “stuck in the middle,” unable to compete on price with low-cost leaders or on quality with premium brands.

substitute

A substitute is a product or service that comes from outside the existing industry but fills the same need for existing industry customers while offering some additional value.

supply chain

A supply chain includes the steps of product production from multiple entities, ranging from raw materials to the final delivered product.

sustainability

Sustainability refers to meeting our own needs without compromising the ability of future generations to meet their own needs. Sustainability addresses issues of climate change, resource scarcity, social issues, and social justice.

sustainability strategy

A company's sustainability strategy is meant to reduce adverse environmental and social impacts resulting from business operations while still pursuing profitable growth. Such strategies include corporate social responsibility (CSR) strategies and environmental, social, and governance (ESG) strategies.

synergy

Synergy occurs when two or more strategic business units or businesses perform more effectively together than they do independently.

synthesize

Synthesize means to review, critically examine, and combine diverse elements into a coherent whole.

technology strategy

Technology strategy involves the use of digital technology to improve an organization's processes, operations, products, and services. Technology strategy is the “rewiring” of an organization with the goal of creating value by continuously deploying technology at scale.

theories

Theories are collections of concepts. Business theories explain occurrences in the business world.

total assets

A company's total assets are everything it owns that has economic value, including both current and long-term assets. Buildings owned by the company, alongside cash, equipment, and inventory, all contribute to total assets.

total liabilities

A company's total liabilities are made up of all its debts and financial obligations, such as loans taken from a bank.

total revenue

The total income generated from sales of goods or services before any expenses are deducted.

Example: If a store sells \$150,000 worth of products in a month, that amount is its total revenue for that month.

transnational strategy

Transnational strategy is a strategy involving the balance of global efficiency with local responsiveness by standardizing core elements while adapting others to meet the unique needs of individual markets.

unrealized strategy

An unrealized strategy refers to the abandoned parts of the intended strategy. It is one strategy in Mintzberg and Waters's (1985) model that considers intended, deliberate, emergent, realized, and unrealized strategies.

unrelated diversification

Unrelated diversification describes expansion into new markets, market segments, and businesses in a new industry that has little or no similarities to a firm's current industry or industries.

value chain analysis

A value chain analysis is a systematic process for evaluating the steps involved in creating a product or service, from the

initial design to delivery to the customer. The analysis helps to deliver the most value at the lowest cost and helps to identify strengths and weaknesses a firm needs to address in the strategy formulation process.

value statements

Value statements define the core principles that companies stand by and expect their employees to uphold.

vertical integration

Vertical integration is a business expansion strategy in which a company takes control over one or more stages in the production or distribution of its products.

vision statement

A vision statement is a forward-looking or aspirational statement that captures what a company or organization wants to achieve in the long run.

VRIO framework

The VRIO framework identifies sources of a sustainable competitive advantage for a firm by analyzing whether resources, capabilities, and core competences are valuable, rare, hard to imitate, and organized to capture value.

wholly owned subsidiaries

A wholly owned subsidiary is a company whose common stock is 100% owned by another company. In the context of multinational corporations, wholly owned subsidiaries involve full ownership and control of foreign operations. They can be established through either greenfield investments or acquisitions.

ACKNOWLEDGMENTS

Publication of this work was made possible in part by the University Libraries at Virginia Tech through its [Open Education Initiative](#), which provides development assistance and financial support to Virginia Tech faculty who wish to use, create, or adapt openly licensed teaching materials to support student learning. The University Libraries also contributed faculty and staff labor. Lori Anderson's, Dirk Buengel's, and Joseph Simpson's contributions were further supported by the Pamplin College of Business at Virginia Tech.

Lori Anderson and Anita Walz, co-primary investigators, are grateful recipients of the 2024 University Libraries' Collaborative Research Grant. They thank the University Libraries at Virginia Tech's Center for Digital Research and Scholarship for their generous support of this project.

Lori Anderson, Dirk Buengel, and Joseph Simpson are indebted to their colleagues in the Pamplin College of Business, acknowledging that they are “standing on the shoulders of giants.” Prior collaborations between the University Libraries at Virginia Tech and the Pamplin College of Business produced the adapted textbooks *Fundamentals of Business* (2016) by Stephen Skripak, now in its fourth edition, and Reed Kennedy's *Strategic Management* (2020) in addition to numerous texts and other learning resources in a variety of disciplines. Steven Skripak's and Reed Kennedy's work was visionary. Kennedy and his collaborators (Eli Jamison, Joseph Simpson, Pankaj Kumar, Ayenda Kemp, Kiran Awate, and Kathleen Manning) were pioneers and paved the way for this book; they continue to inspire others in the Pamplin College of Business and in other disciplines to produce open textbooks and other openly licensed, customizable learning resources. Lori Anderson, Dirk Buengel, and Joseph Simpson would like to further acknowledge the early work on the project of their colleague, Richard Curtis.

Peer reviews were generously provided by two Pamplin colleagues—Pankaj Kumar (*professor, Virginia Tech*) and Manisha Singal (*professor, Virginia Tech*)—in addition to one colleague who wishes to remain anonymous.

Lori Anderson further acknowledges the support and guidance of Associate Professor Pankaj Kumar of the Management Department.

Lori Anderson also acknowledges the leadership support she received throughout this project, especially from Ron Poff, Assistant Department Head of the Management Department, and Devi Gnyawali, Department Head of the Management Department. Finally, Lori Anderson extends her gratitude to the talented support of three brilliant graduate students: Claire Lympus, Anthony Brozey, and Sabrina Duque-Lewis.

The cover art for the book is an original work designed by Claire Lympus, a Virginia Tech graduate student whose talents include both business analytics and art. The cover design was by Kindred Grey.

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