Chapter 1
Strategic management and strategic competitiveness

Learning Objectives

1. Analyse the components of the strategic management process.
2. Describe the competitive landscape and explain how globalisation and technological changes shape it.
3. Use the industrial organisation (I/O) model to explain how organisations can earn above-average returns.
4. Use the resource-based model to explain how organisations can earn above-average returns.
5. Describe vision and mission and discuss their value.
6. Define and classify the four major stakeholder groups and describe their ability to influence organisations.
7. Describe the work of strategic leaders.

Lecture Notes

Chapter Introduction: You may want to begin this lecture with a general comment that Chapter 1 provides an overview of the strategic management process. This chapter introduces a number of key terms and models that students will study in more detail in Chapters 2 to 13. Stress the importance of students paying careful attention to the concepts introduced in this chapter so that they are well grounded in strategic management concepts before proceeding further.

OPENING CASE

McDonald's and brand recognition

McDonald's, a well-known global brand, has achieved international success over the years. For example, in 2018 it had 37,855 restaurants around the globe. This has resulted in very strong brand recognition. For example, a recent survey found that 88% of people were able to identify the iconic McDonald's Golden Arches logo. A key factor influencing McDonald's international growth is its strategic competitiveness. The case demonstrates that McDonald's has different competitive positions in different countries, some stronger and some weaker than competitors. For example, it is facing stiff competition with KFC in China. In India, it is still relatively a small brand but expanding strategically by alliances with local organisations, sourcing almost all products locally. Hence, it has complex country-specific challenges which necessitate a country-specific response. For example, McDonald's is responding to local consumer needs very well. In Australia, McDonald's offers a flexible menu, such as 'gourmet coffee' and fresh-food bars. Similarly, it is responding to consumer demand in the UK by offering details on what goes into their food.

Teaching Note: To kick off discussion, ask how the case lays the groundwork for the importance of strategy as defined in the chapter – the coordinated set of commitments and actions designed to achieve competitive advantage. Ask students why McDonald's has different strategic competitiveness in different countries and how it is linked to an external environment. How does McDonald's respond to country-specific challenges by accommodating the local business environment and consumer demand. The case also provides a good link with strategic leadership. How can effective leadership maintain McDonald's success in future, particularly post-COVID?

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1 Analyse the components of the strategic management process.

A framework that can assist organisations in their quest for strategic competitiveness is the ***strategic management process***, the full set of commitments, decisions and actions required for an organisation to systematically achieve strategic competitiveness and earn above-average returns. This process is illustrated in *Figure 1.1*.

Strategic competitiveness is achieved when an organisation successfully formulates and implements a value-creating strategy. By implementing a value-creating strategy that current and potential competitors are not *simultaneously* implementing and that competitors are *unable* to duplicate, or find too costly to imitate, an organisation achieves a ***competitive advantage***.

Strategy can be defined as an integrated and coordinated set of commitments and actions designed to exploit core competencies and gain a competitive advantage.

So long as an organisation can sustain (or maintain) a competitive advantage, investors will earn above-average returns. ***Above-average returns*** are returns that exceed returns that investors expect to earn from other investments with similar levels of ***risk*** (investor uncertainty about the economic gains or losses that will result from a particular investment). In other words, the above-average returns exceed investors' *expected* levels of return for given risk levels. In smaller new venture organisations, performance is sometimes measured in terms of the amount and speed of growth rather than more traditional profitability measures – new ventures require time to earn acceptable returns.

Teaching Note: Point out that in the long run, organisations must earn at least average returns and provide investors with average returns if they are to survive. If an organisation earns below-average returns, investors will withdraw their funds and place them in investments that earn returns that are at least average. At this point, it may be useful to highlight the role institutional investors play in regulating above-average performance.

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FIGURE 1.1

The strategic management process

Figure 1.1 illustrates the dynamic, interrelated nature of the elements of the strategic management process and provides an outline of where the different elements of the process are covered in this text.

Feedback linkages among the three primary elements indicate the dynamic nature of the strategic management process: strategic inputs, strategic actions and strategic outcomes.

- **Strategic inputs**, in the form of information gained by scrutinising the internal environment and scanning the external environment, are used to develop the organisation's vision and mission.
- **Strategic actions** are guided by the organisation’s vision and mission and are represented by strategies that are formulated or developed and subsequently implemented or put into action.
- Desired **strategic outcomes** – strategic competitiveness and above-average returns – result when an organisation is able to successfully formulate and implement value-creating strategies that others are unable to duplicate.
- **Feedback** links the elements of the strategic management process together and helps organisations continuously adjust or revise strategic inputs and strategic actions in order to achieve desired strategic outcomes.

This chapter also discusses two approaches to the strategic management process. The first, the *industrial organisation or I/O model*, suggests that the external environment should be considered as the primary determinant of an organisation’s strategic actions. The second is the *resource-based model*, which perceives the organisation’s resources and capabilities (the internal environment) as critical links to strategic competitiveness. Following the discussion in this chapter, as well as in Chapters 2 and 3, students should see that these models must be integrated to achieve strategic competitiveness.

> ***Teaching Note:*** The transient nature of strategic competitiveness is illustrated even more clearly when one realises that only 52 of the 500 largest US industrial corporations in 1955 remained competitive in 2019. To be more precise, half of the Fortune 500 companies have disappeared since 2000 (in the last 21 years) due to their lack of strategic competitiveness.
>
> ***Teaching Note:*** The section also reviews *Figure 1.1* (The strategic management process), providing both an outline of the process and the framework for the next 12 chapters. *Figure 1.1* is a helicopter view to show how different chapters are aligned with different steps of the strategic management process.

Chapters 2 and 3 provide more detail regarding the strategic inputs to the strategic management process: assessments of organisations’ external and internal environments that must be performed so that sufficient knowledge is developed regarding external opportunities and internal capabilities. This enables the development of an organisation's vision and mission.

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Chapters 4 to 9 discuss the strategy formulation stage of the process. Topics covered include:

- Deciding on business-level strategy, or how to compete in a given business (Chapter 4).
- Understanding competitive dynamics, in that strategies are not formulated and implemented in isolation but require understanding and responding to competitors' actions (Chapter 5).
- Setting corporate-level strategy, or deciding in which industries or businesses the organisation will compete, how resources will be allocated, and how the different business units will be managed (Chapter 6).
- The acquisition of business units and the restructuring of the organisation's portfolio of businesses (Chapter 7).
- Selecting appropriate international strategies that are consistent with the organisation's resources, capabilities and core competencies and external opportunities (Chapter 8).
- Developing cooperative strategies with other organisations to gain competitive advantage (Chapter 9).

The final section of the text, Chapters 10–13, examines actions necessary to effectively implement strategies:

- Methods for governing to ensure satisfaction of stakeholder demands and attainment of strategic outcomes (Chapter 10).
- Structures that are used and actions taken to control an organisation's operations (Chapter 11).
- Patterns of strategic leadership that are most appropriate given the competitive environment (Chapter 12).
- Linkages among corporate entrepreneurship, innovation and strategic competitiveness (Chapter 13).

Teaching Note: Students should realise that none of the chapters stands alone, just as no single step or facet of the strategic management process stands alone. If the strategic management process is to result in an organisation being strategically competitive and earning above-average returns, all facets of the process must be treated as both interdependent and interrelated.

2	Describe the competitive landscape and explain how globalisation and technological changes shape it.

THE COMPETITIVE LANDSCAPE

The ***competitive landscape*** can be described as one in which the fundamental nature of competition is changing in a number of the world's industries. Further, the boundaries of industries are becoming blurred and more difficult to define. This results in a volatile business world, where organisations compete on a global scale, and need huge investment with huge risk.

Consider changes that have taken place in the telecommunications and TV industries –

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e.g. not only cable companies and satellite networks compete for entertainment revenue from television, but telecommunications companies also are stepping into the entertainment business through significant improvements in fibre-optics.

The twenty-first century competitive landscape thus implies that traditional sources of competitive advantage – economies of scale and large advertising budgets – may not be as important in the future as they were in the past. The rapid and unpredictable technological change that characterises this new competitive landscape implies that managers must adopt new ways of thinking. The new competitive mind-set must value flexibility, speed, innovation, integration and the challenges that evolve from constantly changing conditions.

A term often used to describe the new realities of competition is ***hyper-competition***, a condition where competitors engage in intense rivalry, markets change quickly and often, and entry barriers are low. This results from the dynamics of strategic moves and countermoves among innovative, global organisations: a condition of rapidly escalating competition that is based on price-quality positioning, efforts to create new know-how and achieve first-mover advantage, and battles to protect or to invade established product or geographic markets (discussed in more detail in Chapter 5).

The global economy
G*lobal economy* is where goods, services, people, skills and ideas move freely across geographic borders.

The emergence of the global economy results in several challenges. For instance, it is under pressure due to trade tensions, inequality, geopolitical uncertainty and most recently the COVID 19 pandemic. At the same time, there are many opportunities: Europe, for example, is now one of the world's largest markets, with 700 million potential customers (despite the difficulties of adapting to multiple national cultures).

Today, China and India are seen as extremely competitive markets in which local market-seeking MNCs (multinational corporations) fiercely compete against other MNCs and local low-cost producers. China has long been viewed as a low-cost producer of goods, but here's an interesting twist. China is now an exporter of local management talent. Procter & Gamble exports Chinese management talent; it has been dispatching more Chinese abroad than it has been importing expatriates to China. GE estimates that by 2024, China will be the world's greatest consumer of electricity and will also be the world's largest consumer and consumer-finance market. GE is making strategic decisions today, such as significant investments in China and India, that will enhance its competitive posture in both countries in the future.

Organisations need to closely monitor the size of the global economy to understand the competitive landscape. For example, in 2019, the United States, China, Japan, Germany, the United Kingdom, and India were the world's largest economies. In the present decade, how the global economy will be driven by developed and emerging economies should be analysed. Furthermore, what opportunities and challenges will be faced should be anticipated by organisations to plan forward, particularly post-COVID. For

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example, during the coronavirus pandemic, Netflix has grown considerably but it is still mindful of future challenges.

> ***Teaching Note:*** The relative competitiveness of nations can be found in the World Economic Forum's *Global Competitiveness Report*, which can be accessed for free on the internet. It is useful to assemble these data into an overhead or PowerPoint slide and show it in class. Students find it interesting to see where their country stands relative to the others listed. Allow enough time for them to see these numbers and sort out what it all means.

STRATEGIC FOCUS

Starbucks is a new-economy multinational, yet has had failures in key markets

The case demonstrates how Starbucks has attempted to grow its business internationally using a multinational strategy – that is, it engages in major strategic actions to enter new international and product markets with a focus on selling coffee in a cafe-style environment.

The multinational strategy requires that an organisation's core product offering be consistent across national boundaries, yet at the same time be mindful of local cultural preferences in their product and service delivery. For example, despite a strong tea-drinking culture in Asia, Starbucks is continuously growing in China, by developing larger stores and catering to tea drinkers. Similarly, it is growing in India and Vietnam by working with local organisations.

Starbucks' success in the United States was predicated on its ability to offer café-style coffee experiences that meet the expectations of the US consumer. However, Starbucks didn't fit Australians' tastes. In its first seven years in Australia, Starbucks accumulated $105 million in losses, forcing the company to close 61 locations. It failed to cater for the well-established coffee-culture in Australia with its premium price and taste. The case demonstrates how a range of different variables impacted Starbucks' ability to achieve the same level of success in Australia and Europe as it had in its domestic US context.

> ***Teaching Note:*** This case provides an excellent opportunity for students to discuss the variables that impacted Starbucks' success outside of the United States: the variability in the cafe cultures, the expected quality standards in different markets, and the role of store location can each be seen to have played a negative role in Starbucks' performance in Australia and Europe. This case poses the question: what additional information should Starbucks' senior management have taken into account in their decision to implement a multinational structure for their organisation?

The march of globalisation

Globalisation is the increasing economic interdependence among countries as reflected in the flow of goods and services, financial capital and knowledge across country borders. This is illustrated by the following:

- Financial capital might be obtained in one national market and used to buy raw

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materials in another.
- Manufacturing equipment bought from another market produces products sold in a third market.
- Globalisation enhances the available range of opportunities for organisations.
- Organisations incorporate culture dimensions in strategic decisions
- Organisations continuously monitor complex operations as goods, services and people move across the world

Global competition has increased performance standards in many dimensions, including quality, cost, productivity, product introduction time and operational efficiency. Moreover, these standards are not static; they are exacting, requiring continuous improvement from an organisation and its employees. Thus, companies must improve their capabilities and individual workers need to sharpen their skills. In the twenty-first century competitive landscape, only organisations that meet and perhaps exceed global standards are likely to achieve strategic competitiveness.

> ***Teaching Note:*** As a result of the new competitive landscape, organisations of all sizes must re-think how they can achieve strategic competitiveness by positioning themselves to ask questions from a more global perspective that will enable them to (at least) meet or exceed global standards:
> - Where should value-adding activities be performed?
> - Where are the most cost-effective markets for new capital?
> - Can products designed in one market be successfully adapted for sale in others?
> - How can we develop cooperative relationships or joint ventures with other organisations that will enable us to capitalise on international growth opportunities?
> - How can the local cultural dimension guide strategic management processes?

Although globalisation seems an attractive strategy for competing in the current competitive landscape, there are risks as well. These include such factors as:
- The ‘liability of foreignness’ (i.e. the risks of competing internationally).
- Over-diversification beyond the organisation’s ability to successfully manage operations in multiple foreign markets.

A point to emphasise: entry into international markets requires proper use of the strategic management process.

Though global markets are attractive strategic options for some companies, they are not the only source of strategic competitiveness. In fact, for most companies, even for those capable of competing successfully in global markets, it is critical to remain committed to, and strategically competitive in, the domestic market. And domestic markets can be testing grounds for possibly entering an international market at some point in the future.

> ***Teaching Note:*** Indicate that the risks that often accompany internationalisation and strategies for minimising their impact on organisations are discussed in

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more detail in Chapter 8.

Teaching Note: As a result of globalisation and the spread of technology, competition will become more intense. Some principles to consider include the following:

- Customers will continue to expect high levels of product quality at competitive prices.
- Global competition will continue to pressure companies to shorten product development-introduction time frames.
- Strategically competitive companies successfully leverage insights learned both in domestic and global markets, modifying them as necessary.
- Before a company can hope to achieve any measure of success in global markets, it must be strategically competitive in its domestic market.

Technology and technological changes

According to the Boston Consultancy Group, organisations must analyse the impact of technology starting from sourcing of material to customer service. Particularly, there are three technological trends and conditions that significantly affect today's organisations and the nature of competition:

- Increasing rate of technological change and diffusion.
- The information age.
- Increasing knowledge intensity.

Technology diffusion and disruptive technologies

Technology diffusion is the speed at which new technologies become available and are used. This has increased greatly over the last 20 years. Technology diffusion greatly impacts organisations and industry competition. For example, Blockbuster had 9000 stores in 2004 to rent videotapes of movies, but filed for bankruptcy in 2010 thanks to change in technology. Only the organisations which adapt to change survive.

A term that is used to describe the rapid and consistent replacement of current technologies by new, information-intensive technologies is ***perpetual innovation***. This implies that innovation – discussed in more detail in Chapter 13 – must be continuous and carry a high priority for all organisations.

The shorter product life cycles that result from rapid diffusion of innovation often means that products may be replicated within very short periods, placing a competitive premium on an organisation's ability to rapidly introduce new products into the marketplace. In fact, speed-to-market may become the sole source of competitive advantage. In the computer industry during the early 1980s, hard disk drives would typically remain current for four to six years, after which a new and better product became available. By the late 1980s, the expected life had fallen to two to three years. By the 1990s, it was just six to nine months.

Now the source of competitive advantage is constant innovation and speed to market. Apple is a great example as it innovates continuously, with frequent new product launches around the world. Similarly, the fast-fashion brand Zara, makes sure

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that it only takes four weeks from design to store display, compared to an industry average of four months. This can be a challenge for mature and traditional organisations.

The rapid diffusion of innovation may have made patents a source of competitive advantage only in the pharmaceutical and chemical industries. Many organisations do not file patent applications to safeguard (for at least a time) the technical knowledge that is disclosed in a patent application.

Disruptive technologies (in line with the Schumpeterian notion of 'creative destruction') can destroy the value of existing technologies by replacing them with new ones. Current examples include the success of Air Pods, Google Chromecast and 5g.

The information age

Changes in information technology have made rapid access to information available to organisations all over the world, regardless of size. Consider the rapid growth in the following technologies: personal computers (PCs), mobile phones, computers, personal digital assistants (PDAs), artificial intelligence, virtual reality and massive databases. Such examples show how information is used differently as a result of new technologies. The ability to access and use information has become an important source of competitive advantage in almost every industry because:

- Data is vital to understanding customers' needs and to accommodate the interest of other stakeholders.
- IT is a great source for product and supply chain innovation.

The ability to access a high level of relatively inexpensive information has created strategic opportunities for many information-intensive businesses. For example, retailers now can use the internet to provide shopping to customers virtually anywhere.

STRATEGIC FOCUS

The core of Apple: Technology and innovation

Apple has been on a hot streak for a couple of decades. It is an exceptionally innovative company and its products including iPod, iTunes, iPhone, iPad, Apple Watch, and Air pods have revolutionised multiple industries. Its brand is incredibly strong on a global scale and customers continue to purchase its expensive products even though cheaper substitutes abound. As a result, there were 1.4 billion active Apple devices in 2019, earning revenue of 260 billion in 2019! The core factor in this success story is technology development and innovative products.

> ***Teaching Note:*** Apple illustrates the power of well-conceived and managed innovation. Over the years, it has produced a number of breakthrough products that are in high demand. Ask students to compare some of Apple's products with those of competitors, particularly Samsung. What do they know about the products and how important is the strength of the Apple brand in shaping perceptions? Ask students if they think that Apple will be able to continue this momentum into the future.

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Increasing knowledge intensity
It is becoming increasingly apparent that knowledge – information, intelligence and expertise – is a critical organisational resource, and increasingly, a source of competitive advantage. As a result:

- Many companies are working to convert the accumulated knowledge of employees into a corporate asset.
- Shareholder value is increasingly influenced by the value of an organisation's intangible assets, such as knowledge.

Note: Intangible assets are discussed more fully in Chapter 3.

> ***Teaching Note:*** To achieve competitive advantage in the information-intensive competitive landscape, organisations must move beyond accessing information to exploiting information by:
> - Capturing intelligence.
> - Transforming intelligence into usable knowledge.
> - Embedding it as organisational learning.
> - Diffusing it rapidly throughout the organisation.

This discussion implies that to achieve strategic competitiveness and earn above-average returns, organisations must develop the ability to adapt rapidly to change or achieve strategic flexibility.

Strategic flexibility represents the set of capabilities – in all areas of their operations – that organisations use to respond to the various demands and opportunities that are found in dynamic, uncertain environments. This implies that organisations must develop certain capabilities, including the capacity to learn continuously, that will provide the organisation with new skill sets. However, those working within organisations to develop strategic flexibility should understand that the task is not an easy one, largely because of inertia that may build up over time. An organisation's focus and past core competencies may actually slow change and strategic flexibility.

> ***Teaching Note:*** Organisations must be capable of rapidly and broadly applying what they learn to achieve strategic flexibility and develop capacity to change in ways that will increase the probability of succeeding in uncertain, hypercompetitive environments. Some organisations must change dramatically to remain competitive or to return to competitiveness. How often are organisations able to make this shift? Overall, does it take more effort to make small, periodic changes, or to wait and make more dramatic changes when these become necessary?

Two models describing key strategic inputs to an organisation's strategic actions are discussed next: the Industrial Organisation (or externally focused) model and the Resource-Based (or internally focused) model.

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