Strategic Management-The Competitive Edge
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Lecture No. # 24
Functional Strategy- 1

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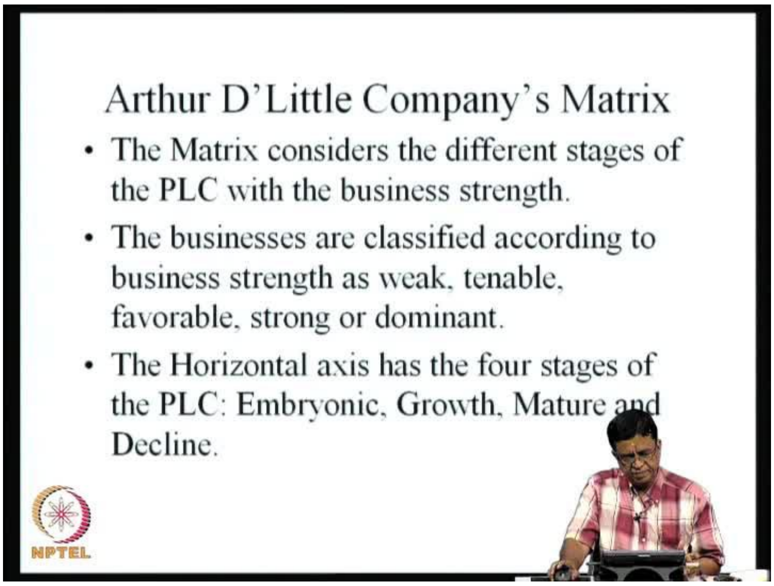

So, welcome to this class. In the last class, we discussed this Arthur D'little company's matrix. Another portfolio matrix, it makes use of the different stages of P L C with the business strength.

So, the businesses are classified, according to the business strength as weak, tenable, favorable, strong or dominant, that is on the vertical axis. The horizontal axis has the four stages of the P L C, that is, embryonic, growth, mature, and decline.

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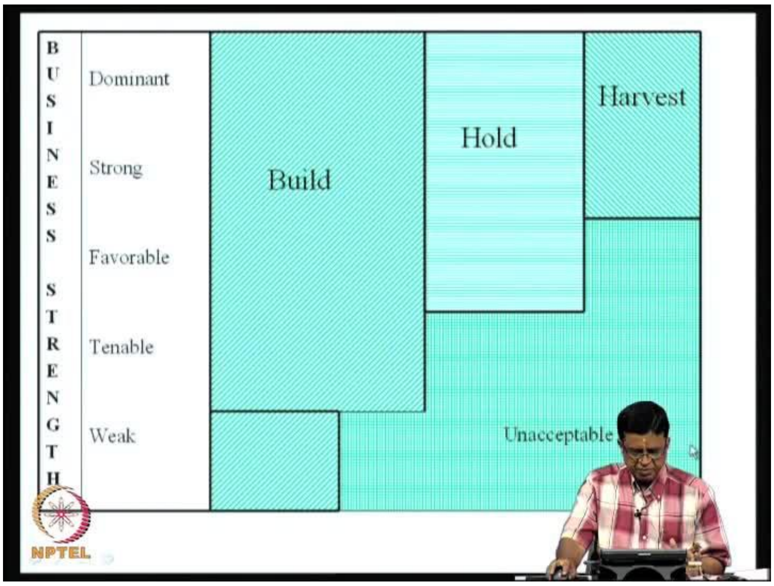

So, as I mentioned, the matrix looks something like this. On the horizontal axis, you have the embryonic, not written down here due to shortage of space, but the different stages of P L C, that is, embryonic, growth, then maturity, and decline.

This is the unacceptable region; this unacceptable region means where the return on investment is not acceptable. So, that is what it means. So, this is the region where you build; this is the region where you hold on to your market share; and this is the region where you harvest.

So, harvesting is a similar to the cash cow type of scenario in the b c g matrix. The build is similar to the question marks, where there is a possibility of converting some of the products or product lines into leadership positions.

Hold is where the product or the product line is already a leader, and you hold on to that position as far as possible. So, this is the way this Arthur D'little company's matrix looks like. So, the main point is it looks at the business strength along with the different stages of PLC.

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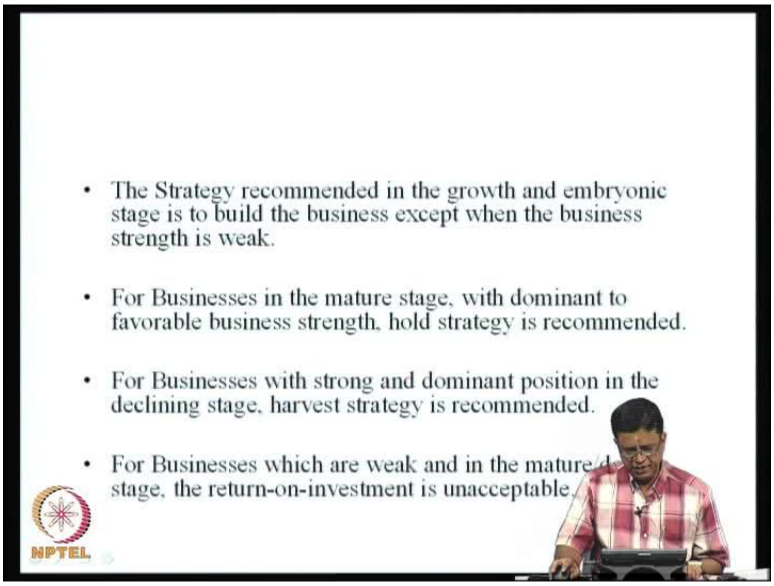

So, the strategy recommended in the growth and the embryonic stage is to build the business except when the business strength is weak. For businesses in the mature stage with dominant to favorable strength, hold strategy is recommended.

For businesses with strong and dominant position in the declining stage, harvest strategy is recommended. For businesses which are weak and in the mature stroke decline stage, the return-on-investment is unacceptable.

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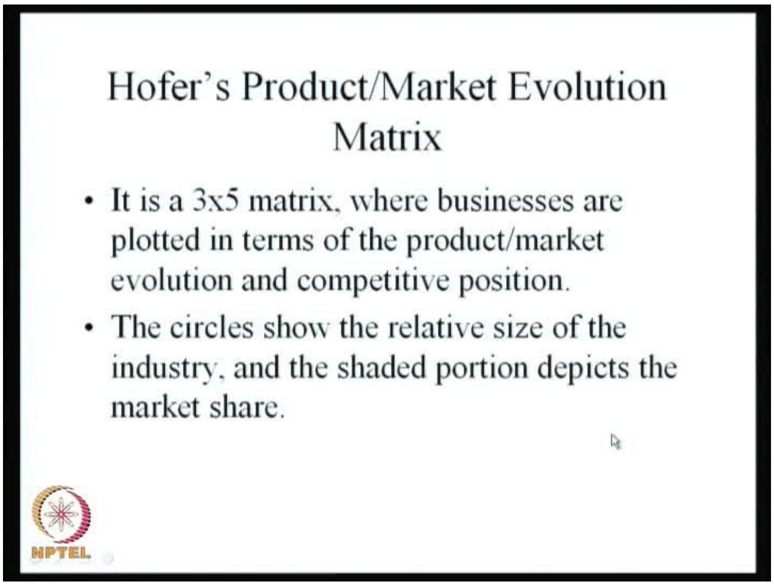

So, you must salvage as much value as possible for these business units. Now, we come to the next matrix that is the Hofer's product stroke market evolution matrix. It is a 3 by 5 matrix where businesses are plotted in terms of the product stroke market evolution and competitive position.

So, businesses are plotted in terms of product stroke market evolution and competitive position. The circles show the relative size of the industry, and the shaded portion depicts the market share. Note that the circles show the relative size of the industry and the shaded portion depicts the market share.

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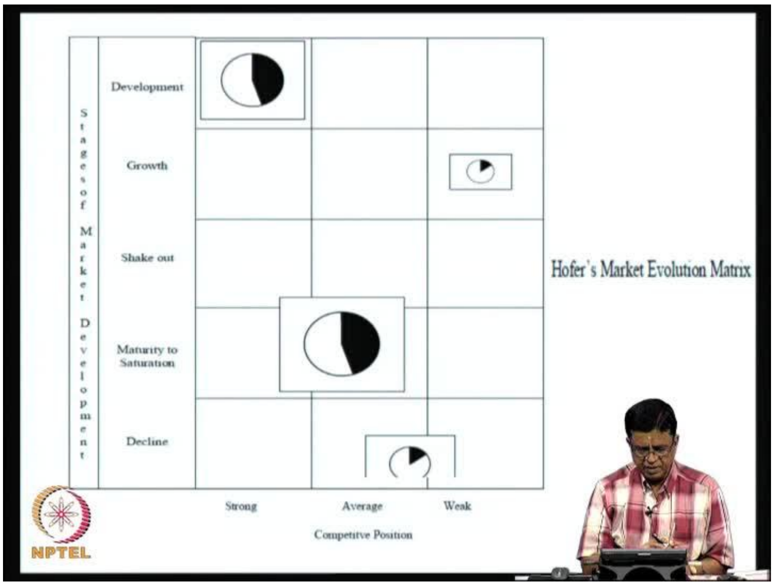

This is the way this Hofer's product market evolution matrix looks like. If you look at this, on the x axis, you have the competitive position. In the competitive position, you are going from weak to average to strong. Then on the business, on the y axis, you have the market development.

The strategic market, the stages of market development, so, you are going from development to growth to shake out, then to maturity to saturation, then to decline. So, you are seeing in the stages of market development; typically five stages going from development, growth, shake out, then maturity to saturation, then decline.

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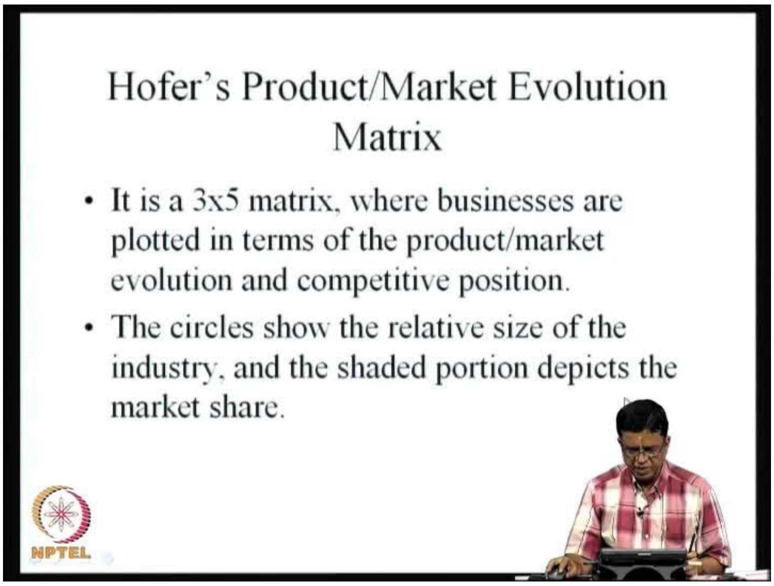

Then in competitive position, you are going from weak to average to strong. So, put in this manner. So, the circle, as was mentioned in the previous slide, the circle shows the relative size of the industry and the shaded portion depicts the market share.

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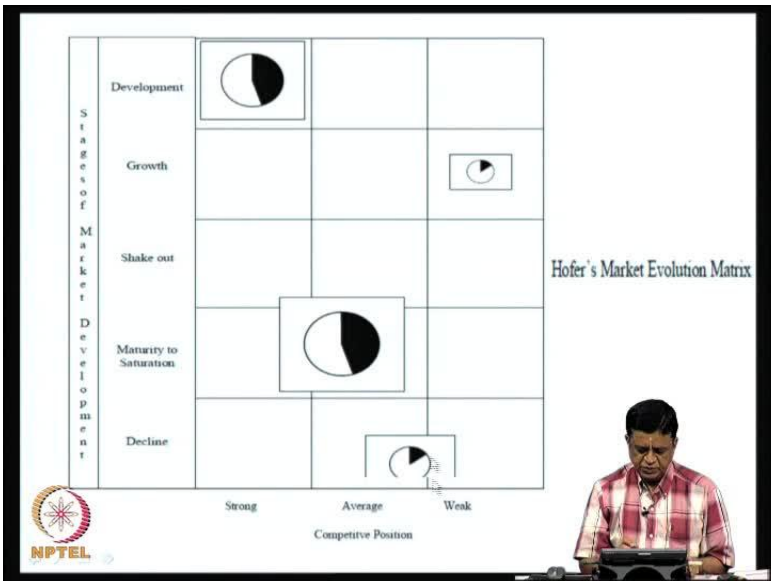

So, this is with respect to your company, that is the company where it operates the market share. So, the circle shows the industry market size, and this shows what is the share of the company's market.

So, if you take a typical circle here with respect to a particular product line, you see the circle size showing the industries this size, whereas, this particular company nearly closing in on half of that market size; so, the market share of that company, as we can make out is somewhere between 45 to 50 percent which is very good.

So, there is a very good chance that these products or the product lines are going to become market leaders. So, you should build on them, whereas, when you come to this, you find that the size of the industry size is represented by this circle.

The share of the company is this small portion, black portion shown there which is not very high; so, there is a need for revisiting the strategy with respect to this particular product or product line of the company.

Whether it is possible to continue with that, the company has to take the decision. If you come to this particular circle, what you are seeing here is again the size of the circle representing the industry market and the shaded black portion representing the market share of the company nearly coming to half.

What does that mean? It means that here is a product or product lines of the company which can be harvested well. So, without much investment from the company side, the company can harvest this particular business.

So, this is what it means. So, when you look at this circle here, what are you trying to, what can you make out? You find that here the stage of market development is in the declining stage, so, you do not have a strong market; it is it has gone down for that particular product or product lines, product line.

So, in that market the size of the industries represented by this circle, whereas, the size of the company's market share is relatively small. So, it is a candidate for salvaging as much value as possible before it becomes 0.

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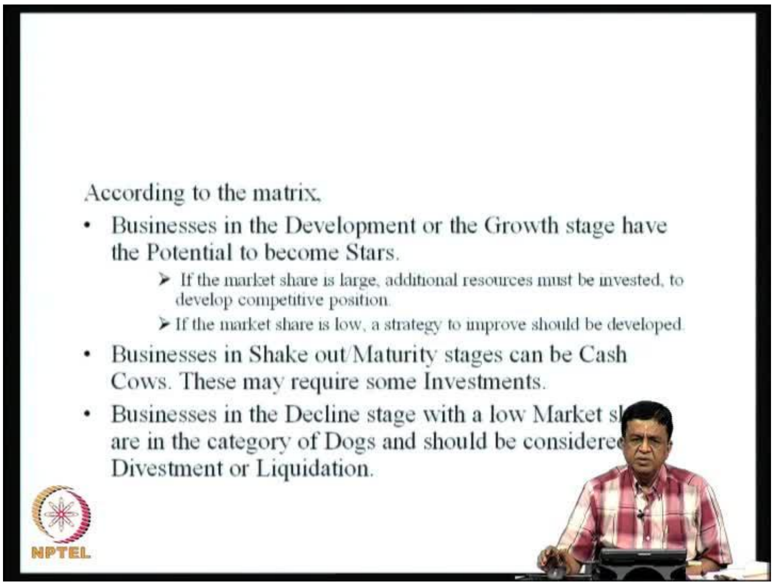

So, the, you would like to salvage or the company would like to salvage as much value as possible in this type of a situation. So, this is the way the whole market evolution matrix looks like, that is the Hofer's matrix evolution matrix.

So, what does it say? According to the matrix, that Hofer is the name of the person who gave this matrix. Businesses in the development or the growth stage have the potential to become stars. If the market share is large, additional the resources must be invested to develop competitive position.

If the market share is low, a strategy to improve should be developed. Businesses in shake out stroke maturity stages can be cash cows. This may require some investments but not always. Businesses in the decline stage with a low market share or in the category of Dogs and should be considered for divestment or liquidation.

So, you would like to salvage as much value as possible with respect to these products or product lines.

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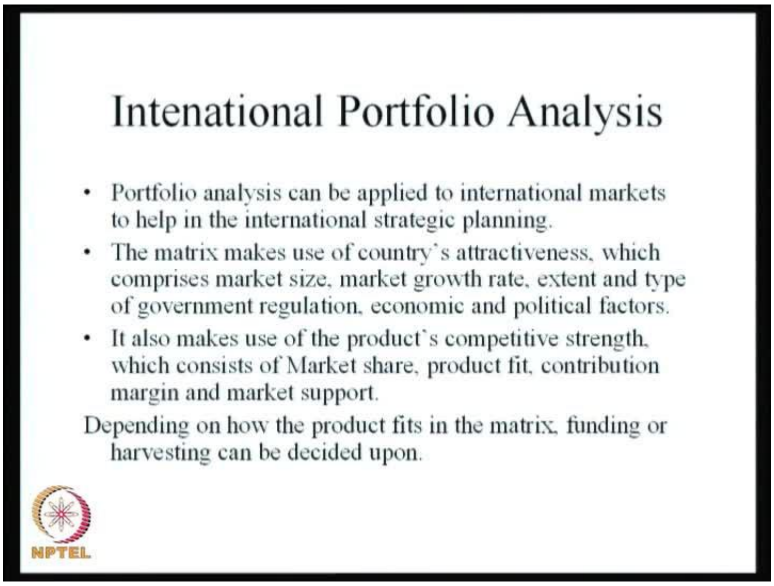

Now, having this background, the new things which are coming in in business. Now firms are looking at not just the country markets, we are looking at international markets.

If you look at our own companies, especially the software companies, they are looking at global markets. So, (( )) Infosys or Wipro or TCS or cognizant, name it, they are looking at global markets. So, when companies are looking at global markets, it may be more appropriate for them to look at international portfolio analysis.

So, the companies could consider looking at their international portfolios. So, what does that mean? They have graduated from these national portfolios or the country markets to international markets. So, the question that comes is - how does the international portfolio change?

What will be the type of changes which the company, companies have to put up with in this international scenario? Some points on this - portfolio analysis can be applied to international markets to help in the international strategic planning.

So, suppose, you are taking the strategic planning exercises one notch up to the international level; so, we looked at how the planning exercise has to be done.

So, starting from setting up objectives, then reworking on the objectives; if it is required, then drawing up short range plans, then drawing up medium range plans, then drawing up long range plans or drawing up appropriate alternatives.

So, we looked at different block diagrams. So, be it corporate planning or be it strategic planning, so, we looked at different approaches towards this whole planning process.

Now, when we are looking at international strategic planning, what can this portfolio analysis do? It can be applied to international markets to help in international strategic planning. What does this matrix, that is the international portfolio analysis matrix, what does it make use of? It makes use of the country's attractiveness.

What is meant by country's attractiveness? The country which you have picked up has market segment. Now, note that when you are moving to international market, that country itself becomes a market segment.

In that country, you may have different segments, but when you are looking at international portfolio analysis, let us say you look at Germany, Germany is the country segment for you. Similarly, you look at England, England is the country segment for you.

So, this is how the segments keep changing or the international segments start coming in when you are looking at international portfolio analysis. So, the matrix makes use of country's attractiveness, then how do you get this country's attractiveness.

It comprises market size, market growth rate, extent and type of government regulation, economic and political factors. So, what does that mean? You start giving index values to each one of these and draw this particular matrix.

So, this is a of the many of the international marketing texts, tell you, give you ideas about this index numbers. So, some of the papers written by Cavusgil, especially one particular paper tells you how to develop this index numbers for international marketing.

That can be very useful for this international portfolio analysis. So, it also makes use of products competitive strength which consists of market share, product fit, contribution margin, and market support.

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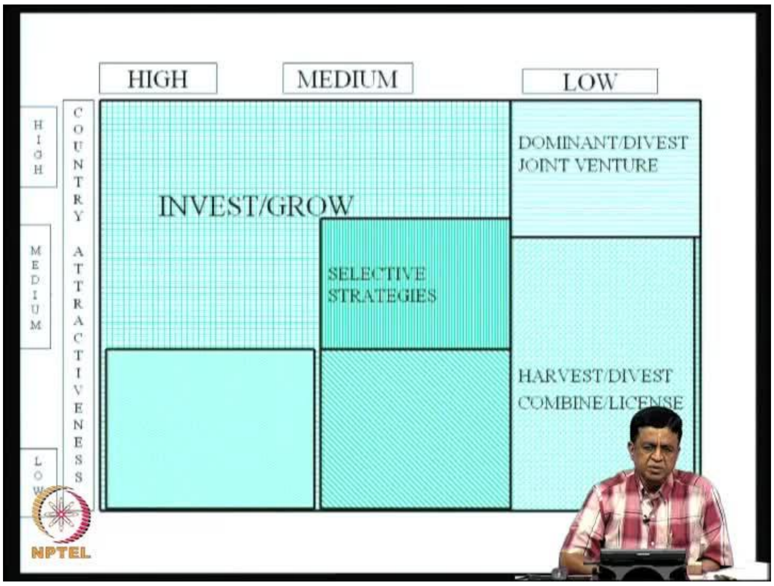

Depending on how the product fits in the matrix, funding or harvesting can be decided upon; so, typically it looks like this. If you look at the horizontal axis, not written in this, the horizontal axis represents the competitive strength of the product. The vertical axis represents the country attractiveness going from low to medium on both the axis, that is, you are going from low to medium on the competitive strength of the product; you are going from low to medium also on the country attractiveness.

Now, what does, what does this matrix tell you, or what is the type of ideas that it can reinforce? If you look at some of the regions here, the region where you are having high and medium competitive strength and you are having high and medium country attractiveness, those can be the regions where you can pick them for investment and growth.

Suppose, you have the market, the country attractiveness has medium and also the competitive strength of the product also has medium, then you have to be selective. So, you have to see whether investment is justified or not justified, and how much of investment can be done, all these types of questions required to be answered.

Now, suppose, the country attractiveness, that is the market attractiveness of the country is high, but your competitive strength, that is the company's competitive strength of product is low. Then you can consider whether you can enter into a joint venture with a dominant company which is already existing in the market place; it can be some sort of reseller type of things. So, which we can consider? Let us say, if you look at a typical scenario in the Indian market; the typical scenario could be the one which we can look at the space market.

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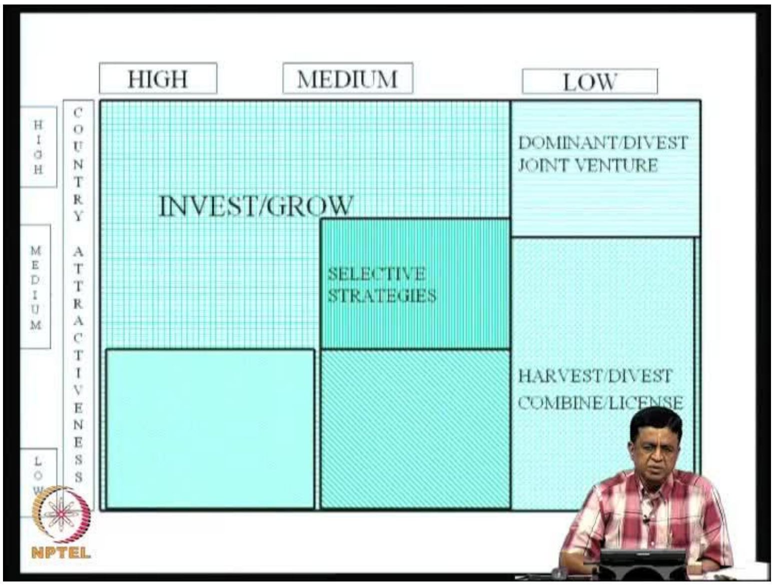

The space market with respect to international remote sensing data products and services. - IRS data products and services - Here this is the product or the product line for which ISRO through its commercial arm, the Antrix Corporation is looking for international market opportunities, trying to tap international market opportunities.

Now, take a typical, who are the competitors for this type of product or product line? So, you have competition from developed countries like the United States; so, you have the Geospatial, the Ikonos, all these types of different satellites which have been launched by these developed countries.

We have got competition from Russia also. So, sometimes there is a competition from Israel as well. So, given this type of a scenario, where is the, which country would you choose to make your presence felt. This is the one of the leading questions, which a, which an organization like ISRO will have to address first.

So, one of the typical markets which you can think of could be with the Latin American markets; the Latin American markets where like this Brazil, Chile, all these types of countries. So, look at the market size of these countries and find out what is the type of strategy that you can adopt to enter these markets.

This is typically your international portfolio analysis. So, put the country markets on the vertical axis. Now Brazil is on one side, do you want to make use of Brazil and enter the adjoining Latin American countries?

So, in which case, do you want to have a joint venture in Brazil? That is, there will be a dominant player, may be the US player is already having an office in Brazil. You can find out whether he would be interested in entering into a joint venture with you.

If he is interested in entering into a joint venture with you, then you can consider appropriate terms, and then, using these appropriate terms, you can see whether you can tap the other adjacent country markets through this dominant players. So, this can be, this could be the one of the methods of entry.

So, a joint venture, when you enter in that manner, what does it mean? This means that the risk is getting less. So, you are not making investment into setting up the facilities like the ground station. That is ISRO is not making investments to set up facilities like the ground station, all those types of things in this different Latin American markets, but it is making use of the facilities which is already there by this existing players.

So, and then trying to find out whether it can tap some of these markets. Of course, there is a certain amount of transfer of funds which are going to be involved in all this, which has to be worked out. So, this is the typical scenario which you will find in this type of market.

So, where you, in this joint venture type of situations. Now, let us say you look at this particular cell, where you have the markets, that is the attractiveness of the country markets going from medium to low.

So, you are really typically going from medium to low, then what does it mean? These are candidates for harvesting or divesting, so, in such a type of situation, you can see, you can consider whether you can combine with the existing players or license, suppose, you have already got your production units since in your country, you want whether you can license it to some of those local players, that is, he will be producing some of the products under license from you.

So, this is the type of scenario which you can think of, so that the losses that you may incur or the investment that you may incur may get minimized, to that extent, the risk also gets minimized.

So, you can typically see in this type of international portfolio analysis sells where you can invest and grow; where you can be, where you have to be selective, not very sure of, how to, what could be the most appropriate strategy, but depending on the situation, select the most appropriate one.

Then, see whether you can be a dominant player, whether calls were divestment, whether you can make use of the joint venture option, or where, in some of the countries with respect to your businesses, that is a competitive strength of the product, whether you can make use of harvesting or divesting.

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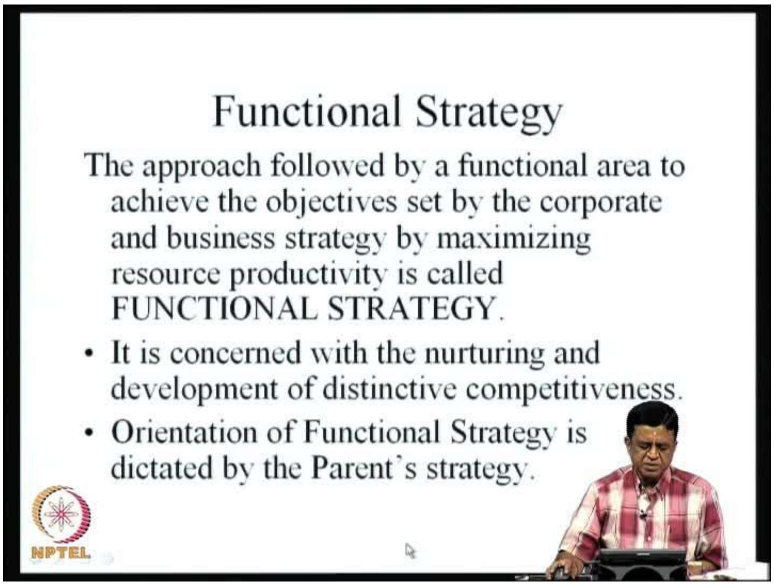

So, there, in such situations, you can combine with an existing player or give the license of production to some player's, local players. So, this could be the typical, this is the typical way this international portfolio analysis matrix looks like.

So, the, when you, as I said this matrix makes use of the countries attractiveness, so, depending on those different shares. So, this is, and depending on that, the funding or harvesting can be considered.

So, if you look at what Porter says, Porter says in a global industry, according to him, it may not be advisable to use portfolio analysis on a country by country basis. According, as to port, he may say in a global industry, however managing international activities like a portfolio will undermine the possibility of achieving competitive advantage.

In a global industry, a firm must in some way integrate its activities on a worldwide basis to capture the linkages among countries. So, this is what he advocates. Now, this is the, this is one of the things which can be used, when the company is go international. Now, the companies can also make use of, what we call the corporate parenting?

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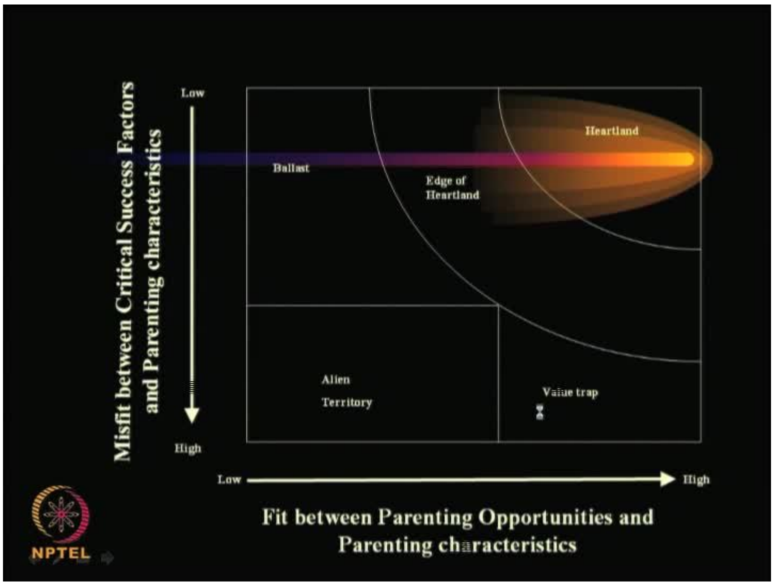

What is corporate parenting? This corporate parenting, it looks, it is something like this. How does, what does this parenting do? It looks at the fit between parenting opportunities and parenting characteristics.

It also looks at the misfit between critical success factors and parenting characteristics. This is a matrix given by this Campbell et al.

So, corporate, according to them, corporate parenting views the corporation in terms of resources and capabilities to build business unit value and generate synergies across business units.

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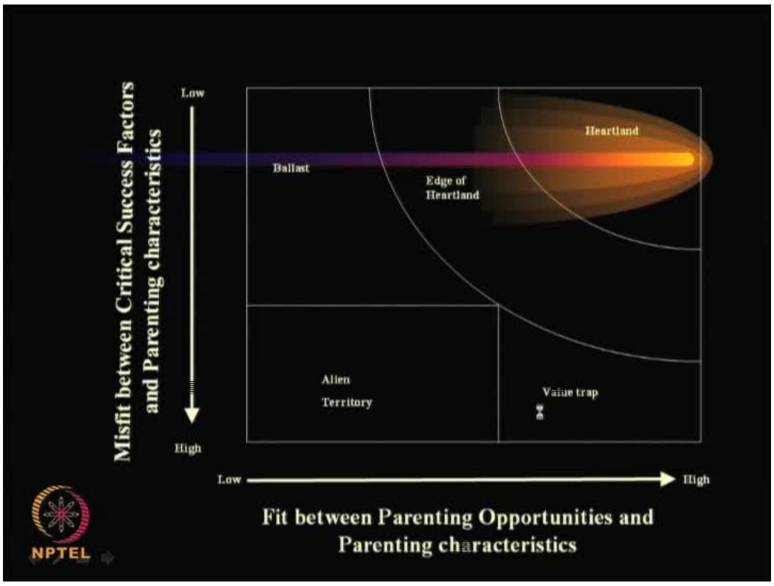

According to them, corporate parenting can help generate corporate strategies on by focusing on core competencies of the parent corporation, and the value created from the relationship between the parent and its business unit.

So, this portfolio fit matrix, that is the corporate parenting portfolio fit matrix, which, these three people gave that is Campbell, Bolt, and Alexander, it can help form a judgment on the corporate stroke business units fit in the whole corporation.

What does it do? It emphasizes the fit of the business with the parent. The matrix is composed of two dimensions. The positive contribution of the parent can make, and the parent’s negative effects can again be a, what do you call, if you really look at it, the positive contributions of the parent can be good for the company.

That is the subsidiary for the negative effects. It can take care of the negative effects also sometimes, that is, some of the negative effects will also get lessened by the impact of this positive effect of the parent.

So, you may be having when you are operating in a particular region some negative effects. So, if the parent is able to give some positive effects on you, this negative effects can get lessened the different combinations of these dimensions. If you really see create five different positions, each having an implication for corporate strategy.

If you look at the top point here, that is the heartland. So, this heartland, what does it tell you? That is the top right corner of this matrix. They are the heart of the corporate future, these heartland businesses present opportunities for improvement by the parent and the parent understands their critical success factors well.

So, they should have priority for all corporate activities. now, when you are looking at the edge of the heartland, that is the second one, here, the parent may not have all the characteristics needed by the unit or may not understand the units at critical success factors.

In such circumstances, the parent needs to know when to interfere in the business units activities and strategies and other times should stay away. So, that means to say, that is, what I was trying to say, some, in some of the situations, the positive effect of the parent can be felt, and sometimes it can also take care of some of the negative aspects of the unit which is operating there.

So, parent, it can be the main unit, that is a corporate unit; the other one could be the subsidiary operating at a different place. What about the third? This thing ballast these business units, refer to units that have been with the company for a long time and have been successful.

They fit well with the corporation. Since there is always a danger, that environmental changes can move a ballast unit to an to Allen territory corporate decision makers should divest this business unit as soon as they get a price exceeding the value of future cash flows.

So, these are units for divesting, then what about Allen territory? They have very little opportunity to be improved by the parent. So, there is a misfit there. So, when there is a misfit exist between the parent characteristics and the unit, that is the misfit exist between the parenting characteristics and the units critical value.

Generally, these business units are small and often remnants of past diversification, so, it may be better to divest these units. So, investments in the value trap business. This is the last cell which is put here. They fit well with the parental opportunity, but are a misfit with parents understanding critical success factors.

So, thus, there is a good chance of the parent making a big mistake. So, these are, what do you call? Where, you get into the doom loop type of a situation which we discussed earlier.

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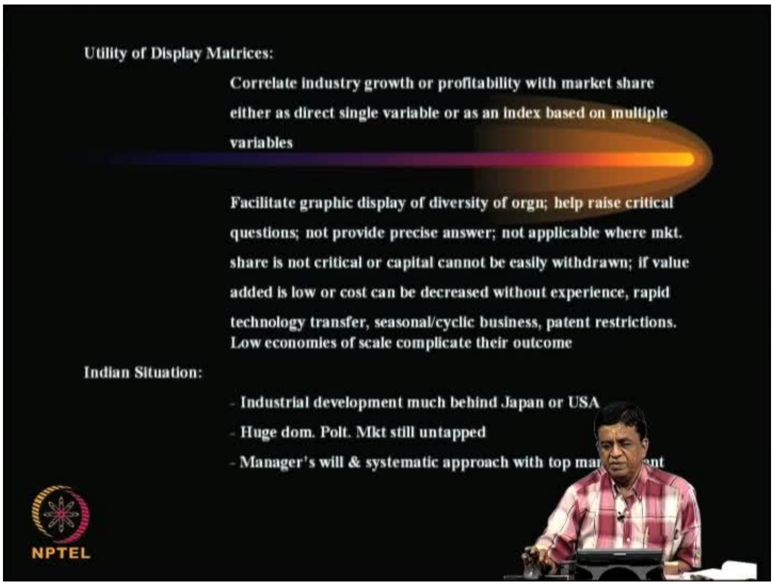

So, the parent should avoid getting into this doom loop. So, this is called value trap by these three people. So, this is the way you can represent corporate parenting. Now, this is, these are the different matrices that can be used.

Now, let us look at what is the utility of these display matrices in general. So, we looked at so many display matrices starting from the first matrix down to this particular matrix; we have looked at the BCG growth share matrix.

We looked at the new BCG growths, BCG matrix; we looked at the G-Businessgreen, then we looked at the Mckinsey matrix; then we looked at the strategic planning institute matrix or the Kim’s model; then we looked at the shelves directional policy matrix.

Then we looked at the Arthur D’little company’s matrix; then we looked at the Hofer’s product stroke market evolution matrix; then we looked at international portfolio analysis; then we capped all of this with this corporate parenting.

So, these are some of the matrices that you can make use of for portfolio analysis. What is the utility of all these display matrices? They correlate industry growth or profitability with market share either as direct single variable or as an index based on multiple variables.

This is what I kept on mentioning to you. So, you have to develop an index, they facilitate graphic display of diversity of organization help raise critical questions, not provide the precise answer kindly note that.

Many times they may not be providing you the precise answer, not applicable where market share is not critical or capital cannot be easily withdrawn. In other words, what does it mean? Capital cannot be easily withdrawn; you should be able to exit the market without too much of a hassle.

Suppose, your exit routes are blocked. Sometimes, in some markets, your exit routes are blocked. In that type of a scenario, you cannot make use of this portfolio analysis. So, when the exit is blocked there is not much for the company to do, so, you have to operate in that particular market.

So, that is the situation where you find many of the monopoly firms. Suppose, you are a monopoly firm, you cannot exit the market, your exit is virtually blocked, no route open for you. So, in that type of a situation, the utility of these display matrices, what all we considered, it is very minimal, you cannot make use of them.

So, the, if value added is low or cost can be decreased without experience, that is where experience curve does not operate, then again the utility of this display matrices is low.

So, your experience curve should operate, that is based on the experience in producing the product. The cost of production should come down with the number of units increasing that is the experience curve effect.

Suppose, you are you are learning in the process. So, when the number of units of production increases, the cost per unit should come down. Suppose, it is not following this particular principle, then this utility of these display matrices becomes a question mark there also.

Then rapid technology transfer seasonal stroke cyclic business patent restrictions low economies of scale all this complicate there outcome. So, what is the Indian scenario? If you really, see, if you make, a, an analysis of the Indian scenario, the Indian scenario is typical scenario.

The industrial development is much behind in Japan or USA. There is a huge domestic market potentials till untapped. So, that means, there is a lot of domestic market; so, that is also one of the reasons why you are finding large number of foreign players entering different markets in India.

So, you name the market - whether it is the mobile phones market, or whether it is the automotive market, or whether it is the textiles market, or sometimes, whether it is a simple consumable consumer eatable market.

You find almost all the well-known foreign players have made their foray into these markets. So, you take the soft drinks market. All the global players are there even you take a simple market like the cornflakes, even that is being attacked, that is a local player's market share is being attacked by a well-known company like Kellogg's.

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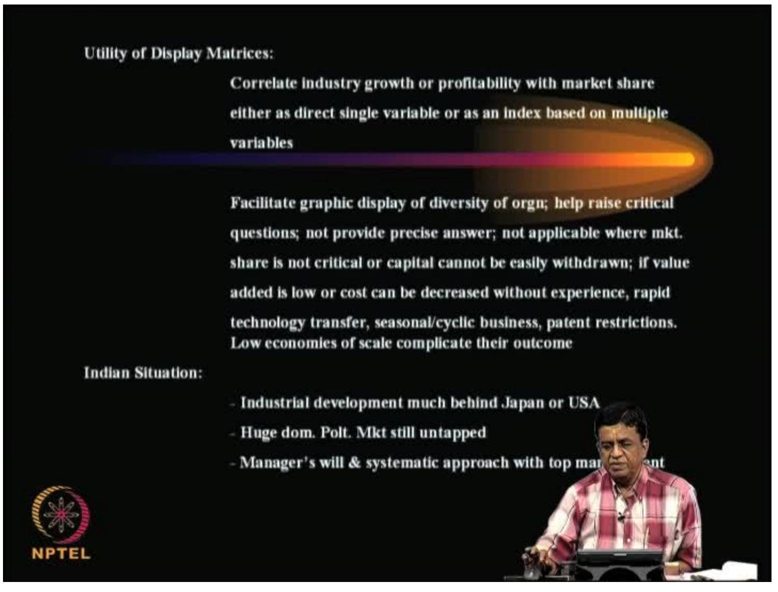

Now, take the restaurant market. You have many foreign restaurants operating in India; you have the McDonalds; you have the KFC's; and you have day in and out different players entering the market.

So, in other words, this market situation in India is becoming more and more competitive, that is the local players, if they are not able to adopt to this type of market influx, that is influx of players from the foreign markets trying to gobble up their market share.

Then, what is likely to happen? You may find that these local players may become extinct or the local players may be forced to join hands with these foreign players. They may be suppliers of products to these foreign players only, and the product may be coming to you.

The earlier local player’s product might be coming to you from the foreign player. So, that type of scenario also can come in that is, because of the type of domestic market potential which is existing in our country.

So, you have a huge domestic market potential, which, this foreign firms want to tap. So, if you really look at it, I can recall one particular brand of mango juice which was available in the city of Bangalore, which was considered very good, very tasty. Now, what is the scenario? That particular brand of mango juice is not available to you in Bangalore, but it has been virtually gobbled up by these major players.

So, this small industry which was putting out this wonderful juice taking the mango extracts which were available in the state virtually has close down, in the sense, that it is not operating under its brand name.

So, this foreign players to the extent, they can make use of their production. The local player’s production facilities, they are making use of it, otherwise, have made that player to become extinct from the market place.

So, this is what can happen in a typical scenario, where you have too many market players influx. This is also happening as you are seeing what is the recent thing you find that even the education field is not being spared?

You find now some of the foreign universities also trying to enter the Indian market. So, the government is trying to facilitate their entry into the Indian education scenario as well.

So, what is the likely scenario? You can see what is the type of reasoning which is being advanced by the government. The government is saying, why should, the, our students go to foreign countries to study and make that country rich instead they can study here, only, and we will be getting those types of, what do you call, the fees or whatever.

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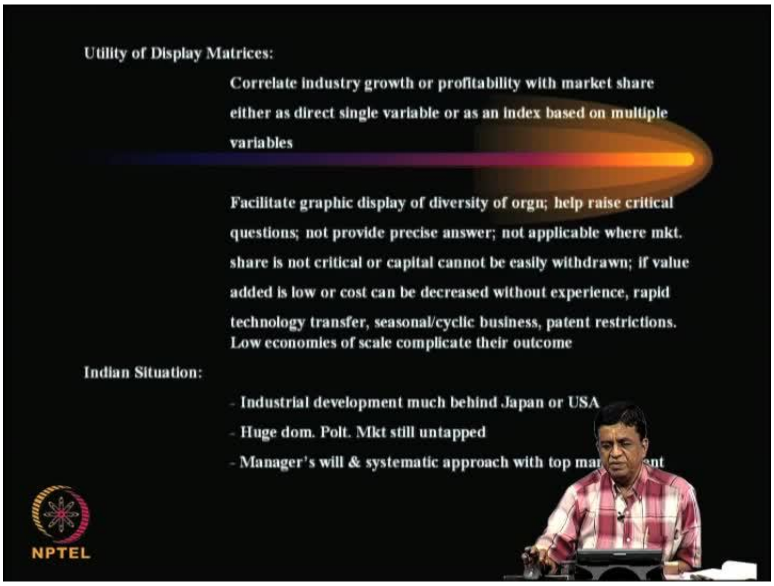

That money can be paid to the Indian government's. This thing only the Indian government gets revenues whatever it is in that time the way of understanding between the foreign universities and the government of India.

The type of (( )) which can be gotten into. So, this is what again the same concept of huge domestic potential market, the education sector is being viewed as a huge domestic potential market which can be tapped, not fully tapped allowed to be tapped even by the foreign universities.

So, this is the type of scenario which you are likely to see in a few years from now. Now, the next point that can come in is the manager's will and systematic approach with top management support can help make use of these matrices for developing competitive strength and corporate growth.

So, unless and until the manager gets the top management support, he has virtually no possibility of implementing many of these things. Having looked at all these, let us look at some of the other types of strategies that can be adopted in organizations.

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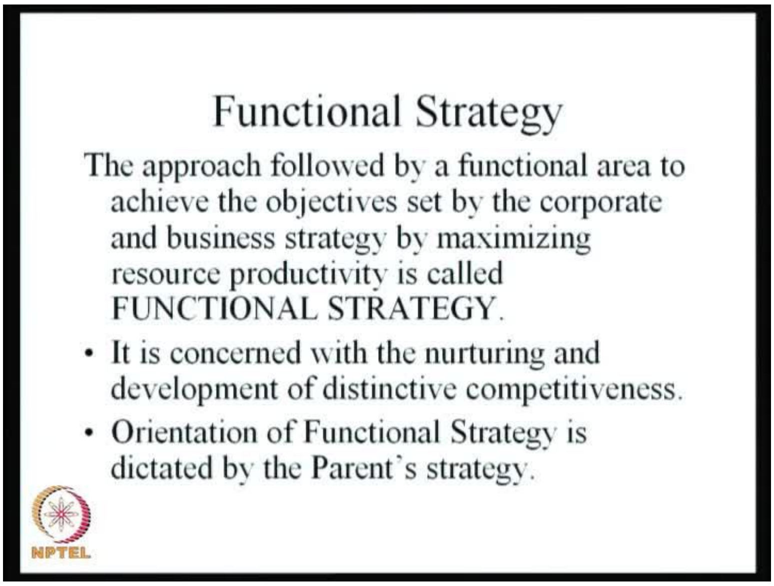

Some of these strategies could be, the, this is, what is called the functional strategy? What is this functional strategy? This is an approach followed by a functional area to achieve the objectives set by the corporate and business strategy by maximizing resource productivity.

So, you look at productivity of the resources. So, try to maximize the productivity of your resources that is looking at your production line per (( )) can be labour productivity, can be machine productivity, all types of productivities.

So, you look at productivities from all angles maximize that productivity. Then you have this functional strategic approach, so, this is what many of these automotive units are looking at now. So, a typical TVS, let us say looks at this functional strategy very closely, so, wants to make use of its resources productively. So, the productivity of these resources, it wants to maximize. So, in other words, this functional strategy is a very important component for a company like this TVS.

So, it is concerned with what does this give the company. It can help create a distinctive competitiveness for the company. So, you are trying to maximize your productivity, so, what does it do for the company?

It can help in nurture and develop distinctive competence again this orientation of the functional strategy is dictated by the parent, that is functional area. What should be the strategy the company will dictate?

The functional area itself cannot take the decisions. The parent has to accept this decisions, and then, allow the functional areas strategy team to operate. This is what the functional strategy means stands for.

So, what is this distinctive competency which we are looking at it has to meet three test - one is the customer value; second is the uniqueness of the competitor, that is the competitor unique; then the extendibility of this whole scenario, that is how much can you extend this extendibility.

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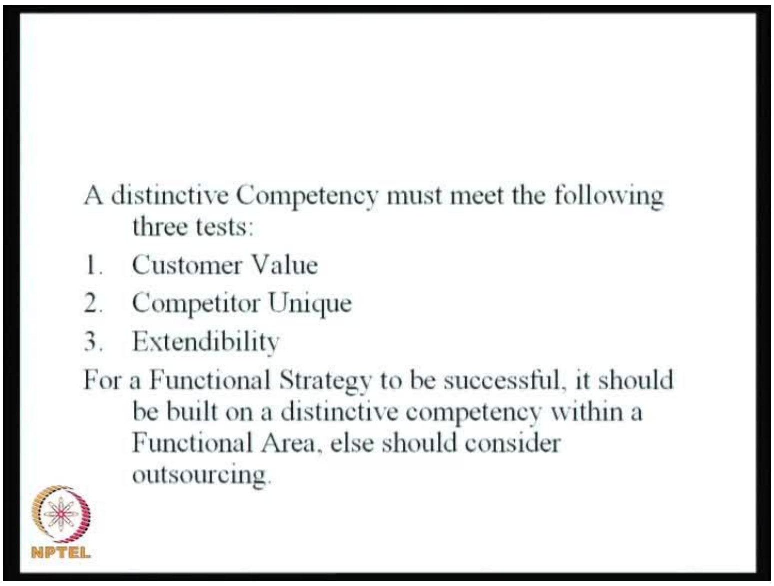

So, what does this customer value stand for? It must make a disproportionate contribution to the customer's pursued value. Suppose, the customer pursues your product value as rupees x initially by using the product, he must say it has given me two x.

Similarly, what does this competitor unique mean, it must be unique and superior to competitor's capabilities compared in terms of the customer's perception. He must think that your product is much better or superior to the competitors' product.

Then, what is this extendibility? You can make use of this product to develop new products or services and enter new markets. So, this is the three competence, three test of this distinctive competency.

So, for this functional strategy to be successful, it should be based on a distinctive competency within a functional area. If it is not else, you should consider outsourcing. Suppose, you are having that distinctive competency in your functional area, fine, go ahead and with this functional strategy.

If you do not have that, then you should consider outsourcing that particular activity. Suppose, it is a software firm, you are not an expert in transport activities; the transportation department can be outsourced.

So, if you look at most of these software major companies, they do not operate their transport departments earlier, the, our (( )) whether it was whether it is HAL or ITI or Bell, they are having their own transport departments.

It is a huge out go of money. Now, what are these software companies done? They have considered this activity for outsourcing, they said: we do not want to get involved in this exercise. Let this activity be outsourced, so, this what it means.

For a functional strategy to be successful, it should be built on distinctive competency within a functional area. Suppose, you are not able to, else, it should consider outsourcing. We will stop here, we will continue in the next class. Thank you.