

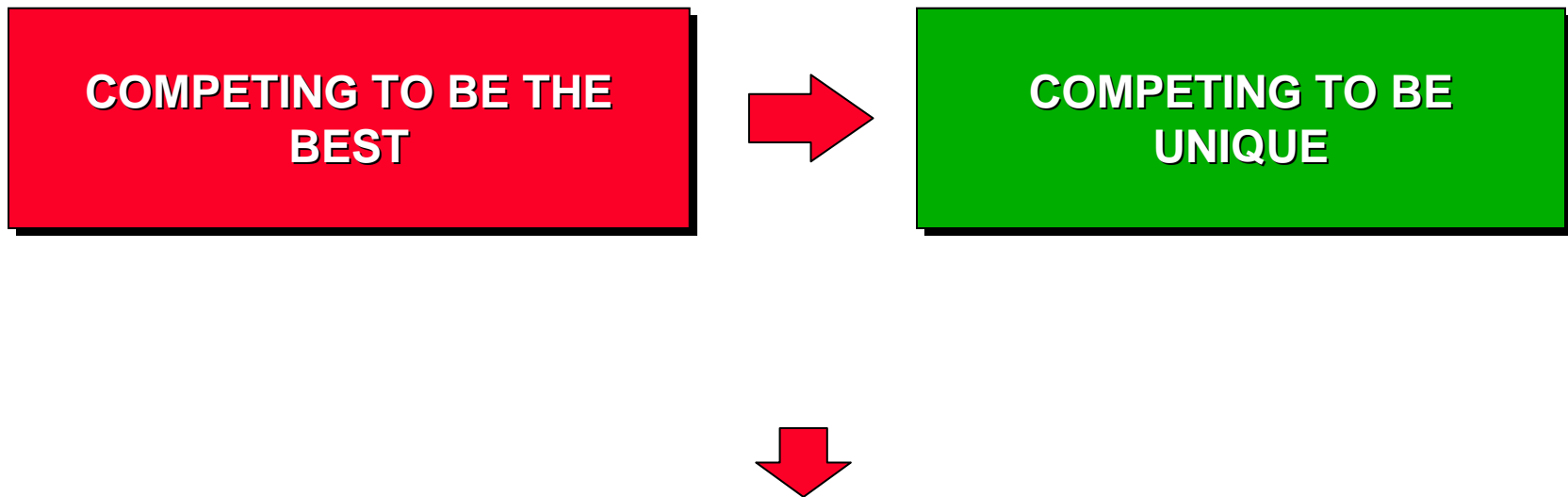
Strategic Thinking: Implications for Turkish Companies

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Harvard Business School
Istanbul, Turkey

October 17, 2009

This presentation draws on ideas from Professor Porter's books and articles, in particular, *Competitive Strategy* (The Free Press, 1980); *Competitive Advantage* (The Free Press, 1985); "What is Strategy?" (*Harvard Business Review*, Nov/Dec 1996); "Strategy and the Internet" (*Harvard Business Review*, March 2001) and *On Competition* (*Harvard Business Review*, 2008). No part of this publication may be reproduced, stored in a retrieval system, or transmitted in any form or by any means—electronic, mechanical, photocopying, recording, or otherwise—without the permission of Michael E. Porter. Additional information may be found at the website of the Institute for Strategy and Competitiveness, www.isc.hbs.edu. Version: Oct 14, 2009

Strategic Thinking



- The worst error in strategy is to compete with rivals on the **same dimensions**

Flawed Concepts of Strategy

- Strategy as **action**
 - “Our strategy is to merge...”
 - “... internationalize...”
 - “... consolidate the industry...”
 - “...double our R&D budget...”
- Strategy as **aspiration**
 - “Our strategy is to be #1 or #2...”
 - “Our strategy is to grow at...”
 - “Our strategy is to provide superior returns to our shareholders...”
- Strategy as **vision**
 - “Our strategy is to best understand and satisfy our customers’ needs...”
 - “...to advance technology for mankind...”



- Strategy defines the company’s **distinctive approach** to competing and the **competitive advantages** on which it will be based

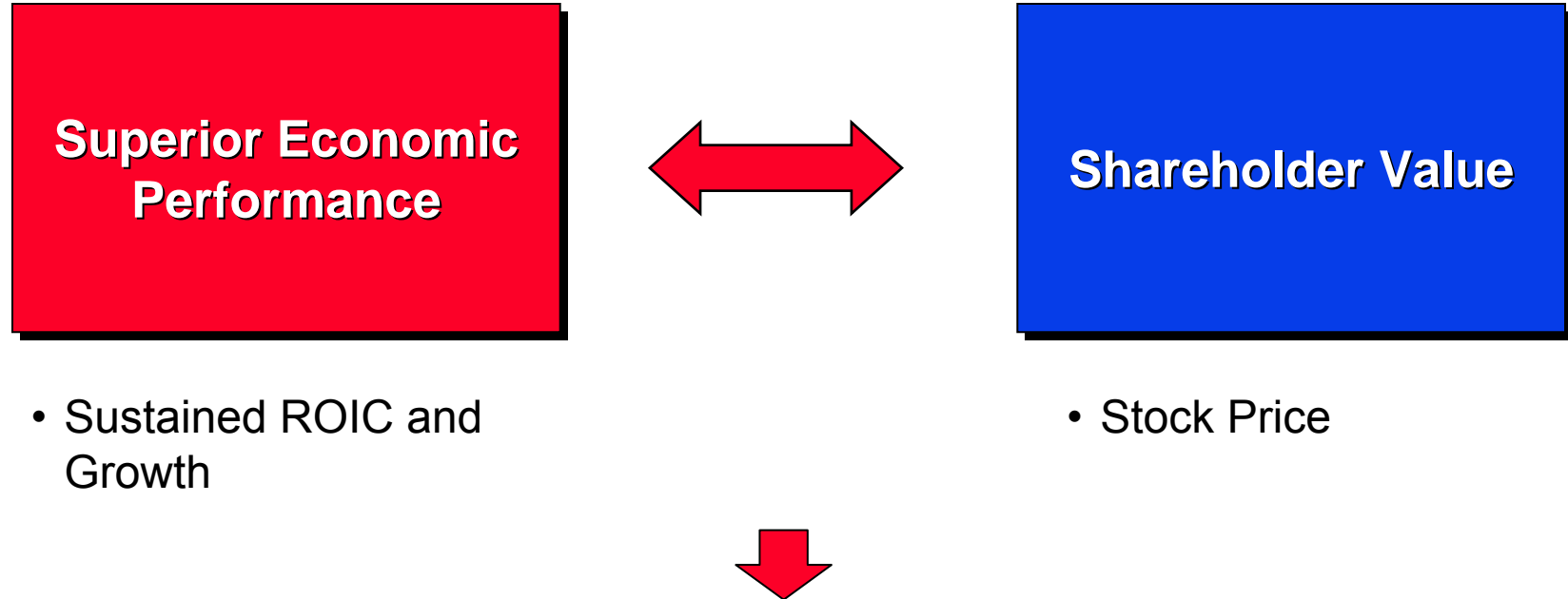
Setting the Right Goals

- Strategic thinking starts with setting **proper financial goals** for the company



- The fundamental goal of a company is **superior long-term return on investment**
- Growth is good only if superiority in ROIC is **achieved and sustained**
 - ROIC threshold
- Setting **unrealistic profitability** or **growth targets** can undermine strategy

Shareholder Value Is Not The Goal



- Sustained ROIC and Growth

- Stock Price

- Shareholder value is the **result** of creating real economic value
- Pleasing today's shareholders is **not** the goal

Levels of Strategy

Competitive or Business Strategy

- How to compete in each **distinct business or industry**



Corporate or Portfolio Strategy

- The company's **overall mix of businesses** and the integration of **business unit strategies**

Economic Fundamentals of Competition

- The unit of strategic analysis is the industry
 - **Defining the relevant industry** is essential to sound strategy
- Company economic performance results from **two distinct causes**



- *Overall Rules of Competition*

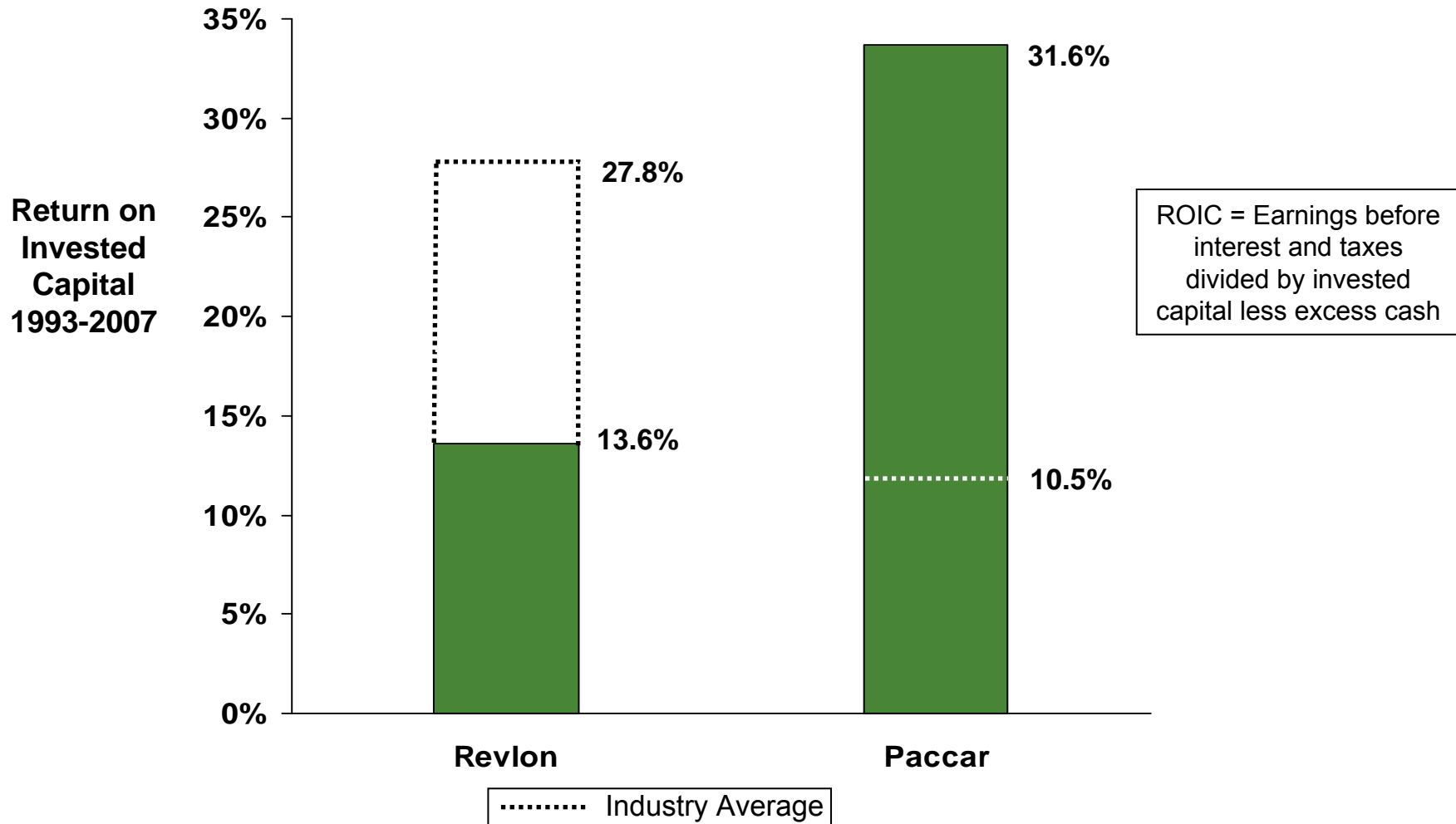


- *Sources of Competitive Advantage*



- Strategic thinking must encompass **both**

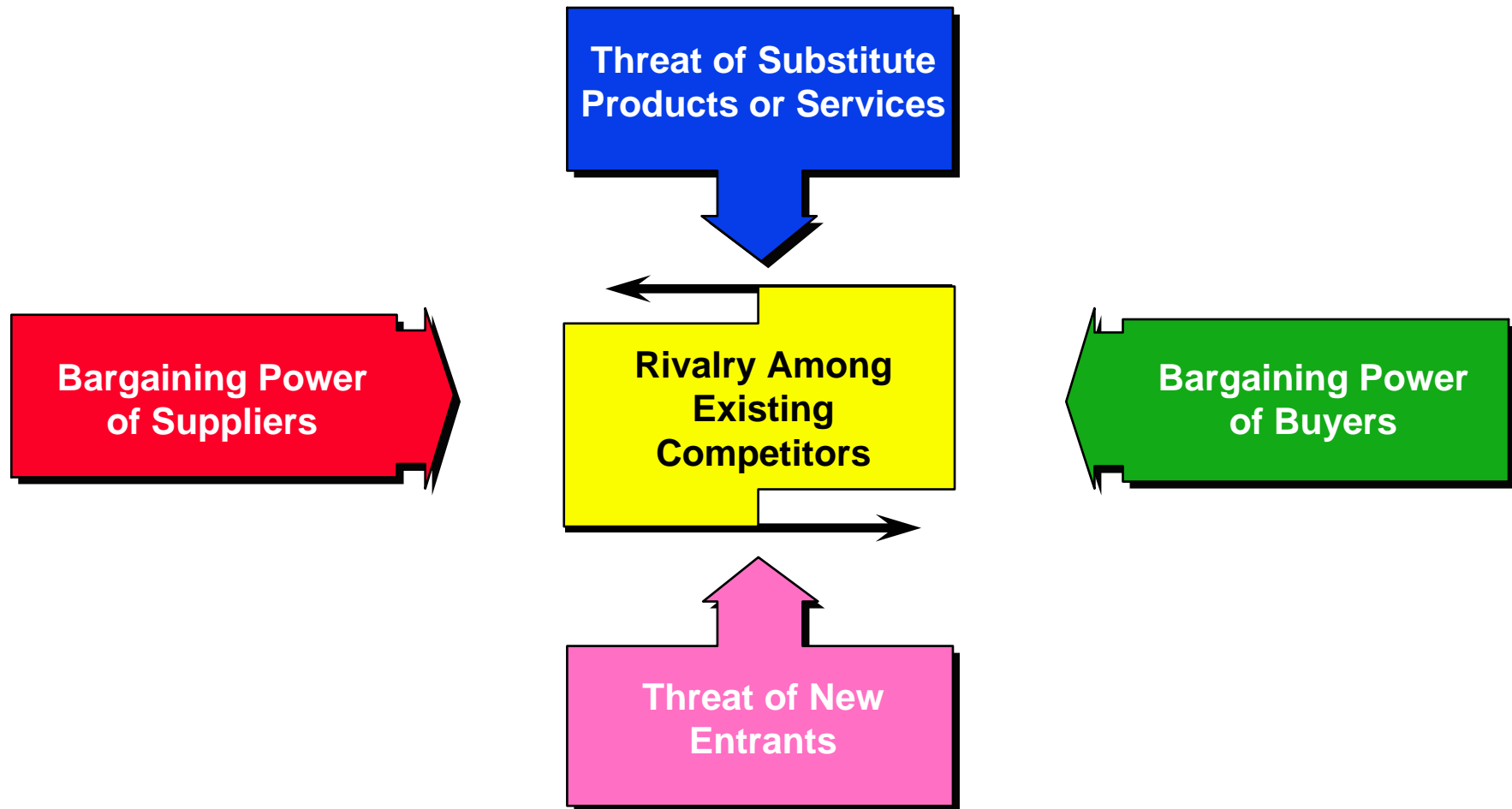
Disaggregating Economic Performance: Industry vs. Position



Note: Excess cash is calculated by subtracting cash in excess of 10% of annual revenue.

Source: Compustat (2008), author's analysis

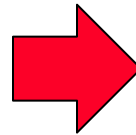
Understanding Industry Structure



Redefining Industry Competition

Zero Sum Competition

- Compete **head to head**
- One company's **gain** requires other companies **loss**
- Competition **undermines** industry value



Positive Sum Competition

- Compete on **strategy**
- **More than one** company can be successful
- Competition **expands the value pool**

Positioning and Industry Structure

Heavy Trucks

Threat of Substitute Products or Services

- Railroads
- Water transportation

Bargaining Power of Suppliers

- Large independent suppliers of engines and drive train components
- Unionized labor

Rivalry Among Existing Competitors

- Heavy price competition on standardized models


Bargaining Power of Buyers

- Large fleets
- Leasing companies
- Small fleets and owner operators

Threat of New Entrants

- Many truck producers are assemblers

Paccar Strategic Positioning

- Focus on **owner-operators**
 - Design trucks with **special features** and **amenities**
 - Customization and **build-to-order**
 - Design for low truck **operating** costs
 - Offer extensive **roadside assistance** to truckers
- 
- **Premium** price
 - **Different** customers / **different** basis of competing

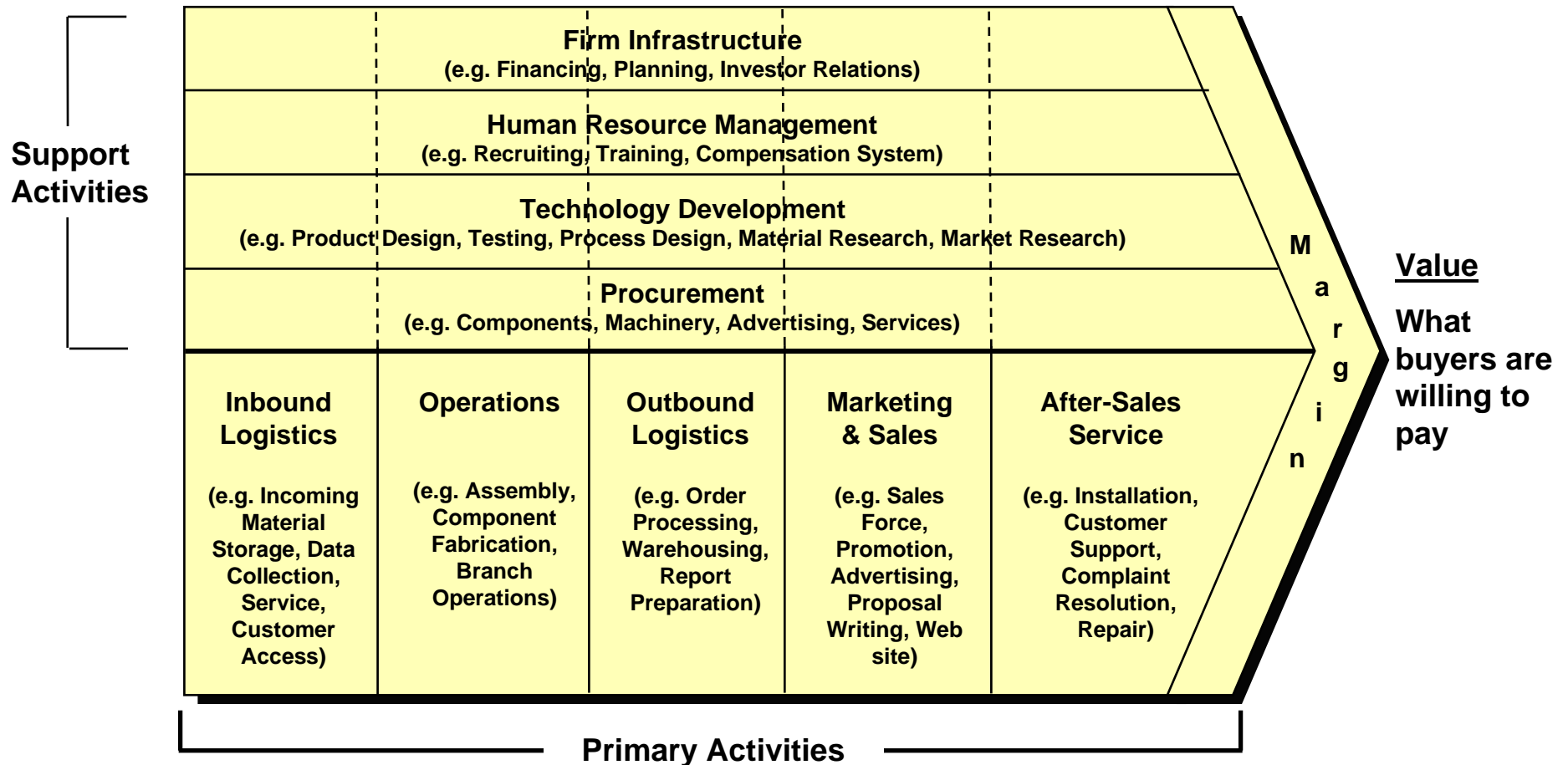
Strategic Positioning

Economic Fundamentals



Foundations of Competitive Advantage

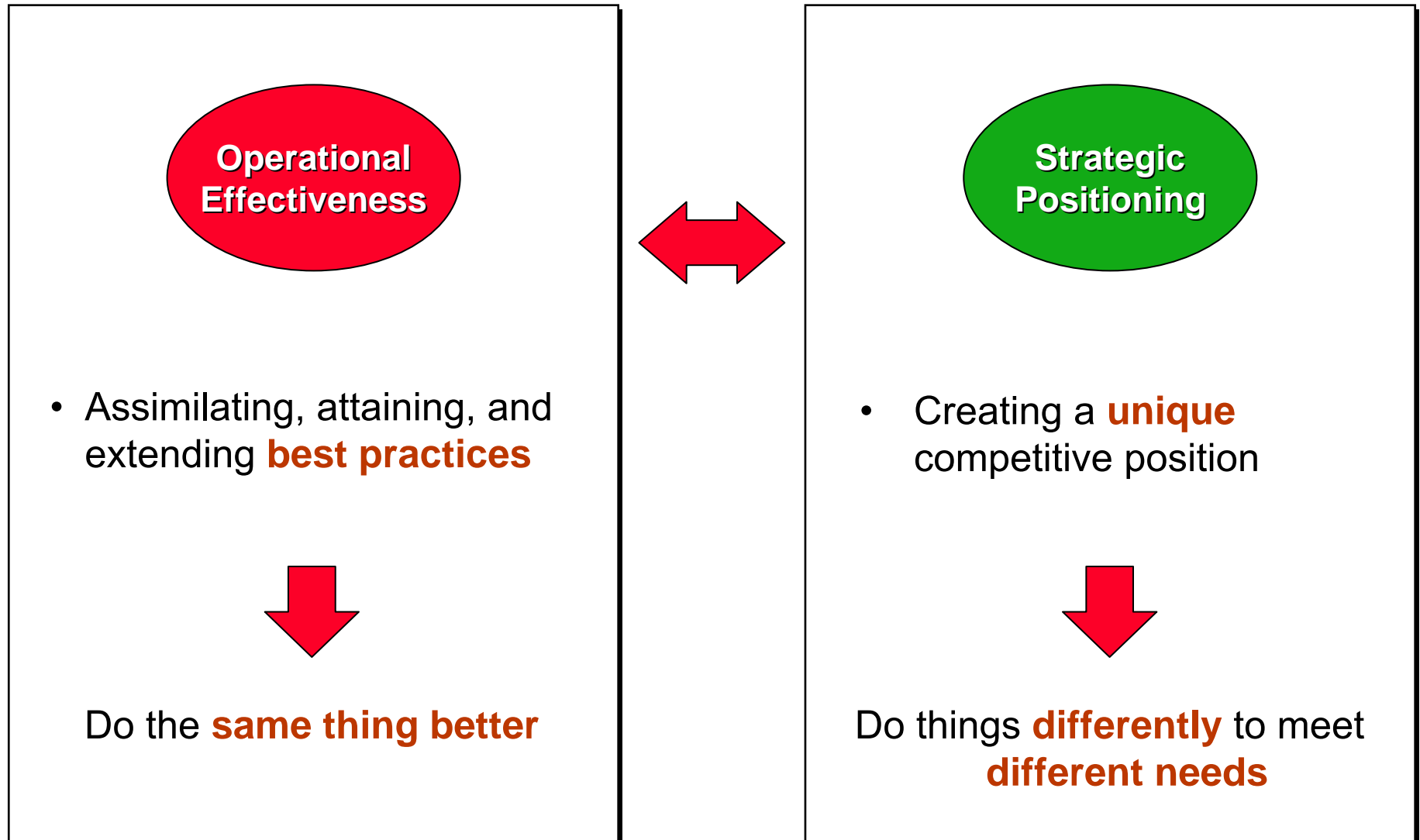
The Value Chain



- Competing in a business involves performing a set of discrete **activities**, in which **competitive advantage resides**
- Strategy is reflected in how activities in the value chain are **configured** and **linked together**

Achieving Superior Performance

Operational Effectiveness is Not Strategy



Five Tests of an Excellent Strategy

- A **unique value proposition**
- A **different**, tailored value chain
- Clear tradeoffs, and choosing what **not to do**
- Activities in the value chain that **fit together and reinforce each other**
- **Strategic continuity** with continual improvement in realization

Strategic Positioning

IKEA, Sweden

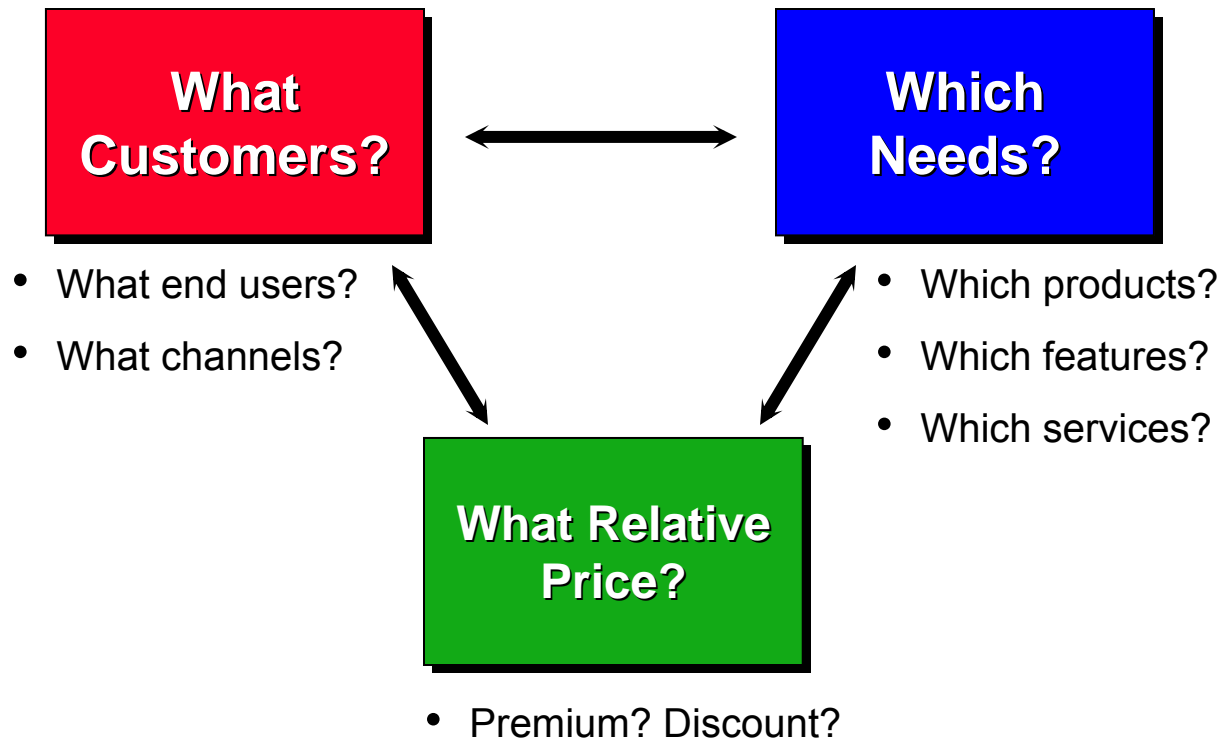
Value Proposition

- Young, first time, or price-sensitive buyers
- Stylish, space efficient and scalable furniture and accessories at very low price points.

Distinctive Activities

- Modular, ready-to-assemble, easy to package designs
- In-house design of all products
- Wide range of styles displayed in huge warehouse stores with large on-site inventories
- Self-selection
- Extensive customer information in the form of catalogs, explanatory ticketing, do-it-yourself videos, and assembly instructions
- Ikea designer names attached to related products to inform coordinated purchases
- Long hours of operation
- Suburban locations with large parking lots
- On-site, low-cost, restaurants
- Child care provided in the store
- Self-delivery by most customers

Defining the Value Proposition



- A distinctive value proposition usually **expands the market**

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Making Strategic Tradeoffs

- Tradeoffs exist where strategic positions are **incompatible**

Strategic Tradeoffs

- Incompatible product or service **features or attributes**
- **Differences in the value chain** deliver a chosen value proposition
- Inconsistencies in **image or reputation** across positions
- Limits on organizational capacity to **implement** multiple ways of competing simultaneously



- Tradeoffs make strategy **hard** for competitors to imitate
- An essential part of strategy is choosing what **not** to do

Strategic Tradeoffs

IKEA, Sweden

IKEA

Product

- Low-priced, modular, ready-to-assemble designs
- No custom options
- Furniture design driven by cost, manufacturing simplicity, and style

Value Chain

- Centralized, in-house design of all products
- All styles on display in huge warehouse stores
- Large on-site inventories
- Limited sales help, but extensive customer information
- Long hours of operation

Typical Furniture Retailer

Product

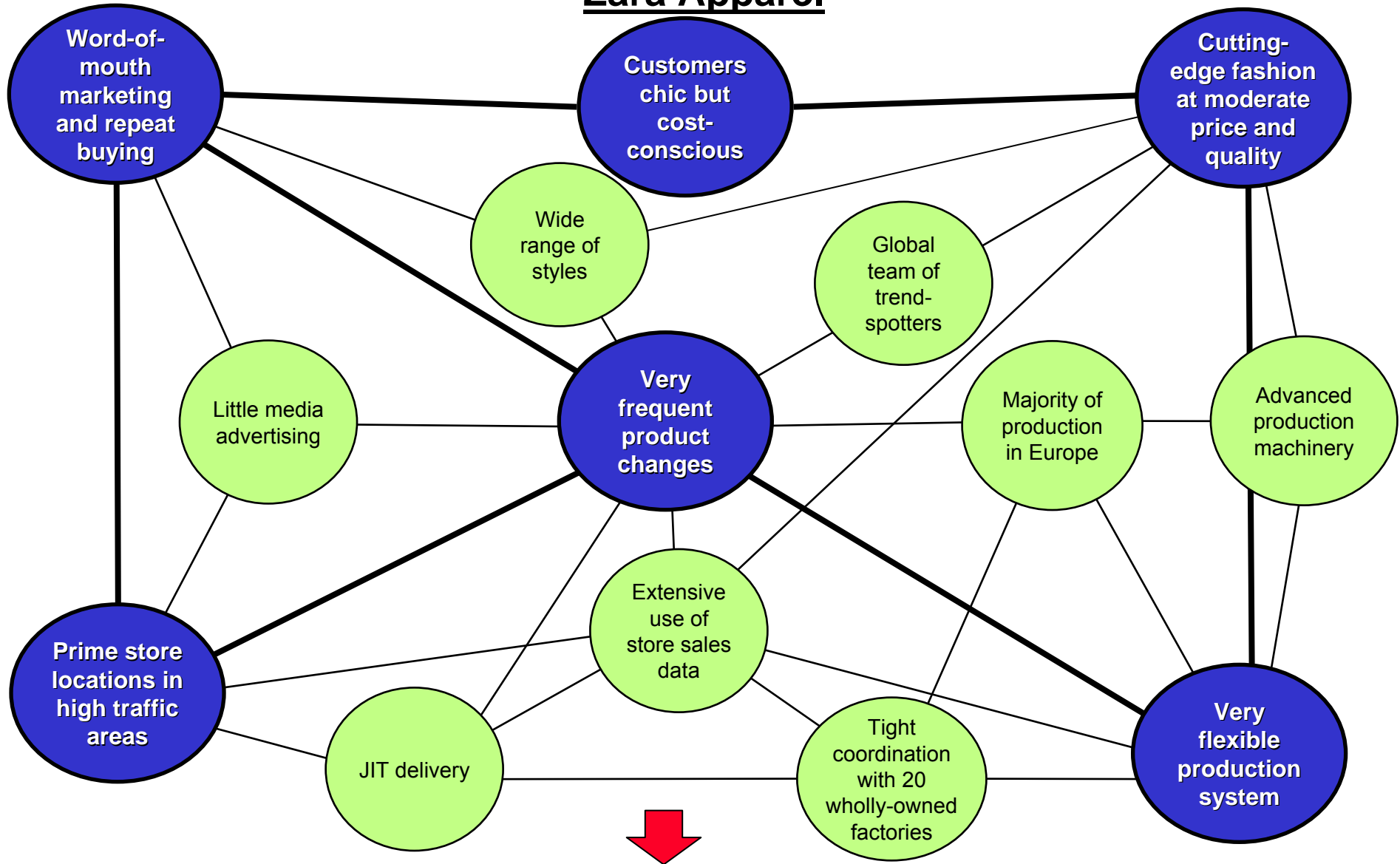
- Higher priced, fully assembled products
- Customization of fabrics, colors, finishes, and sizes
- Design driven by image, materials, varieties

Value Chain

- Source some or all lines from outside suppliers
- Medium sized showrooms with limited models on display
- Limited inventories / order with lead time
- Extensive sales assistance
- Traditional retail hours

Integrating the Value Chain

Zara Apparel



- Strategic fit comes from leveraging what is different to be **more** different

Strategic Continuity

- **Continuity of strategy** is a precondition for sustainable competitive advantage
 - e.g., **understanding** the strategy
 - building truly **unique skills** and **assets**
 - establishing a clear **identity**
 - strengthening **fit**
- **Reinvention** and **frequent shifts in direction** are costly and confuse the customer, the industry, and the organization



- Strategic continuity requires an **enduring value proposition** while **continuously improving** ways to **realize it**
 - Strategic continuity and continuous change should occur **simultaneously**
 - Continuity of strategy allows learning and change to be **faster and more effective**

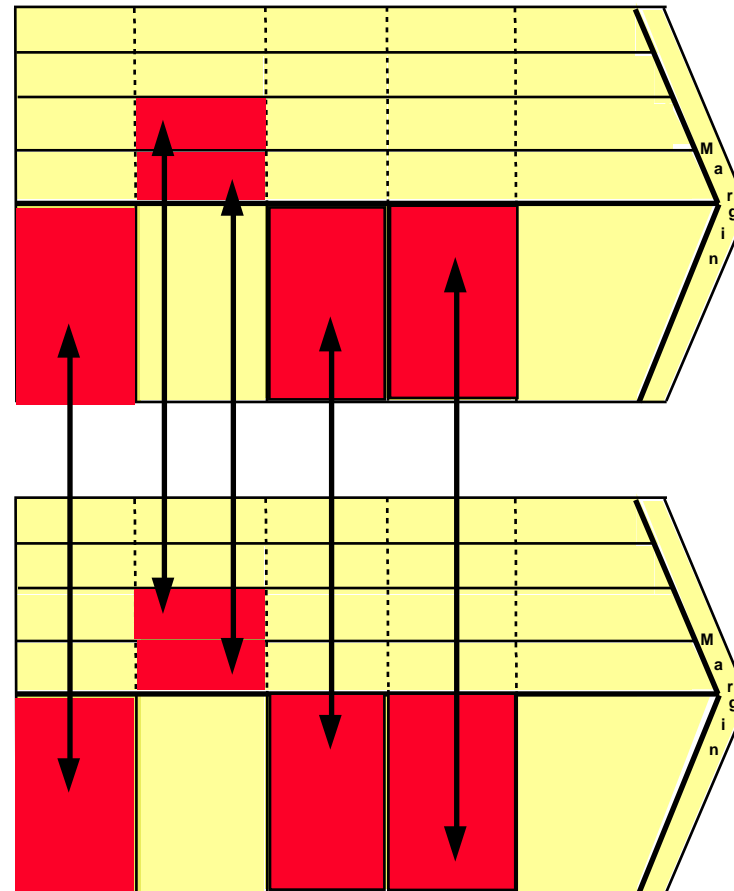
Growing Strategically

1. Make the strategy even **more distinctive**
2. **Deepen** the strategic position with target customers (rather than broaden it)
3. **Expand geographically** to tap new regions or countries using the **same positioning**
4. **Expand the market** for what the company can uniquely deliver



- It is an **illusion** that growth in new, unserved segments **is profitable**
- It is dangerous to attempt to **grow faster than the underlying market** for an extended period.
- Industry leaders should concentrate as much, or more, on **growing the industry** as on growing market share

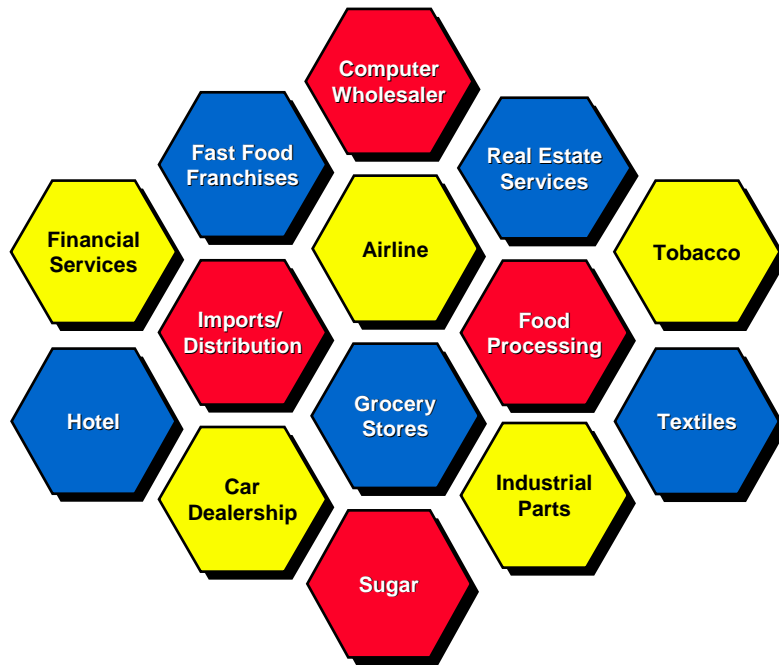
Creating Corporate Value Added



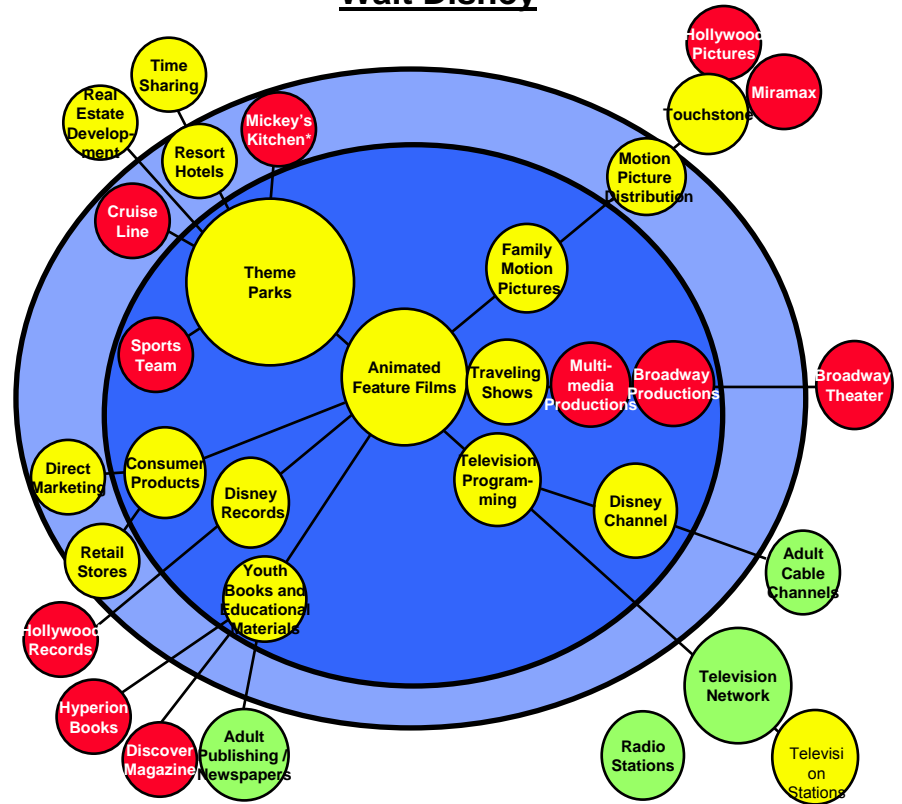
- Successful companies capture interrelationships **across the value chains** of business units
 - Transferring **proprietary** knowledge and skills across units
 - **Sharing activities** across business unit value chains

Diversification in an Emerging Economy

Emerging Country Business Groups



Diversified Companies in Advanced Economies Walt Disney



Strategic Thinking at Turkish Companies

- Low Price  Superior Value
- Share of Market  Unique Position
- Product / Product Innovation  Customer Experience
Total Customer Support
- Export Uniform Products  Locally-Tailored Regional and Global Strategy
- Large Business Groups  Integrated Multi-Business Companies

Obstacles to Strategic Thinking

- **Misunderstanding** of strategy principles
- **Industry conventional wisdom** leads all companies to follow common practices
- **Customers** ask for incompatible features or request new products or services that do not fit the strategy
- Inappropriate **goals** and **performance metrics** bias strategy choices
- A desire for **consensus blurs** strategic tradeoffs
- Short term pressure to **please shareholders**

The Role of Leaders in Strategy

- Drive **operational improvement**, but clearly distinguish it from **strategy**
- Lead the **process of choosing** the company's unique position
 - The CEO is the chief strategist
 - The choice of strategy **cannot** be entirely democratic
- **Communicate** the strategy relentlessly to all constituencies
 - Harness the **moral purpose** of strategy
- Maintain **discipline** around the strategy, in the face of many distractions.
- Decide **which** industry changes, technologies, and customer needs to respond to, and how the response can be **tailored** to the company's strategy
- **Measure progress** against the strategy using metrics that capture the implications of the strategy for serving customers and performing particular activities
- **Sell the strategy** and **how to evaluate** progress against the strategy to the financial markets



- Commitment to strategy is **tested every day**