

# Strategy: Creating and Sustaining Competitive Advantage

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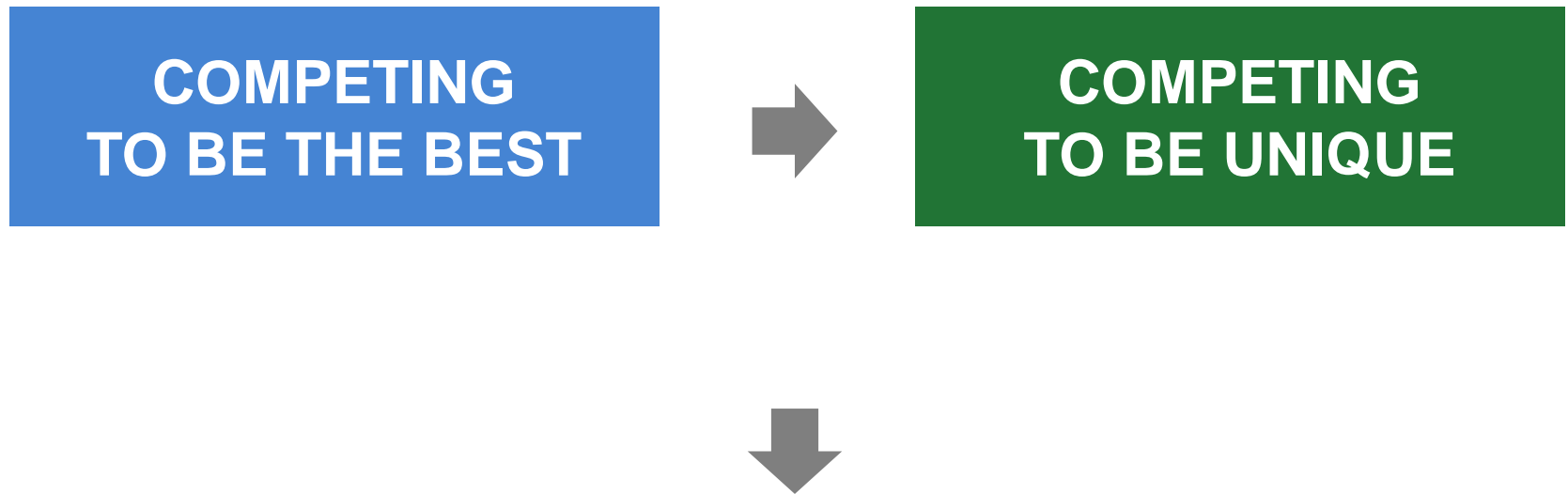
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This presentation draws on ideas from Professor Porter's books and articles, in particular, *Competitive Strategy* (*The Free Press*, 1980); *Competitive Advantage* (*The Free Press*, 1985); "What is Strategy?" (*Harvard Business Review*, Nov/Dec 1996); *On Competition* (*Harvard Business Review*, 2008); and "Creating Shared Value" (*Harvard Business Review*, Jan 2011). 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. For further materials, see the website of the Institute for Strategy and Competitiveness, [www.isc.hbs.edu](http://www.isc.hbs.edu), and FSG website, [www.fsg.org](http://www.fsg.org).

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# Thinking Strategically



- There is **no one best way** to compete
- The worst error in strategy is to compete with rivals on the **same dimensions**

# What Do We Mean by a Strategy?

- Strategy is the set of **long term** choices that an organization makes to **distinguish itself** from competitors
- Strategy defines a company's **distinctive approach** to competing, and the **competitive advantages** on which it will be based

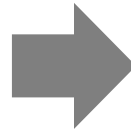


- Strategy is different than **aspirations**
  - “*Our strategy is to be #1 or #2...*”
  - “*Our strategy is to grow...*”
- Strategy is more than **particular actions**
  - “*Our strategy is to merge...*”
  - “*Our strategy is to cut costs...*”
- Strategy is not the same as **mission / values**
  - “*Our strategy is to serve our customers and communities while meeting the highest standards of integrity...*”

# Economic Performance Versus Shareholder Value

## Economic Performance

- Sustained ROIC
- Sustainable revenue growth



## Shareholder Value

- EPS growth
- TSR



- Shareholder value is the **result** of creating real economic value

# Levels of Strategy

## Corporate Strategy

- Strategy for the **overall company** competing in multiple business



## Business Strategy

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

# Business Strategy

## Drivers of Business Unit Performance

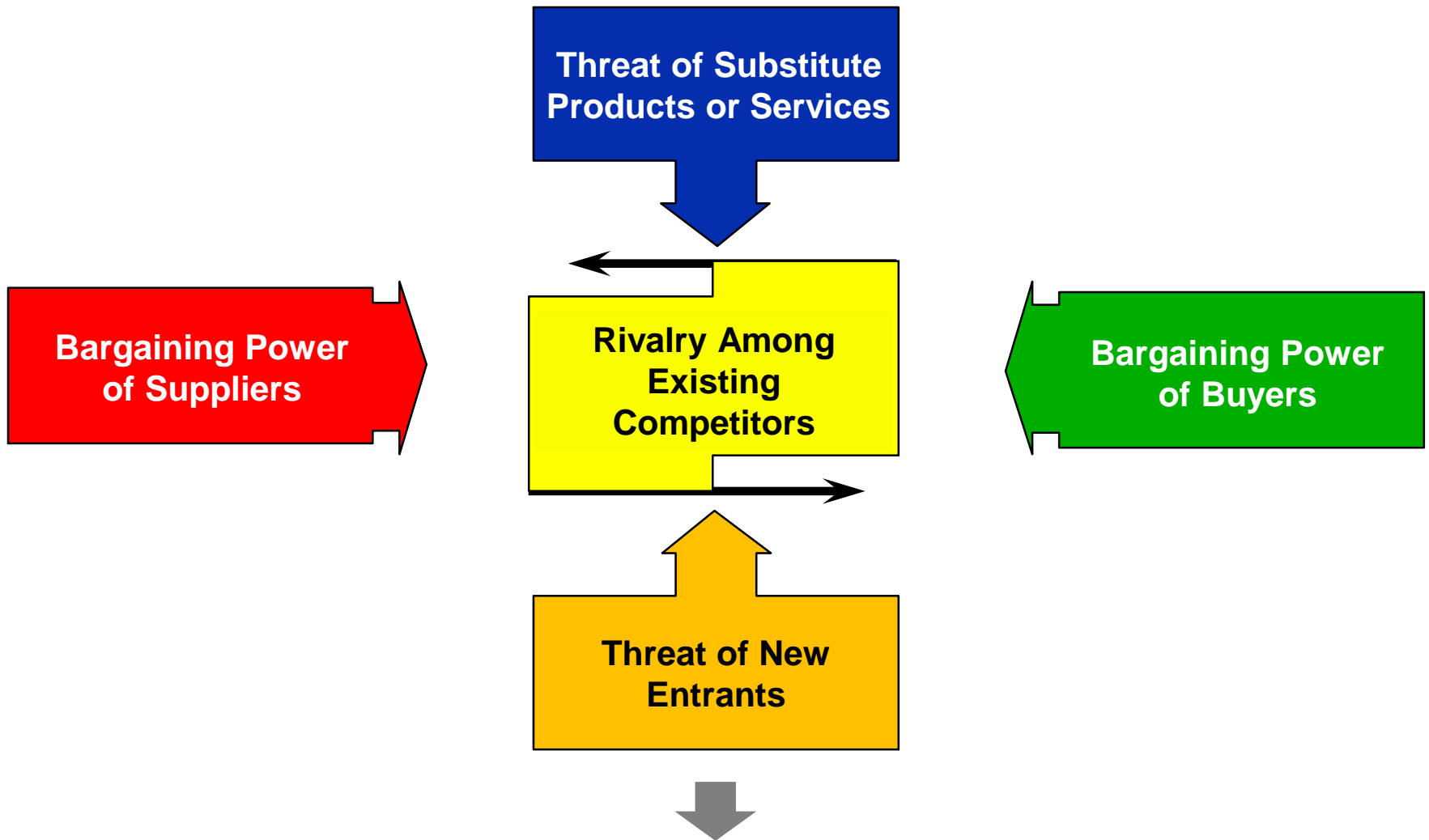


- *Nature of Industry Competition*

- *Sustainable Competitive Advantage*

- Business units need to focus both on the **attractiveness of their industry** as well as their **own competitive position**

# Analyzing Industry Structure



- Part of strategy is to drive a **positive transformation** in industry structure

# Industry Structure and Positioning

## U.S. Heavy Trucks

### Threat of Substitute Products or Services

- Railroads
- Water transportation

### Bargaining Power of Suppliers

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

### Rivalry Among Existing Competitors

- Vigorous **price competition** on standard models
- Rising **environmental** and **energy efficiency** requirements

### Bargaining Power of Buyers

- Trucking company consolidation into **large fleets**
- Large **leasing companies** account for substantial truck volume
- Small **owner operators** account for about 30% of the market

### Threat of New Entrants

- **Limited** entry barriers for assemblers
- **Significant** barriers to assembling a dealer and service network



# Analyzing Industry Structure

## Industrial Gases

### Threat of Substitute Products or Services

- **Captive** production by customers

### Bargaining Power of Suppliers

- Gas producers are **price takers** for feedstocks and energy

### Rivalry Among Existing Competitors

- The products are **commodities**

### Bargaining Power of Buyers

- Customers often have **buying power**

### Threat of New Entrants

- The products are **commodities**

# Analyzing Industry Structure

## Industrial Gases

### Threat of Substitute Products or Services

- **Captive** production by customers



- Captive production widely **managed** by industrial gas companies

### Bargaining Power of Suppliers

- Gas producers are **price takers** for feedstocks and energy
- Contracts **pass through** input costs



### Rivalry Among Existing Competitors

- The products are **commodities**
- **High transport costs** create benefits of customer density and mitigate rivalry



### Bargaining Power of Buyers

- Customers often have **buying power**
- Gases are a **small part of total cost** but significant to customer productivity
- **Switching costs** are often significant due to long-term contracts and on-site facilities

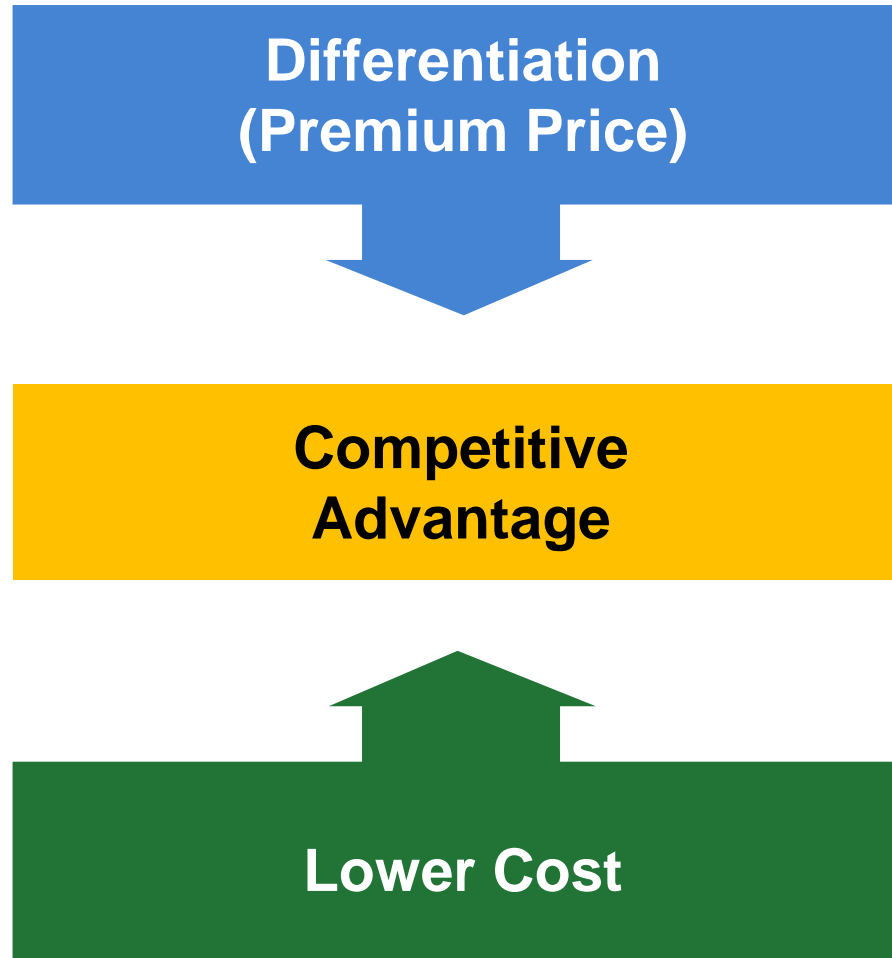


### Threat of New Entrants

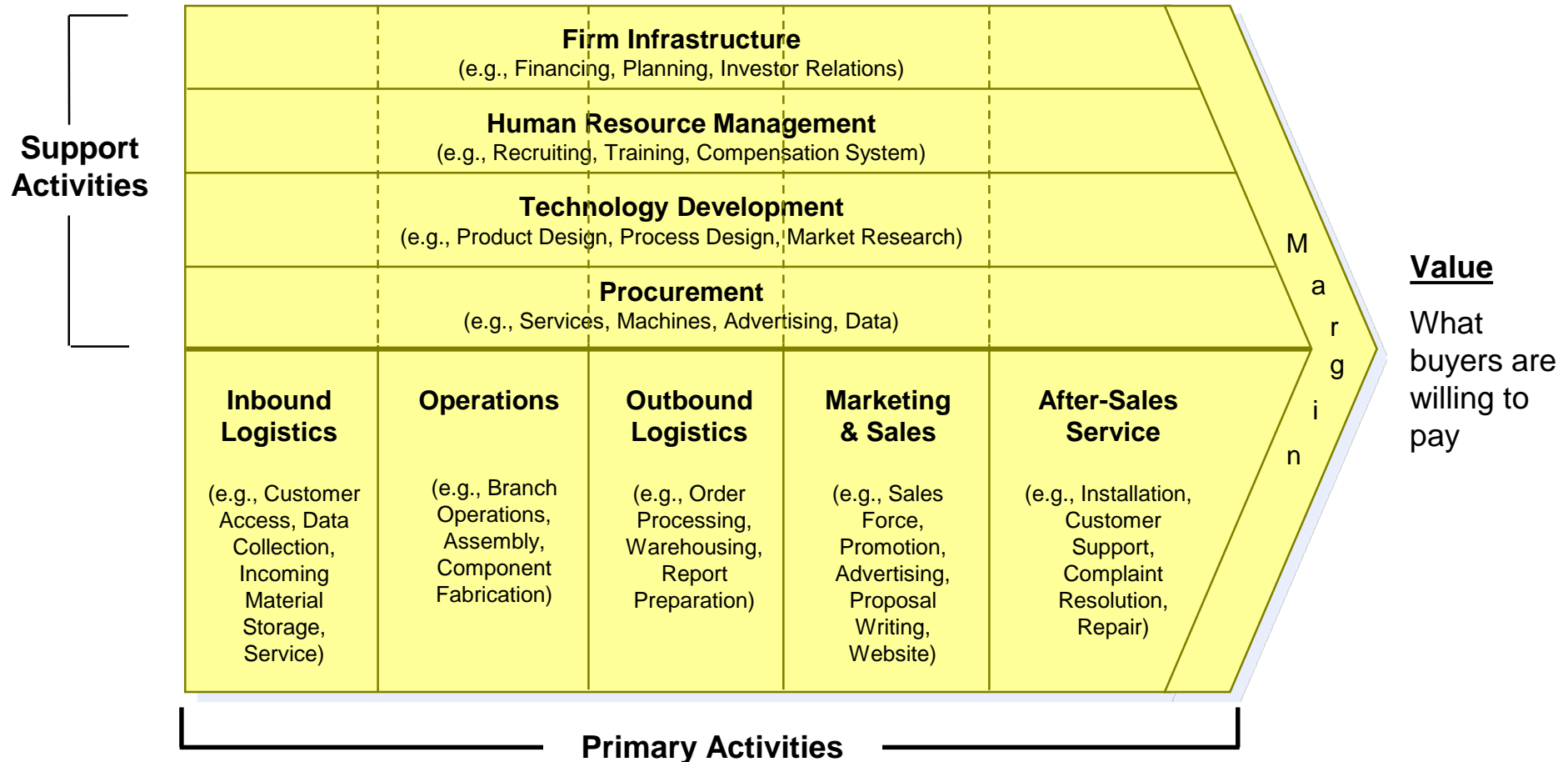
- The products are **commodities**
- Need for **customer density** raises the share needed to be viable



# Achieving Superior Profitability **Within** an Industry



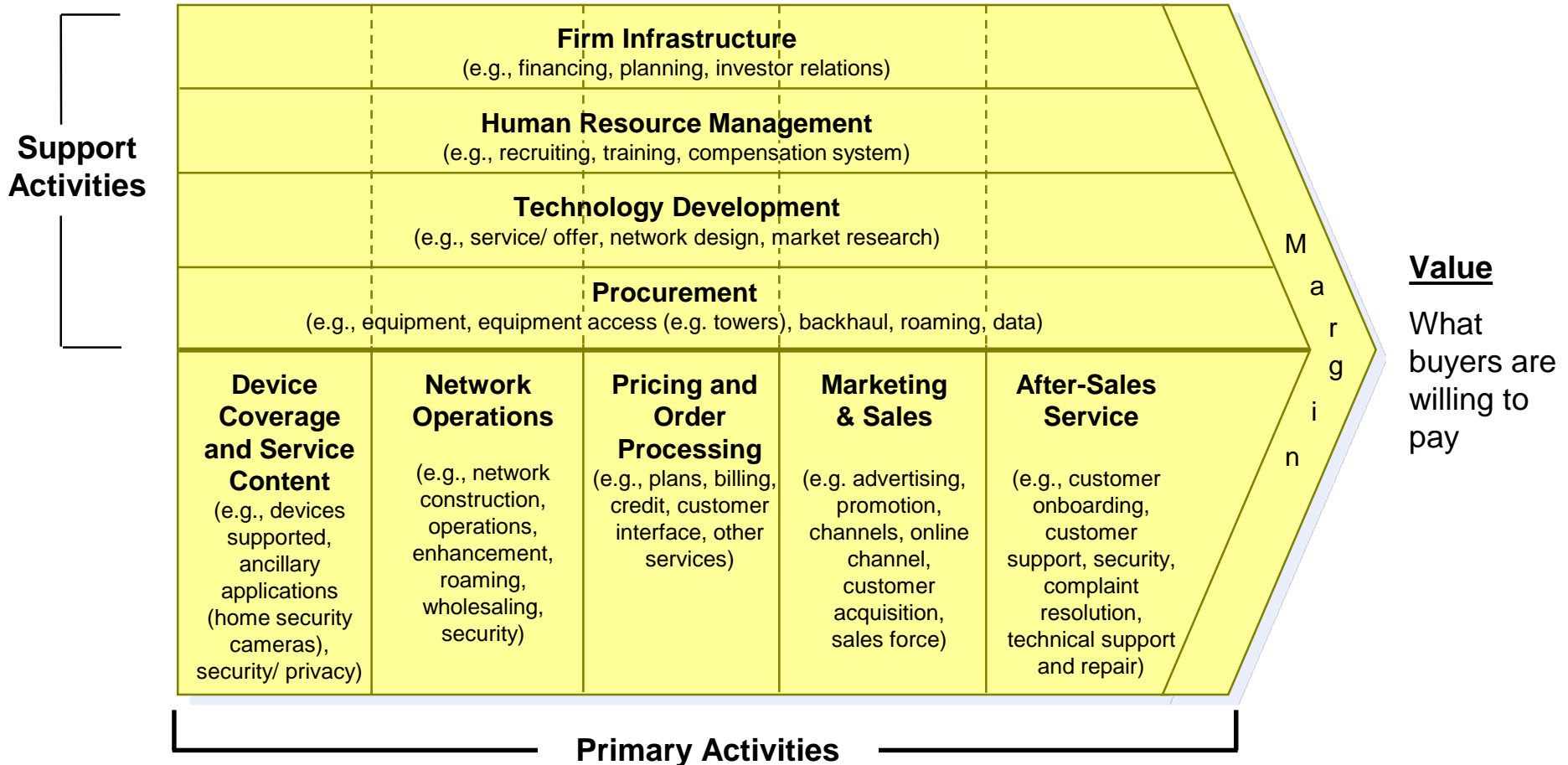
# Competitive Advantage and the Value Chain



- The value chain is the set of **activities** involved in delivering value to customers
- **Strategy** is reflected in the **choices** about how activities are configured and linked together

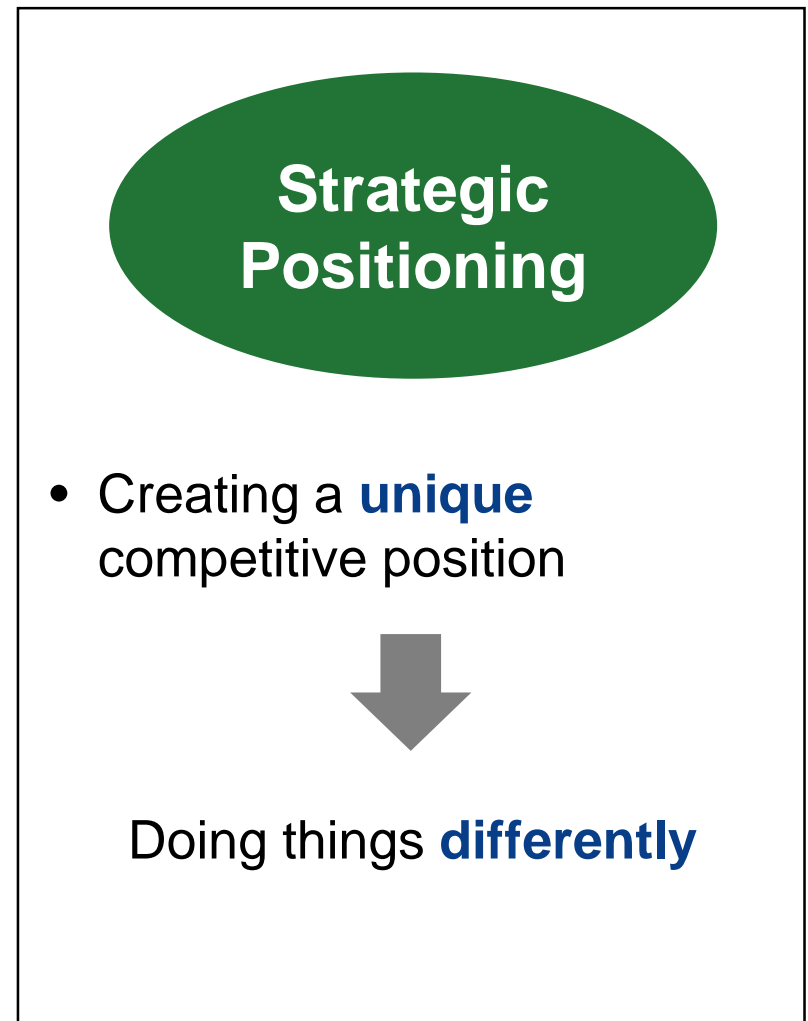
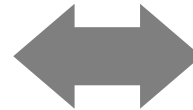
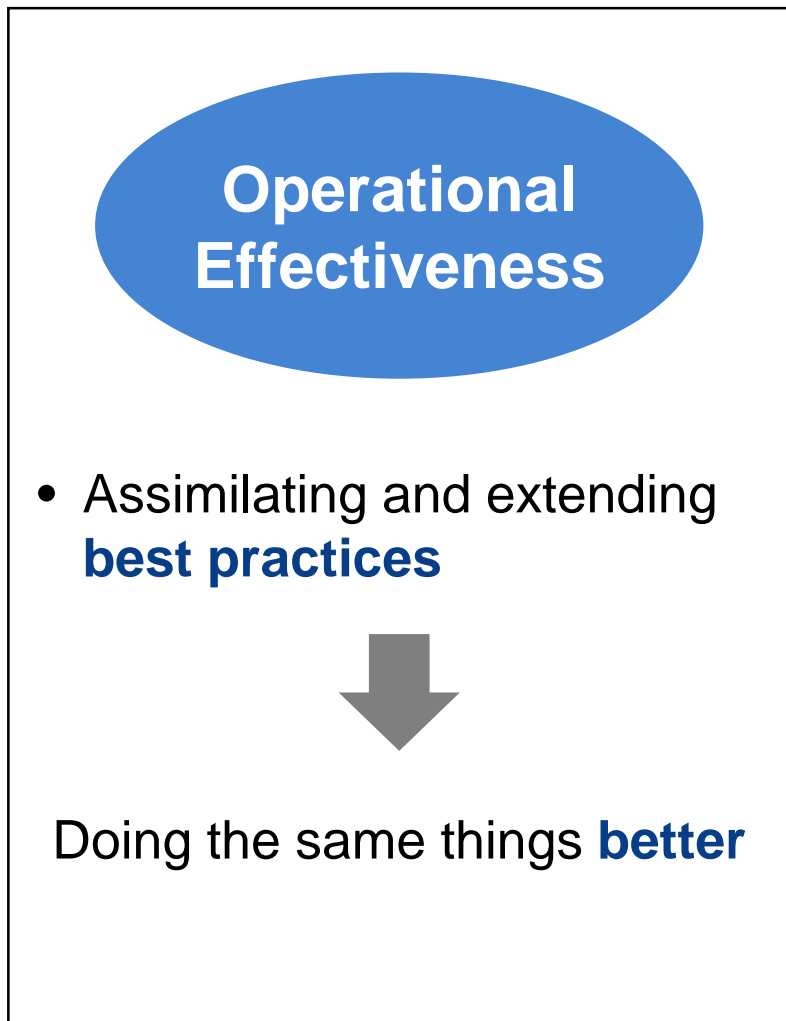
# Competitive Advantage and the Value Chain

## Mobile Communications



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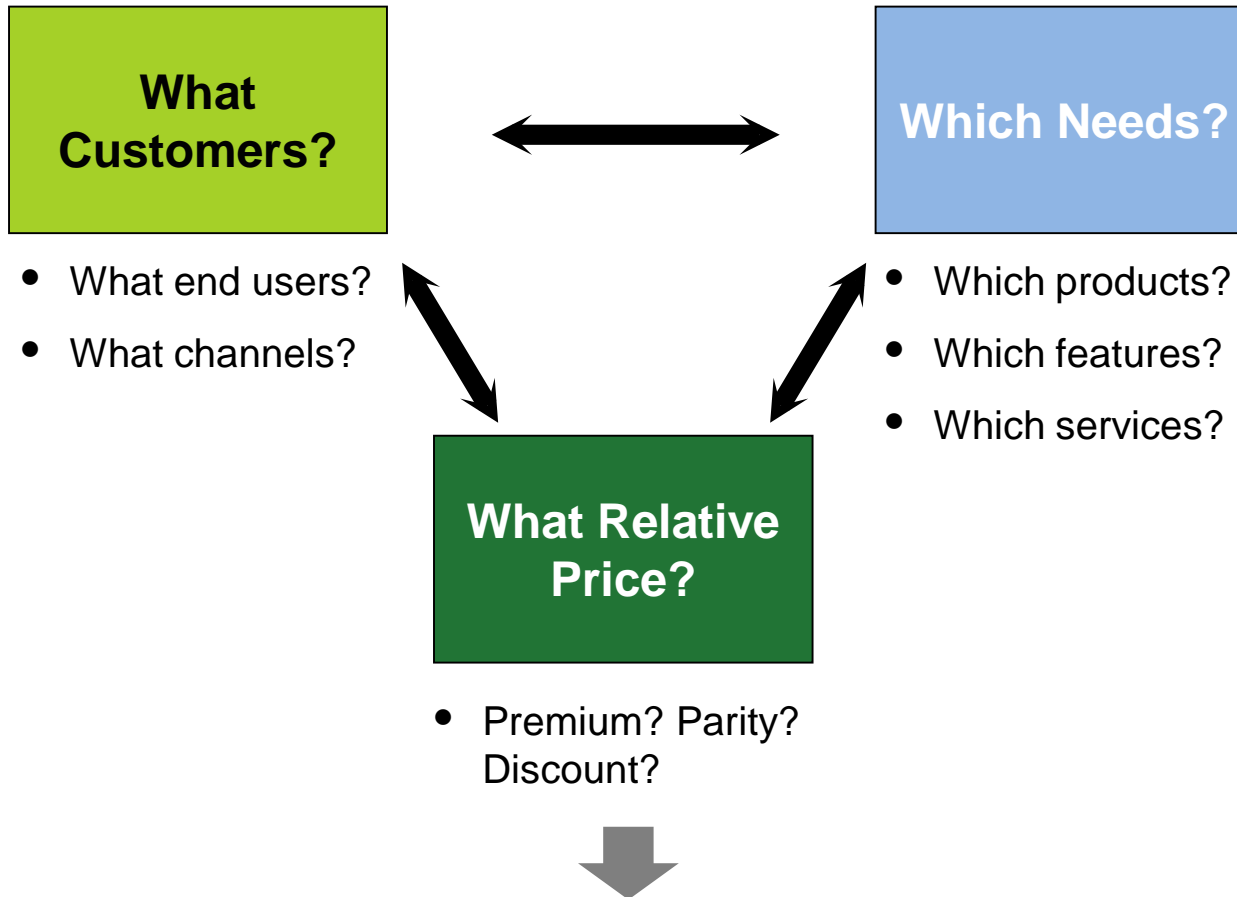
# Operational Effectiveness Versus Strategic Positioning



# Tests of a Successful Strategy

- A **unique value proposition** versus competitors

# Defining the Value Proposition



- Finding a unique value proposition often involves identifying **new needs**, new ways of **segmenting**, or **innovation** in the product
- A novel value proposition often **expands the market**



# Strategic Positioning

## IKEA, Sweden

### Value Proposition

- Customers with smaller living spaces, who are **style** and **design conscious**, but have a limited budget
- A wide line of **stylish, functional** and **good quality** furniture and accessories
- **Limited** ancillary services
- **Very low** price points

# Strategic Positioning

## PACCAR

### Value Proposition

- Highly **customized** trucks targeted at **owner-operators**, offering superior amenities but low cost of operation along with extensive customer after sale support
- Command a **10% premium price**

# Tests of a Successful Strategy

- A **unique value proposition** versus competitors
- A **distinctive value chain**, involving clear choices about how the company will **operate differently** to deliver on its value proposition

# Strategic Positioning

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### Distinctive Activities

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

# Strategic Positioning

## PACCAR

### Value Proposition

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### Distinctive Activities

- Customized **features and amenities** geared toward owner-operators (e.g., luxurious sleeper cabins, plush leather seats, noise-insulated cabins, sleek exterior styling, etc.)
- Products designed for **durability and resale value**
- Industry leader in **fuel efficiency** and **emissions** reduction, including hybrids
- Provide **diagnostic services** for customers (e.g., fuel efficiency, remote service analysis)
- Offer truck **financing**, leasing and insurance services
- **Flexible manufacturing** system configured for customization
- Built to **order**, not to stock
- **Extensive dealer network** (1,800 locations) to provide extensive customer contact and aftermarket support
- Extensive **roadside assistance** network
- 24-hour **parts distribution** system providing rapid repair and uptime

# Tests of a Successful Strategy

- A **unique value proposition** versus competitors
- A **distinctive value chain**, involving clear choices about how the company will **operate differently** to deliver on its value proposition
- Making clear **tradeoffs**, and choosing what **not** to do

# Positioning Tradeoffs

## IKEA, Sweden

### IKEA

#### Product

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

#### 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
- No delivery included

### 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 portion of available models on display
- Limited inventories / order with lead time
- Extensive sales assistance
- Traditional retail hours
- Delivery part of product



- Tradeoffs create the need for **choice**
- Tradeoffs make a strategy **sustainable** against imitation by established rivals

# Tests of a Successful Strategy

- A **unique value proposition** versus competitors
- A **distinctive value chain**, involving clear choices about how the company will **operate differently** to deliver on its value proposition
- Making clear **tradeoffs**, and choosing what **not** to do
- Integrating choices across the parts of the value chain so that the functions **fit together** and **reinforce each other**
- **Continuity** of strategic direction, with continuous improvement in realizing the unique value proposition



- The essence of strategy is making **choices**



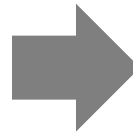
# Shifting the Nature of Industry Competition

## Zero Sum Competition

- Compete **head to head** on price, with similar products to the same customers
- One company's **gain** requires another company's **loss**



- Competition **dissipates profitability** and often undermines industry structure



## Positive Sum Competition

- Compete on **strategy**
- **More than one** company can be successful



- Competition **expands** the customers served, needs met, and overall value

# Levels of Strategy: Continued

## Corporate Strategy

- Strategy for the **overall company**



## Group Strategy

- Strategy for **groups** of **related businesses**



## Business Unit Strategy

- Strategy for each **distinct business**

# Defining the Distinct Businesses

## Product Scope

- What **set of products** constitute a distinct business?  
E.g., Trucks vs Heavy Trucks

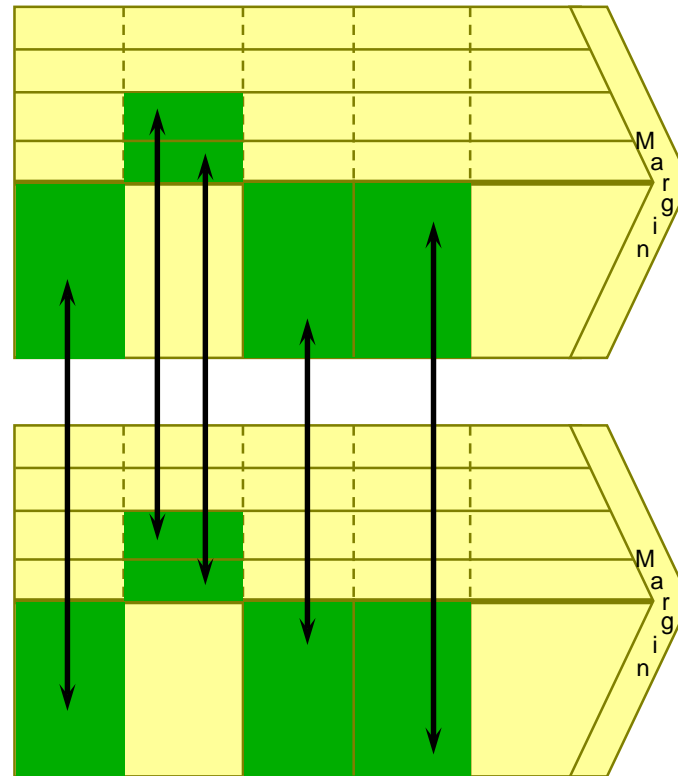
## Geographic Scope

- Is the business **local, state, national, regional, global**?
  - Commercial aircrafts versus distributors

# Corporate Strategy: The Essential Questions

- **What distinct businesses** are we in?
- Does the company have the **right portfolio of businesses**?
  - Is each business structurally attractive?
  - Is the company the best owner for each business?
- Is there a **compelling strategic logic** for how the businesses fit together?
- Is the company actually **capturing the synergies** across related businesses?
- Do organizational structure, goals, and incentives **reinforce** synergy versus work against it?

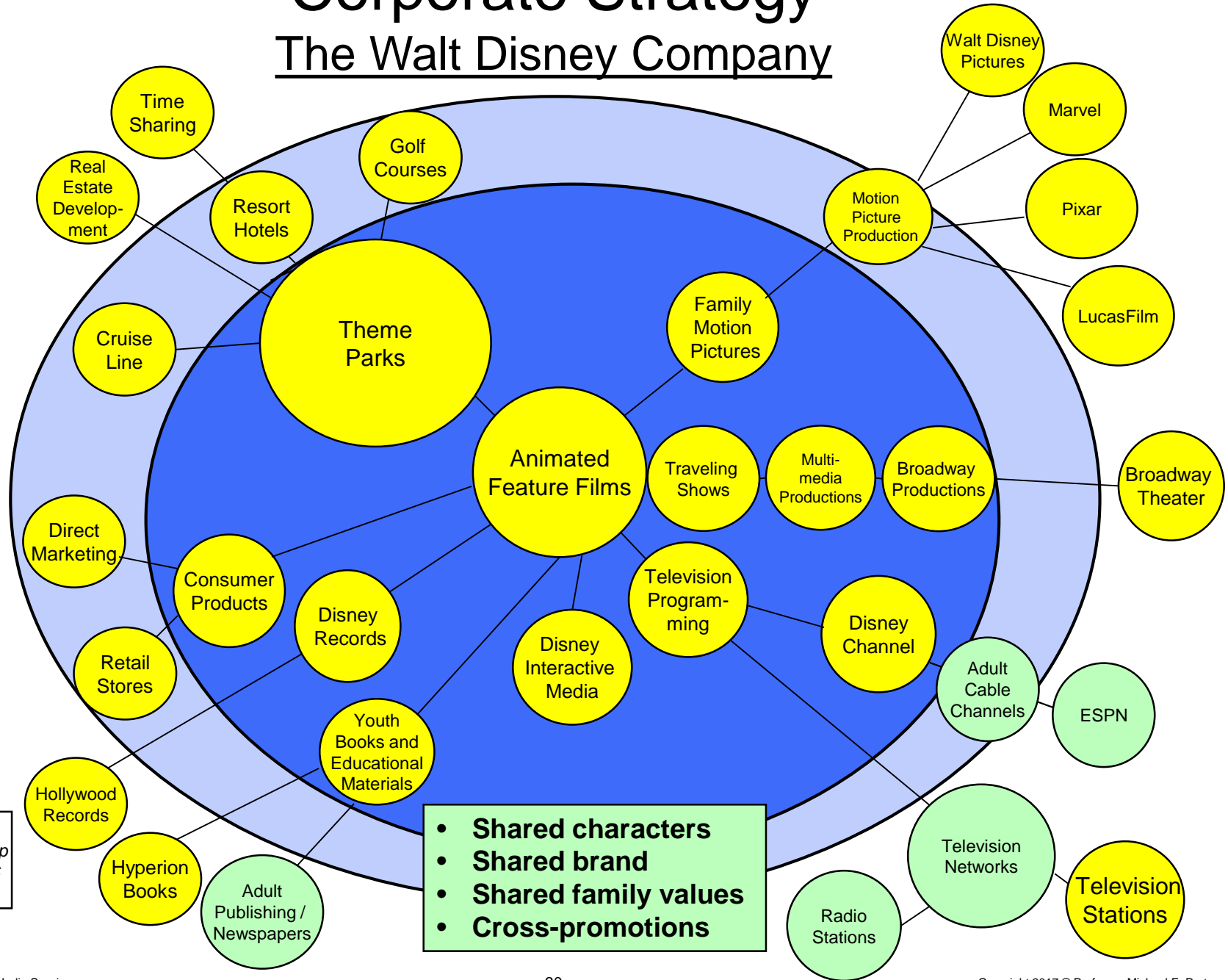
# Corporate Strategy: Creating Synergy Across Businesses



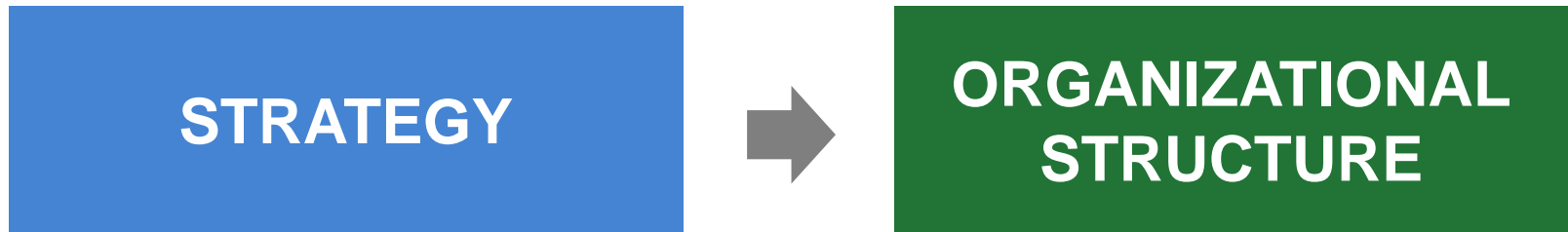
- Advantages that cut **across the value chains** of business units (synergy)
    - Common **customers**
    - **Integrating** products/ services
    - **Sharing key activities** (e.g. manufacturing, brand development, sales channels, relationship development)
    - Leveraging **proprietary reputation, knowledge, and skills** across businesses
- ↓
- Sharing corporate overhead is **not enough**
  - Achieving synergy requires **aligning strategies** and **coordinating** goals, culture, and incentives

# Corporate Strategy

## The Walt Disney Company



# Organizing for Strategy



- Key principles

- Organizational structure should **follow and reinforce** the strategy
- Companies should organize around **customers** and **customer needs**, not around functions, products per se, or broad line channels

# The CEO's Role in Strategic Planning

- The CEO must be **Chief Strategy Officer**
  - Lead the process but not all the work
- The CEO should be the **chief architect** of the strategy process
  - Define the relevant business units and business groups
  - Set the questions to be addressed at each level of strategy
  - Determine who should be involved at each level
- Get input from the **Board** before the strategy is fully set



- How the CEO participates **personally**

Design the  
process and  
review the  
results



Monitor  
and  
check in



Lead  
the process



# Role of Leaders in Strategy

- Distinguish **operational improvement** from **strategy**
- Lead the **process of strategic choice**
  - The leader is the chief strategist
- **Communicate** the strategy relentlessly to all constituencies
  - Find vivid ways to **disseminate** the strategy
  - Strategy creates **alignment** and **motivation**
- Maintain **discipline** around the strategy, in the face of many distractions
- **Measure progress** against the strategy using metrics that measure success against a company's unique value proposition



**Commitment to strategy is tested every day**