Learning Objectives

After studying this chapter, you should be able to:

• Describe the three steps of the planning process.

• Explain the relationship between planning and strategy.

• Explain the role of planning in predicting the future and in mobilizing organizational resources to meet future contingencies.

• Outline the main steps in SWOT analysis.

• Differentiate among corporate-, business-, and functional-level strategies.

• Describe the vital role played by strategy implementation in determining managers’ ability to achieve an organization’s mission and goals.
What is the best way to compete in an industry?

In 1971, Federal Express (FedEx) turned the package delivery world upside down when it began to offer overnight package delivery by air. Its founder, Fred Smith, had seen the opportunity for next-day delivery because both the U.S. Postal Service and United Parcel Service (UPS) were, at that time, taking several days to deliver packages. Smith was convinced there was pent up demand for such a unique new service, overnight delivery, and he was also convinced that customers would be willing to pay a high premium price to get it, at least $15 a package at that time. Smith was right, customers were willing to pay high prices for fast reliable delivery; when he discovered and tapped into an unmet customer need, he redefined the package delivery industry.

Several companies imitated FedEx’s new strategy and introduced their own air overnight service. None, however, could match FedEx’s efficiency and its state-of-the-art information systems which allowed continuous tracking of all packages while in transit. Several of its competitors went out of business. A few, like Airborne Express, managed to survive by focusing or specializing on serving the needs of one particular group of customers—corporate customers—and by offering lower prices than FedEx. Its strategy earned FedEx huge returns through the 1980s, even though the costs of operating its

The “bricks and mortar” store and “virtual” storefront of bookseller Barnes and Noble. As of 2001, Barnes and Noble had still not yet made a profit from its on-line activities and the company as a whole was experiencing losses.
As the battle between FedEx and UPS suggests, there is more than one way to compete in an industry. To find a viable way to enter and compete in an industry, managers must study the way other organizations behave and identify their strategies. By studying the strategies of FedEx, UPS was able to devise a strategy that allowed it to enter the overnight package industry and take on FedEx. So far, it has had considerable success and appears to have achieved a competitive advantage over FedEx.

In an uncertain competitive environment, managers must engage in thorough planning to find a strategy that will allow them to compete effectively. This chapter explores the manager’s role both as planner and as strategist. We discuss the different elements involved in the planning process, including its three major steps: (1) determining an organization’s mission and major goals, (2) choosing strategies to realize the mission and goals, and (3) selecting the appropriate way of organizing resources to implement the strategies. We also discuss scenario planning and SWOT analysis, important techniques that managers use to analyze their current situation. By the end of this chapter, you will understand the role managers play in the planning and strategy-making process to create high-performance organizations.

Overview

As the battle between FedEx and UPS suggests, there is more than one way to compete in an industry. To find a viable way to enter and compete in an industry, managers must study the way other organizations behave and identify their strategies. By studying the strategies of FedEx, UPS was able to devise a strategy that allowed it to enter the overnight package industry and take on FedEx. So far, it has had considerable success and appears to have achieved a competitive advantage over FedEx.

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Planning, as we noted in Chapter 1, is a process that managers use to identify and select appropriate goals and courses of action for an organization. The organizational plan that results from the planning process details the goals of the organization and specifies how managers intend to attain those goals. The cluster of decisions and actions that managers take to help an organization attain its goals is its strategy. Thus, planning is both a goal-making and a strategy-making process.

In most organizations, planning is a three-step activity (see Figure 8.1). The first step is determining the organization’s mission and goals. A mission statement is a broad declaration of an organization’s overriding purpose; this statement is intended to identify an organization’s products and customers as well as to distinguish the organization in some way from its competitors. The second step is formulating strategy. Managers analyze the organization’s current situation and then conceive and develop the strategies necessary to attain the organization’s mission and goals. The third step is implementing strategy. Managers decide how to allocate the resources and responsibilities required to implement those strategies between people and groups within the organization. In subsequent sections of this chapter we look in detail at the specifics of each of these steps. But first, we examine the general nature and purpose of planning, one of the four managerial functions identified by Henri Fayol.

Levels of Planning

In large organizations planning usually takes place at three levels of management: corporate, business or division, and department or functional. Figure 8.2 shows the link between the three steps in the planning process and these three levels. To understand this model, consider how General Electric (GE), a large organization that competes in many different businesses, operates. GE has three main levels of management: corporate level, business level, and functional level (see Figure 8.3). At the corporate level are CEO and Chairman Jeffrey Immelt, three other top managers, and their corporate support staff. Below the corporate level is the business level. At the business level are the different divisions of the
A division is a business unit that competes in a distinct industry; GE has over 150 divisions, including GE Aircraft Engines, GE Financial Services, GE Lighting, GE Motors, GE Plastics, and NBC. Each division has its own set of divisional managers. In turn, each division has its own set of functions or departments—manufacturing, marketing, human resource management, R&D, and so on. Thus, GE Aircraft has its own marketing function, as do GE Lighting, GE Motors, and NBC.

At GE, as at other large organizations, planning takes place at each level. The corporate-level plan contains top management’s decisions pertaining to the organization’s mission and goals, overall (corporate-level) strategy, and structure (see Figure 8.2). Corporate-level strategy indicates in which industries and national markets an organization intends to compete. One of the goals stated in GE’s corporate-level plan is that GE should be first or second in market share in every industry in which it competes. A division that cannot attain this goal may be sold to another company. GE Medical Systems was sold to Thompson of France for this reason. Another GE goal is the acquisition of other companies to help build market share. Over the last decade, GE has acquired several financial services companies and has transformed the GE Financial Services Division into one of the largest financial service operations in the world.

The corporate-level plan provides the framework within which divisional managers create their business-level plans. At the business level, the managers of each division create a business-level plan that details (1) long-term goals that will allow the division to meet corporate goals and (2) the division’s busi-
**business-level strategy** states the methods a division or business intends to use to compete against its rivals in an industry. Managers at GE Lighting (currently number two in the global lighting industry behind the Dutch company Philips NV) develop strategies designed to help the division take over the number-one spot and better contribute to GE’s corporate goals. The lighting division’s competitive strategy might emphasize, for example, trying to reduce costs in all departments in order to lower prices and gain market share from Philips. GE is currently planning to expand its European lighting operations, which as we discussed in Chapter 6, is based in Hungary.7

A **function** is a unit or department in which people have the same skills or use the same resources to perform their jobs. Examples include manufacturing, accounting, and sales. The business-level plan provides the framework within which **functional managers** devise their plans. A **functional-level plan** states the goals that functional managers propose to pursue to help the division attain its business-level goals, which, in turn, allow the organization to achieve its corporate goals. **Functional-level strategy** sets forth the actions that managers intend to take at the level of departments such as manufacturing, marketing, and R&D to allow the organization to attain its goals. Thus, for example, consistent with GE Lighting’s strategy of driving down costs, the manufacturing function might adopt the goal “To reduce production costs by 20 percent over three years,” and its functional strategy to achieve this goal might include (1) investing in state-of-the-art European production facilities, and (2) developing an electronic global business-to-business network to reduce the cost of inputs and inventory-holding costs.

An important issue in planning is ensuring consistency in planning across the three different levels. Functional goals and strategies should be consistent with divisional goals and strategies, which in turn should be consistent with corporate goals and strategies, and vice versa. Once complete, each function’s
plan is normally linked to its division’s business-level plan, which, in turn, is linked to the corporate plan. Although few organizations are as large and complex as GE, most plan as GE does and have written plans to guide managerial decision making.

Who Plans?

In general, corporate-level planning is the primary responsibility of top managers. At General Electric, the corporate-level goal that GE be first or second in every industry in which it competes was first articulated by former CEO Jack Welch who stepped down in September 2001. Now, Welch’s hand-selected successor, Jeffrey Immelt, and his top-management team decide which industries GE should compete in. Corporate-level managers are responsible for approving business- and functional-level plans to ensure that they are consistent with the corporate plan.

Corporate planning decisions are not made in a vacuum. Other managers do have input to corporate-level planning. At General Electric and many other companies, divisional and functional managers are encouraged to submit proposals for new business ventures to the CEO and top managers, who evaluate the proposals and decide whether to fund them. Thus, even though corporate-level planning is the responsibility of top managers, lower-level managers can and usually are given the opportunity to become involved in the process.

This approach is common not only at the corporate level but also at the business and functional levels. At the business level, planning is the responsibility of divisional managers, who also review functional plans. Functional managers also typically participate in business-level planning. Similarly, although the functional managers bear primary responsibility for functional-level planning, they can and do involve their subordinates in this process. Thus, although ultimate responsibility for planning may lie with certain select managers within an organization, all managers and many nonmanagerial employees typically participate in the planning process.

Time Horizons of Plans

Plans differ in their time horizon, or intended duration. Managers usually distinguish among long-term plans with a horizon of five years or more, intermediate-term plans with a horizon between one and five years, and short-term plans with a horizon of one year or less. Typically, corporate- and business-level goals and strategies require long- and intermediate-term plans, and functional-level goals and strategies require intermediate- and short-term plans.

Although most organizations operate with planning horizons of five years or more, it would be inaccurate to infer from this that they undertake major planning exercises only once every five years and then “lock in” a specific set of goals and strategies for that time period. Most organizations have an annual planning cycle, which is usually linked to their annual financial budget (although a major planning effort may be undertaken only every few years).

Although a corporate- or business-level plan may extend over five years or more, it is typically treated as a rolling plan, a plan that is updated and amended every year to take account of changing conditions in the external environment. Thus, the time horizon for an organization’s 2002 corporate-level plan might be 2007; for the 2003 plan it might be 2008; and so on. The use of rolling plans is essential because of the high rate of change in the environment and the diffi-
culty of predicting competitive conditions five years in the future. Rolling plans allow managers to make midcourse corrections if environmental changes warrant, or to change the thrust of the plan altogether if it no longer seems appropriate. The use of rolling plans allows managers to plan flexibly, without losing sight of the need to plan for the long term. As discussed earlier, UPS is a master at using rolling plans to improve its long-run efficiency. It constantly updates its plans as its systems experts develop improved IT systems that provide it with new opportunities to improve its operating effectiveness as discussed in the “Information Technology Byte.”

Rolling Plans and Global Supply Chain Management

As discussed in the opening case, UPS is gaining on FedEx because its managers are committed to constantly upgrading and developing the potential of its IT systems as new technology becomes ever more powerful and useful. Using this new technology, UPS has also gained ground on FedEx in providing another important service that is becoming increasingly important given the growth of B2B networks—global supply chain management.

Both UPS and FedEx offer companies such as Compaq, Ford, and Dell a complete global pickup, warehousing, transportation, tracking, and delivery service of their products to customers. Also, they can manage the delivery of inputs these companies require to make their products so that they do not have to carry large stocks of inventory which is expensive. Thus, UPS and FedEx are now in the business of using IT to manage the flow of a company’s inputs and the distribution of its outputs—global supply chain management.

FedEx had the early lead in this business, it had opened such a service in Japan and in the United States, building warehouses near major customers to facilitate the flow of Japanese products to the United States. However in the 1990s, UPS managers realized the huge growth potential of the supply chain management business because of soaring international trade and the growth of foreign specialist suppliers that could supply low-cost inputs. They initiated a series of rolling plans and set targets to develop an IT system that would continuously improve customer service and increase UPS’s efficiency.

By contrast, FedEx managers did not capitalize on their early lead in the business. Although they used to have the best tracking and IT systems, they apparently did not set in place a program to update and improve them, believing their competitive advantage was too strong. This was a mistake. By 2000, the constant improvements in its IT systems had given UPS the lead; large corporate customers were increasingly choosing UPS to manage their supply chains. In 2000, Ford, for example, saved $250 million by allowing UPS to manage the shipping, tracking, and distribution of its new cars to dealers throughout the United States. Some analysts believe that UPS currently has the best supply-chain services in place.

Currently, both companies are competing to redefine and control the global shipping business, something largely made possible by the growth of new IT systems and the Internet. Indeed, the emergence of the dot-coms, and companies like Amazon.com, which ship hundreds of millions of packages a year was a major factor in shaping the competitive strategies of these two companies. Interestingly, because of its lower prices in 2001, UPS was the shipper of choice for Amazon.com.
Standing Plans and Single-Use Plans

Another distinction often made between plans is whether they are standing plans or single-use plans. Managers create standing and single-use plans to help achieve an organization’s specific goals. *Standing plans* are used in situations in which programmed decision making is appropriate. When the same situations occur repeatedly, managers develop policies, rules, and standard operating procedures (SOP) to control the way employees perform their tasks. A *policy* is a general guide to action; a *rule* is a formal, written guide to action; and a *standing operating procedure* is a written instruction describing the exact series of actions that should be followed in a specific situation. For example, an organization may have a standing plan about ethical behavior by employees. This plan includes a *policy* that all employees are expected to behave ethically in their dealings with suppliers and customers; a *rule* that requires any employee who receives from a supplier or customer a gift larger than $10 to report the gift; and an *SOP* that obliges the recipient of the gift to make the disclosure in writing within 30 days.

In contrast, *single-use plans* are developed to handle nonprogrammed decision making in unusual or one-of-a-kind situations. Examples of single-use plans include *programs*, which are integrated sets of plans for achieving certain goals, and *projects*, which are specific action plans created to complete various aspects of a program. One of NASA’s major programs was to reach the moon, and one project in this program was to develop a lunar module capable of landing on the moon and returning to the earth.

Why Planning Is Important

Essentially, planning is ascertaining where an organization is at the present time and deciding where it should be in the future and how to move it forward. When managers plan, they must consider the future and forecast what may happen in order to take actions in the present and mobilize organizational resources to deal with future opportunities and threats. As we have discussed in previous chapters, however, the external environment is uncertain and complex, and managers typically must deal with incomplete information and bounded rationality. This is one reason why planning is so complex and difficult.

Almost all managers engage in planning, and all should participate because they must try to predict future opportunities and threats. The absence of a plan often results in hesitations, false steps, and mistaken changes of direction that can hurt an organization or even lead to disaster. Planning is important for four main reasons:

1. Planning is a useful way of getting managers to participate in decision making about the appropriate goals and strategies for an organization. Effective planning gives all managers the opportunity to participate in decision making. At Intel, for example, top managers, as part of their annual planning process, regularly request input from lower-level managers to determine what the organization’s goals and strategies should be.

2. Planning is necessary to give the organization a sense of direction and purpose. A plan states what goals an organization is trying to achieve and what strategies it intends to use to achieve them. Without the sense of direction and purpose that a formal plan provides, managers may interpret their own tasks and roles in ways that best suit themselves. The result will be an organization
that is pursuing multiple and often conflicting goals and a set of managers who do not cooperate and work well together. By stating which organizational goals and strategies are important, a plan keeps managers on track so that they use the resources under their control effectively.

3. A plan helps coordinate managers of the different functions and divisions of an organization to ensure that they all pull in the same direction. Without a good plan, it is possible that the members of the manufacturing function will produce more products than the members of the sales function can sell, resulting in a mass of unsold inventory. Implausible as this might seem, it happened to the high-flying Internet router supplier, Cisco Systems in 2000 when manufacturing, which had been able to sell all the routers that it produced, had over $2 billion of unsold inventory because of the combination of an economic recession and customers’ demands for new kinds of optical routers that Cisco did not have in stock.

4. A plan can be used as a device for controlling managers within an organization. A good plan specifies not only which goals and strategies the organization is committed to but also who is responsible for putting the strategies into action to attain the goals. When managers know that they will be held accountable for attaining a goal, they are motivated to do their best to make sure the goal is achieved.

Henri Fayol, the originator of the model of management we discussed in Chapter 1, said that effective plans should have four qualities: unity, continuity, accuracy, and flexibility. Unity means that at any one time only one central, guiding plan is put into operation to achieve an organizational goal; more than one plan to achieve a goal would cause confusion and disorder. Continuity means that planning is an ongoing process in which managers build and refine previous plans and continually modify plans at all levels—corporate, business, and functional—so that they fit together into one broad framework. Accuracy means that managers need to make every attempt to collect and utilize all available information at their disposal in the planning process. Of course, managers must recognize the fact that uncertainty exists and that information is almost always incomplete (for reasons we discussed in Chapter 7). Despite the need for continuity and accuracy, however, Fayol emphasized that the planning process should be flexible enough so that plans can be altered and changed if the situation changes; managers must not be bound to a static plan.

**Scenario Planning**

One way in which managers can try to create plans that have the four qualities that Fayol described is by utilizing scenario planning, one of the most widely used planning techniques. Scenario planning (also known as contingency planning) is the generation of multiple forecasts of future conditions followed by an analysis of how to respond effectively to each of those conditions.

As noted previously, planning is about trying to forecast and predict the future in order to be able to anticipate future opportunities and threats. The future, however, is inherently unpredictable. How can managers best deal with this unpredictability? This question preoccupied managers at Royal Dutch Shell, the third largest global oil company in the 1980s. In 1984, oil was $30 a barrel, and most analysts and managers, including Shell’s, believed that it would hit $50 per barrel by 1990. Nevertheless, Shell conducted a scenario-planning exercise for its managers. Shell’s managers were asked to use scenario planning.
planning to generate different future scenarios of conditions in the oil market, and then to develop a set of plans that detailed how they would respond to these opportunities and threats if any such scenario occurred.

One scenario used the assumption that oil prices would fall to $15 per barrel and managers had to decide what they should do in such a case. Managers went to work with the goal of creating a plan consisting of a series of recommendations. The final plan included proposals to cut oil exploration costs by investing in new technologies, to accelerate investments in cost-efficient oil-refining facilities, and to weed out unprofitable gas stations.13 In reviewing these proposals, top management came to the conclusion that even if oil prices continued to rise, all of these actions would benefit Shell by widening the company’s profit margin. They decided to put the plan into action. As it happened, in the mid-1980s oil prices did collapse to $15 a barrel, but Shell, unlike its competitors, had already taken steps to be profitable in a low-oil-price world. Consequently, by 1990, the company was twice as profitable as its major competitors, and of course when oil prices once again rose beyond $30 in 2000 Shell enjoyed record profits.

Because the future is unpredictable the only reasonable approach to planning is first to generate “multiple futures”—or scenarios of the future—based on different assumptions about conditions that might prevail in the future, and then to develop different plans that detail what a company should do in the event that any of these scenarios actually occurs. Managers at Shell believe that the advantages of scenario planning were not only the plans that were generated but also the education of managers at all levels about the dynamic and complex nature of Shell’s environment and the breadth of strategies available to Shell. Scenario planning is a learning tool that raises the quality of the planning process and can bring real benefits to an organization.14

Shell’s success with scenario planning influenced many other companies to adopt similar systems. By 1990, more than 50 percent of Fortune 500 companies were using some version of scenario planning (it is also called contingency planning), and the number has increased since then.15 The great strength of scenario planning is its ability not only to anticipate the challenges of an uncertain future but also to educate managers to think about the future—to think strategically.16

Tips For New Managers

Planning

1. Think ahead by using exercises like scenario planning on a regular basis.
2. See plans as a guide to action. Don’t become straitjacketed by plans that may no longer be appropriate in a changing environment.
3. Make sure that the plans created at each of the three organizational levels are compatible with one another and that managers at all levels recognize how their actions fit into the overall corporate plan.
4. Give managers at all levels the opportunity to participate in the planning process to best analyze an organization’s present situation and the future scenarios that may affect it.
Determining the Organization’s Mission and Goals

Determining the organization’s mission and goals is the first step of the planning process. Once the mission and goals are agreed upon and formally stated in the corporate plan, they guide the next steps by defining which strategies are appropriate and which are inappropriate.\(^7\)

Defining the Business

To determine an organization’s mission, managers must first define its business so that they can identify what kind of value they will provide to customers. To define the business, managers must ask three questions: (1) Who are our customers? (2) What customer needs are being satisfied? (3) How are we satisfying customer needs?\(^8\) They ask these questions to identify the customer needs that the organization satisfies and the way the organization satisfies those needs. Answering these questions helps managers to identify not only what customer needs they are satisfying now but what needs they should try to satisfy in the future and who their true competitors are. All of this information helps managers plan and establish appropriate goals. The case of Mattel shows the important role that defining the business has in the planning process.

Mattel RedisCOVERS ITSELF

In the 1990s, Mattel Inc., the well-known maker of such classic toys as Barbie dolls and Hot Wheels believed that the toy market and customer preferences for toys were changing rapidly. This was because of the growing popularity of electronic toys and computer games. Sales of computer games had increased dramatically as more and more parents saw the educational opportunities offered by games that children would also enjoy playing. Moreover, many kinds of computer games could be played with other people over the Internet so it seemed that in the future the magic of electronics and information technology would turn the toy world upside down.

Mattel’s managers feared that core products, such as its range of Barbie dolls, might lose their appeal and become old given the future possibilities opened up by chips, computers, and the Internet. Mattel’s managers believed that its customers’ needs were changing, and that it needed to find new ways to satisfy those needs if it was to remain the biggest toy seller in the United States. Fearing they would lose their customers to the new computer game companies, Mattel’s managers decided that the quickest and easiest way to redefine its business and become a major player in the computer game market would be to acquire one of these companies. So, in 1998 Mattel paid $3.5 billion for The Learning Company, the maker of such popular games as “Thinking Things.” Its goal was to use this company’s expertise and knowledge both to build an array of new computer games, and to take Mattel’s toys such as Barbie and create new games around them. In this way it hoped to better meet the needs of its existing customers and cater to the needs of the new computer game customers.\(^9\)

In addition, while some classic toys like Barbie have the potential to satisfy customers’ needs for generations, the popularity of many toys is temporary
and is often linked to the introduction of a new movie from Disney, Pixar, or Dreamworks. To ensure that it could meet the changing needs of customers for these kinds of toys, Mattel signed contracts with these companies to become the supplier of the toys linked to these movies. For example in 2001 it agreed to pay Warner Brothers, 15 percent of the gross revenues, and a guaranteed $20 million, for the rights to produce toys linked to the Harry Potter movie, based upon the books of the same name. It plans to fill many of these toys with electronics to allow them to move and make sounds and also to create Harry Potter computer games that will give it even greater ability to satisfy its customers’ needs.20

While Mattel’s managers correctly sensed that customers’ needs were changing, the way in which it decided to satisfy these customer needs—namely by buying The Learning Company—was not the right decision. It turned out that the skills to rapidly develop new games linked to Mattel’s products were not present in The Learning Company and few popular games were forthcoming. Moreover, it had underestimated the need to promote and update its core toys and that the $3.5 billion could have been much better spent boosting and developing these toys. In 2001, CEO Bob Eckert sold off The Learning Company and decided that henceforth it would hire independent specialist companies to develop new electronic toys and computer games, including many related to its well-known products.

In the fast-changing toy market where customers’ needs change and evolve, and where new groups of customers do emerge as new technologies result in new kinds of toys, toy companies like Mattel must learn to define and redefine their businesses to satisfy those needs. By 2001, Mattel had begun to turn out whole new ranges of electronic products linked to Barbie, a new Diva Starz doll line, and new electronic games, and its profits started to recover. Companies have to listen closely to their customers and decide how best to meet their changing needs and preferences.

Establishing Major Goals

Once the business is defined, managers must establish a set of primary goals to which the organization is committed. Developing these goals gives the organization a sense of direction or purpose. In most organizations, articulating major goals is the job of the CEO, although other managers have input into the process. Thus, as noted previously, under the leadership of Jack Welch, General Electric operated with the primary goal that it be first or second in every business in which it competes.

The best statements of organizational goals are ambitious—that is, they stretch the organization and require managers to improve its performance capabilities.21 For example, in 2001 Cisco Systems CEO John Chambers outlined a very challenging goal. This high-flying Internet hardware company has been the success story of the 1990s. It has enjoyed yearly growth of 30 to 50 percent in sales revenue, but was hit in 2000 with over $2.2 billion in excess inventory it could not sell as many of the dot-com companies went belly up and its sales plummeted.22 Nevertheless Chambers announced that the company intended to return to its 30 to 50 percent growth rate within three years and was taking the
appropriate steps to get there. Steps that included the firing of thousands of employees, a big push to increase global sales, and the investment of billions in research to produce new generations of optical networking equipment. This goal represents a significant challenge for Cisco because by the top-management team’s own admission, many of its largest customers are cutting back on Internet expenditures, the dot-com boom has ended, and evolving technology may well require a change in strategic direction. Cisco’s managers’ vision of the mission and goals of their company, and those of Compaq, AT&T, and Wal-Mart, are presented in Figure 8.4.

Although goals should be challenging, they should be realistic. Challenging goals give managers an incentive to look for ways to improve an organization’s operation, but a goal that is unrealistic and impossible to attain may prompt managers to give up.23 For example, Cisco set a challenging goal to reduce its costs by $1 billion a year and managers moved to make many significant improvements in the efficiency of Cisco’s operations to achieve this goal.24 Experience at other companies, like Compaq, Dell, and IBM, however, has shown that it is possible to achieve these cost reductions provided that managers at all levels are involved in these efforts to increase efficiency.25

The time period in which a goal is expected to be achieved should be stated. Cisco’s managers have committed themselves to achieving the sales increases by 2004. Time constraints are important because they emphasize that a goal must be attained within a reasonable period; they inject a sense of urgency into goal attainment and act as a motivator.

### Formulating Strategy

**Strategy formulation** involves managers analyzing an organization’s current situation and then developing strategies to accomplish its mission and achieve its goals.26 Strategy formulation begins with managers analyzing the factors within an organization and outside, in the task and general environments,
that affect or may affect the organization’s ability to meet its goals now and in the future. SWOT analysis and the Five Forces Model are two useful techniques managers use to analyze these factors.

**SWOT Analysis**

**SWOT analysis** is a planning exercise in which managers identify organizational strengths (S), weaknesses (W), and environmental opportunities (O), and threats (T). Based on a SWOT analysis, managers at the different levels of the organization select the corporate-, business-, and functional-level strategies to best position the organization to achieve its mission and goals (see Figure 8.5). Because SWOT analysis is the first step in strategy formulation at any level, we consider it first, before turning specifically to corporate-, business-, and functional-level strategies.

In Chapters 5 and 6 we discussed forces in the task and general environments that have the potential to affect an organization. We noted that changes in these forces can produce opportunities that an organization might take advantage of and threats that may harm its current situation. The first step in SWOT analysis is to identify an organization’s strengths and weaknesses. Table 8.1 lists many important strengths (such as high-quality skills in marketing and in research and development) and weaknesses (such as rising manufacturing costs and outdated technology). The task facing managers is to identify the strengths and weaknesses that characterize the present state of their organization.

The second step in SWOT analysis begins when managers embark on a full-scale SWOT planning exercise to identify potential opportunities and threats in the environment that affect the organization at the present or may affect it in the future. Examples of possible opportunities and threats that must be anticipated (many of which were discussed in Chapter 5) are listed in Table 8.1.

With the SWOT analysis completed, and strengths, weaknesses, opportunities, and threats identified, managers can begin the planning process and determine strategies for achieving the organization’s mission and goals. The resulting strategies should enable the organization to attain its goals by taking advantage of opportunities, countering threats, building strengths, and correcting organizational weaknesses. To appreciate how managers use SWOT analysis to formulate strategy, consider how Douglas Conant, CEO of Campbell Soup, used it to select strategies to try to turn around this troubled food products maker in 2001.
A Transformation at Campbell Soup

Campbell Soup Co. is one of the oldest and best known companies in the world. However, in recent years Campbell’s has seen demand for its major products like condensed soup plummet as customers have switched from high-salt, processed soups to healthier low-fat, low-salt varieties. Indeed, its condensed soup business fell by 20 percent between 1998 and 2000. By 2001, Campbell’s market share and profits were falling, and its new CEO Douglas Conant had to decide what to do to turn around the company and maintain its market position.

One of Conant’s first actions was to initiate a thorough SWOT planning exercise. An analysis of the environment identified the growth of the organic and health food segment of the food market and the increasing number of

### Table 8.1
Questions for SWOT Analysis

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<thead>
<tr>
<th>Potential Strengths</th>
<th>Potential Opportunities</th>
<th>Potential Weaknesses</th>
<th>Potential Threats</th>
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<tr>
<td>Well-developed strategy?</td>
<td>Expand core business(es)?</td>
<td>Poorly developed strategy?</td>
<td>Attacks on core business(es)?</td>
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<tr>
<td>Strong product lines?</td>
<td>Exploit new market segments?</td>
<td>Obsolete, narrow product lines?</td>
<td>Increase in domestic competition?</td>
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<td>Broad market coverage?</td>
<td>Widen product range?</td>
<td>Rising manufacturing costs?</td>
<td>Increase in foreign competition?</td>
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<td>Manufacturing competence?</td>
<td>Extend cost or differentiation advantage?</td>
<td>Decline in R&amp;D innovations?</td>
<td>Change in consumer tastes?</td>
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<tr>
<td>Good marketing skills?</td>
<td>Diversify into new growth businesses?</td>
<td>Poor marketing plan?</td>
<td>Fall in barriers to entry?</td>
</tr>
<tr>
<td>Good materials management systems?</td>
<td>Expand into foreign markets?</td>
<td>Poor materials management systems?</td>
<td>Rise in new or substitute products?</td>
</tr>
<tr>
<td>R&amp;D skills and leadership?</td>
<td>Apply R&amp;D skills in new areas?</td>
<td>Loss of customer goodwill?</td>
<td>Increase in industry rivalry?</td>
</tr>
<tr>
<td>Human resource competencies?</td>
<td>Enter new related businesses?</td>
<td>Inadequate human resources?</td>
<td>New forms of industry competition?</td>
</tr>
<tr>
<td>Brand-name reputation?</td>
<td>Vertically integrate forward?</td>
<td>Loss of brand name?</td>
<td>Potential for takeover?</td>
</tr>
<tr>
<td>Cost of differentiation advantage?</td>
<td>Vertically integrate backward?</td>
<td>Growth without direction?</td>
<td>Changes in demographic factors?</td>
</tr>
<tr>
<td>Appropriate management style?</td>
<td>Overcome barriers to entry?</td>
<td>Loss of corporate direction?</td>
<td>Changes in economic factors?</td>
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<tr>
<td>Appropriate organizational structure?</td>
<td>Reduce rivalry among competitors?</td>
<td>Infighting among divisions?</td>
<td>Downturn in economy?</td>
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<tr>
<td>Appropriate control systems?</td>
<td>Apply brand-name capital in new areas?</td>
<td>Loss of corporate control?</td>
<td>Rising labor costs?</td>
</tr>
<tr>
<td>Ability to manage strategic change?</td>
<td>Seek fast market growth?</td>
<td>Inappropriate organizational structure and control systems?</td>
<td>Slower market growth?</td>
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<tr>
<td>Others?</td>
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<td>High conflict and politics?</td>
<td>Others?</td>
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### Management Insight

**A Transformation at Campbell Soup**

Campbell Soup Co. is one of the oldest and best known companies in the world. However, in recent years Campbell’s has seen demand for its major products like condensed soup plummet as customers have switched from high-salt, processed soups to healthier low-fat, low-salt varieties. Indeed, its condensed soup business fell by 20 percent between 1998 and 2000. By 2001, Campbell’s market share and profits were falling, and its new CEO Douglas Conant had to decide what to do to turn around the company and maintain its market position.

One of Conant’s first actions was to initiate a thorough SWOT planning exercise. An analysis of the environment identified the growth of the organic and health food segment of the food market and the increasing number of...
other kinds of convenience foods as a threat to Campbell’s core soup business. The analysis of the environment also revealed three growth opportunities. One opportunity was in growing market for health and sports drinks in which Campbell’s already was a competitor with its V8 juice, the second was the growing market for salsas in which Campbell competed with its Pace salsa, and the third was in chocolate products where Campbell’s Godiva brand had enjoyed increasing sales throughout the 1990s.

With the analysis of the environment complete, Conant turned his attention to his organization’s resources and capabilities. His internal analysis of Campbell’s identified a number of major weaknesses. These included staffing levels that were too high relative to its competitors, and high costs associated with manufacturing its soups because of the use of old, outdated machinery. Also, Conant noted that Campbell’s had a very conservative culture, people seemed to be afraid to take risks, something that was a real problem in the fast-changing food industry where customer tastes are always changing and new products must be developed constantly. At the same time, the SWOT analysis identified an enormous strength. Campbell enjoyed huge economies of scale because of the enormous quantity of food products that it makes, and it also had a first-rate research and development division which had the capability to develop exciting new food products.

Using the information gained from this SWOT analysis, Conant and his managers decided that Campbell needed to use its product development skills to revitalize its core products and modify or reinvent them in ways that would appeal to increasingly health conscious and busy consumers who did not want to take the time to prepare old-fashioned condensed soup. Campbell’s needed to reinvent them to suit the changing needs of its customers. Moreover, it needed to expand its franchise in the health and sports, snack, and luxury food segments of the market.

Another major need that managers saw was to find new ways to deliver its products to customers. To increase sales Campbell’s needed to tap into new food outlets, such as corporate cafeterias, college dining halls, and other mass eateries to expand consumers’ access to its foods. Finally, Campbell’s had to decentralize authority to managers at lower levels in the organization and give them the responsibility to bring new kinds of soups, salsas, and chocolate products to the market. In this way he hoped to revitalize Campbell’s slow-moving culture and speed the flow of improved and new products to the market.

Analysts are waiting to see if Conant can make the changes necessary to turn around its ailing condensed soup business. Its competitors like Pillsbury, which acquired Progresso soup, and Heinz are driving ahead with their own product innovations and their goal is also to increase their share of the food market.
The Five Forces Model

A well-known model that helps managers isolate particular forces in the external environment that are potential threats is Michael Porter’s five forces model. We discussed the first four in Chapter 5. Porter identified these five factors that are major threats because they affect how much profit organizations competing within the same industry can expect to make:

- **The level of rivalry among organizations in an industry.** The more that companies compete against one another for customers—for example, by lowering the prices of their products or by increasing advertising—the lower is the level of industry profits (low prices mean less profit).

- **The potential for entry into an industry.** The easier it is for companies to enter an industry—because, for example, barriers to entry, such as brand loyalty, are low—the more likely it is for industry prices and therefore industry profits to be low.

- **The power of suppliers.** If there are only a few suppliers of an important input, then suppliers can drive up the price of that input, and expensive inputs result in lower profits for the producer.

- **The power of customers.** If only a few large customers are available to buy an industry’s output, they can bargain to drive down the price of that output. As a result, producers make lower profits.

- **The threat of substitute products.** Often, the output of one industry is a substitute for the output of another industry (plastic may be a substitute for steel in some applications, for example). Companies that produce a product with a known substitute cannot demand high prices for their products, and this constraint keeps their profits low.

Porter argued that when managers analyze opportunities and threats they should pay particular attention to these five forces because they are the major threats that an organization will encounter. It is the job of managers at the corporate, business, and functional levels to formulate strategies to counter these threats so that an organization can respond to its task and general environments, perform at a high level, and generate high profits.

Formulating Corporate-Level Strategies

Corporate-level strategy is a plan of action concerning which industries and countries an organization should invest its resources in to achieve its mission and goals. In developing a corporate-level strategy, managers ask: How should the growth and development of the company be managed in order to increase its ability to create value for its customers (and thus increase performance) over the long run? Managers of most organizations have the goal to grow their companies and actively seek out new opportunities to use the organization’s resources to create more goods and services for customers. Examples of organizations growing rapidly are AOL Time Warner and Microsoft, whose CEOs Gerald Levin and Bill Gates pursue any feasible opportunity to use their companies’ skills to provide customers with new products.
In addition, some managers must help their organizations respond to threats due to changing forces in the task or general environment. For example, customers may no longer be buying the kinds of goods and services a company is producing (typewriters or black and white televisions), or other organizations may have entered the market and attracted away customers (this happened to FedEx when UPS entered the overnight delivery market). Top managers aim to find the best strategies to help the organization respond to these changes and improve performance.

The principal corporate-level strategies that managers use to help a company grow, to keep it on top of its industry, and to help it retrench and reorganize to stop its decline are (1) concentration on a single business, (2) diversification, (3) international expansion and (4) vertical integration. These four strategies are all based on one idea: An organization benefits from pursuing any one of them only when the strategy helps further increase the value of the organization’s goods and services for customers. To increase the value of goods and services, a corporate-level strategy must help an organization, or one of its divisions, differentiate and add value to its products either by making them unique or special or by lowering the costs of value creation.

Concentration on a Single Business

Most organizations begin their growth and development with a corporate-level strategy aimed at concentrating resources in one business or industry in order to develop a strong competitive position within that industry. For example, McDonald’s began as one restaurant in California, but its managers’ long-term goal was to focus its resources in the fast-food business and use those resources to quickly expand across the United States.

Sometimes, concentration on a single business becomes an appropriate corporate-level strategy when managers see the need to reduce the size of their organizations to increase performance. Managers may decide to get out of certain industries, for example, when particular divisions lose their competitive advantage. Managers may sell off those divisions, lay off workers, and concentrate remaining organizational resources in another market or business to try to improve performance. This happened to electronics maker Hitachi in 2001 when it was forced to get out of the CTR computer monitor business. Intense low-price competition existed in the computer monitor market because customers were increasingly switching from bulky CTR monitors to the newer flat, LCD monitors. In July 2001, Hitachi announced it was closing three factories in Japan, Singapore, and Malaysia that produced CTR monitors and would use its resources to invest in the new LCD technology. In contrast, when organizations are performing effectively, they often decide to enter new industries in which they can use their resources to create more value.

Diversification

Diversification is the strategy of expanding operations into a new business or industry and producing new goods or services. Examples of diversification include PepsiCo’s diversification into the snack-food business with the purchase of Frito Lay, tobacco giant Philip Morris’s diversification into the brewing industry with the acquisition of Miller Beer, and General Electric’s move into broadcasting with its acquisition of NBC. There are two main kinds of diversification: related and unrelated.
**RELATED DIVERSIFICATION**

Related diversification is the strategy of entering a new business or industry to create a competitive advantage in one or more of an organization’s existing divisions or businesses. Related diversification can add value to an organization’s products if managers can find ways for its various divisions or business units to share their valuable skills or resources so that synergy is created. Synergy is obtained when the value created by two divisions cooperating is greater than the value that would be created if the two divisions operated separately. For example, suppose two or more divisions within a diversified company can utilize the same manufacturing facilities, distribution channels, advertising campaigns, and so on. Each division that shares resources has to invest less in the shared functions than it would have to invest if it had full responsibility for the activity. In this way, related diversification can be a major source of cost savings. Similarly, if one division’s R&D skills can be used to improve another division’s products, the second division’s products may receive a competitive advantage.

Procter & Gamble’s disposable diaper and paper towel businesses offer one of the best examples of the successful production of synergies. These businesses share the costs of procuring inputs such as paper and developing new technology to reduce manufacturing costs. In addition, a joint sales force sells both products to supermarkets, and both products are shipped by means of the same distribution system. This resource sharing has enabled both divisions to reduce their costs, and as a result, they can charge lower prices than their competitors and thus attract more customers.

In pursuing related diversification, managers often seek to find new businesses where they can use the existing skills and resources in their departments to create synergies, add value to the new business, and hence improve the competitive position of the company. Alternatively, managers may acquire a company in a new industry because they believe that some of the skills and resources of the acquired company might improve the efficiency of one or more of their existing divisions. If successful, such skill transfers can help an organization to lower its costs or better differentiate its products because they create synergies between divisions.

**UNRELATED DIVERSIFICATION**

Managers pursue unrelated diversification when they enter new industries or buy companies in new industries that are not related in any way to their current businesses or industries. One main reason for pursuing unrelated diversification is that, sometimes, managers can buy a poorly performing company, transfer their management skills to that company, turn around its business, and increase its performance, all of which creates value.

Another reason for pursuing unrelated diversification is that purchasing businesses in different industries lets managers engage in portfolio strategy, which is apportioning financial resources among divisions to increase financial returns or spread risks among different businesses, much as individual investors do with their own portfolios. For example, managers may transfer funds from a rich division (a “cash cow”) to a new and promising division (a “star”) and, by appropriately allocating money between divisions, create value. Though used as a popular explanation in the 1980s for unrelated diversification, portfolio strategy has run into increasing criticism in the 1990s.

Today, many companies and their managers are abandoning the strategy of unrelated diversification because there is evidence that too much diversification can cause managers to lose control of their organization’s core business.
Management experts suggest that although unrelated diversification might initially create value for a company, managers sometimes use portfolio strategy to expand the scope of their organization’s businesses too much. When this happens, it becomes difficult for top managers to be knowledgeable about all of the organization’s diverse businesses. Managers do not have the time to process all of the information required to adequately assess the strategy and performance of each division objectively, and organizational performance often suffers.

This problem began to occur at General Electric in the 1970s. As former CEO Reg Jones commented: “I tried to review each business unit plan in great detail. This effort took untold hours and placed a tremendous burden on the corporate executive office. After awhile I began to realize that no matter how hard we would work, we could not achieve the necessary in-depth understanding of the 40-odd business unit plans.” Unable to handle so much information, top managers are overwhelmed and eventually make important resource allocation decisions on the basis of only a superficial analysis of the competitive position of each division. This usually results in value being lost rather than created.

Thus, although unrelated diversification can create value for a company, research evidence suggests that many diversification efforts have reduced value rather than created it. As a consequence, during the 1990s there has been a trend among many diversified companies to divest many of their unrelated divisions. Managers have sold off divisions and concentrated organizational resources on their core business and focused more on related diversification. In the 1990s, for example, Sears divested all of the stock brokerage, insurance, and real-estate businesses it acquired during the 1980s, to concentrate on strengthening its core retailing activities and survive in its fight with Wal-Mart and Target.

**International Expansion**

As if planning the appropriate level of diversification was not a difficult enough decision, corporate-level managers also must decide on the appropriate way to compete internationally. A basic question confronts the managers of any organization that competes in more than one national market: To what extent should the organization customize features of its products and marketing campaign to different national conditions?

If managers decide that their organization should sell the same standardized product in each national market in which it competes, and use the same basic marketing approach, they adopt a *global strategy*. Such companies undertake very little, if any, customization to suit the specific needs of customers in different countries. But if managers decide to customize products and marketing strategies to specific national conditions, they adopt a *multidomestic strategy*. Matsushita has traditionally pursued a global strategy, selling the same basic TVs and VCRs in every market in which it does business and often using the same basic marketing approach. Unilever, the European food and household products company, has pursued a multidomestic strategy. Thus, to appeal to German customers, Unilever’s German division sells a different range of food products and uses a different marketing approach than its North American division.

Global and multidomestic strategies both have advantages and disadvantages. The major advantage of a global strategy is the significant cost savings associated with not having to customize products and marketing approaches to different national conditions. For example, products like Rolex watches, Ralph Lauren or Tommy Hilfiger clothing, Channel or Armani accessories or perfume, Dell computers, Chinese-made plastic toys and buckets, and U.S. grown

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**global strategy** Selling the same standardized product and using the same basic marketing approach in each national market.

**multidomestic strategy** Customizing products and marketing strategies to specific national conditions.
rice and wheat are all products that be sold using the same marketing across many countries by simply changing the language. Thus, companies can save a significant amount of money.

The major disadvantage of pursuing a global strategy is that, by ignoring national differences, managers may leave themselves vulnerable to local competitors that do differentiate their products to suit local tastes. This occurred in the British consumer electronics industry. Amstrad, a British computer and electronics company, got its start by recognizing and responding to local consumer needs. Amstrad captured a major share of the British audio market by ignoring the standardized inexpensive music centers marketed by companies pursuing a global strategy, such as Sony and Matsushita. Instead, Amstrad’s product was encased in teak rather than metal and featured a control panel tailor-made to appeal to British consumers’ preferences. To remain competitive in this market, Matsushita had to place more emphasis on local customization of its Panasonic and JVC brands.

The advantages and disadvantages of a multidomestic strategy are the opposite of those of a global strategy. The major advantage of a multidomestic strategy is that by customizing product offerings and marketing approaches to local conditions, managers may be able to gain market share or charge higher prices for their products. The major disadvantage is that customization raises production costs and puts the multidomestic company at a price disadvantage because it often has to charge prices higher than the prices charged by competitors pursuing a global strategy. Obviously, the choice between these two strategies calls for trade-offs. Managers at Gillette have created a strategy that combines the best features of both international strategies, as profiled in this “Managing Globally” feature.

**Gillette’s New International Strategy**

Gillette, the well-known razor blade maker, has been a global company from the beginning as its managers quickly saw the advantages of selling its products abroad. By 2000, 60 percent of Gillette’s revenues came from global sales and this percentage is expected to increase. Gillette’s strategy over the years has been pretty constant: Find a new foreign country with a growing market for razor blades, form a strategic alliance with a local razor blade company and take a majority stake in it; invest in a large marketing campaign and then build a modern factory to make razor blades and other products for the local market. For example, when Gillette entered Russia after the break up of the Soviet Union it saw a huge opportunity to increase sales. It formed a joint venture with a local company called Leninets Concern which made a razor known as the Sputnik, and then with this base began to import its own brands into Russia. When sales growth rose sharply it decided to offer more products in the market and built a new plant in St. Petersburg.

Today, Gillette operates 54 manufacturing facilities in more than 20 countries. It establishes its factories in countries where labor and other costs are low, and then distributes and markets its products to countries in that region of the world. So, in this sense it pursues a global strategy. However, all of Gillette’s research and development and design takes place in the United States. As it develops new kinds of razors it equips its foreign factories to manufacture them when it decides that local customers are ready to trade up to the new product. So, for example, Gillette’s latest razor may be introduced in a foreign country years later than in the United States. Thus, Gillette is customizing its product
offering to the needs of different countries and also pursues a multidomestic strategy. By pursuing this international strategy Gillette achieve low costs and still differentiates and customizes its product range to suit the needs of each country or world region. This strategy has proved very effective for Gillette. In 2001 Gillette Chairman and CEO James F. Kilts reported that, “There are few consumer products companies with more powerful global brands than Gillette. I believe that there is a huge opportunity to maximize the potential of Gillette’s global brands by tailoring its products to the needs of different countries.”

**Vertical Integration**

When an organization is doing well in its business, managers often see new opportunities to create value by either producing their own inputs or distributing their own outputs. Managers at E. & J. Gallo Winery, for example, realized that they could lower Gallo’s costs if they produced their own wine bottles rather than buying them from a glass company. As a result, Gallo established a new division to produce glass bottles.

**Vertical integration** is the corporate-level strategy through which an organization becomes involved in producing its own inputs (backward vertical integration) or distributing and selling its own outputs (forward vertical integration). A steel company that supplies its iron ore needs from company-owned iron ore mines is engaging in backward vertical integration. A personal computer company that sells its computers through company-owned distribution outlets, as Tandy did through its Radio Shack stores, is engaging in forward vertical integration.

Figure 8.6 illustrates the four main stages in a typical raw-materials-to-consumer value chain; value is added at each stage. Typically, the primary operations of an organization take place in one of these stages. For a company based in the assembly stage, backward integration would involve establishing a new division in intermediate manufacturing or raw-material production, and forward integration would involve establishing a new division to distribute its...
products to wholesalers or to sell directly to customers. A division at one stage receives the product produced by the division in the previous stage, transforms it in some way—adding value—and then transfers the output at a higher price to the division at the next stage in the chain.

As an example of how the value chain works, consider the cola segment of the soft-drink industry. Raw-materials suppliers include sugar companies and G. D. Searle, manufacturer of the artificial sweetener NutraSweet, which is used in diet colas. These companies sell their products to companies that make concentrate—such as Coca-Cola and PepsiCo that mix these inputs with others to produce the cola concentrate that they market. In the process, they add value to these inputs. The concentrate producers then sell the concentrate to bottlers, who add carbonated water to the concentrate and package the resulting drink—again adding value to the concentrate. Next, the bottlers sell the packaged product to various distributors, including retail stores such as Price Costco and Wal-Mart, and fast-food chains such as McDonald’s. These distributors add value by making the product accessible to customers. Thus, value is added by companies at each stage in the raw-materials-to-consumer chain.

A major reason why managers pursue vertical integration is that it allows them either to add value to their products by making them special or unique or to lower the costs of value creation. For example, Coca-Cola and PepsiCo, in a case of forward vertical integration to build brand loyalty and enhance the differentiated appeal of their colas, decided to buy up their major bottlers to increase control over marketing and promotion efforts that had been handled by the bottlers. An example of using forward vertical integration to lower costs is Matsushita’s decision to open company-owned stores to sell its Panasonic and JVC products and thus keep the profit that otherwise would be earned by independent retailers.

Although vertical integration can help an organization to grow rapidly, it can be a problem when forces in the environment counter the strategies of the organization and make it necessary for managers to reorganize or retrench. Vertical integration can reduce an organization’s flexibility to respond to changing environmental conditions. For example, IBM used to produce most of its own components for mainframe computers. While this made sense in the 1970s, it become a major handicap for the company in the fast-changing computer industry of the 1990s. The rise of organizationwide networks of personal computers meant slumping demand for mainframes. As demand fell, IBM found
itself with an excess-capacity problem, not only in its mainframe assembly operations but also in component operations. Closing down this capacity cost IBM over $5 billion.\(^{45}\)

When considering vertical integration as a strategy to add value, managers must be careful because sometimes vertical integration actually reduces an organization’s ability to create value when the environment changes. This is why so many companies now outsource the production of component parts to other companies. IBM, however, has found a new opportunity for forward vertical integration in the 1990s.\(^{46}\) It decided to provide IT consulting services to mainframe users and to advise them on how to install and manage any software packages they chose on their mainframes. Providing such IT services was so profitable for IBM that by 2000 it had recovered its market position.

Michael Porter, the researcher who developed the five forces model discussed earlier, also formulated a theory of how managers can select a business-level strategy, a plan to gain a competitive advantage in a particular market or industry.\(^{47}\) According to Porter, managers must choose between the two basic ways of increasing the value of an organization’s products: differentiating the product to add value or lowering the costs of value creation. Porter also argues that managers must choose between serving the whole market or serving just one segment or part of a market. Based on those choices, managers choose to pursue one of four business-level strategies: low cost, differentiation, focused low cost, or focused differentiation (see Table 8.2).

### Low-Cost Strategy

With a low-cost strategy, managers try to gain a competitive advantage by focusing the energy of all the organization’s departments or functions on driving the organization’s costs down below the costs of its rivals. This strategy, for example, would require manufacturing managers to search for new ways to reduce production costs, R&D managers to focus on developing new products that can be manufactured more cheaply, and marketing managers to find ways to lower the costs of attracting customers. According to Porter, organizations pursuing a low-cost strategy can sell a product for less than their rivals sell it and yet still make a profit because of their lower costs. Thus, organizations that pursue a low-cost strategy hope to enjoy a competitive advantage based on their low prices. For example, BIC pursues a low-cost strategy; it offers customers razor blades priced lower than Gillette’s and ballpoint pens less expensive than those offered by Cross or Waterford.

### Differentiation Strategy

With a differentiation strategy, managers try to gain a competitive advantage by focusing all the energies of the organization’s departments or functions on distinguishing the organization’s products from those of competitors in one or more important dimensions, such as product design, quality, or after-sales service. Often, the process of making products unique and different is expensive. This strategy, for example, often requires managers to increase
spending on product design or R&D to differentiate the product, and costs rise as a result. Organizations that successfully pursue a differentiation strategy may be able to charge a premium price for their products, a price usually much higher than the price charged by a low-cost organization. The premium price allows organizations pursuing a differentiation strategy to recoup their higher costs. Coca-Cola, PepsiCo and Procter & Gamble, are some of the many well-known companies that pursue a strategy of differentiation. They spend enormous amounts of money on advertising to differentiate, and create a unique image for, their products.

“Stuck in the Middle”

According to Porter’s theory, managers cannot simultaneously pursue both a low-cost strategy and a differentiation strategy. Porter identified a simple correlation: Differentiation raises costs and thus necessitates premium pricing to recoup those high costs. For example, if BIC suddenly began to advertise heavily to try to build a strong global brand image for its products, BIC’s costs would rise. BIC then could no longer make a profit simply by pricing its blades or pens lower than Gillette or Cross. According to Porter, managers must choose between a low-cost strategy and a differentiation strategy. He refers to managers and organizations that have not made this choice as being “stuck in the middle.” According to Porter, organizations stuck in the middle tend to have lower levels of performance than do those that pursue a low-cost or differentiation strategy. To avoid being stuck in the middle, top managers must instruct departmental managers to take actions that will result in either low cost or differentiation.

However, exceptions to this rule can be found. In many organizations managers have been able to drive costs below those of rivals and simultaneously differentiate their products from those offered by rivals. For example, Toyota’s production system is reportedly the most efficient in the world. This efficiency gives Toyota a low-cost strategy vis-à-vis its rivals in the global car industry. At the same time, Toyota has differentiated its cars from those of rivals on the basis of superior design and quality. This superiority allows the company to charge a premium price for many of its popular models. Thus, Toyota seems to be simultaneously pursuing both a low-cost and a differentiated business-level strategy. This example suggests that although Porter’s ideas may be valid in most cases, very well managed companies such as Toyota, McDonald’s, and Dell Computer may have both low costs and differentiated products.
Focused Low-Cost and Focused Differentiation Strategies

Both the differentiation strategy and the low-cost strategy are aimed at serving many or most segments of a particular market such as for cars or computers. Porter identified two other business-level strategies that aim to serve the needs of customers in only one or a few market segments. Managers pursuing a focused low-cost strategy serve one or a few segments of the overall market and aim to be the lowest-cost company serving that segment.

For example, Cott Corporation is the world’s leading supplier of retailer brandname carbonated soft drinks. With production facilities in Canada, the United States and the United Kingdom, it produces, packages, and distributes a wide selection of retailer brand beverages for grocery, mass-merchandise, drugstore, and convenience store chains. For example, all Wal-Mart soda sold under the Sam’s brand-name is made by Cott. However, note that while it is the world’s leading supplier of retailer-brand name sodas, it is focusing on a low cost strategy. It makes no attempt to compete with Coke and Pepsi, which, as noted earlier, pursue a differentiation strategy, and whose brand-name sodas dominate the global soda market.

By contrast, managers pursuing a focused differentiation strategy serve just one or a few segments of the market and aim to be the most differentiated company serving that segment. BMW, for example, pursues a focused strategy, producing cars exclusively for higher-income customers. By contrast, Toyota pursues a differentiation strategy and produces cars that appeal to consumers in almost all segments of the car market, from basic transportation (Toyota Tercel), through the middle of the market (Toyota Camry), to the high-income end of the market (Lexus).

As these examples suggest, companies pursuing either of these focused strategies have chosen to specialize in some way by directing their efforts at a particular kind of customer (such as serving the needs of babies or affluent customers) or even the needs of customers in a specific geographical region (customers on the east or west coast). An excellent example of how a company can pursue both a low-cost and a differentiated focused strategy at the same time by using new information technologies is provided by Zara, a manufacturer of fashionable Spanish clothing.

IT and Just-in-Time Low-Cost Fashion

Well-known fashion houses like Channel, Dior, and Armani can charge thousands of dollars for the fashionable collections of suits and dresses that they introduce twice yearly in the fall and in the spring. Only the very rich can afford such differentiated and expensive clothing and this has opened up a gap in the fashion market for companies that can supply fashionable clothes at lower prices. Essentially, these companies have the capabilities to pursue a focused differentiation and cost-leadership strategy.

While many clothing companies, such as the United States’s The Gap, Sweden’s Hennes & Mauritz, and England’s Jaeger and Laura Ashley, have attempted to supply fashionable clothes at lower prices, none has succeeded as well as Spanish clothes maker, Zara, whose sales have soared in recent
Zara has managed to position itself as the low price/cost leader in the fashion segment of the clothing market because of the way it uses information technology. It has created an information system that allows it to manage its design and manufacturing process in a way that minimizes the inventory it has to carry—the major cost borne by a clothing retailer. However, its IT also gives instantaneous feedback on which clothes are selling well, and in which countries, which gives it a competitive advantage from differentiation. Specifically, Zara can manufacture more of a particular kind of dress or suit to meet high customer demand, decide which clothing should be sold in its rapidly expanding network of global stores, and constantly change the mix of clothes it offers customers to keep up with fashion. Moreover, it can do this at relatively small output levels, something which is also a part of a specialized, focused strategy.

Zara’s IT also allows it to manage the interface between its design and manufacturing operations more efficiently. Zara only takes five weeks to design a new collection and then a week to make it. Other fashion houses, by contrast, can take six or more months to design the collection and then three more before it is available in stores. This short time-to-market gives Zara great flexibility and allows the company to respond quickly to the rapidly changing fashion market which fashions can change several times a year. Because of the quick manufacturing to sales cycle and just-in-time fashion, Zara offers its clothes collections at relatively low prices and still makes profits that are the envy of the fashion clothing industry.

When Zara offered its shares to the public for the first time in 2001, its shares soared in price. Investors believe that there will soon be a Zara store in most major cities across the world and that its name will become as common to customers as the more well-known clothes designers.

**Formulating Functional-Level Strategies**

*Functional-level strategy* is a plan of action to improve the ability of an organization’s departments to create value. It is concerned with the actions that managers of individual departments (such as manufacturing or marketing) can take to add value to an organization’s goods and services and thereby increase the value customers receive. The price that customers are prepared to pay for a product indicates how much they value an organization’s products. The more customers value a product, the more they are willing to pay for it.

There are two ways in which departments can add value to an organization’s products:

1. Departmental managers can lower the costs of creating value so that an organization can attract customers by keeping its prices lower than its competitors’ prices.
2. Departmental managers can add value to a product by finding ways to differentiate it from the products of other companies.

If customers see more value in one organization’s products than in the products of its competitors, they may be willing to pay premium prices. Thus, there must be a fit between functional- and business-level strategies if an organization is to achieve its mission and goal of maximizing the amount of value it gives customers. The better the fit between functional- and business-level strategies, the greater will be the organization’s competitive advantage—its ability to attract customers and the revenue they provide.

Each organizational function has an important role to play in the process of lowering costs or adding value to a product (see Table 8.3). Manufacturing can find new ways to lower production costs or to build superior quality into the product to add value. Marketing, sales, and after-sales service and support can add value by, for example, building brand loyalty (as Coca-Cola and PepsiCo have done in the soft-drink industry) and finding more effective ways to attract customers. Human resource management can lower the costs of creating value by recruiting and training a highly productive workforce. The R&D function can lower the costs of creating value by developing more efficient production processes. Similarly, R&D can add value by developing new and improved products that customers value over established product offerings. Managers can lower the costs of creating value and can add value through their effective leadership and coordination of the whole organization (see Chapter 13).

In trying to add value or lower the costs of creating value, all functional managers should attend to these four goals:54

1. To attain superior efficiency. Efficiency is a measure of the amount of inputs required to produce a given amount of outputs. The fewer the inputs required to produce a given output, the higher is the efficiency and the lower the cost of outputs. For example, in 1990 it took the average Japanese auto company 16.8 employee-hours to build a car, while the average American auto company took 25.1 employee-hours. Japanese companies at that time were more efficient and had lower costs than their American rivals.55 By 2000, U.S. companies adopted more efficient manufacturing methods and narrowed that gap significantly; matching Japanese quality levels, however, has been more difficult.

2. To attain superior quality. Quality here means producing goods and services that are reliable—they do the job they were designed for and do it well.56 Providing high-quality products creates a brand-name reputation for an organization’s products. In turn, this enhanced reputation allows the organization to charge a higher price. In the automobile industry, for example, not only does Toyota have an efficiency-based cost advantage over many American and European competitors, but the higher quality of Toyota’s products has also enabled the company to earn more money because customers are willing to pay a premium price for its cars.

3. To attain superior innovation. Anything new or novel about the way an organization operates or the goods and services it produces is the result of innovation. Innovation leads to advances in the kinds of products, production processes, management systems, organizational structures, and strategies that an organization develops. Successful innovation gives an organization something unique that its rivals lack. This uniqueness may enhance value added and thereby allow the organization to differentiate itself from its rivals and attract customers who will pay a premium price for its product. For example, Toyota is widely credited with pioneering a number of critical innovations in the way cars
are built, and these innovations have helped Toyota achieve superior productivity and quality—the basis of Toyota’s competitive advantage.

4. **To attain superior responsiveness to customers.** An organization that is responsive to customers tries to satisfy their needs and give them exactly what they want. An organization that treats customers better than its rivals treats them provides a valuable service for which customers may be willing to pay a higher price.

Attaining superior efficiency, quality, innovation, and responsiveness to customers requires the adoption of many state-of-the-art management techniques and practices, such as total quality management, flexible manufacturing systems, just-in-time inventory, self-managing teams, cross-functional teams, process reengineering, and employee empowerment. It is the responsibility of managers at the functional level to identify these techniques and develop a functional-level plan that contains the strategies necessary to develop them. We discuss these techniques at length in Part 6 where we focus on the management of operations and processes. The important issue to remember here is that all of these techniques can help an organization achieve a competitive advantage by lowering the costs of creating value, or by adding value above and beyond that offered by rivals.

### Planning and Implementing Strategy

Planning and Implementing Strategy

After identifying appropriate strategies to attain an organization’s mission and goals, managers confront the challenge of putting those strategies into action. Strategy implementation is a five-step process:

1. Allocating responsibility for implementation to the appropriate individuals or groups

### Table 8.3

How Functions Can Lower the Costs and Create Value or Add Value to Create a Competitive Advantage

<table>
<thead>
<tr>
<th>Value-Creating Function</th>
<th>Ways to Lower the Cost of Creating Value (Low-Cost Advantage)</th>
<th>Ways to Add Value (Differentiation Advantage)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sales and marketing</td>
<td>• Find new customers</td>
<td>• Promote brand-name awareness and loyalty</td>
</tr>
<tr>
<td>Materials management</td>
<td>• Find low-cost advertising methods</td>
<td>• Tailor products to suit customers’ needs</td>
</tr>
<tr>
<td>Research and development</td>
<td>• Use just-in-time inventory system/computerized warehousing</td>
<td>• Develop long-term relationships with suppliers to provide high-quality inputs</td>
</tr>
<tr>
<td>Manufacturing</td>
<td>• Develop long-term relationships with suppliers and customers</td>
<td>• Reduce shipping time to customers</td>
</tr>
<tr>
<td>Human resource management</td>
<td>• Improve efficiency of machinery and equipment</td>
<td>• Create new products</td>
</tr>
<tr>
<td></td>
<td>• Design products that can be made more cheaply</td>
<td>• Improve existing products</td>
</tr>
<tr>
<td></td>
<td>• Develop skills in low-cost manufacturing</td>
<td>• Increase product quality and reliability</td>
</tr>
<tr>
<td></td>
<td>• Reduce turnover and absenteeism</td>
<td>• Hire highly skilled employees</td>
</tr>
<tr>
<td></td>
<td>• Raise employee skills</td>
<td>• Develop innovative training programs</td>
</tr>
<tr>
<td></td>
<td>• Find low-cost advertising methods</td>
<td></td>
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<tr>
<td></td>
<td>• Use just-in-time inventory system/computerized warehousing</td>
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</tr>
</tbody>
</table>

Planning and Implementing Strategy

After identifying appropriate strategies to attain an organization’s mission and goals, managers confront the challenge of putting those strategies into action. Strategy implementation is a five-step process:

1. Allocating responsibility for implementation to the appropriate individuals or groups
2. Drafting detailed action plans that specify how a strategy is to be implemented
3. Establishing a timetable for implementation that includes precise, measurable goals linked to the attainment of the action plan
4. Allocating appropriate resources to the responsible individuals or groups
5. Holding specific individuals or groups responsible for the attainment of corporate, divisional, and functional goals

As an example of how the strategy implementation process works in practice, consider the situation of Citibank, one of the largest financial institutions in the United States. While analyzing the strengths and weaknesses of Citibank (during a SWOT analysis), managers identified poor responsiveness to customers, and a lack of innovation within the organization as major weaknesses. Customers who are forced to wait in line, or wait several days for an answer to their personal banking inquiries, are not satisfied customers.

To correct this weakness, Citibank’s managers decided to reengineer or redesign the bank’s customer service processes to reduce waste and inefficiencies and to speed responsiveness to customers. Managers at all levels from the top down were charged with the implementation of this initiative. At each level, managers were requested to draft a plan that specified how this initiative would be implemented.

The plan called for the bank to train a small group of its own employees in reengineering techniques designed to build new customer service skills and to use this group as a reengineering team. The action plan also established a formal process for identifying reengineering opportunities within the organization and for deciding which customer service problems the reengineering team should tackle first. A detailed timetable was established; it laid out deadlines for identifying and training the reengineering team, for identifying reengineering opportunities, for prioritizing opportunities, and for beginning the actual reengineering process. The individuals responsible were given a budget to provide them with the financial resources necessary to complete the project. Finally, top management informed the individuals responsible that they would be held accountable for meeting the timetable associated with the plan and for the overall success of the strategic initiative.

As the case of Citibank illustrates, the planning process goes beyond the mere identification of strategies; it also includes actions taken to ensure that the organization actually puts its strategies into action. It should be noted that the plan for implementing a strategy may require radical redesign of the structure of the organization, the development of new control systems, and the adoption of a program for changing the culture of the organization. These are all issues that we address in the next three chapters.

Tips for New Managers

Strategy

1. Periodically define an organization’s business to determine how well it is achieving its mission. Use this planning exercise to determine its future goals.
2. Make SWOT analysis an integral part of the planning process.

3. Always be alert for opportunities to increase the value of an organization’s goods and services so it can better serve its customers’ needs.

4. Ensure that functional managers focus on finding new ways in which to lower the costs of value creation or to add value to products so that an organization can pursue both a low-cost strategy and a differentiation strategy.

5. Carefully assess the costs and benefits associated with using a corporate-level strategy and only enter a new business when it can clearly demonstrate that it will increase the value of your products.

Summary and Review

PLANNING  Planning is a three-step process: (1) determining an organization’s mission and goals; (2) formulating strategy; (3) implementing strategy. Managers use planning to identify and select appropriate goals and courses of action for an organization and to decide how to allocate the resources they need to attain those goals and carry out those actions. A good plan builds commitment for the organization’s goals, gives the organization a sense of direction and purpose, coordinates the different functions and divisions of the organization, and controls managers by making them accountable for specific goals. In large organizations planning takes place at three levels: corporate, business or divisional, and functional or department. Although planning is typically the responsibility of a well-defined group of managers, the subordinates of those managers should be given every opportunity to have input into the process and to shape the outcome. Long-term plans have a time horizon of five years or more; intermediate-term plans, between one and five years; and short-term plans, one year or less.

DETERMINING MISSION AND GOALS AND FORMULATING STRATEGY  Determining the organization’s mission requires managers to define the business of the organization and establish major goals. Strategy formulation requires managers to perform a SWOT analysis and then choose appropriate strategies at the corporate, business, and functional levels. At the corporate level, organizations use strategies such as concentration on a single business, diversification, international expansion, and vertical integration to help increase the value of the goods and services provided to customers. At the business level, managers are responsible for developing a successful low-cost or differentiation strategy, either for the whole market or for a particular segment of it. At the functional level, departmental managers strive to develop and use their skills to help the organization either to add value to its products by differentiating them or to lower the costs of value creation.

IMPLEMENTING STRATEGY  Strategy implementation requires managers to allocate responsibilities to appropriate individuals or groups, draft detailed action plans that specify how a strategy is to be implemented, establish a timetable for implementation that includes precise, measurable goals linked to the attainment of the action plan, allocate appropriate resources to the responsible individuals or groups, and hold individuals or groups accountable for the attainment of goals.
1. Describe the three steps of planning. Explain how they are related.
2. How can scenario planning help managers predict the future?
3. Ask a manager about the kinds of planning exercises he or she regularly uses. What are the purposes of these exercises, and what are their advantages or disadvantages?
4. What is the role of divisional and functional managers in the formulation of strategy?
5. Why is it important for functional managers to have a clear grasp of the organization’s mission when developing strategies within their departments?
6. What is the relationship among corporate-, business-, and functional-level strategies and how do they create value for an organization?
7. Ask a manager to identify the corporate-, business-, and functional-level strategies used by his or her organization.

**Building Management Skills**

**How to Analyze a Company’s Strategy**

Pick a well-known business organization that has received recent press coverage and for which you can get the annual reports or 10K filings from your school library for a number of years. For this organization do the following:

1. From the annual reports or 10K filings identify the main strategies pursued by the company over a ten-year period.
2. Try to identify why the company pursued these strategies. What reason was given in the annual reports, press reports, and so on?
3. Document whether and when any major changes in the strategy of the organization occurred. If changes did occur, try to identify the reason for them.
4. If changes in strategy occurred, try to determine the extent to which they were the result of long-term plans and the extent to which they were responses to unforeseen changes in the company’s task environment.
5. What is the main industry that the company competes in?
6. What business-level strategy does the company seem to be pursuing in this industry?
7. What is the company’s reputation with regard to productivity, quality, innovation, and responsiveness to customers in this industry? If the company has attained an advantage in any of these areas, how has it done so?
8. What is the current corporate-level strategy of the company? What is the company’s stated reason for pursuing this strategy?
9. Has the company expanded internationally? If it has, identify its largest international market. How did the company enter this market? Did its mode of entry change over time?
Small Group Breakout Exercise

Low Cost or Differentiation?

Form groups of three or four people, and appoint one member as spokesperson who will communicate your findings to the class when called on by the instructor. Then discuss the following scenario.

You are a team of managers of a major national clothing chain, and you have been charged with finding a way to restore your organization’s competitive advantage. Recently, your organization has been experiencing increasing competition from two sources. First, discount stores such as Wal-Mart and Target have been undercutting your prices because they buy their clothes from low-cost foreign manufacturers while you buy most of yours from high-quality domestic suppliers. Discount stores have been attracting your customers who buy at the low end of the price range. Second, small boutiques opening in malls provide high-price designer clothing and are attracting away your customers at the high end of the market. Your company has become stuck in the middle, and you have to decide what to do: Should you start to buy abroad so that you can lower your prices and start to pursue a low-cost strategy? Should you focus on the high end of the market and become more of a differentiator? Or should you try to do both and pursue both a low-cost strategy and a differentiation strategy?

1. Using scenario planning, analyze the pros and cons of each alternative.
2. Think about the various clothing retailers in your local malls and city, and analyze the choices they have made about how to compete with one another along the low-cost and differentiation dimensions.

Exploring the World Wide Web

Search for a website that contains a good description of a company’s strategy. What is the company’s mission? Use the concepts and terminology of this chapter to describe the company’s strategy to achieve its mission.

You’re the Management Consultant

A group of investors in your city is considering opening a new upscale supermarket to compete with the major supermarket chains that are currently dominating the city’s marketplace. They have called you in to help them determine what kind of upscale supermarket they should open. In other words, how can they best develop a competitive advantage against existing supermarket chains?

Questions
1. List the supermarket chains in your city and identify their strengths and weaknesses.
2. What business-level strategies are these supermarkets currently pursuing?
3. What kind of supermarket would do best against the competition? What kind of business-level strategy should it pursue?

BusinessWeek

Cases in the News 1

Ford’s Gamble on Luxury: Can It Make Its Portfolio of Acquired Brands Work Together?

Over the past decade, Ford Motor Co. has grown fat on profits from its pickup trucks and sport-utility vehicles. Last year, those trucks accounted for 80 percent of its pretax auto earnings in North America. But now that foreign auto makers have finally found their groove with light-truck vehicles that are truly competitive, those earnings are in jeopardy. Faced with such hot-selling models as the Toyota Sequoia and the BMW X5, Ford could see its share of the light-truck market fall by as
Ford, he says, can “fill all the needs of their garage” at a single dealership. Construction recently began near Phoenix on the first of about 10 such dealerships that are scheduled to open in the next 18 months. Those dealerships will include a quarter-mile test track so that while an owner’s car is being serviced, the customer can test-drive another luxury marque.

Most dealers would jump at the chance to own a megastore selling all of Ford’s luxury brands. But many are worried that investing in such a dealership, which could cost up to $25 million, would be too expensive. “Most of us are waiting to see how it will work,” says Harold Kuhn, owner of Park Lincoln Mercury in Detroit. One big issue: Ford has to persuade dealers of different brands to sell their stores to other car dealers to form the consolidated luxury operations. Already, Ford has encouraged Lincoln Mercury dealers to sell their businesses to reduce the number of dealers in certain regions.

Some critics say the idea won’t fly because Ford’s premium lineup just can’t encompass everything luxury owners want. Susan Jacobs, president of Jacobs & Associates, a Rutherford (N.J.) firm specializing in luxury-market analysis, gives this example: A Jaguar enthusiast who likes sporty cars is more likely to want the European high-performance experience of a BMW or Mercedes for his new SUV than a Lincoln Navigator or Land Rover. With rivals adding SUVs and entry-level models to their lineups, Ford can forget about stealing customers from European brands, says Jacobs. “The mistake they’re making, in a very crowded market,” Jacobs says, “is that you just can’t manage all these boutique brands.”

Reitzle believes that by carefully deciding which new models to add...
under each brand name, collisions between brands can be avoided. “You can only do what we’re doing when you have a brand portfolio that is complementary. Our setup is unique,” he says.

So are the problems. And Reitzle can’t ignore each brand’s particular issues as he pursues his integrated luxury strategy. Jaguar, having overcome longstanding quality problems, has perhaps the most aggressive growth plans. Its sales grew about 25% last year, to 87,000 units, with the addition of the $45,000 S-type, a sedan built on the same platform as Ford’s Lincoln LS and the upcoming Ford Thunderbird. Jaguar is moving further downscale with the $30,000 X-type, a competitor to BMW’s 3-series, which goes on sale this summer. And to expand its market, Jaguar is also going after younger drivers and African-American purchasers by using marketing that is geared toward them. But the low end of the luxury category is perhaps the most competitive segment, and as the economy softens, it’s the one that could be subject to a price war.

**Fixer-Upper**

Ford also has to find a way to make Land Rover profitable, something its previous owner, BMW, couldn’t do. Land Rover isn’t as bad off as Jaguar was when Ford purchased it in 1989, but company execs estimate that it will take as long as two years just to shore up the British auto maker. Long term, the plan is to share platforms with Ford’s trucks to lower costs and improve quality. For now, growth will come from the addition of lower-priced models, such as the Freelander, which debuts in the U.S. later this year.

Perhaps the toughest challenge is turning around Ford’s own Lincoln brand. Even though sales climbed in the late ‘90s with the success of the big Lincoln Navigator SUV, the brand was eclipsed by faster-growing import rivals Mercedes and Lexus. Ford execs are trying to reshape Lincoln around the theme “American luxury.” This spring, the $52,000 Lincoln Blackwood, an SUV-pickup hybrid, goes on sale. And within a few years, Lincoln will add an entry-level sedan and a compact SUV. More Lincolns are also on the drawing board.

Even Volvo, the Swedish carmaker known for its boxy sedans and wagons, is beginning to introduce more stylish models, such as the new S60 sedan now on sale. Volvo is Ford’s biggest luxury brand, selling 477,000 units worldwide, but the goal is to boost that figure to 600,000 within five years. More important, Volvo’s growth is key to Ford’s turnaround efforts in Europe, where Ford can stem losses by building Volvos in underutilized Ford factories.

Building the Premier Automotive Group into the profit machine Ford envisions will take time. “We are now on a 10-year journey,” says Reitzle. With so many brands under its belt, Ford is hoping for a comfortable ride.


**Questions**

1. What is Ford’s business-level strategy? What are its main features? Why does it have so many different brandname cars?

2. What are the main problems, opportunities, and threats Ford’s managers encounter in managing this strategy?
the Gateway Country Store model. And it will give Apple fresh outlets to sell its own products such as the titanium PowerBook and other companies’ consumer gadgets such as Handspring Inc.’s Visor handheld line. The company would gain new revenue as a reseller of other electronic goodies and have more control over marketing and servicing of its products. What’s more, Apple could boost margins by cutting out middlemen and wooing buyers to higher-priced models. The way Jobs sees it, the stores look to be a sure thing. But even if they attain a measure of success, few outsiders think new stores, no matter how well-conceived, will get Apple back on the hot-growth path. Jobs’s focus on selling just a few consumer Macs has helped boost profits, but it is keeping Apple from exploring potential new markets. And his perfectionist attention to aesthetics has resulted in beautiful but pricey products with limited appeal outside the faithful: Apple’s market share is a measly 2.8%. “Apple’s problem is it still believes the way to grow is serving caviar in a world that seems pretty content with cheese and crackers,” gripes former Chief Financial Officer Joseph Graziano.

Rather than unveil a Velveeta Mac, Jobs thinks he can do a better job than experienced retailers at moving the beluga. Problem is, the numbers don’t add up. Given the decision to set up shop in high-rent districts in Manhattan, Boston, Chicago, and Jobs’s hometown of Palo Alto, Calif., the leases for Apple’s stores could cost $1.2 million a year each, says David A. Goldstein, president of researcher Channel Marketing Corp. Since PC retailing gross margins are normally 10% or less, Apple would have to sell $12 million a year per store to pay for the space. Gateway does about $8 million annually at each of its Country Stores. Then there’s the cost of construction, hiring experienced staff. “I give them two years before they’re turning out the lights on a very painful and expensive mistake,” says Goldstein.

Harsh words. Still, Job’s instinct that Apple has to take some dramatic steps is on target. In recent years, Apple has succeeded mainly by getting its 25 million-strong customer base to upgrade to pricier machines with higher margins. But only 12 million of them are due for upgrades in the next couple of years, analysts estimate. Meantime, Dell Computer Corp. and Compaq Computer Corp. have been stealing share from Apple in the key education market.


Questions
1. Why is Steve Job’s opening Apple retail stores? How will this help it build competitive advantage? What is Apple’s business-level strategy?
2. Why does Business Week think these stores will have a problem? Now, search the Internet and find out how well these stores are doing today. Was Business Week correct?