

**Strategic Management / International Strategic Management Stage 3****June 2010****Solutions****SECTION A (34 marks)****Question A1**

- (a) Table 1 was constructed to help organise the strategic characteristics outlined for each company discussed in the case study. Constructing such a table helps to identify any important patterns, i.e. similarities or differences between the companies strategies along key competitive variables.

**Table 1: Strategic characteristics identified for each of the key players**

<b>Company (market share)</b>	<b>Strategy</b>	<b>Price</b>	<b>Breath of products</b>	<b>Quality/Styling</b>	<b>Number of stores</b>	<b>Advertising spend  (£ Millions)</b>
Next (11.5)	Broad differentiation	Above average	Extensive	Good/superior	515	5.4
Asda (10.4)	Low cost strategy	Below average	Limited	Good	340	2
Primark (9.7)	Low cost strategy	Below average	Limited	Good	138	0
Tesco (8.7)	Low cost strategy	Below average	Limited	Good	2,306	1.5
M&S (6.4)	Broad differentiation	Average	Limited	Good	668	1.5
Niche (53.3)	Focused differentiation	Premium	Limited	Good/superior	1	0

The patterns discovered in Table 1 for the companies involved are discussed below. Next occupies a distinct and lone position within the industry due to its fashionable, and large and varied range of segmented clothes for children. The company is able to charge higher than average prices due to its successful efforts to target relevant segments of the children's market. Its success at targeting relevant customers has been rewarded with high levels of brand loyalty, which is reflected in its market leading position. Despite the economic recession, Next has maintained industry leadership.

The low cost retailers have been positioned in the same strategic group as they largely display the same key characteristics, i.e. good quality products at low prices. As the market share figures indicate the low cost retailers have prospered over recent years due to their combination of good quality and low prices. This approach has helped to gain this strategic group even further sales success during the economic recession as more consumers have become price-sensitive and seek

value-for-money in these uncertain times.

Marks and Spencer have been positioned in a region of the diagram overlapping success likely and success highly uncertain. Differentiation is important for M&S, but consumers do not perceive major differences in the quality between its products and low cost retailers. M&S was placed half-way between success likely and success uncertain because of the mixed performance of its clothing range. Its non-school is perceived to be uncompetitive with low cost retailers and the outcome of its repositioning exercise is unknown, while the school range has continued to do well. Pricing around the average for its non-school range appears to be overpriced compared to low cost retailers which offer the same quality clothing at lower prices.

Finally, niche retailers have been positioned between the success likely and success uncertain region. Niche retailers are positioned in this overlapping region, because of variations in their performances, i.e. some niche retailers match customers' expectations on price and quality, while other stock less desirable brands, attempt to serve too many segments and therefore struggle to create a clear identity and for that reason suffer poor sales.

Based on the above perceptions the following strategic group map was constructed.

Figure 1: Perceived price/differentiation matrix for the children's clothing retail industry in the United Kingdom

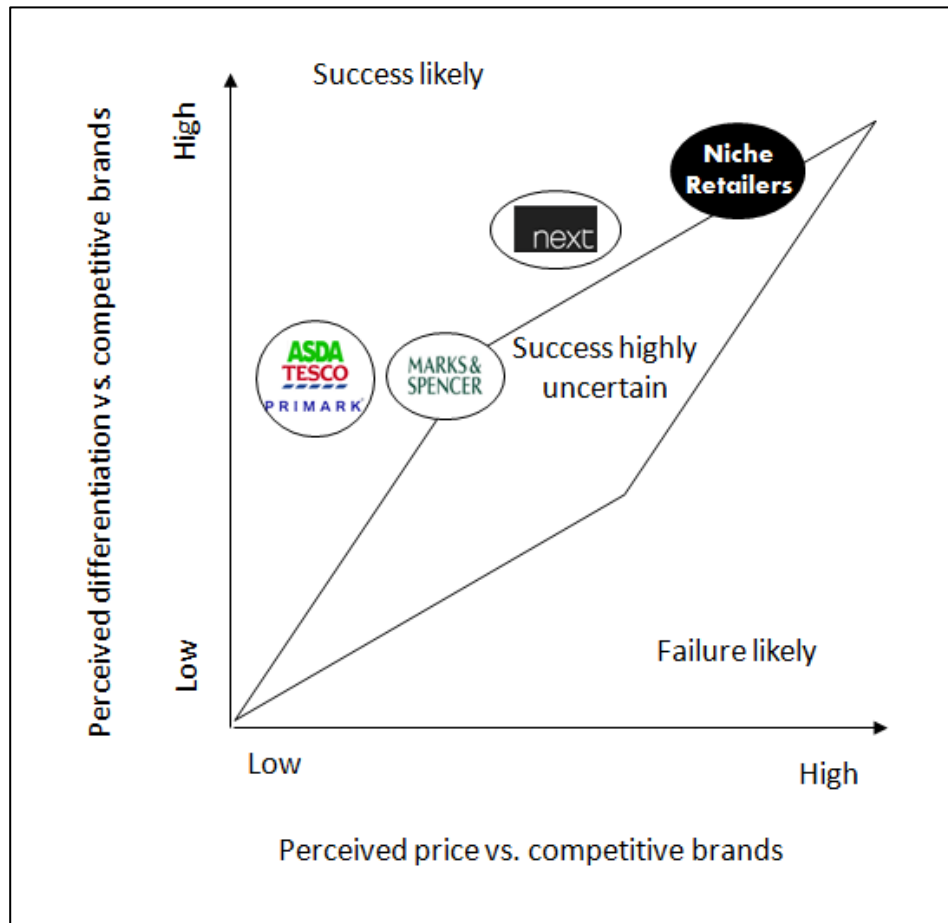
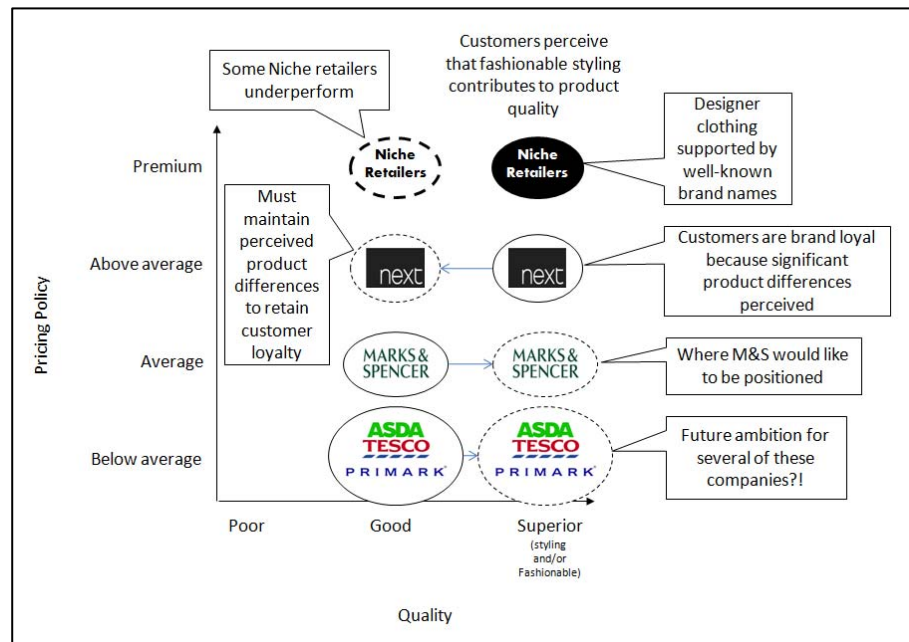


Figure 2: Strategic group map and observations of the children's clothing retail industry in the United Kingdom by pricing policy and perceived quality



The subsequent figures illustrate strategic group maps that reinforce the distinctive positioning Next has crafted in the children's clothing retail industry in the UK. In particular, the maps illustrate that it is not just a few characteristics that determine Next's distinctive position, but a combination of factors skillfully aligned to its strategic purpose.

Figure 3: Strategic group map of the children's clothing retail industry in the United Kingdom by pricing policy and number of stores

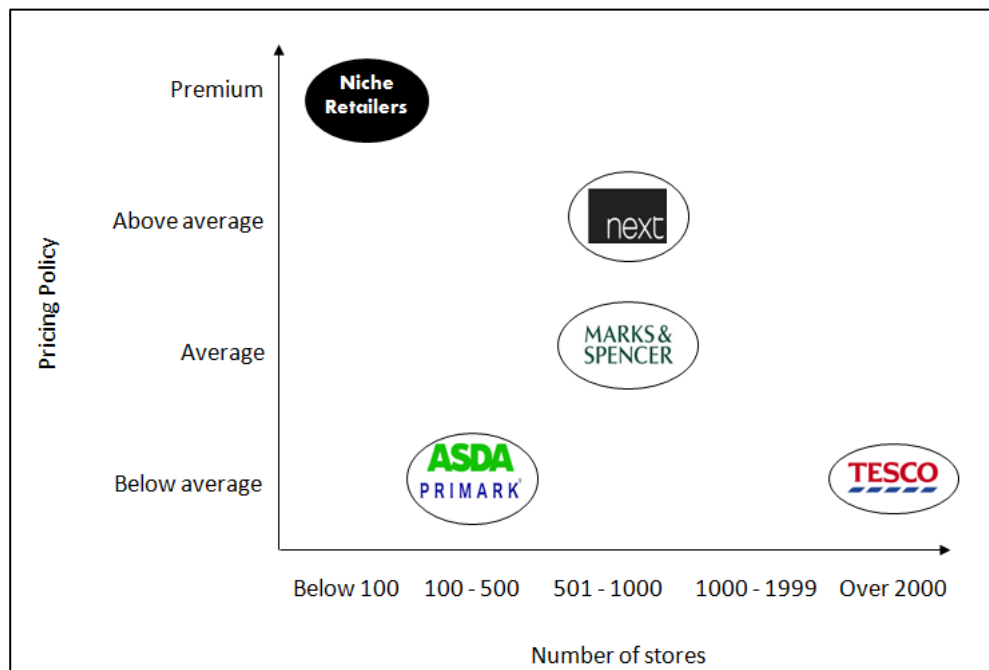


Figure 4: Strategic group map of the children's clothing retail industry in the United Kingdom by pricing policy and advertising spending

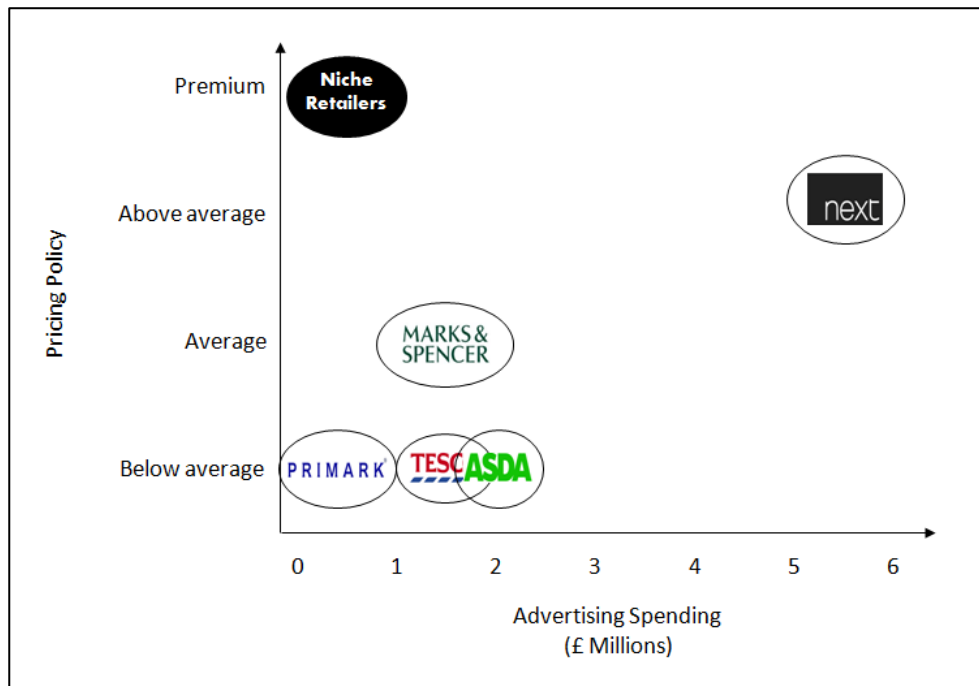


Figure 5: Strategic group map of the children's clothing retail industry in the United Kingdom by pricing policy and breath of range

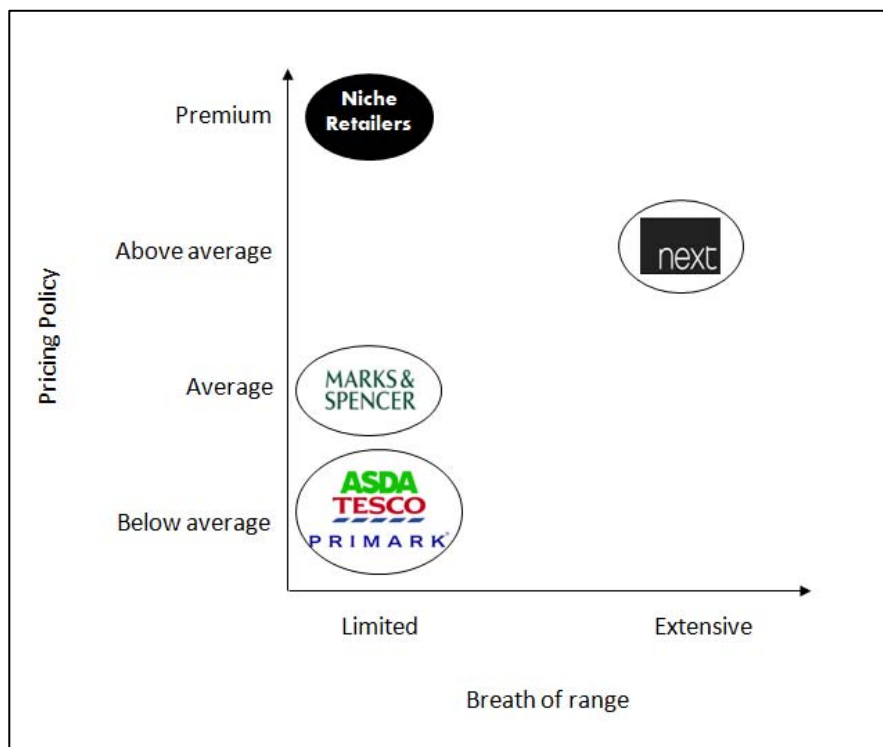
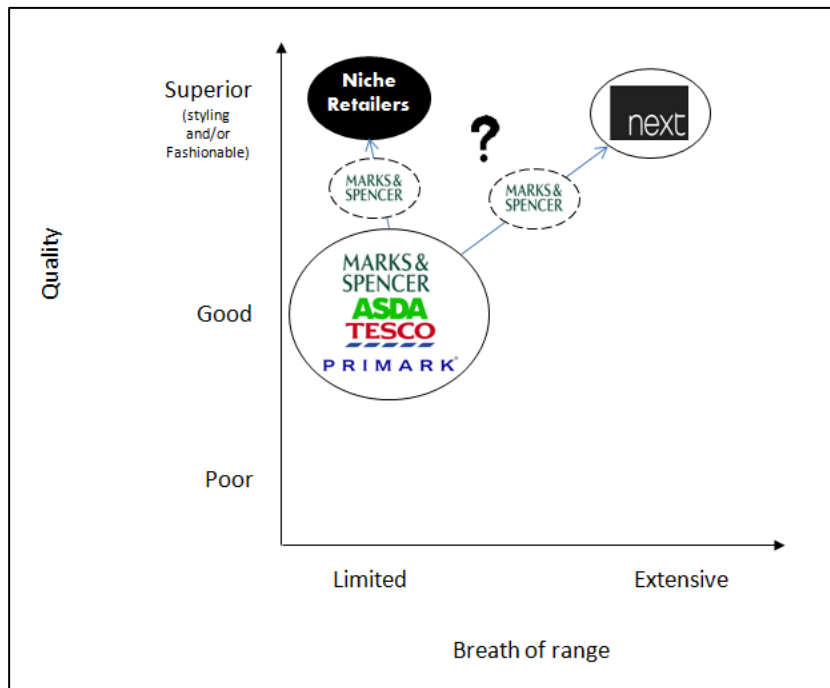


Figure 5: Strategic group map of the children's clothing retail industry in the United Kingdom by perceived quality and breath of range



(b) Next's nearest rival appears to be M&S as they both appeal to mass market customers seeking good quality branded clothes. However, Next's reputation and greater range of stylish clothes for children allows it to charge higher prices than Marks and Spencer. With these issues in mind the following analysis using Porter's five forces was constructed for Next.

- **Industry rivalry: moderate**  
Switching costs are favourably weighted towards M&S (M&S's pricing is around the industry average, Next is slightly higher), but Next holds a dominant position due to its strong branding, and wide range of quality, fashionable clothing styles for children, i.e. customers are willing to pay a price premium for the perceived product differences. However, Next's profitability is competed away through extensive promotions and advertising to maintain its status as a differentiated clothing retailer.
- **Threat of substitutes: high**  
Many other types of retailers compete in the mass-market and specialised niche i.e., Tesco, Primark, Asda and specialised independents for customers discretionary spending. During an economic recession the low cost discounters provide a substantial threat to Next. The existence of substitutes means customers will switch to substitutes in response to price increases i.e., demand is elastic with respect to price.

- Supplier bargaining power: moderate  
Close working relationship with a few key suppliers who can replenish their merchandise rapidly and efficiently. This type of relationship requires “give and take” to cultivate a trusting partnership.
  - Threat of new entrants: low  
Next possesses the advantage of product differentiation and brand loyalty, which makes it difficult for new players to enter this strategic group. The company also possesses industry knowledge which offers an absolute advantage and a network of known distribution outlets. The aforementioned factors mean entry into the mass market would be difficult for new participants but not impossible, especially for cash rich multinational companies such as ASDA and Tesco who originally came from an unrelated industry - groceries.
  - Buyer bargaining power: moderate  
Low switching costs for customers but moderated by perceived product differences and brand loyalty. Nevertheless, over the years, aggressive pricing by the low cost sector has encouraged a quantity of customers to switch loyalty. However, strong branding and product differentiation means some customers are likely to be brand loyal if appeals are aligned to their expectations.
- (c) The evaluation of the competitive conditions confronting Next illustrate that it is operating in a moderately competitive sector of the children's clothing industry. Just one of the five forces was judged to be highly unfavourable to Next's operations; this was the threat of substitutes. Substitutes in the form of cost strategy retailers represent an important challenge for Next in the current environment. Given the economic recession, mass market customers are likely to be more price-sensitive and shop around for cheaper substitutes. Supermarkets are convenient and offer a “one-stop shop”. They also pose the threat of offering wider and higher-priced “premium” clothing that would be in direct competition with Next's clothing range for children. Three out of the other factors contained in Porter's five forces model (i.e. supplier bargaining power, buyer bargaining power and industry rivalry) were judged to have a moderate or neutral impact on Next; this is likely to mean that Next will be able to extract modest profits. However, Next will need to compete much of this modest profitability away to maintain its strong differentiation strategy to defend market share. The only force that was favourable was the threat of new entrances, which was perceived to be low at the moment.

Overall the analysis indicates that the Next's industry sector is to some extent an attractive investment; however, in the future it has the potential to become rapidly unattractive if the economic recession continues and forces more of its existing customer to become increasingly price-sensitive. There is also the danger that supermarkets and discounters begin to enter Next's sector of the industry. While Next and the low cost sector occupy different competitive spaces in the perceived price and differentiation matrix at the moment, aggressive pricing and a growing design and style reputation is building awareness that the differences between the groups are superficial rather than substantive.

## **SECTION B**

### **Question B1**

(a)

The pioneer company establishes the credibility of the product and attempts to build awareness among consumers of its benefits and attributes. In some situations there may be several pioneer companies which target the same market but offer alternative designs of the product technology to customers.

Other competitors may join the pioneer or pioneers during the introduction stage and help in the market's development i.e., build customer awareness of the product technology through their sales and marketing activities. Ease of entry into the market will depend on how difficult the product or service is to produce. A pioneer company may attempt to restrict entry through the use of patent protection. Also the number of competitors attracted to the market will depend on how profitable they perceive the market to be and whether the new product threatens their existing business.

In addition, a characteristic of the introduction stage is a high degree of uncertainty. Amongst customers uncertainty may exist in the introduction stage due to product unfamiliarity and concern over performance. Uncertainties also exist for the producing firm(s), which may be unsure of the most effective marketing strategies to employ. For example, producers will find considerable resistance from retailers to stock products without a history or reputation. A retailer's success relies on effective product selection to maximise the profit potential of limited shelf space. New innovative products that may still have reliability problems are a high-risk choice for retailers. As a result, a producer negotiating retail space for an unproved product will face determined resistance and will need to provide the retailer with promotional pledges and cash discounts to attract an agreement for shelf space.

During introduction stage, marketing activities are typically focused on advertising to build awareness and educate customers about the product. Due to the need for product education producers tend to place a lesser emphasis on promoting their individual brand or company name. Industrial marketers need to reduce the perceived risk for customers and retailers through personal selling that highlights the use and value of the product.

The financial returns for a pioneer company may involve a loss. A company will be prepared to charge a price that does not fully cover total production costs in anticipation that volume will build and all costs, both direct and indirect, will be recovered in the future.

In many cases the pioneering company's finished product will not be completely perfect but will be introduced as early as possible to obtain an advantage over its competitors. The ability to introduce a product early relies on a pioneering company having close co-ordination and co-operation between its production, engineering and marketing functions. A further important requirement for a pioneer company is their willingness to continue to fund the ongoing development of a product so it can be upgraded once it is in the marketplace.

(b)

The challenges of managing a rapidly growing enterprise can be particularly demanding because the essential nature and role of a manager's position changes with growth. With growth the number of employees increases as does the volume and complexity of work required, along with these changes the management of an enterprise must make fundamental changes in their approach. Some of the fundamental impacts of growth on an organisation include:

- (i) an increase in the scope and volume of the enterprises operating activities. For a company to grow it must serve new customers in new markets with new products. To provide this increased level of activity new production facilities and distribution channels are required.
- (ii) the tasks undertaken by the company increasing in their range and complexity. With the expansion of a firm's operating activities, this creates a rapid increase in the number of tasks that need to be defined, organised and managed. With the advent of new products and new geographical markets, issues of production and supply lines need to be organised. In addition, growth will also mean that more customers and competitors will need to be analysed, more prices set, and more products advertised and promoted.
- (iii) increases in the number and variety of people required to work in the organisation. To ensure new people fit within an organisation quickly, procedures for staff selection and training need to be organised and managed. With a greater volume of production, enterprises will attempt to standardise the work they undertake as much as possible so that lower skilled employees can be utilised. Establishing standards of behaviour in the application of company policies is important particularly when employees are spread widely to serve different geographic markets.

The changes that growth brings to companies are usually difficult because they involve more than mere changes in organisational systems and structures. They also demand new attitudes and behaviour from management within an organisation. As an organisation becomes larger the complexity of the organisation becomes beyond any one individual to control. Therefore, the general manager must delegate responsibility to a hierarchy of managers. This pattern of delegation will be determined by the firm's structure.

With the delegation of decision-making responsibility a need is created for formal control systems. Since the general manager is required to delegate more responsibility for the firm's decision-making to more individuals, systems are needed to guide and evaluate the performance of those subordinates who do make decisions. These systems will include methods that establish objectives for all employees, procedures for judging performance against those objectives, and rewards for obtaining desired performance levels. Also senior managers must develop policies and standard procedures to help guide the actions of employees.

(c)

Some companies in a declining industry may become involved in mergers if they are pursuing a leadership strategy option. The leadership strategy option suggests a firm should attempt to dominate an industry. The firm pursuing the leadership position wants to be either the only company or one of the few remaining in the industry. The basis of this strategy is that by dominating the industry a firm is in a much better position to retain a viable level of sales i.e., a strong firm will obtain a more profitable position by forcing out weaker companies and taking possession of their market share.

The acquisition of competitors (horizontal integration) enables a firm to buy market share and obtain economies of scale. For example, discussed in your textbook were the actions of American defence companies, which have been involved in a series of mergers and acquisitions in order to consolidate and rationalise their operations. The rationalisation and consolidation has eliminated excess cost for these American companies, allowing them to compete aggressively on price. In addition, the larger companies are involved in the continuous development of new products such as aircraft or missile defence systems, which require the investment of substantial sums of money. The R&D costs are often prohibitive for smaller firms. As a result, many smaller defence companies are being forced to divest, seek alliances, diversify into other industries or sell their capacity to these larger companies.

(d)

Information provided by the industry life cycle is helpful to confirm the role that an individual business or SBU contributes to the profitability of a firm. A firm will be better off by having a reasonably well-balanced portfolio of businesses. If all businesses in a firm are beginning to age, the firm might enjoy high current profitability, but its future prospects may be low as a result of declining industry sales. In contrast, if a portfolio is biased towards young embryonic businesses, a firm could have great potential, but might be unable to achieve it, because it does not possess sufficient cash for re-investment.

## **SECTION C**

### **Question C1**

Drawing upon the material in Chapter 1 of the provided reading material, answers should consider models such as Simple Stage Theory, International Product Life Cycle Theory, Internalization Theory and The Eclectic Paradigm or OLI model as explanations for business globalization, and illustrate their answer with particular reference to country- and company-specific incentives to globalization, distinguishing between home-country push factors and host-country pull factors. Good answers should offer some critical analysis of the relative merits of the various theories and also provide a range of company/industry examples.

With regard to the choice of structural form for new country market entry, answers should outline the principal contractual, organizational and managerial features of wholly-owned subsidiaries, international strategic alliances and international joint ventures. Good answers in this section should indicate that the choice among these possibilities will depend upon a range of product/market characteristics, and such answers should also include appropriate examples.

### **Question C2**

Drawing upon Chapter 7 of the core reading material provided, candidates should recognise the importance of cultural factors in a number of dimensions of international business management, defining what is meant by culture at the company and country level. Candidates may distinguish these ‘softer’ dimensions of business management from an emphasis purely upon strategy and structure in choosing and implementing an appropriate strategy.

In considering these issues, candidates should have regard to a range of business relationships (partners, customers, host-country government officials, employees etc) and situations (supplier contract negotiations, appointment of local management, liaising with distributors, handling customer complaints) in which culture reveals itself and is important in ensuring business success. These include business protocols such as punctuality and the concept of time, the understanding of business ethics, the role of culture in business negotiations, and the importance of cultural variables in a range of marketing activities, including market research and advertising. Candidates should provide a range of examples – different countries and business situations – to support their analysis.