



## HERIOT-WATT MANAGEMENT PROGRAMME

### STRATEGIC MANAGEMENT – STAGE 3

**June 2009**

*For Official Use Only*

**Surname:** .....

**First Name:** .....

**Registration/Matriculation No:** .....

**Seat No. (if applicable):** .....

**Course:** .....

**Date:** .....

No	Mark
A	
B	
C1	
C2	

**Declaration**

*I certify that I have read the Examination Regulations (see back cover) and understand that I am required to abide by them.*

*Student's Signature:*.....

#### INSTRUCTIONS TO CANDIDATES

1. At the start of the exam ensure that you have written all the details required above.
2. Read the instructions on page 2.
3. Start each question on a new page.
4. Rough workings should be confined to the left hand pages.
5. This book must be handed in entire and unfolded.

**PLEASE READ THE EXAMINATION REGULATIONS ON THE BACK COVER**

### PART I

## EXAMINATION INSTRUCTIONS

The duration of the examination is **3 hours**. The marks value of each section is shown below. You may allocate your time as you see fit.

The paper is in three sections

SECTION A: 34 marks

SECTION B: 33 marks

SECTION C: 33 marks

**Answer ALL sections.**

SECTION A: Answer **ALL PARTS** of Question A1.

SECTION B: Answer **ALL PARTS** of Question B1.

SECTION C: Answer **EITHER** Question C1 **OR** Question C2.

This examination document is in two parts.

**Part I** is the question booklet.

**Part II** is the answer booklet.

Please ensure that **BOTH PARTS** are returned at the end of this examination.

**SECTION A (34 marks)****Answer ALL PARTS of Question A1.****Question A1****Case study of the premium c-segment automotive industry sector in the United Kingdom****Background**

The credit-dependent automotive industry is witnessing an unprecedented sales decline due to the current worldwide economic recession. Certainly most of the main car manufacturers have cut production and jobs at their assembly sites as they respond to falling sales. Like other countries the United Kingdom (UK) has experienced a sharp fall in demand. For example, the number of customers purchasing new vehicles in February 2009 was 54,359, a fall of twenty-two percent from the same time last year. Despite tough economic circumstances there are sectors of the automotive market that are expected to do relatively well or better than others such as the c-segment.

The c-segment is one of the largest sectors in the UK, and Europe in general, and is commonly referred to as the small family car segment. Within the UK this segment accounts for nearly one in three of all cars sold. By and large, the c-segment contains compact saloons and hatchback motor vehicles powered by four cylinder engines with a capacity of between 1.5 and 2.4 litres. The various vehicles produced by European car manufacturers' to compete in this segment include the Ford Focus, Vauxhall Astra, Citroen C4, Peugeot 307, Renault Mégane, and Volkswagen Golf. Japanese and Korean branded examples include Honda Civic, Mazda 3, Subaru Impreza, Toyota Auris, Kia Ceed and Hyundai i30.

**Premium c-segment**

Within the c-segment is a niche sector, which is referred to as the “premium or elite sub-c segment”. The premium c-segment sector was estimated to be worth around £1 billion in 2008. This premium sector of the c-segment is defined by two vehicles, the Audi A3 and BMW 1-series. The Audi A3 and BMW 1-series seek to transfer the high quality attributes of a large luxury vehicle into a much smaller, economical package. A pragmatic consumer would buy a Ford Focus rather than the upmarket and expensive Audi A3 or BMW 1-series, because it offers the same features and more; however, brand-aware consumers with sufficient disposable income are highly likely to buy a Audi or BMW with fewer features because they are enthused and inspired by their image and perceive them as “better” vehicles. This illustrates how Audi and BMW's investment in marketing a strong brand identity and image is paying off; many consumers perceive them as quality



brands and are willing to pay extra, for generally vehicles with fewer features. Thus strong brand recognition and customer loyalty is expected to ensure that sales of Audi A3 and BMW 1-series vehicles remain relatively buoyant despite the recession.

Audi AG is credited with founding and defining this premium sector with the launch of its A3 model in 1996. Since the Audi A3's introduction it has enjoyed increasing popularity amongst UK and European customers and won numerous national and international motoring awards. Consequently the Audi A3 became the envy of other automobile makers by attracting on average a much younger customer profile, strong resale values and high trade-up loyalty (i.e. when owners decide to replace their A3s they are likely to up-grade to a more expensive Audi vehicle). Moreover, the Audi A3 has attracted previously loyal BMW and Mercedes customers, who like the idea of its sporty image, economy and luxury connotations in a small package. When production of A3s began, a single three door hatchback version was produced. Then in 2004, Audi added a five door version, which was called the Sportback and featured improved rear cabin space. This A3 up-date featured a more aesthetically pleasing design, distinctive sporting character, and highly advanced technologies that greatly improved its popularity and appeal amongst customers. The advanced technology added to the up-dated A3 model range included diesel engines that achieved impressive fuel economies and low CO<sub>2</sub> emissions. For example, one of the engines offered in the A3 range is a diesel engine identified as the 1.9 TDIe. This engine obtains an impressive 62.8 miles per gallon. Just over two-thirds of all Audi A3's sold in the UK are powered by diesel engines. Therefore if customers are looking for an economical vehicle, but don't want to compromise on quality, the A3 1.9 TDIe is an attractive option. Another noteworthy engine used in the A3 model range is the 1.4 litre TFSI. This turbocharged petrol engine boasts low CO<sub>2</sub> emissions and fuel consumption, but also provides segment leading performance via its acceleration and top speed.

In response to the success of the Audi A3, the BMW Group launched the 1-series range of vehicles. The BMW 1-Series was first offered to the market in 2004 as a five-door hatchback. During its first full year on the market in 2005, it became one of BMW's



most successful products. Since then BMW has introduced a 3-door sports hatchback and high performance Coupé/Convertible versions. At present it is the smallest and most affordable vehicle (depending on the engine model) in the BMW range. Equipment levels are mediocre on BMW 1-Series base models and rear space/access is restrictive. Audi

A3 and BMW 1-Series vehicles are expensive to purchase and generally cost several thousand pounds more than equivalently powered and equipped c-segment vehicles. In 2007, Audi sold 29,892 A3s in the UK, while BMW sold 23,190 1-series vehicles.

## The Main Rivals



BMW Group is a German-based automobile and motorcycle manufacturing company headquartered in Munich, Bavaria. Currently, the BMW Group is one of the ten largest automotive manufacturers in the world and possesses three of the most famous premium brands in the car industry, i.e. BMW, Mini and Rolls-Royce. In 2008, the BMW Group achieved revenues of €53 billion, which was a five percent fall from the previous year. The Group's net profit was €330 million in 2008, this represented a decline of nearly 90% from 2007. The Company employs over 100,000 people worldwide via its subsidiaries and manufacturing plants and on average sells over one million vehicles per year. The UK is BMW Group's third largest market by sales.



Audi AG is also a German-based company that develops, manufactures and markets motor vehicles under the Audi and Lamborghini brands. Audi is headquartered in Ingolstadt, Bavaria and is a wholly-owned subsidiary of the Volkswagen Group. The company operates through production facilities located in Germany, China, Italy, Hungary and Belgium. Audi's famous corporate catchphrase is *Vorsprung durch Technik*, which means "Advancement through Technology". In 2008 the company sold over a million units, and its profit was around three billion Euros. The unit sales it achieved in 2008 represented its 13th straight yearly increase in a row. Audi provides employment to over fifty thousand people worldwide.

Audi's parent company, Volkswagen Group, is a German-based manufacturer of motor vehicles as well, and is based in Wolfsburg in Lower Saxony. Volkswagen Group is currently the third largest automobile maker in the world, and the largest in Europe. Despite the dramatic deterioration in the business environment, the Volkswagen Group met its unit sales, sales revenue and earnings targets in 2008 and recorded the best financial figures in its history. Industry experts argue that Volkswagen Group's current success is due to the clear positioning of its seven brands (which includes Audi, Bentley, Bugatti, Lamborghini, Skoda and Seat). Moreover, Volkswagen Group makes effective use of synergies gained from close integration amongst its various mass and niche model ranges. Synergies are achieved via joint purchasing, logistics, collaboration on production, common vehicle platforms<sup>1</sup>, components and administrative systems.



The Volkswagen Group and BMW hold diametrically opposed views on the usage of common platforms. This point was affirmed by a former CEO of BMW, Joachim Milberg, when he stated for an interview that: "The marques [brands] and model series within the BMW Group are authentic. They are originals, not just copies based on some kind of 'platform.' Or, to put in other words, the BMW Group sells tailor-made suits and not mass products coming off the platform-rack. . . .The platform strategy applied by mass producers seeks to create several brands out of one and

<sup>1</sup> One of the most commonly adopted synergy strategies in the car industry involves sharing car "platforms" across several models or even brands. A platform principally consists of the chassis and the drive train components (including engine, transmission, and axles) that turn the car's wheels, although sometimes the platform concept is extended to include other key components, such as brake and suspension systems.

the same basic vehicle, simply by making a few cosmetic changes. Clearly there can be no doubt that this may have significant repercussions on the credibility and appeal of a brand. BMW's policy, on the other hand, is to develop and offer our customers unique, distinctive cars with their own independent character and identity. In particular, senior management of BMW hold the view that Volkswagen Group's existing and potential customers will abandon its Volkswagen Golf and Audi model ranges once it becomes common knowledge that ninety percent of their components are identical to the cheaper Skoda Octavia and Volkswagen Passat models, respectively."

### **Supplier relations**

Audi and BMW tend to see their suppliers as close partners and attempt to cultivate reliable, long-term relationships. Both manufacturers involve key suppliers within their interdisciplinary company teams to support research and development, purchasing, production and quality management initiatives. These teams come together to analyse potential



opportunities to reduce costs and improve quality along the entire value chain. According to an annual automotive survey of suppliers, BMW ranks No. 2 in popularity after Toyota. Certainly BMW has been a long time favourite of suppliers because of its commitment to quality over price and its long-term contracts. BMW also tops the list of companies that, in the views of suppliers, provide a good opportunity to make an acceptable return on investment, while Audi was ranked third. Premium car manufacturers like Audi and BMW need to strike a balance between component costs, overall vehicle profitability and quality. Both Audi and BMW consider the relationship they have with their key suppliers to be so important that they have offered those that are struggling, due to the current recession, financial aid so they might survive. For instance, both Audi and BMW pledged to help Edscha, an insolvent supplier. Edscha currently manufactures roofs for the Audi A3 convertible, BMW 3-series and 6-series convertibles as well as door locks for various BMW model lines. Industry experts say that none of Edscha's competitors, such as Webasto or Karmann, can step in as the supplier in the short term. Audi and BMW also plan to help other suppliers in crisis, at least when there is no substitute supplier available.

**Required:**

- (a) Construct a strategic group map or perceived price/differentiation matrix locating the positions of Audi and BMW within the United Kingdom's premium c-segment motor vehicle industry sector. Ensure you provide a rationale for the position you have identified for each company.  
(10 marks)
- (b) Use Porter's Five Forces model to analyse the competitive conditions for Audi within the United Kingdom's premium c-segment motor vehicle industry sector.  
(16 marks)
- (c) Evaluate the attractiveness of the United Kingdom's premium c-segment motor vehicle industry sector based on the five forces analysis undertaken for Question (b).  
(8 marks)

Total 34 marks

**SECTION B (33 marks)****Answer ALL PARTS of Question B1.****Question B1**

- (a) Contrast the different strategies employed by *pioneer* and *follow-the-leader* companies. (10 marks)
- (b) Given the sales figures for widget firms illustrated in Figure 1 evaluate the competitive environment you would expect to encounter in this industry. (6 marks)

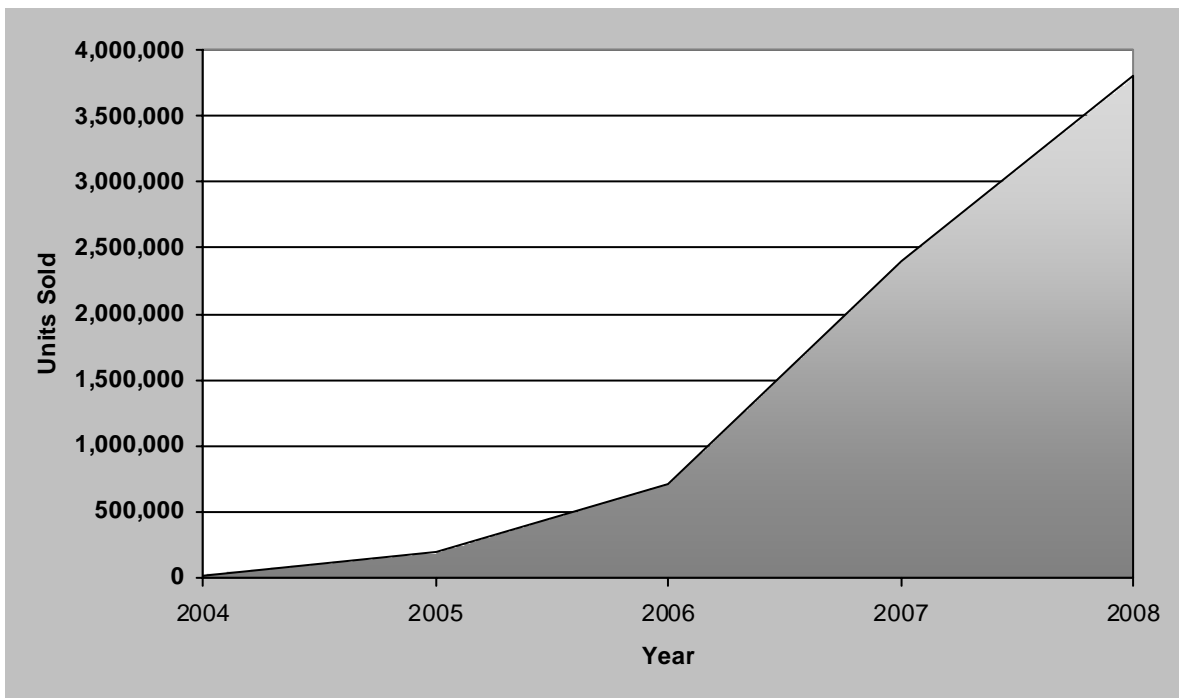


Figure 1: Industry unit sales of widgets from 2004 to 2008

- (c) Why might companies in a declining industry merge? (6 marks)
- (d) Discuss how companies in mature industries might attempt to improve their performance. (11 marks)

Total 33 marks

## **SECTION C (33 marks)**

**Answer EITHER Question C1 OR Question C2.**

### **Question C1**

- (a) Summarise and discuss the main theories that seek to provide an explanation for the internationalisation of business.  
(18 marks)
- (b) Assess the respective merits of wholly-owned subsidiaries, international strategic alliances and international joint ventures as means of achieving global objectives.  
(15 marks)

Total 33 marks

### **Question C2**

- (a) Give examples of ethical issues that international firms may face when operating in an overseas host country.  
(15 marks)
- (b) Explain what can be done to prevent these issues having a negative impact upon business performance abroad.  
(18 marks)

Total 33 marks

**END OF PAPER**

## **EXAMINATION REGULATIONS**

Candidates are subject to the regulations governing examinations which are published by the University. The main points are summarised below.

- 1.** A candidate shall not bring written, printed or any other material into the examination room except such as may be authorised by the examiners. Briefcases and other similar containers, the main purpose of which is to carry papers, shall not be brought into the examination room.
- 2.** A candidate shall not communicate with, receive assistance from or copy from the paper of another candidate during an examination.
- 3.** A candidate shall not leave the examination room less than half an hour after the start of an examination, except with the permission of the invigilator and shall not leave the examination room during the last fifteen minutes of an examination.
- 4.** At the end of the examination a candidate must return the answer book or books to the invigilator together with any other material on which he/she has written or drawn during the examination. Under no circumstances should a candidate remove an answer book, used or unused, from the examination room.