Learning Objectives

1. Identify the ways managers can use functional-level strategy to develop core competences that allow an organization to create value and gives it a competitive advantage

2. Explain how the way managers combine their organization’s distinctive competences can create a successful business-level strategy that allows them to compete for scarce resources
**Learning Objectives (cont.)**

3. Differentiate among the corporate-level strategies companies can use to enter new domains where they can continue to grow and create value.

4. Appreciate the importance of linking strategy to structure and culture at each level to increase the ability to create value.
Learning Objectives (cont.)

5. Understand how global expansion strategies allow an organization to seek new opportunities to exploit its core competences to create value for stakeholders
Organizational strategy: the specific pattern of decisions and actions that managers take to use core competences to achieve a competitive advantage and outperform competitors.

Core competences: the skills and abilities in value creation activities that allow a company to achieve superior efficiency, quality, innovation, or customer responsiveness.
Figure 8.1: The Value-Creation Cycle

1. Ability to obtain scarce resources → allows an organization to create → 2. An organizational strategy

which increases its → and invest resources to develop

3. Core competences → which enable the organization to create → 4. A competitive advantage
Sources of Core Competences

- **Specialized resources**
  - **Functional resources**: the skills possessed by an organization’s functional personnel
  - **Organizational resources**: the attributes that give an organization a competitive advantage such as the skills of the top-management team or possession of valuable and scarce resources
Sources of Core Competences (cont.)

- Coordination ability
  - An organization’s ability to coordinate its functional and organizational resources to create maximal value
  - Effective coordination of resources leads to competitive advantage by means of:
    - Control systems
    - Centralization or decentralization of authority
    - Development and promotion of shared cultural values
Global Expansion and Core Competences

- Transferring core competences abroad
  - Transfer core competence overseas to produce cheaper or improved product
- Establishing a global network
  - Establish value-creation activities in countries where economic, political, and cultural conditions are likely to enhance its low-cost or differentiation advantage
Global Expansion and Core Competences (cont.)

- Gaining access to global resources and skills
  - Different countries have different resources and skills that give them a competitive advantage

- Using global learning to enhance core competences
  - Global activities provide access to knowledge that will allow an organization to improve its core competences
Figure 8.2: The Creation of Value Through Global Expansion

1. Transfer of core competences abroad

2. Establishment of a global network

3. Gaining access to global skills and resources

4. Use of global learning to enhance core competences
Four Levels of Strategy

**Functional-level strategy:** a plan to strengthen an organization’s functional and organizational resources, as well as its coordination abilities, in order to create core competences

**Business-level strategy:** a plan to combine functional core competences to position the organization so that it has a competitive advantage in its domain
Four Levels of Strategy (cont.)

- **Corporate-level strategy:** a plan to use and develop core competences so that the organization not only can protect and enlarge its existing domain but can also expand into new domains.

- **Global expansion strategy:** a plan that involves choosing the best strategy to expand into overseas markets to obtain scarce resources and develop core competences.
Functional-Level Strategy

- The strategic goal of each function is to create a core competence that gives the organization a competitive advantage.

- To gain a competitive advantage, an organization must be able to do at least one of the following:
  - Perform functional activities at a cost lower than that of its rivals, or
  - Perform functional activities in a way that clearly differentiates its goods and services from those of its rivals.
Functional-Level Strategy (cont.)

- Strategies to lower costs or differentiate products
  - The manufacturing function can lower the costs of production by pioneering the adoption of the most efficient production methods
  - The human resource management (HRM) function can lower costs by designing appropriate control and reward systems to increase employee motivation and reduce absenteeism and turnover
Functional-Level Strategy 
(cont.)

Strategies to lower costs or differentiate products (cont.)

- The materials management’s just-in-time inventory systems, computerized warehousing, purchasing managers’ skills in developing long-term links with suppliers and distributors, and fostering of an organization’s reputation can lead to a low-cost or differentiation advantage.
Strategies to lower costs or differentiate products (cont.)

- The skills and expertise of sales and marketing can contribute directly to a low-cost or differentiation advantage
- R&D can reduce costs by developing cheaper ways of making a product
<table>
<thead>
<tr>
<th>Value-Creating Function</th>
<th>Source of Low-Cost Advantage</th>
<th>Source of Differentiation Advantage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Manufacturing</td>
<td>• Development of skills in flexible manufacturing technology</td>
<td>• Increase in product quality and reliability</td>
</tr>
<tr>
<td>Human resource management</td>
<td>• Reduction of turnover and absenteeism</td>
<td>• Hiring of highly skilled personnel</td>
</tr>
<tr>
<td>Materials management</td>
<td>• Use of just-in-time inventory system/computerized warehousing</td>
<td>• Development of innovative training programs</td>
</tr>
<tr>
<td></td>
<td>• Development of long-term relationships with suppliers and customers</td>
<td>• Use of company reputation and long-term relationships with suppliers and customers to provide high-quality inputs and efficient distribution and disposal of outputs</td>
</tr>
<tr>
<td>Sales and marketing</td>
<td>• Increased demand and lower production costs</td>
<td>• Targeting of customer groups</td>
</tr>
<tr>
<td>Research and development</td>
<td>• Improved efficiency of manufacturing technology</td>
<td>• Tailoring products to customers</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• Promoting brand names</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• Creation of new products</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• Improvement of existing products</td>
</tr>
</tbody>
</table>
Functional- Level Strategy (cont.)

- Functional-level strategy and structure
  - The strength of a function’s core competence depends not only on the function’s resources, but on its ability to coordinate the use of its resources.
  - According to contingency theory, each function should develop a structure that suits its human and technical resources.
Figure 8.3: Structural Characteristics Associated with Development of Core Competences in Production, Sales, and R&D
Functional-Level Strategy (cont.)

- Functional-level strategy and culture
  - A competitor can easily imitate an organization’s structure but it is very difficult to imitate their culture
  - The coordination abilities that stem from an organization’s culture emerge gradually and are a product of the property rights system, structure, ethics, and characteristics of its top-management team
Functional-Level Strategy (cont.)

- Functional-level strategy and culture (cont.)
  - The importance of culture for functional-level strategy
    - To gain a competitive advantage, an organization must design its functional structure and culture to provide a setting in which core competences develop
    - If culture is embedded in the day-to-day interactions of functional personnel, it is difficult for a competitor to imitate another organization’s culture
The business-level strategy involves:

- Selecting and managing the domain the organization will compete in
- Positioning the organization so that it can use its resources and abilities to manage its specific and general environments to protect and enlarge that domain
Business-Level Strategy (cont.)

- Strategies to lower costs or differentiate products
  - **Low-cost business-level strategy**: use of skills in low-cost value creation to produce for a customer group that wants low-priced goods and services
  - **Differentiation business-level strategy**: use of skills to differentiate products for customer groups that want and can afford differentiated products that command a high or premium price
Business-Level Strategy (cont.)

- Strategies to lower costs or differentiate products (cont.)
  - **Focus business-level strategy:** specialization in one segment of a market, and focusing all of the organization’s resources on that segment
**Figure 8.4: Types of Business-Level Strategy**

<table>
<thead>
<tr>
<th>Strategy</th>
<th>Many</th>
<th>Few</th>
</tr>
</thead>
<tbody>
<tr>
<td>Low cost</td>
<td>![Marker]</td>
<td></td>
</tr>
<tr>
<td>Focused low cost</td>
<td></td>
<td>![Marker]</td>
</tr>
<tr>
<td>Differentiation</td>
<td>![Marker]</td>
<td></td>
</tr>
<tr>
<td>Focused differentiation</td>
<td></td>
<td>![Marker]</td>
</tr>
</tbody>
</table>
With a differentiation strategy, companies must be able to develop products quickly; therefore close cooperation between functions is required.

A organic structure permits the development of a decentralized, cross-functional team approach to decision making.
A low-cost strategy is associated with the need for close control of functional activities to monitor and lower the costs of production.

A mechanistic structure is often the more appropriate choice.
Business-Level Strategy and Structure (cont.)

Three factors affect an organization’s choice of a structure to create a competitive advantage:

- As an organization produces a wider range of products, it needs greater control over the development, marketing, and production of these products.
- As an organization seeks to find new customer groups for its products, it needs a structure that allows it to serve the needs of its customers.
- As the pace of new product development in an industry increases, an organization will need a structure that increases coordination among its functions.
Figure 8.5: Characteristics of Organizational Structure Associated with Business-Level Differentiation and Low-Cost Strategies

- Matrix structure
- Product team structure
- Product, market, or geographic structure
- Functional structure

### Differentiation Strategy
- Complex structure
- Decentralized decision making
- High differentiation
- High integration
- Organic structure

### Low-Cost Strategy
- Simple structure
- Centralized decision making
- Low differentiation
- Low integration
- Mechanistic structure
Business-Level Strategy and Culture

- Challenge is to develop organization-wide values and specific norms and rules that allow the organization to combine and use its functional resources to the best advantage.
- Organizations pursuing low-cost strategy must develop values of economy and frugality.
- Differentiators must develop values of innovation, quality, excellence, and uniqueness.
Corporate-Level Strategy

- Involves a search for new domains in which to exploit and defend the ability to create value from its core competences

  - **Vertical integration**: a strategy in which an organization takes over and owns its suppliers (backward vertical integration) or its distributors (forward vertical integration)
    - May be more profitable
    - May lead to production cost savings
    - May differentiate its products
    - May avoid opportunistic behavior of suppliers
    - May lead to savings in distribution
Corporate-Level Strategy (cont.)

- **Related diversification**: the entry into a new domain in which it can exploit one or more of its existing competences

- **Unrelated diversification**: the entry into new domains that have nothing in common with its core domain
Figure 8.6: Corporate-Level Strategies for Entering New Domains

<table>
<thead>
<tr>
<th>Input Domains</th>
<th>Core Domain</th>
<th>Related Domains</th>
</tr>
</thead>
<tbody>
<tr>
<td>Backward vertical integration</td>
<td>Related diversification</td>
<td>Unrelated diversification</td>
</tr>
<tr>
<td>Forward vertical integration</td>
<td>Unrelated Domains</td>
<td>Unrelated Domains</td>
</tr>
</tbody>
</table>

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Corporate-Level Strategy and Structure

- For organizations operating in more than one domain, a multidivisional structure is appropriate

- Conglomerate structure and unrelated diversification
  - **Conglomerate structure**: a structure in which each business is placed in a self-contained division and there is no contact between divisions
Figure 8.8: Conglomerate Structure

CEO

Corporate Headquarters Staff

A Division  B Division  C Division  D Division  E Division  F Division  G Division  H Division  I Division
Corporate-Level Strategy and Structure (cont.)

- Related diversification creates value by sharing resources or transferring skills from one division to another.
- Requires lateral communication between divisions as well as vertical communication between divisions and headquarters.
- Integrating roles and teams of functional experts are needed to coordinate skills and resource transfers.
- Multidivisional structures or matrix allow for the coordination needed.
Corporate-Level Strategy and Culture

- Cultural values and the common norms, rules, and goals that reflect those values can greatly facilitate the management of a corporate strategy.

- Organizations need to create cultures that reinforce and build on the strategy they pursue.
Implementing Strategy Across Countries

- Four principal strategies
  - **Multidomestic strategy**: oriented toward local responsiveness by decentralizing control to subsidiaries and divisions in each country
  - **International strategy**: decentralization of all value-creation functions except for R&D and marketing
Four principal strategies (cont.)

- **Global strategy:** oriented toward cost reduction, with all the principal value-creation functions centralized at the lowest-cost global location

- **Transnational strategy:** some functions are centralized, while others are decentralized at the global location best suited to achieving these objectives to achieve both local responsiveness and cost savings
Implementing Strategy Across Countries (cont.)

Choice of structure and control systems for managing a global business is a function of:

- The decision of how to distribute and allocate responsibility and authority between managers at home and abroad so that effective control over a company’s global operations is maintained
Implementing Strategy Across Countries (cont.)

- The selection of the organizational structure that groups divisions both at home and abroad in a way that allows the best use of resources and serves the needs of foreign customers most effectively.

- The selection of the right kinds of integration and control mechanisms and organizational culture to make the overall global structure function effectively.
### Table 8.2: Strategy-Structure Relationships in the International Arena

<table>
<thead>
<tr>
<th>Vertical Differentiation Choices</th>
<th>Multidomestic Strategy</th>
<th>International Strategy</th>
<th>Global Strategy</th>
<th>Transnational Strategy</th>
</tr>
</thead>
<tbody>
<tr>
<td>Levels in the hierarchy</td>
<td>Low</td>
<td>Need for Coordination</td>
<td>Relatively tall</td>
<td>High</td>
</tr>
<tr>
<td>Centralization of authority</td>
<td>Relatively flat</td>
<td>Core competences</td>
<td>Centralized</td>
<td>Relatively flat Simultaneously centralized and decentralized</td>
</tr>
<tr>
<td></td>
<td>Decentralized</td>
<td>decentralized</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Horizontal Differentiation</th>
<th>Global geographic structure</th>
<th>Global product group structure</th>
<th>Global product group structure</th>
<th>Global matrix or “matrix in the mind”</th>
</tr>
</thead>
<tbody>
<tr>
<td>Integration</td>
<td>Low</td>
<td>Medium</td>
<td>Medium</td>
<td>High</td>
</tr>
<tr>
<td>Need for integrating mechanisms</td>
<td>Low</td>
<td>Medium</td>
<td>Medium</td>
<td>High</td>
</tr>
<tr>
<td>such as task forces and integrating roles</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Need for electronic integration</td>
<td>Medium</td>
<td>High</td>
<td>High</td>
<td>Very High</td>
</tr>
<tr>
<td>and management networks</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Need for integration by international organizational culture</td>
<td>Low</td>
<td>Medium</td>
<td>High</td>
<td>Very High</td>
</tr>
</tbody>
</table>

| Bureaucratic Costs              | Low                         | High                           | |

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Implementing a Multidomestic Strategy

- Generally operates with a global geographic structure
  - Duplication of value-creation activities in all countries
  - Authority delegated to each overseas division
  - Managers at global headquarters use market and output controls
Figure 8.9: Global Geographic Structure

- Corporate Headquarters (located in Sweden)
  - Canadian Division
  - United States Division
  - British Division
  - French Division
  - Japanese Division
  - South American Division

Functional activities
Implementing International Strategy

- Companies use a global product group structure and create product group headquarters to coordinate the activities of domestic and foreign divisions
  - Product managers responsible for organizing all aspects of value creation on a global level
  - Managers abroad are in the control of the international division managers
Figure 8.10: Global Product Group Structure

- Corporate Headquarters (located in the United States)
- Worldwide Chemicals Product Group Headquarters
- Worldwide Consumer Goods Product Headquarters
- Worldwide Automotive Product Group Headquarters
- Canadian Division
- British Division
- United States Division
- French Division
- Japanese Division

Legend:
- Grey: Product groups
- Sky blue: Domestic and foreign division
Implementing Global Strategy

- Manufacturing and other value-chain activities placed at the global location that will allow it to increase efficiency and quality
  - Must find ways to reduce bureaucratic costs associated with transfers between corporate headquarters and the global divisions
  - May establish a global product group structure
Implementing Transnational Strategy

- Global matrix structure
  - Lowers global cost structures
  - Differentiates activities through superior innovation and responsiveness to global customers
  - Managers at the regional or country level control local operations
  - Company’s corporate product groups are grouped by world region
  - Decentralizes control to overseas managers
  - Corporate managers exert centralized control to coordinate company’s global activities
Figure 8.11: Global Matrix Structure

- North American Area:
  - Canadian Division
  - Mexican Division
  - United States Division

- European Area:
  - British Division
  - French Division

- Pacific Area:
  - Japanese Division
  - Taiwan Division

- Product groups:
  - Chemicals product group
  - Consumer goods product group
  - Automobile product group

- Individual business division