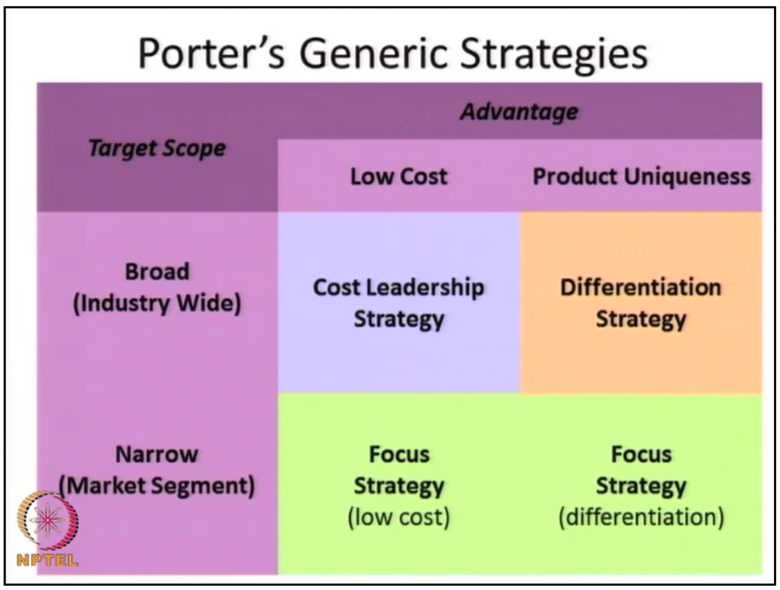
Business Analysis for Engineers
Prof. S. Vaidhyasubramaniam
Adjunct Professor, School of Law
SASTRA University-Thanjavur

Lecture -31
Porter's Generic Strategy

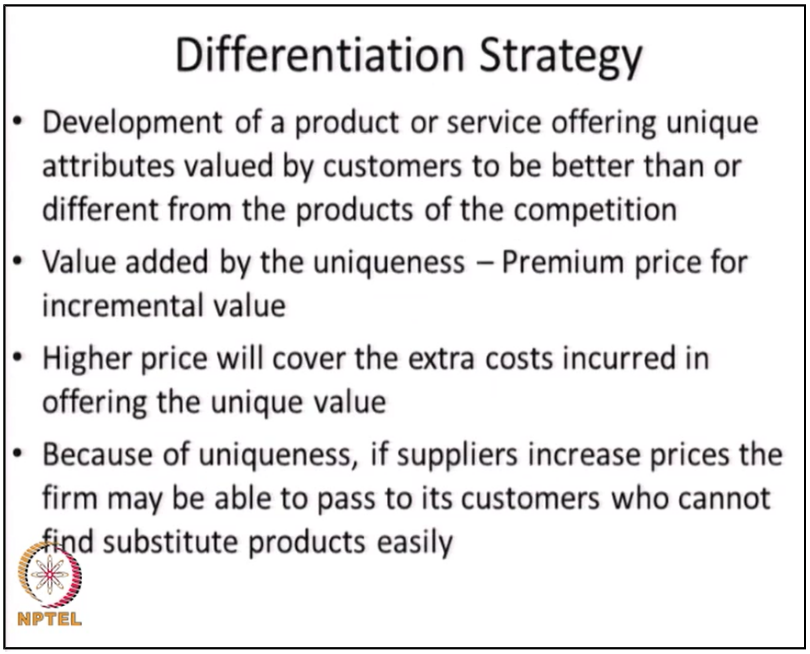
In the previous class we were talking about, various strategic models out of which, the Porter's Generic Strategy, in which firms, organisations, according to Michael Porter, need to take three strategic viewpoints, either to be a cost leader, or capable of differentiating, or remaining very focused.

(Refer Slide Time: 00:37)



And, we saw, what cost leadership was all about. And, the next of Porter's Generic Strategies, is on differentiation. So, if you look at this grid, it is about the uniqueness with which, firms can deliver products or services, over a wide market scope.

(Refer Slide Time: 01:11)



So, in addition to the cost leadership, you can also have firms, that take a conscious decision, of being able to differentiate its products and services, that it offers to its customers. And, that differentiation, is from the ability of the organisation, to offer a set of unique attributes, which not only the organisation considers unique, but those attributes need to be valued by customers, to be better, or completely different from what, competition is offering.

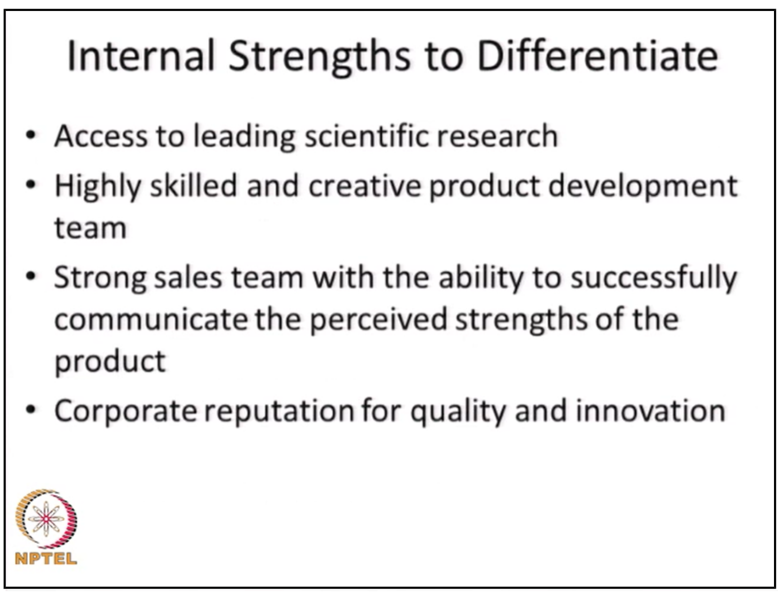
So, the propensity of organisations to develop a product or a service, that is uniquely different from competition, or better than what competition is offered. And, this uniqueness is from the perspective of a customer, is what is key, to a differentiation strategy. as a result of which, the value that is added by the uniqueness, it is because that there is an incremental value addition, that organisations can increase the price. And, that is why, you have a premium price, for an incremental value.

And, if the value is not perceived to be unique by customers, there is no point in just having a premium price. that is why, firms have to be very cautious of the fact that, what they perceive as unique, must be equally perceived, if not more by the customers to be unique. And, if there is a high cost in providing this uniqueness, it is the higher price that the firms are able to command because of this uniqueness, that will take care of these higher costs, that is incurred, in offering this unique value

And, on the other hand, because of the uniqueness, if the suppliers increase prices, then it is relatively easy for firms, to pass this to the customers. Because, it is very difficult to find substitute products, especially when your product or service is delivering, something that is very unique. And, it is a value proposition, that is not easily available from, a substitute product or service.

So, we must understand that, the fundamental to a firm, that decides to choose differentiation as a strategic option, that it has to provide a set of unique attributes, whether it is a product or a service that it is offering. And, this uniqueness must be perceived, to be really value add by the customer. And, the advantage of that, as I said before, it provides the firm, the opportunity to premium price its product. and secondly, the absence of an immediately available substitute, it can easily transfer, increases in prices, to the customers.

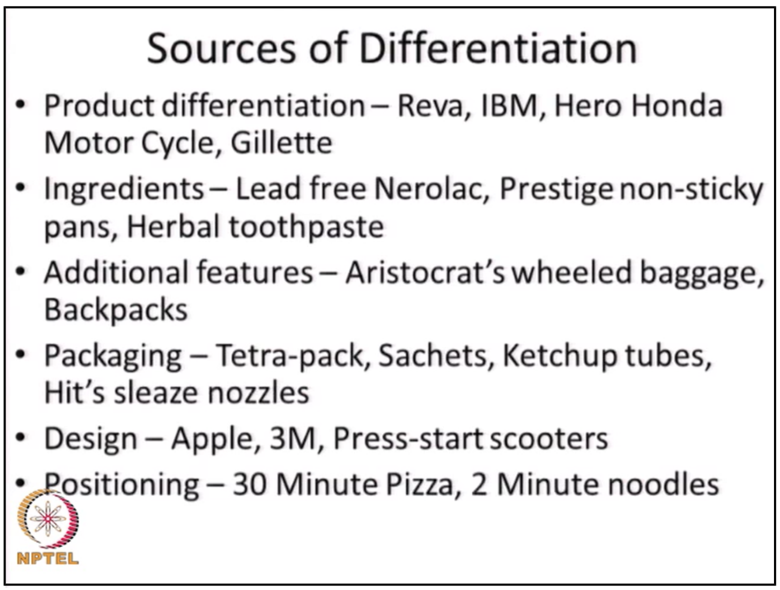
(Refer Slide Time: 04:51)



And, many firms will have different internal resources, that provides the strengths to differentiate. And, these could come from, the presence of scientific research within an organisation, that can provide this value proposition. Or, a very highly skilled and creative product development team, that can come out with a product, with some unique set of features. Or, a skilled team, that can deliver a unique set of services. Or, a very strong sales team, which can forcefully and successfully communicate, the perceived uniqueness of the product or service.

Or, a combination of all of this. and also, a reputation that a firm carry, for its quality and innovation. That, anything from such a firm, is already perceived, to be unique, to be differentiated. So, these are all the various internal combination of factors, that can strengthen the firm's decision to differentiate. the firm's decision to choose differentiation, as its strategic option. And, this differentiation can come in, different forms. to begin with, from the product differentiation itself.

(Refer Slide Time: 06:49)



Examples you could see in this, electric utility vehicle Reva, the product differentiation is clear and telling. Or, IBM's. or, Hero Honda, when it introduces its, first 4-stroke motorcycle. Or, Gillette. So, firms will provide this differentiation, that is clearly visible in the product offering itself. Or, it could also come from, the ingredients that it can use. Examples, could be the lead free, Nerolac paints. as a result of which, the differentiation it says that, the paints are lead free.

And, the resultant health benefits of inhaling the paint smell, does not harm your health. Or, Prestige's non-sticky pans, result of using special types of ingredients, in manufacturing them. or, herbal toothpaste. Or, organic food products. So, these are also, ingredient-based differentiation. Or, I can add more features, to the primary product. Aristocrat's wheeled baggage. it was the one, that started pioneered the concept of having wheels, as part of the baggage.

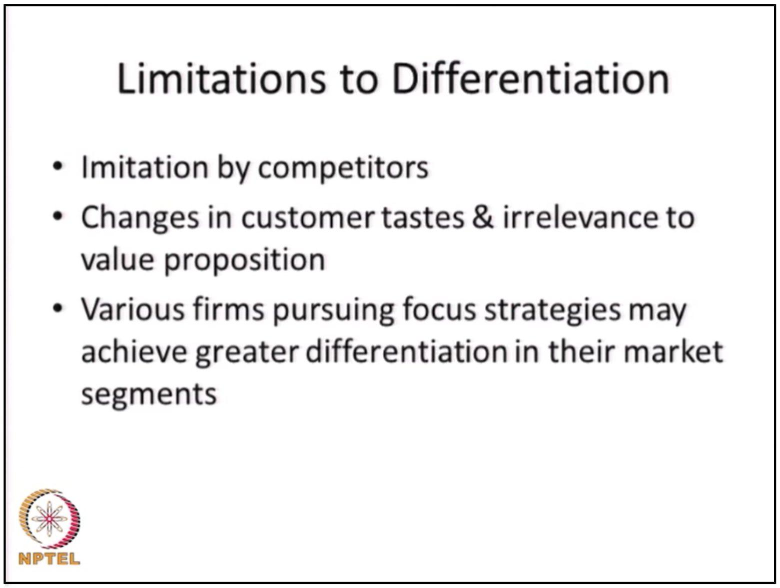
Or today, you see backpacks, with mobile phone holders, with water bottle holders. So, these are all additional features, which are provided to the primary product, as a source of differentiation. Or, differentiation can also come from packaging. And, that you see very much, in the tetra packs, or sachets. Or, today you have ketchup tubes, as against the conventional bottles, in which ketchup come. Or, the cockroach, the HIT's sleaze nozzles, that provides access to places, that are otherwise difficult to reach.

Or, differentiation can also come from, the design capabilities. That, explains why, Apple is very strong. it is able to provide a differentiation, because of its capability to come out with new designs, in its product offerings. Or, 3M. or, the electronic ignition scooters, the press start scooters. because of the design, that comes from the electronic ignition, has made the TVS Scooty, or the Kinetic Honda, very popular.

Or, differentiation from the positioning itself. 30-Minute pizza. Order, you get your pizza in 30 Minutes. Or, your 2 Minute noodles, that was Maggie's differentiation strategy. a noodles, within 2 Minutes. So, positioning is also a very strong source for, differentiation. And, you can add, others as well to this list. But, primarily differentiation can come from product, or the ingredients, it uses.

Or, the capability to add additional features to a product. Or, presenting the product in a unique pat format, packaging. Or, design to provide that differentiation. Or, a simple positioning, that conveys this differentiation. So, these are things, that provides the uniqueness, to the product or a service. just as, it can provide uniqueness, and that is the strength, there are also limitations, for differentiation.

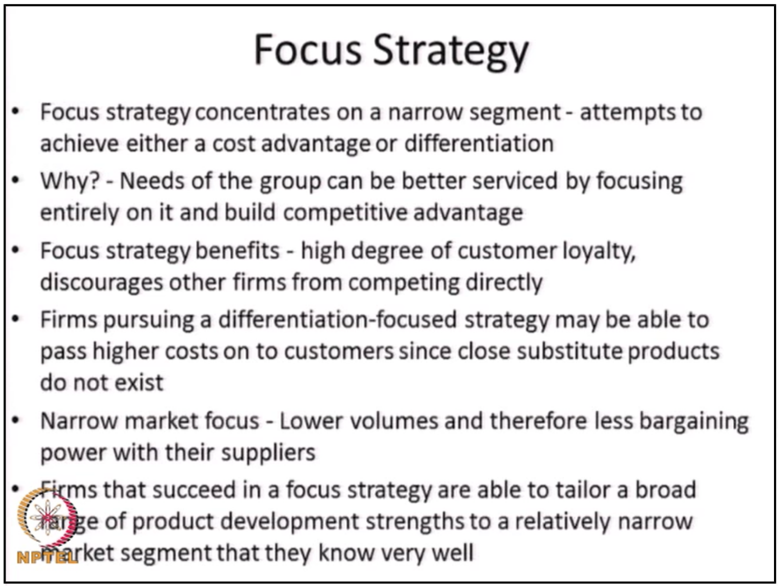
(Refer Slide Time: 10:35)



It can be imitated by competitors. Or, the customers taste will change altogether, making the value proposition, which was so relevant at one point of time, becoming irrelevant at a later point of time. and, also that there might be firms, that pursue focused strategies, which may end up even achieving greater differentiation, in their market segments. about which, I will be talking later. But, there are limitations, to a differentiation strategy. But, the fact is, if firms are able to differentiate the product or service, then it is able to optimally use its resources, just as resources for firms using cost leadership strategy, ensure that, cost is reduced at different parts, in the value chain.

Differentiation strategy ensures that, the resources that are used by the firm, are used in such a way, that it adds value, which is perceived to be unique, by the customers. And, these are all examples, that just drives the point, a simple point, that differentiation can be a very powerful source, for competitive advantage. the third and the last important strategic option, in Porter's Generic Strategies is about, focus.

(Refer Slide Time: 12:31)



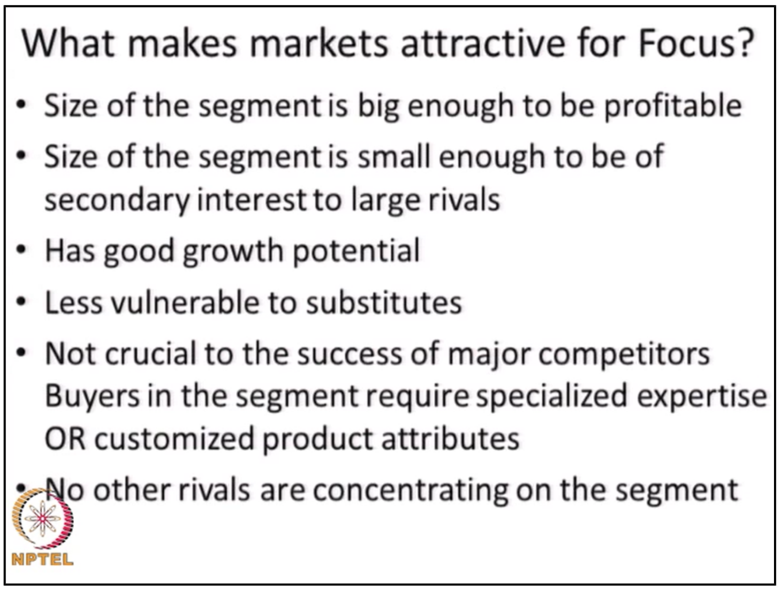
And, the very name focus means that, it has to be narrowed down. which means, we need to concentrate on a narrow segment, from a scope perspective. the target scope cannot be as broad and as wide as, companies embarking on cost leadership, and differentiation have, but necessarily has to be in a narrow segment, because, the reasonable assumption is, it is difficult to remain focused, when the market segment is very broad. And, having chosen to remain focused, you can either achieve, cost competitiveness in the narrow segment, or differentiation in the narrow segment.

Now, why is that there is a need, to remain focused. at times, there will be smaller groups of customers, whose needs can be served better, if the resources of a firm are focused, only towards that narrow group. and, in the process, you can build a competitive advantage. And, if this narrow group of customers, may also be a premium group of customers. which means, you can price your products higher. niche customers. So, what is the benefit, of this focus strategy. you satisfy a niche market. And, since you are satisfying that, either through low cost or differentiation, there is a high degree of customer loyalty.

And, also discourages other firms from competing, directly into this niche market. And, assume that, you are a firm, that has chosen the focus strategy. And, pursue a differentiation focus strategy. So, you have the benefit of differentiation, as well. which means, that you will be able to pass, higher cost to customers. Since, you are in the niche segment, close substitutes do not exist. And, the fact that, you are serving a narrow market, will also have the other effect of having, less bargaining power with the suppliers. Because, the requirement itself is narrow.

But, nevertheless, firms that are able to successfully have a focus strategy in place, will be able to provide a range of product or services, to a relatively narrow market segment, not as broad as cost leadership, or differentiation strategies would have. but then, the biggest advantage is that, they know the niche market, so well. that is, an inherent competitive advantage, which builds a high degree of customer loyalty, which is an inherent entry barrier, that discourages other firms from competing directly, trying to get market share, from this niche narrow market.

(Refer Slide Time: 16:33)



So, what makes, markets attractive for focus strategy. One, since it is narrow, we must ensure that the size of the segment is, big enough to be profitable. So, just because it is small at times, it might even become a loss-making proposition. if it is small, and it is profitable, it makes it attractive because, every firm would be interested in making more profit, with a small market segment. And, the fact that it is small, also makes it of secondary importance to big rivals.

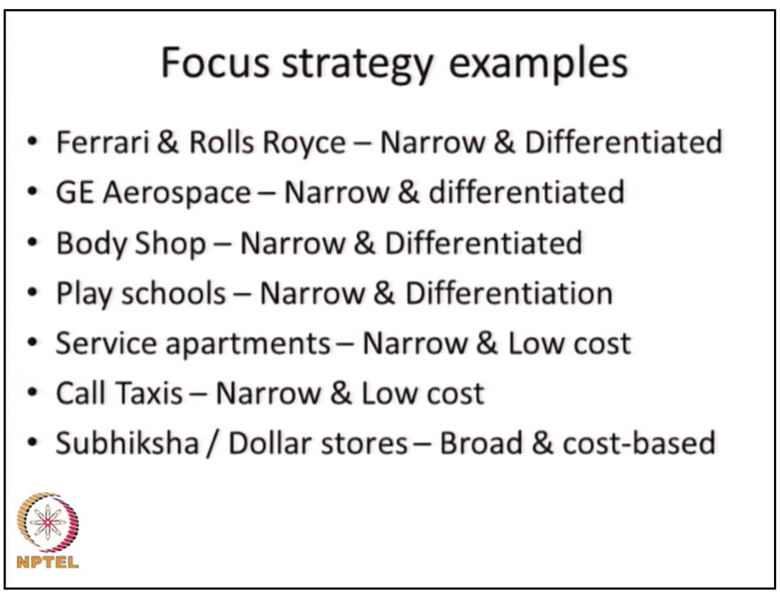
For example, the Southwest airlines example. low cost. the model of operation, is entirely different, point-to-point, small size of segment, that is frequent travelling. And, this makes, this customer, less important to big rivals. for example, you take a British Airways, or a Lufthansa. So, the size of the segment should be small enough, to be of secondary interest to large rivals.

Added, if it has a good growth potential, that that makes focus markets, very attractive.

And, that it is a niche means, that it is less vulnerable to substitutes. And, as I said before, such markets are not crucial, to the success of major competitors. and remember, the buyers of this, they require specialised expertise. Or, at times, each of them needing, customised product attribute. Which, only firms, that have a focus strategy, can deliver. And, it also makes it very attractive. because, there is no other rival, that is concentrating on the segment. Because, this is narrow.

So, it is the propensity of a firm, the capabilities of a firm, to identify a market, that is characterised by all of these, and still is able to have a substantive customer base, big enough to be profitable. And, in the process, build a great degree of customer loyalty, that makes it less vulnerable to competition, as well as substitutes, that makes market attractive, for a focus strategy. And, there are a number of examples, for that.

(Refer Slide Time: 19:42)

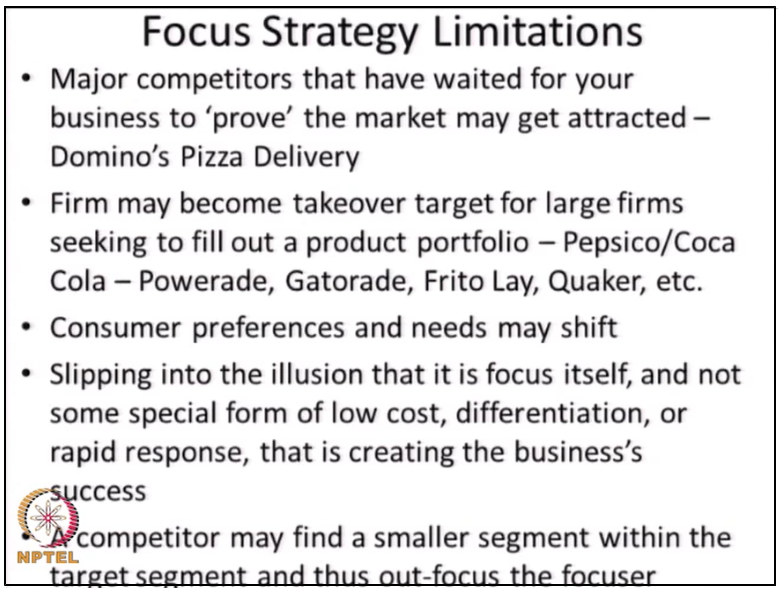


In the auto industry, Ferrari and Rolls Royce, a narrow market, but highly differentiated. GE Aerospace, very narrow, and highly differentiated. Differentiation comes from, the R&D, the technology behind it. Or, body shop, differentiation comes from, the ingredients. Body shop is known for its, natural products. Play schools. Again, very narrow. Differentiation comes from the fact that, it is just meant for those, who need preschool care, day cares. Service apartments.

Again, a very narrow market, low-cost solution.

It is a good bridge between, the five star hotels, or permanent houses. So, this is again, an example of focus strategy, with low-cost option. Call taxi's in airports. Again, a very narrow, catering only to the flying customers, a low-cost solution. Or, the one-dollar store. Till recently, the Subiksha. Here is a slight deviation, but still, I would categorise this as a, focus strategy. It is a broad, and cost base. But, focus especially towards, a different set of customers. There are limitations for focus strategies, as well.

(Refer Slide Time: 21:35)



Some of the competitors would have, this wait and watch syndrome. So, they might just wait and see, whether this focus strategy has proven to be a success. and then, if it is successful, they might get attracted. And, the good example was the, Domino's Pizza delivery. it started the pizza delivery, and build a market focused, towards a set of customers, who would always, would want a pizza to be delivered. And, it was a big success. And, only then, others jumped into this focused market.

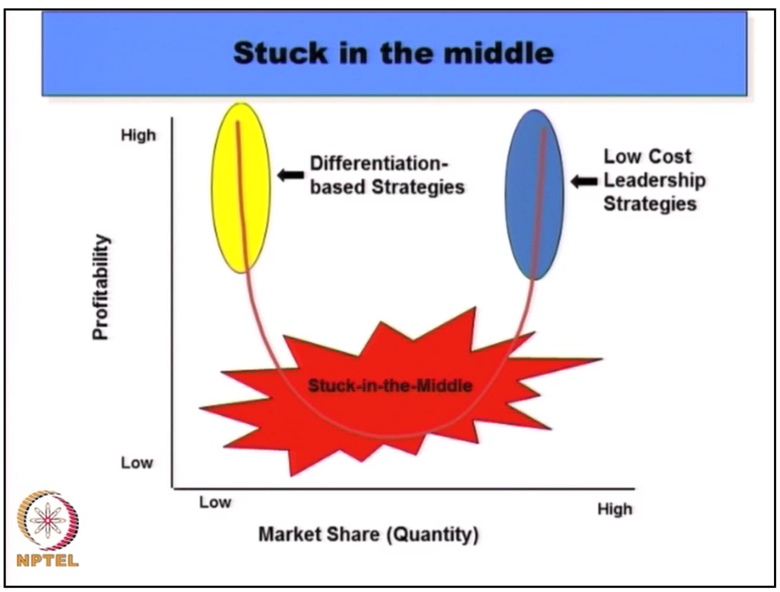
Or, firms may become easy takeover targets, for large firms, who would like to fill a missing product portfolio. Now, very good example for this is, how the cola companies, extended their product line. Coke buying PowerAde. Or, PepsiCo buying Gatorade. PowerAde and Gatorade are popular sports drinks. Or, Frito-Lay, PepsiCo bought this chips. Or, Quaker Oats, again

PepsiCo. Pepsi bought Quaker Oats, extending the product line.

And, the most expected limitation is that, consumer preferences, and needs may shift. they no longer, need to be niche. another internal limitation also comes from, the fact that organisations might slip into this illusion, that it is only this focus strategy, that is creating this competitive advantage. And, at times, they might miss, seeing the bigger picture. Or, fail to realise that, even in this focus, they have some form of low-cost. Or, they are able to differentiate.

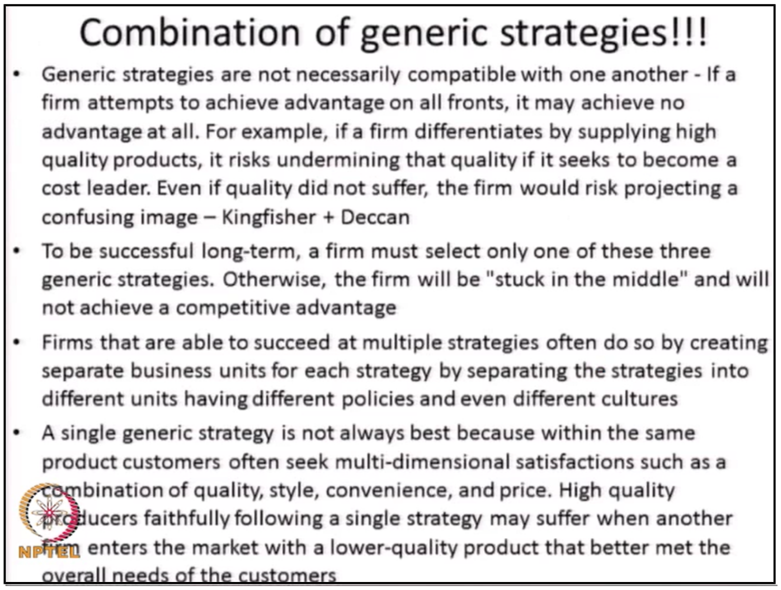
And, that they are not able to leverage this low-cost, or the ability to differentiate, if they fall under this illusion that it is only focus, that is responsible for the success. another limitation is probably a competitor, can still find a smaller segment within the target segment, and out focus the focused firms. it is a possibility. So, these are the limitations of, the focus strategy. So, you find organisations, either to be low-cost leaders, or differentiators, or focused.

(Refer Slide Time: 24:39)



And, organisations, that do not know what they are doing, are stuck in the middle, somewhere.

(Refer Slide Time: 24:56)



It is very difficult, for Generic Strategies, to be compatible within each other, within a given firm. it means that, a firm must not try to have, all of them in place, with a view that it can achieve advantages, on all fronts. that is the biggest mistake, that many firms do. trying to put in place, in bits and pieces, all the three Generic Strategies with the hope, that it will acquire advantages from each of them. believing that, these three are compatible, against each other, with one another.

And, at the end of the day, they realise that, they have not got any advantages, because of this amalgam of these three Generic Strategies. if a firm differentiates by, supplying high-quality products. for example, assume that a firm differentiates, by supplying high-quality products. it might undermine this differentiation, by also trying to become a low-cost provider. I am not saying that, it is very difficult to give, high quality at low cost.

But then, if you choose to differentiate by providing high quality, and also attempt to become low-cost, then you run the risk of losing, the advantages of being both. another disadvantage is, assuming that, your quality did not suffer, the imagery before a customer itself, becomes a little confusing. And, this is what, when competition to Southwest, wanted to become a low-cost, as well as the, conventional airline company, they could not do it.

And, the failure of Kingfisher plus Deccan. Kingfisher's differentiation, came from its service.

Whereas, the Deccan's success, was from its low-cost. And, it was very difficult to seamlessly integrate, a low-cost with a highly differentiated airline, projecting one brand imagery as Kingfisher. And. to be successful, that is why Michael Porter strongly believes that, a firm must select only one of these, three Generic Strategies. Otherwise, they are just stuck in the middle.

And, it is very difficult to achieve, a long-term sustainable competitive advantage, if you do not carefully choose, any one of these three Generic Strategies. Or, it is possible that, if you want to have multiple strategies, we still can do that, by creating separate business units, for each of this strategy. And, each of the business units will have, different units, with their own policy-making, with their own culture, that is very distinctly separate from, another business unit.

This way, they are not business unit stuck in the middle, and giving a confusing imagery, that I explained before. And, I must also give a disclaimer at an end, that a single Generic Strategy is not always best. Because, you might find that, within the same product or service, there is always a set of customers, who have multidimensional expectations, who would want a combination of, convenience, price, style, quality.

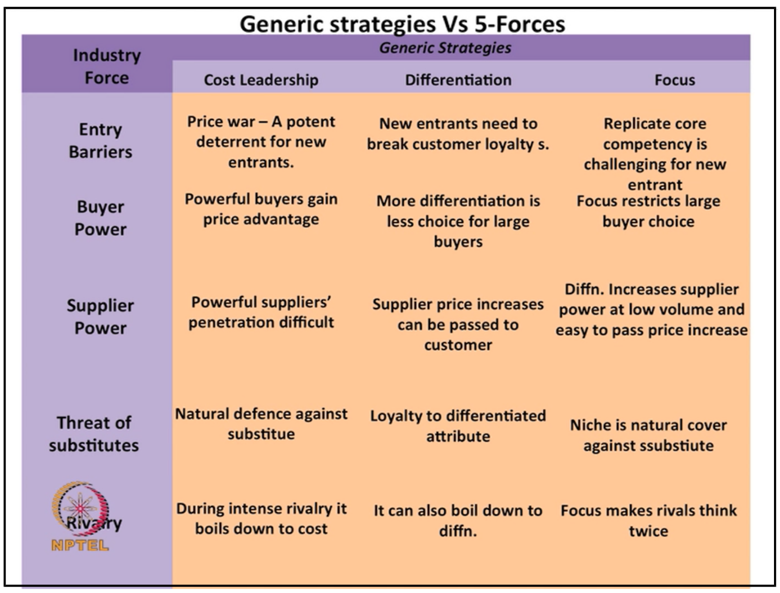
And, this multidimensional expectation, or the satisfaction of a customer, makes a case strong, that it is just not enough, if you have a single strategy in place. Because, let us say, if I am differentiating with high quality. And, I am faithfully following this, differentiation strategy. at one point of time, it may suffer. if there is another firm, that enters the market. which offers lower quality, but then meets the multidimensional expectation of a customer. Then, no longer is my, differentiation strategy unique.

So, a single Generic Strategy, is a good way to start. And, at the same time, organisations must realise, that it is not necessarily the only best way. So, we need to always look out, to improvise on these Generic Strategies, or also choose a different strategic model. the one, that we saw before was, Ansoff. that does not mean that, that is the best. that is one. And, what we saw today was, Porter's Generic Strategies. which, just relies on three corner pieces, cost leadership, differentiation, and focus.

And, that organisations need to carefully choose, which one they need to adopt as a strategic imperative. and then, use the resources within an organisation, to ensure, that they either cost leaders, or they are able to provide a product or a service, in a unique way, or remained focus, attending to a very niche market segment.

But, never a combination of all of this, that only puts an organisation, completely lost in the middle, not knowing, what type of an organisation it is. whether, it is a cost leader, or a differentiator, or focused one. And, it is possible that, these Generic Strategies, if we compare it with the 5-Forces, that also give, some internal strengths viewed from a 5-Forces perspective, that makes the industry also attractive.

(Refer Slide Time: 32:46)



Generic strategies Vs 5-Forces

Industry Force	Generic Strategies		
	Cost Leadership	Differentiation	Focus
Entry Barriers	Price war – A potent deterrent for new entrants.	New entrants need to break customer loyalty s.	Replicate core competency is challenging for new entrant
Buyer Power	Powerful buyers gain price advantage	More differentiation is less choice for large buyers	Focus restricts large buyer choice
Supplier Power	Powerful suppliers' penetration difficult	Supplier price increases can be passed to customer	Diffn. Increases supplier power at low volume and easy to pass price increase
Threat of substitutes	Natural defence against substitue	Loyalty to differentiated attribute	Niche is natural cover against ssubstiute
Rivalry	During intense rivalry it boils down to cost	It can also boil down to diffn.	Focus makes rivals think twice

For example, a cost leadership, provides the ability for the firm to cut-price. And, this deters potential new entrants. So, from an entry barrier perspective, from 5-Forces model, the ability to cut-price, deters potential entrants, if I am a cost leader. if I am a differentiator, customer loyalty can also discourage potential entrants. and similarly, if my strategy is to focus, it develops a set of core competencies, that is acting as an entry barrier. Because, these competencies cannot be, easily delivered by competition.

And, from buyer power, ability to offer low prices, to powerful buyers, because I am a cost leader, provides an inherent strength. if I am a differentiator, large buyers have less power to negotiate, because of very few close alternatives. this again is, good news for the firm. and similarly, if I am focusing. Likewise, large buyers will have less bargaining power, because of the absence of substitute, since I am in this niche segment already. And, cost leadership, insulates the firm from powerful suppliers.

And, if I am a differentiator, I can just pass on price increase, from suppliers to the customers. if I am a focused firm, I might have limitations, because suppliers have more bargaining power, because I am a low volume purchaser. But, if I am a differentiated focused firm, then I will be able to pass on the, any increases in price to the customer. from a threat of substitute point of view, a cost leader can use low price, to defend against substitutes. but again, it is not long-term sustainable.

But, if I am a differentiator, since I am perceiving this product or service, to deliver differentiating attributes, threat from substitute is lowered. And, if I am focused, since I am already concentrating on a niche market segment, specialised products, which requires core competencies, to deliver the product and service, is a natural insolation against, any threat from substitutes. And, as a cost leader, I can take on competition. because, I am able to better price my product, as a cost leader.

As a differentiator, I will fully rely on customer loyalty, to keep customers from rivals. and similarly, as a firm that is very focus, rivals cannot meet a differentiated focused firm. Because, a customer needs of, a focused firm that differentiates, as well as a focused firm that is a cost leader. it is difficult for rivals to, reach those customers. But, that does not mean that, all of the 5-Forces are favourably placed.

It only points to the fact that, at this point of time, for a cost leader, or a differentiator, or a firm, that is focused. a majority of the five factors of the 5-Forces, favour a cost leader, or a differentiator, or a firm that is focused. But, organisations need to be mindful of the fact, that each of them have their limitations, which over a period of time, will also alter the structural attractiveness of the industry, as measured using these 5-Forces.

This snapshot just gives, an initial map fit between each of the 5-Forces, and the firm as a cost leader, differentiator, or a focused firm. So, Generic Strategies, of Michael Porter comprise, three options that are available for organisations. And, they have to choose. And, it is better that they choose, only one of those. Either, be a cost leader, or be a differentiator, or be a focused product or service provider. And, by being any one of these, you would have to make sure that, the resources within the firm, are utilised to achieve, the very purpose of being any one of these.

And, it is extremely difficult, for organisations to choose, more than one of these Generic Strategies, and still remain successful. Because, a combination of two or all the three, has always worked counter-productive, to the strategic objective of an organisation. very rarely, have we seen examples of organisations, being a differentiator, as well as a low-cost provider. it is this clarity, that organisations need to have. that is very important. So, from the strategic options point of view, we saw the Ansoff Product Market Grid, and we saw the Generic Strategies Grid.

There are two other strategic options that are available. which will be, the core competency, as a strategic option. core competency, as developed by, C K Prahalad, and Gary Hammel. And. the fourth, as I said before, is the Blue Ocean Strategy. So, the next class, I will be spending time on, core competency as a strategic tool, and Blue Ocean as a strategic tool. And, before we close this session, I would also encourage you to, just watch a small video with some examples, to understand the thought process, behind Michael Porter's Three Generic Strategies. thank you, very much.