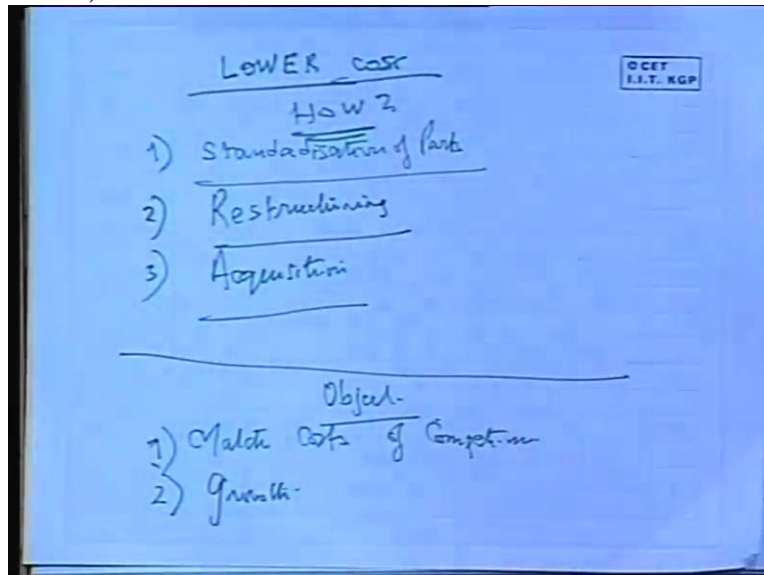


Strategic Management
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Lecture No. 02
Strategy: Philosophy; Competition; Competitive Advantage-I

Right. So, they have a problem of high cost manufacturer with a low cost high value competitor on the horizon. So, then they do some strategizing, and say we have to reduce our cost and then as we discussed a little earlier, there are several ways of reducing cost, all right? What way did they choose? What they will probably do when you when you when you want to strategize, what will you do? You will probably do an ABC analysis? Is it not? Saying that these are our cost drivers, list them out; these are the costs where about eighty percent of our cost is accounted by these items. So let us attack these items first because even a ten percent reduction on this will be a total eight percent reduction of total cost which is significant. They might have done that kind of analysis but we have to do that analysis. After doing the analysis what did they decide? What will reduce the cost? Okay, so one thing they found is their objective is to lower their cost, okay? Lower cost. Then they said how? This is where their strategizing started. How?

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First is, rationalize the design. Does it say so anywhere? Can you read it out? That means what, standardization? Is it not standardization? All right. So, one-standardization of parts. You know, when you design products, this is one thing the design engineer has to bear in mind all the time, whether it is cars or switchgear or anything. You will be, you will be amazed at each designer when he designs, even fasteners you know, nuts, screws, washers, bolts, all right, studs. You have hundreds of such varieties. You choose the part number. In the warehouse you procure it separately look at the enormous cost that is added. Yes?

It seems so because in Europe they were making designs of cars smaller on different platforms, okay and they were selling those cars. In America, they were making cars on different platforms which were bigger and there doesn't seem to be any interaction, any interlinking, between the, the parts which were used, the models that were used, because they were customer oriented with good reason. When they took this decision, this must have been the right decision. With the competitive forces in the market place of that time, they made good profits.

Right. If you, if you see after the world war, what had happened is the automotive industry in Europe and England had been mainly destroyed. So the Americans moved in fast, fast, to fill the gap. Then, when they moved in fast then they thought all right, the best thing to do is let us see what the customer wants here. They don't want the kind of cars we make in America, so, let us give them what they want and the best way to do it is to focus on this customer. So, it was customer focused-for this customer they made products. They were really not concerned with what were the products being made in North America because there the requirement of the customer was different.

So, I do not think there was standardization of parts. That is why Alex Trotman said, one of the ways of reducing the cost significantly is standardize the parts and you save significant amount on cost. Any other questions? I don't think it is short sighted but I want to hear opinions of others and I will justify my thinking also. Do you think it is short sighted? Nityashree, what is your view? Was shortsighted, why? But how many years can you anticipate in advance? I am asking you.

One more. Let us take this to a logical conclusion. For planning, you see, remember one thing. A plan is made against two yardsticks- one is the present status and second, easy predicted status over a period of time. Now, as you know, the more you go into the future the less in, the less perfect is your prediction. So, earlier they used to have five year plan. When we started strategic planning in Larson and Toubro, it was ten-year plan then later on it become five-year and now most companies do a three-year. Look, beyond three years the pace of change has increased, accelerated so much. Beyond three years, they say it is just not relevant because things change totally. So, now you do it with a predicted situation of a market, three year or five years ahead and then you also do it in the present state. Now my submission to you is I don't fault the planing if with the plan adopted there, they made good profits and good money for the next five six seven eight years till the new phenomenon of low cost, high value Japanese car came because it took Japan time to build their auto industry.

It was a master plan, you know. Basically, the war destroyed economies of Japan, middle Europe, Germany also. So, then that was a certain decision taken by America basically and their allies that, you must rebuild them so that they don't become a liability. I mean they have got the expertise on the know-how, give them financial help and rebuild but in the process also, of course, they took over quite a bit of the economy in Europe, you know. Every American business moved in, they acquired plants they set up business there.

Now, I think the test is did they make money with this structure and this division, of European division? If the answer is yes I think it was a good plan to start with but no plan has an indefinite life and the reason is simple because you are embedded in a market, which constantly is in turbulence and turmoil. So, you have to keep watching, keep watching what is happening in the

market. Sometimes we call this environmental scanning and some, some authority say in fact for top management, environmental scanning and planning is the main part of the job, not involving in operations. Yeah? How will you keep it in mind?

Accepting without admitting, for the question, that you should do it. How do you plan? Tell me practically that there will not be a competitor. Say you and I form a company and we are going to make these pens because we have a new process, we have patented it and gives us a terrific cost advantage, all right? So, we estimate our cost will be half of what the existing guys do with the technology, right and we can charge a little lower than the going price which they charge. So, we have big margin to support our profits. How do we plan that there will no competitor coming a year later who has the better who has a better technology than us or some other unique advantage? Can we plan that? How? You tell me.

If we could plan, of course we should take it into account and we will be foolish not to. But how do we do that because it is in constant, everyone is jockeying for an advantage, aren't they? Every player in the field is doing his best to find some competitive advantage. Today we have found it. I think what we decide, you and I, we make this investment, we make this money over the next five years, we make a plan and it is good. Why should we, why should we get bogged down in trying to say, look there may be ten competitors who will come or twenty competitors or no competitors? Why should we do that? Convinced? Not convinced? No? Convinced. Good.

Like what? Well as I said, there is no right or wrong answers here. This is a, this is a classroom debate to bring out points. May be they should have anticipated at that time. Yes, you were saying something. No no. How do you react to this? They say to, he said that they planned for an exit policy when they started. They said we must make such a plant out here. There is, there is a point he is trying to make. Have you understood?

What is the point? Tell me. One moment. No cross talk.

No, people, people do. I can tell you when we setup our factory in Faridabad, L&T Switchgear, we had exactly that because it was fraught with lots of labour problems in those days, you know. I am talking of the, the late seventies, militant labour and so on.

So, our, our strategy which we did is we won't set up manufacturing, we will first set up assembly, okay? We will stage all the parts for the switchgear from Bombay, send it by truck, assemble it, test it and sell it and no heavy infrastructure investment will be done there. So, if we have to exit quickly, just simply close the plant and move out. We cut our losses. So, no testing facilities. Of, of type testing because that will be heavy investments.

I am only, I am only supporting him, I am supporting him as sometimes you do build in an exit policy even when you where you make an investment. You do it.

You look at all the forts, which were built, in the old days. In the Sahayadri, you know, Maharashtra, you have all Shivaji Maharaj forts; all of them had a uh tunnel. It was literally an exit policy when they build the fort that if you had to give up the fort, you know, then you could at least.

He did he did he did. What did he do it for? When you rule, when you rule you collect taxes, my friend, isn't it?

It is all about money and I, I repeat this, that's why we have subjects called economics and political science- they go hand in hand. You do politics, you do economics, they are same coin with two different sides. They are inextricably linked.

So, Japanese did an innovation by people management, basically. Not so much due to technology because even today, remember the technological founder of the world is still America. But what the Japanese did, they took that technology, adapted it, used it to make products which were cheaper and high quality. That was a Japanese miracle. The image they had after the war or basically copies, duplicates and shoddy products, they dramatically changed that in two decades and more drama is because those Pandits [Foreign Language] you know, like Berlitz, Deming who are accepted as gurus and Japanese would touch their feet, they were not accepted in their own country, America. Americans woke up when the Japanese accepted them. They really said that they are the people who have helped our country because we have followed what they told us to do in terms of quality. Yeah. There we are something like the Americans. No prophet they say is accepted in his own country. So, if you do some wonders here, then we don't accept in India. When we go abroad and in abroad you are acclaimed then we always fete you and bring you and so on, give you a dual passport. Okay?

Good question. He has a very generic question. Why should standardization of parts give a significant cost advantage? Any one can answer that? I think, apart from design it is, it is the administrative cost of ordering, warehousing, all right and disposing. It is an inventory carry. Plus, plus, not only stocking but scheduling, planning. Those of us who have been in the scheduling function and the production planning function, you know it is a nightmare to see that the right. Sometimes, we have the whole assembly which is held up because of two types of studs or bolts, because of high tensile strength we have two vendors, both are failed. So, it is a nightmare.

So, standardization saves you cost, not so much design, because once you design, it is sunk cost. Design cost is sunk. But essentially inventory carrying and operational cost, which is opportunity cost, delays of assemblies, sub-assemblies or even the main assembly. I know. So what is Alex Trotman saying now? He is saying let us build platforms, let us build platforms which, a)-gives economies of scale. , I don't want to, you should say all this. He is also trying for economies of scale. Is he not?

Large volumes. He is trying to centralize now. Is it not trying to do that?

Earlier, what was it? What was the organization structure earlier, uh?

So, it was a geographical structure, okay? Geographical structure. And now what are they trying to make it into? It is a product – world-wide but different platforms.

Some of these platforms will be in Europe but not only for European clients. It will be for the other clients also. Similarly, in America. You might be able to say that because if the plan was to get eighty-two models, each for a little segment of the market, you know. If that is so, then you might say and Michael Porter, if you read the whole book, he also says that we should not try to focus on everything because then by definition you are defeating the whole purpose of focus, you see. Focus is something, which are niche. Now, I don't know on what basis they chose it but big companies they proliferate it, you know. There are several reasons for it. See, one standard argument which is put forward by vice presidents and all. You see, we are the big company, we are 'Ford'. So, we must have the entire range of products, you know. We should be

a one stop shop-any one comes in, what do you want? Uh, a small car? Right we have it. You want a big car, we have it. You want a macho car, we have it. It this is a kind of reason, which is given.

Remember, all decisions in industries are not taken based on a rigorous analysis, right and a very informed and deliberate type of decision-making process. We learnt something about group decision-making, did we not? What happens really? You wrote some short notes on groupthink, groupthink? Now you see what is happening? See how everything is tied up, all we try to teach you in this curriculum. What happens typically, you know? When a presentation is made, it is a big important meeting, everyone comes suited and all that. So they have to decide today whether to bring out this new model for the new market. So, lovely presentation everyone made, then the pecking order is there, you know. The big boss is sitting on one side, then next to him you know his son, and the junior guys are sitting, you know, but they are still the expert power, you know. The designer, he actually designs, is sitting there. As often as not these are taken on consideration which is other than analytical considerations.

Many of the decisions, believe me, are taken on empire building basis, empire building because it is human beings who are there. Who knows, the vice president of Europe may have thought that I am not, you know, I am I am I am I am not to be toyed with, you know. I have eighty-two models here, you know. I have so many plants. Do you know that the seniority of executives, okay, in India and elsewhere, even two decades ago before all this crunch and competition came, you know the design of the process was such that in order to get a promotion, when the recommendation went, I think I mentioned this before, they said how many departments report to him.

How many people in the departments? What geographical locations? And people went to ridiculous extents to proliferate departments because if you wanted a promotion later you have to show here more departments no, more people.

How did companies become unproductive? There were some built-in mechanisms, which were stupid, very stupid. Then we tried to propagate saying the heroes are those who have lean and mean departments, you know. So, you cut out all these annexures which you have to give with the recommendations for promotion-how many departments, how many levels, this that. You proliferate levels then. This is called empire building, in management jargon. You build your empires and the empire you build is good for you in that dispensation. It is not good for the company necessarily. So, I am saying this, only to say there is always human elements, which come into decision-making.

Now, in this case, when we were saying, uh, it appears ridiculous on the face of it if you analyze it clinically that for Europe there are eighty two models. I agree. What for? But they had it. Yeah, but it is terribly costly if you are experimenting because you are adding on overheads and costs, no. Imagine the amount of profit that would have come if instead of eighty-two they had forty-two models only. Yeah, you are right. Probably that is how it was justified but at the same time you have to bring in some critical analysis saying, all right, let us do a product audit which big companies do. All right, we have eighty-two, let us see how many units were sold of each of these, okay? And per unit what is the margin because if you have eighty-two models, each will

not have the same margin. The margin will vary also widely because the costs will vary widely. So, having done that, see good companies, they built it into the system. They discontinue products, which are no longer remunerative. And that may be for two or three reasons. , at the time when the product was made there was a good potential and a good business happened. But along the way that business disappeared but the product remained unless someone comes and does an audit. It is like files. Have you seen, when you go, after four years or two years from here, you will have such a lot of paper. None of them I think you will ever need again but you will like to hold it up because once something comes in you don't like to dispense with it.

Okay. Right. The role of a strategy is, is to build up a unique advantage for the company. When I say unique, that means other competitors will not have disadvantage.

Yes, certainly. Of course it involved. It does involve. You cannot do a strategy in vacuum. There is lot of data which you have to get-you have to get data of forecast, you have to get data of as it varies, is it not? You see, let me give an example. You probably know that General Motors, about two decades ago, they made a massive investment in automating their assembly plants. Have you, do you know about this? Huge investments, that came in for lot of criticism also. That investment naturally affected the bottom line for a year or two or more and and the risk you take when you make heavy investment in automation is that, whether the benefits that you project in order to justify the project, comes back or it doesn't come back and the benefits coming back is based on several assumptions, isn't it?

First is the volume itself. If you have highly automated plants, you require big volumes flowing through in order to realize a benefit. You don't have the big volumes flowing through. You are sunk. You have sunk your cost and the benefits are not coming.

So, when they did their process, it was part of their strategy, no? Thinking that cost is going to become a very important factor and at that time, if we have economic of scale we have large volumes and we make this investment at this time then our unit manufacturing cost will give us a real unique advantage and we will be able to grab market share. That was the reasoning. When you set up a plant, all right, or let us put it the other way. When you, when you increase the capacity, say, when you have one plant, okay? And you are making capacity, x. You do a strategizing as, uh, look we are today in number two or number three in our industry, we have so much market share but either we have to be number one or two. Three, four is no good because one day we will be displaced. How to become number one or number two? We want more market share. Do we think that we have the business potential in this industrial market? So you survey that, you analyze. Yes we have. Then what size of plant shall we build? So, say, we will double our capacity. Shall we do it in this location where we all ready or shall we go elsewhere-these are all strategic issues. We say we go elsewhere. Why we go elsewhere? Two things-that here we don't what to put too many eggs in the same basket. God forbade, we have some labour problem, we have some lock out and this one plant will be operating. But then you have a doubt and say how do you know? May be the new plant will join this old plant union.

So, if you have a lock out, it will affect both plants. But anyway we can, then we say all right, there is a benefit-backward region benefit, you know. Most of these states, when they want to have industry in India, they give incentives, you know, deferral of sales tax or waiver of sales tax which throws up more cash flow for you. You know your liquidity position is better. So, we say

we have that. So, initially our cost of manufacture will be lower. Then we say, also we will take new people. We will take trainees and young people whereas in this plant we have average profile of workmen, which is forty-five years or fifty years. They are all highly skilled or skilled workmen.

What Kalyan, you are, these are real life problems, no? When you start new, you take youngsters, you pay them a good salary by industry-cum-region principle but much lower than what we are paying to your people in the mother plant. So with all these considerations you put in fifty crore, you start the plant of hundred crore. And then, what happens? The predictions of the industry, the compounded average rate of growth is going to be fifteen percent or ten percent, which just doesn't fructify. Okay? Various things happen.

America declared war on Iraq, okay? These are important over the business. Okay? The excise and the customs duty, the structure changes. We are joining WTO. We thought that government is not going to reduce the customs duty on these components, you see, but they do it on the finished goods. So we have more competition coming in from outside. So all these things started happening. Net result is you have put in fifty crore, in your project report you've said that the revenues will come in with these sales. So much, so many units will be sold at this price. It doesn't happen.

So, this factory, when you do this division it is a loss, okay. Now, where does the loss show up? On your company's balance sheet, okay. So this division loss is reflected on the bottom line of your company and then what happens? You go to the annual general meeting and shareholders say you made the wrong decision. Where is our dividend, says you, this year we can't give dividend. We have to be prudent and all that, you see.

So, last year we gave you only twenty five percent, this year we give you ten percent and there is [Foreign Language] in the AGM. So, these are the real issues. So, you can plan but in every plan there is a business risk. Our attempt, you know, why we had MBA's in industry? They at least tell us all this, you know. The analytical part, the MBAs at least should be well equipped to do but not only that. You must see the broader issues and broader issues are sometimes very very practical issues and they are all human related issues. So standardization of parts is one. Exit policy has been thrown out, uh, by the way. People didn't accept it. What else?

Restructure. Restructuring. Restructuring.

What else?

Acquisition. Where? What does it say?

Tell me. When do you acquire and when do you, when do you build? Tell me. General principle, do you know? You always have a choice. You can acquire or you can build.

When we don't have time, yes. When we don't have time. It can be on various planes. May be you have a technology, which is obsolete when compared to the another company. So, if you acquire the company it becomes yours otherwise it never becomes yours and it becomes yours at a price, which is acceptable to you. If you have to redo that, you have to make heavy investments-in time, in money and so on. So this is one on technology front. On the marketing front, may be they have a network and distributors, which are very very extensive and large, and by the act of acquisition you immediately acquire that.

May be they have got, you see, under-valued assets. In the sense, they have huge land, you know, which they have got. Like Godrej, when they first set up business in Bombay, massive land they had. Maybe they have that which itself, see a land is carried on your balance sheet at the acquisition price unless it is revalued sometime, but usually not. So, this is a hidden asset, which is lying right there. Acquiring it, you get it. So there are many considerations by which you decide and another thing is to grow fast. Time is very important. So, these are some of the advantages. What are the disadvantages? Tell me.

I don't know. Sometimes if you, if you may get a smart deal you may not pay more than if you have to get to all the advantages on your own after five years of slogging. Uh, but if the company is not going well, the management is poor; you know they are very good companies where just because of poor management they don't do well. Any other reason? What are the problems of acquisition? Immediate, here and now. Cultural integration. Cultural integration is a big problem. So, you have to have good HR guides, you know. MBA's from, you know, Gupta School of Management, to tackle those problems- a) with union b) with your managerial staff and net net you have to do it without demoralizing your own people, you know, the parent company.

No, it depends on what the employees see as a threat or an opportunity. Is it not? That's the key idea. If all the employees in turn felt that it is good for us because our salary scales are low, now we have opportunity, the Birla salary scales are higher so we will fit it in. Number two. We were at dead end because our company was not growing. So middle management will feel, now we have opportunity to get higher promotion if we do well in Birla Company, okay?

On the other hand, if they perceive a threat that the Birla's will feel that we don't want so many people to start with, right, so we are going to have a VRS. Are they going to be happy? No. Say they perceive a threat; the Birlas really want to strip some assets. These are all perceptions. That means, they will sell off this land, they will sell off this number of flats in Malabar hill and so on and there you get a few crores; that is not good for the company. So, I think it all depends on the handling, which the acquiring management does, uh, to build up positive feelings about their company, with the company, which is being acquired. But usually there is always a 'demoralization'. When Standard Chartered acquired Grindlays Bank, I remember, I have some accounts with Grindlays Bank. I used to go and I, I noticed a perceptible change, you know, of all the people in the, in the bank, retail office. So I asked the manager and few others, you know, casually, that what has happened. You know now Stan Chart has taken. How do you think and all? And it all came pouring out. They didn't feel good at all. They felt, you know, that they have been acquired means, they have they have lost their status and their position and so on.

So, all these things happen. So this is one of the costs of acquiring but that doesn't mean to say that you don't acquire because there are many companies who have a strategy of growth simply by acquisition, fast acquisition. There are other companies who don't believe in it. They believe in building their own, okay? Ambanis, for instance. They have not acquired too many companies. The major investments they have done is their own, okay? So, what did they want to achieve finally? What was the objective of this strategy for Ford? One objective is match costs of competitor, at least match if not lower. Right?

Second objective is...

What does it say? Does it state any objective? Did they have it as a growth? Was growth an objective, growth of the company? Market share was there? What does it say?

More responsive to change, that means they look beyond their immediate threat. Entire new market means growth, so growth was definitely. When you want to grow, as we just discussed, we have two routes-we have the acquisition route which is faster etcetera etcetera and you can set up plants also there, isn't it? So, growth was one and what was just said, just, they wanted to be nimble. That means they wanted to position themselves in such a way, have an attitude change where in the next phase, let us say five years hence, they could change fast, you know and respond fast to any other major threats or opportunity which came into the market. That was another objective they had.

So, I am calling it style. Style is a product of culture. Style of operation and if you want to change the style you have to change the culture and there are many ways of changing the culture. You can do it by OD-organizational development-that is people-oriented interventions. You do it by restructuring, okay? That is, systemic changes. You can also do it by personnel changes-take out the old guard, bring in young people, dynamic people or old people who are very dynamic. Take out young people who are not so dynamic, okay? We always associate old with non-dynamism and young with dynamism, right?

It is a fallacy. It is not true all the time. Okay. Any other questions? Otherwise we will wind down this session. So anyone would like to summarize the learning points here?

Why did you set...

Come on. Who has not spoken today? Who has not spoken?

Who has not spoken today? Yeah. What is a learning point?

Remember, the thing here is we had a little bit of a strategy followed by implementation. So, it is about implementation. What are the points you have learned on how to implement a strategy?

Okay. Good. Anyone wants to add anything? No? So, for the next class, next week you will have a do a little reading of Michael Porter-competitive strategy, right? That is important to know the analysis, how do you analyze. Do you have any textbooks in the library? You don't have? The books, which we have given as learning material, these books are not there? Okay we will get some. I will tell, , Professor Dey to buy two copies of at least Michael Porter's book and the book from which, , Professor Dey is teaching, all right? Right then. Thank you very much. Have a nice day.