

Crafting & Executing **STRATEGY**

THE QUEST FOR COMPETITIVE ADVANTAGE

Concepts and Cases

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Crafting and Executing Strategy

THE QUEST FOR COMPETITIVE ADVANTAGE

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Crafting and Executing Strategy

THE QUEST FOR COMPETITIVE ADVANTAGE

Concepts and Cases | TWENTIETH EDITION



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CRAFTING AND EXECUTING STRATEGY: THE QUEST FOR COMPETITIVE ADVANTAGE,
CONCEPTS AND CASES, TWENTIETH EDITION

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To our families and especially our spouses:
Hasseline, Paul, and Kitty.



ABOUT THE AUTHORS



Arthur A. Thompson, Jr., earned his B.S. and Ph.D. degrees in economics from The University of Tennessee, spent three years on the economics faculty at Virginia Tech, and served on the faculty of The University of Alabama's College of Commerce and Business Administration for 24 years. In 1974 and again in 1982, Dr. Thompson spent semester-long sabbaticals as a visiting scholar at the Harvard Business School.

His areas of specialization are business strategy, competition and market analysis, and the economics of business enterprises. In addition to publishing over 30 articles in some 25 different professional and trade publications, he has authored or co-authored five textbooks and six computer-based simulation exercises. His textbooks and strategy simulations have been used at well over 1,000 college and university campuses worldwide.

Dr. Thompson spends much of his off-campus time giving presentations, putting on management development programs, working with companies, and helping operate a business simulation enterprise in which he is a major partner.

Dr. Thompson and his wife of 53 years have two daughters, two grandchildren, and a Yorkshire Terrier.



Margaret A. Peteraf is the Leon E. Williams Professor of Management at the Tuck School of Business at Dartmouth College. She is an internationally recognized scholar of strategic management, with a long list of publications in top management journals. She has earned myriad honors and prizes for her contributions, including the 1999 Strategic Management Society Best Paper Award recognizing the deep influence of her work on the field of Strategic Management. Professor Peteraf is a fellow of the Strategic Management Society and the Academy of Management. She served previously as a member of the Board of Governors of both the Society and the Academy of Management and as Chair of the Business Policy and Strategy Division of the Academy. She has also served in various editorial roles and on numerous editorial boards, including the *Strategic Management Journal*, the *Academy of Management Review*, and *Organization Science*. She has taught in Executive Education programs in various programs around the world and has won teaching awards at the MBA and Executive level.

Professor Peteraf earned her Ph.D., M.A., and M.Phil. at Yale University and held previous faculty appointments at Northwestern University's Kellogg Graduate School of Management and at the University of Minnesota's Carlson School of Management.

John E. Gamble is a Professor of Management and Dean of the College of Business at Texas A&M University–Corpus Christi. His teaching and research for nearly 20 years has focused on strategic management at the undergraduate and graduate levels. He has conducted courses in strategic management in Germany since 2001, which have been sponsored by the University of Applied Sciences in Worms.

Dr. Gamble’s research has been published in various scholarly journals and he is the author or co-author of more than 75 case studies published in an assortment of strategic management and strategic marketing texts. He has done consulting on industry and market analysis for clients in a diverse mix of industries.

Professor Gamble received his Ph.D., Master of Arts, and Bachelor of Science degrees from The University of Alabama and was a faculty member in the Mitchell College of Business at the University of South Alabama before his appointment to the faculty at Texas A&M University–Corpus Christi.



Dr. A. J. (Lonnie) Strickland is the Thomas R. Miller Professor of Strategic Management at the Culverhouse School of Business at The University of Alabama. He is a native of north Georgia, and attended the University of Georgia, where he received a Bachelor of Science degree in math and physics; Georgia Institute of Technology, where he received a Master of Science in industrial management; and Georgia State University, where he received his Ph.D. in business administration.

Lonnie’s experience in consulting and executive development is in the strategic management arena, with a concentration in industry and competitive analysis. He has developed strategic planning systems for numerous firms all over the world. He served as Director of Marketing and Strategy at BellSouth, has taken two companies to the New York Stock Exchange, is one of the founders and directors of American Equity Investment Life Holding (AEL), and serves on numerous boards of directors. He is a very popular speaker in the area of strategic management.

Lonnie and his wife, Kitty, have been married for 48 years. They have two children and two grandchildren. Each summer, Lonnie and his wife live on their private game reserve in South Africa where they enjoy taking their friends on safaris.






By offering the most engaging, clearly articulated, and conceptually sound text on strategic management, *Crafting and Executing Strategy* has been able to maintain its position as the leading textbook in strategic management for 30 years. With this latest edition, we build on this strong foundation, maintaining the attributes of the book that have long made it the most teachable text on the market, while updating the content, sharpening its presentation, and providing enlightening new illustrations and examples.

The distinguishing mark of the 20th edition is its enriched and enlivened presentation of the material in each of the 12 chapters, providing an as up-to-date and engrossing discussion of the core concepts and analytical tools as you will find anywhere. As with each of our new editions, there is an accompanying lineup of exciting new cases that bring the content to life and are sure to provoke interesting classroom discussions, deepening students' understanding of the material in the process.

While this 20th edition retains the 12-chapter structure of the prior edition, every chapter—indeed every paragraph and every line—has been reexamined, refined, and refreshed. New content has been added to keep the material in line with the latest developments in the theory and practice of strategic management. In other areas, coverage has been trimmed to keep the book at a more manageable size. Scores of new examples have been added, along with 15 new Illustration Capsules, to enrich understanding of the content and to provide students with a ringside view of strategy in action. The result is a text that cuts straight to the chase in terms of what students really need to know and gives instructors a leg up on teaching that material effectively. It remains, as always, solidly mainstream and balanced, mirroring *both* the penetrating insight of academic thought and the pragmatism of real-world strategic management.

A standout feature of this text has always been the tight linkage between the content of the chapters and the cases. The lineup of cases that accompany the 20th edition is outstanding in this respect—a truly appealing mix of strategically relevant and thoughtfully crafted cases, certain to engage students and sharpen their skills in applying the concepts and tools of strategic analysis. Many involve high-profile companies that the students will immediately recognize and relate to; all are framed around key strategic issues and serve to add depth and context to the topical content of the chapters. We are confident you will be impressed with how well these cases work in the classroom and the amount of student interest they will spark.

For some years now, growing numbers of strategy instructors at business schools worldwide have been transitioning from a purely text-case course structure to a more robust and energizing text-case-simulation course structure. Incorporating a competition-based strategy simulation has the strong appeal of providing class members with *an immediate and engaging opportunity to apply the concepts and analytical tools covered in the chapters and to become personally involved in crafting and executing a strategy for a virtual company that they have been assigned to manage and that competes head-to-head with companies run by other class members*. Two widely used and pedagogically effective online strategy simulations, *The Business Strategy Game* and *GLO-BUS*, are optional companions for this text. Both simulations were created by Arthur Thompson, one of the text authors, and, like the cases, are closely linked to the content of each chapter in the text. The Exercises for Simulation Participants, found at the end of each chapter, provide clear guidance to class members in



applying the concepts and analytical tools covered in the chapters to the issues and decisions that they have to wrestle with in managing their simulation company.

To assist instructors in assessing student achievement of program learning objectives, in line with AACSB requirements, the 20th edition includes a set of Assurance of Learning Exercises at the end of each chapter that link to the specific learning objectives appearing at the beginning of each chapter and highlighted throughout the text. An important instructional feature of the 20th edition is its more closely *integrated* linkage of selected chapter-end Assurance of Learning Exercises and cases to the publisher’s web-based assignment and assessment platform called Connect™. Your students will be able to use the online Connect™ supplement to (1) complete two of the Assurance of Learning Exercises appearing at the end of each of the 12 chapters, (2) complete chapter-end quizzes, and (3) enter their answers to a select number of the suggested assignment questions for 7 of the 31 cases in this edition. Many of the Connect™ exercises are automatically graded, thereby enabling you to easily assess the learning that has occurred.

In addition, both of the companion strategy simulations have a built-in Learning Assurance Report that quantifies how well each member of your class performed on nine skills/learning measures *versus tens of thousands of other students worldwide* who completed the simulation in the past 12 months. We believe the chapter-end Assurance of Learning Exercises, the all-new online and automatically graded Connect™ exercises, and the Learning Assurance Report generated at the conclusion of *The Business Strategy Game* and *GLO-BUS* simulations provide you with easy-to-use, empirical measures of student learning in your course. All can be used in conjunction with other instructor-developed or school-developed scoring rubrics and assessment tools to comprehensively evaluate course or program learning outcomes and measure compliance with AACSB accreditation standards.

Taken together, the various components of the 20th-edition package and the supporting set of instructor resources provide you with enormous course design flexibility and a powerful kit of teaching/learning tools. We’ve done our very best to ensure that the elements constituting the 20th edition will work well for you in the classroom, help you economize on the time needed to be well prepared for each class, and cause students to conclude that your course is one of the very best they have ever taken—from the standpoint of both enjoyment and learning.

DIFFERENTIATING FEATURES OF THE 20TH EDITION

Six standout features strongly differentiate this text and the accompanying instructional package from others in the field:

1. *Our integrated coverage of the two most popular perspectives on strategic management—positioning theory and resource-based theory—is unsurpassed by any other leading strategy text.* Principles and concepts from both the positioning perspective and the resource-based perspective are prominently and comprehensively integrated into our coverage of crafting both single-business and multibusiness strategies. By highlighting the relationship between a firm’s resources and

capabilities to the activities it conducts along its value chain, we show explicitly how these two perspectives relate to one another. Moreover, in Chapters 3 through 8 it is emphasized repeatedly that a company's strategy must be matched *not only* to its external market circumstances *but also* to its internal resources and competitive capabilities.

2. *Our coverage of cooperative strategies and the role that interorganizational activity can play in the pursuit of competitive advantage, is similarly distinguished.* The topics of the value net (newly added), strategic alliances, licensing, joint ventures, and other types of collaborative relationships are featured prominently in a number of chapters and are integrated into other material throughout the text. We show how strategies of this nature can contribute to the success of single-business companies as well as multibusiness enterprises, whether with respect to firms operating in domestic markets or those operating in the international realm.
3. *With a stand-alone chapter devoted to this topic, our coverage of business ethics, corporate social responsibility, and environmental sustainability goes well beyond that offered by any other leading strategy text.* Chapter 9, "Ethics, Corporate Social Responsibility, Environmental Sustainability, and Strategy," fulfills the important functions of (1) alerting students to the role and importance of ethical and socially responsible decision making and (2) addressing the accreditation requirement of the AACSB International that business ethics be visibly and thoroughly embedded in the core curriculum. Moreover, discussions of the roles of values and ethics are integrated into portions of other chapters to further reinforce why and how considerations relating to ethics, values, social responsibility, and sustainability should figure prominently into the managerial task of crafting and executing company strategies.
4. *Long known as an important differentiator of this text, the case collection in the 20th edition is truly unrivaled* from the standpoints of student appeal, teachability, and suitability for drilling students in the use of the concepts and analytical treatments in Chapters 1 through 12. The 31 cases included in this edition are the very latest, the best, and the most on target that we could find. The ample information about the cases in the Instructor's Manual makes it effortless to select a set of cases each term that will capture the interest of students from start to finish.
5. *The text is now more tightly linked to the publisher's trailblazing web-based assignment and assessment platform called Connect™.* This will enable professors to gauge class members' prowess in accurately completing (a) selected chapter-end exercises, (b) chapter-end quizzes, and (c) the creative author-developed exercises for seven of the cases in this edition.
6. *Two cutting-edge and widely used strategy simulations—The Business Strategy Game and GLO-BUS—are optional companions to the 20th edition.* These give you an unmatched capability to employ a text-case-simulation model of course delivery.

ORGANIZATION, CONTENT, AND FEATURES OF THE 20TH-EDITION TEXT CHAPTERS

- Chapter 1 serves as a brief, general introduction to the topic of strategy, focusing on the central questions of "What is strategy?" and "Why is it important?" As such, it serves as the perfect accompaniment for your opening-day lecture on what

the course is all about and why it matters. Using the newly added example of Starbucks to drive home the concepts in this chapter, we introduce students to what we mean by “competitive advantage” and the key features of business-level strategy. Describing strategy making as a process, we explain why a company’s strategy is partly planned and partly reactive and why a strategy tends to co-evolve with its environment over time. We show that a viable business model must provide both an attractive value proposition for the company’s customers and a formula for making profits for the company. New to this chapter is a depiction of how the Value-Price-Cost Framework can be used to frame this discussion. We show how the mark of a winning strategy is its ability to pass three tests: (1) the *fit test* (for internal and external fit), (2) the *competitive advantage test*, and (3) the *performance test*. And we explain why good company performance depends not only upon a sound strategy but upon solid strategy execution as well.

- Chapter 2 presents a more complete overview of the strategic management process, covering topics ranging from the role of vision, mission, and values to what constitutes good corporate governance. It makes a great assignment for the second day of class and provides a smooth transition into the heart of the course. It introduces students to such core concepts as strategic versus financial objectives, the balanced scorecard, strategic intent, and business-level versus corporate-level strategies. It explains why *all managers are on a company’s strategy-making, strategy-executing team* and why a company’s strategic plan is a collection of strategies devised by different managers at different levels in the organizational hierarchy. The chapter concludes with a section on the role of the board of directors in the strategy-making, strategy-executing process and examines the conditions that led to recent high-profile corporate governance failures.
- The next two chapters introduce students to the two most fundamental perspectives on strategy making: the positioning view, exemplified by Michael Porter’s “five forces model of competition”; and the resource-based view. Chapter 3 provides *what has long been the clearest, most straightforward discussion of the five forces framework to be found in any text on strategic management*. It also offers a set of complementary analytical tools for conducting competitive analysis and demonstrates the importance of tailoring strategy to fit the circumstances of a company’s industry and competitive environment. What’s new in this edition is the inclusion of the value net framework for conducting analysis of how cooperative as well as competitive moves by various parties contribute to the creation and capture of value in an industry.
- Chapter 4 presents the resource-based view of the firm, showing why resource and capability analysis is such a powerful tool for sizing up a company’s competitive assets. It offers a simple framework for identifying a company’s resources and capabilities and explains how the VRIN framework can be used to determine whether they can provide the company with a sustainable competitive advantage over its competitors. Other topics covered in this chapter include dynamic capabilities, SWOT analysis, value chain analysis, benchmarking, and competitive strength assessments, thus enabling a solid appraisal of a company’s relative cost position and customer value proposition vis-à-vis its rivals. *An important feature of this chapter is a table showing how key financial and operating ratios are calculated and how to interpret them*. Students will find this table handy in doing the number crunching needed to evaluate whether a company’s strategy is delivering good financial performance.

- Chapter 5 sets forth the basic approaches available for competing and winning in the marketplace in terms of the five generic competitive strategies—low-cost leadership, differentiation, best-cost provider, focused differentiation, and focused low cost. It describes when each of these approaches works best and what pitfalls to avoid. It explains the role of *cost drivers* and *uniqueness drivers* in reducing a company's costs and enhancing its differentiation, respectively.
- Chapter 6 focuses on *other strategic actions* a company can take to complement its competitive approach and maximize the power of its overall strategy. These include a variety of offensive or defensive competitive moves, and their timing, such as blue-ocean strategies and first-mover advantages and disadvantages. It also includes choices concerning the breadth of a company's activities (or its *scope* of operations along an industry's entire value chain), ranging from horizontal mergers and acquisitions, to vertical integration, outsourcing, and strategic alliances. This material serves to segue into the scope issues covered in the next two chapters on international and diversification strategies.
- Chapter 7 takes up the topic of how to compete in international markets. It begins with a discussion of why differing market conditions across countries must necessarily influence a company's strategic choices about how to enter and compete in foreign markets. It presents five major strategic options for expanding a company's geographic scope and competing in foreign markets: export strategies, licensing, franchising, establishing a wholly owned subsidiary via acquisition or "greenfield" venture, and alliance strategies. It includes coverage of topics such as Porter's Diamond of National Competitive Advantage, profit sanctuaries, and the choice between multidomestic, global, and transnational strategies. This chapter explains the impetus for sharing, transferring, or accessing valuable resources and capabilities across national borders in the quest for competitive advantage, connecting the material to that on the resource-based view from Chapter 4. The chapter concludes with a discussion of the unique characteristics of competing in developing-country markets.
- Chapter 8 concerns strategy making in the multibusiness company, introducing the topic of corporate-level strategy with its special focus on diversification. The first portion of this chapter describes when and why diversification makes good strategic sense, the different means of diversifying a company's business lineup, and the pros and cons of related versus unrelated diversification strategies. The second part of the chapter looks at how to evaluate the attractiveness of a diversified company's business lineup, how to decide whether it has a good diversification strategy, and what the strategic options are for improving a diversified company's future performance. The evaluative technique integrates material concerning both industry analysis and the resource-based view, in that it considers the relative attractiveness of the various industries the company has diversified into, the company's competitive strength in each of its lines of business, and the extent to which its different businesses exhibit both *strategic fit* and *resource fit*.
- Although the topic of ethics and values comes up at various points in this textbook, Chapter 9 brings more direct attention to such issues and may be used as a stand-alone assignment in either the early, middle, or late part of a course. It concerns the themes of ethical standards in business, approaches to ensuring consistent ethical standards for companies with international operations, corporate social responsibility, and environmental sustainability. The contents of this chapter are sure to give students some things to ponder, rouse lively discussion, and

help to make students more *ethically aware* and conscious of *why all companies should conduct their business in a socially responsible and sustainable manner*.

- The next three chapters (Chapters 10, 11, and 12) comprise a module on strategy execution that is presented in terms of a 10-step framework. Chapter 10 provides an overview of this framework and then explores the first three of these tasks: (1) staffing the organization with people capable of executing the strategy well, (2) building the organizational capabilities needed for successful strategy execution, and (3) creating an organizational structure supportive of the strategy execution process.
- Chapter 11 discusses five additional managerial actions that advance the cause of good strategy execution: (1) *allocating resources* to enable the strategy execution process, (2) ensuring that *policies and procedures* facilitate rather than impede strategy execution, (3) using *process management tools* and *best practices* to drive continuous improvement in the performance of value chain activities, (4) installing *information and operating systems* that help company personnel carry out their strategic roles, and (5) using *rewards and incentives* to encourage good strategy execution and the achievement of performance targets.
- Chapter 12 completes the framework with a consideration of the roles of corporate culture and leadership in promoting good strategy execution. The recurring theme throughout the final three chapters is that executing strategy involves deciding on the specific actions, behaviors, and conditions needed for a smooth strategy-supportive operation and then following through to get things done and deliver results. The goal here is to ensure that students understand that the strategy-executing phase is a *make-things-happen and make-them-happen-right* kind of managerial exercise—one that is critical for achieving operating excellence and reaching the goal of strong company performance.

In this latest edition, we have put our utmost effort into ensuring that the 12 chapters are consistent with the latest and best thinking of academics and practitioners in the field of strategic management and provide the topical coverage required for both undergraduate and MBA-level strategy courses. The ultimate test of the text, of course, is the positive pedagogical impact it has in the classroom. If this edition sets a more effective stage for your lectures and does a better job of helping you persuade students that the discipline of strategy merits their rapt attention, then it will have fulfilled its purpose.

THE CASE COLLECTION

The 31-case lineup in this edition is flush with interesting companies and valuable lessons for students in the art and science of crafting and executing strategy. There's a good blend of cases from a length perspective—21 of the 31 cases are under 15 pages yet offer plenty for students to chew on; 5 are medium-length cases; and the remainder are detail-rich cases that call for more sweeping analysis.

At least 28 of the 31 cases involve companies, products, people, or activities that students will have heard of, know about from personal experience, or can easily identify with. The lineup includes at least 15 cases that will deepen student understanding of the special demands of competing in industry environments where product life cycles are short and competitive maneuvering among rivals is quite active. Twenty-four of the cases involve situations in which company resources and competitive capabilities

play as large a role in the strategy-making, strategy executing scheme of things as industry and competitive conditions do. Scattered throughout the lineup are 12 cases concerning non-U.S. companies, globally competitive industries, and/or cross-cultural situations. These cases, in conjunction with the globalized content of the text chapters, provide abundant material for linking the study of strategic management tightly to the ongoing globalization of the world economy. You'll also find 5 cases dealing with the strategic problems of family-owned or relatively small entrepreneurial businesses and 25 cases involving public companies and situations where students can do further research on the Internet.

The "Guide to Case Analysis" follows the last case. It contains sections on what a case is, why cases are a standard part of courses in strategy, preparing a case for class discussion, doing a written case analysis, doing an oral presentation, and using financial ratio analysis to assess a company's financial condition. We suggest having students read this guide before the first class discussion of a case.

A number of cases have accompanying videotape segments on the DVD.

THE TWO STRATEGY SIMULATION SUPPLEMENTS: THE BUSINESS STRATEGY GAME AND GLO-BUS

The Business Strategy Game and *GLO-BUS: Developing Winning Competitive Strategies*—two competition-based strategy simulations that are delivered online and that feature automated processing and grading of performance—are being marketed by the publisher as companion supplements for use with the 20th edition (and other texts in the field).

- *The Business Strategy Game* is the world's most popular strategy simulation, having been used by over 2,500 instructors in courses involving approximately 750,000 students on 1,050 university campuses in 66+ countries.
- *GLO-BUS*, a somewhat simpler strategy simulation introduced in 2004, has been used by more than 1,450+ instructors in courses involving over 180,000 students at 640+ university campuses in 48+ countries.

How the Strategy Simulations Work

In both *The Business Strategy Game (BSG)* and *GLO-BUS*, class members are divided into teams of one to five persons and assigned to run a company that competes head-to-head against companies run by other class members.

- In *BSG*, team members run an athletic footwear company, producing and marketing both branded and private-label footwear.
- In *GLO-BUS*, team members operate a digital camera company that designs, assembles, and markets entry-level digital cameras and upscale, multifeatured cameras.

In both simulations, companies compete in a global market arena, selling their products in four geographic regions—Europe-Africa, North America, Asia-Pacific, and Latin America. Each management team is called upon to craft a strategy for their company and make decisions relating to plant operations, workforce compensation, pricing and marketing, social responsibility/citizenship, and finance.

Company co-managers are held accountable for their decision making. Each company's performance is scored on the basis of earnings per share, return-on-equity

investment, stock price, credit rating, and image rating. Rankings of company performance, along with a wealth of industry and company statistics, are available to company co-managers after each decision round to use in making strategy adjustments and operating decisions for the next competitive round. You can be certain that the market environment, strategic issues, and operating challenges that company co-managers must contend with are *very tightly linked* to what your class members will be reading about in the text chapters. The circumstances that co-managers face in running their simulation company embrace the very concepts, analytical tools, and strategy options they encounter in the text chapters (this is something you can quickly confirm by skimming through some of the Exercises for Simulation Participants that appear at the end of each chapter).

We suggest that you schedule 1 or 2 practice rounds and anywhere from 4 to 10 regular (scored) decision rounds (more rounds are better than fewer rounds). Each decision round represents a year of company operations and will entail roughly two hours of time for company co-managers to complete. In traditional 13-week, semester-long courses, there is merit in scheduling one decision round per week. In courses that run 5 to 10 weeks, it is wise to schedule two decision rounds per week for the last several weeks of the term (sample course schedules are provided for courses of varying length and varying numbers of class meetings).

When the instructor-specified deadline for a decision round arrives, the simulation server automatically accesses the saved decision entries of each company, determines the competitiveness and buyer appeal of each company's product offering relative to the other companies being run by students in your class, and then awards sales and market shares to the competing companies, geographic region by geographic region. The unit sales volumes awarded to each company *are totally governed by*:

- How its prices compare against the prices of rival brands.
- How its product quality compares against the quality of rival brands.
- How its product line breadth and selection compare.
- How its advertising effort compares.
- And so on, for a total of 11 competitive factors that determine unit sales and market shares.

The competitiveness and overall buyer appeal of each company's product offering *in comparison to the product offerings of rival companies* is all-decisive—this algorithmic feature is what makes *BSG* and *GLO-BUS* “competition-based” strategy simulations. Once each company's sales and market shares are awarded based on the competitiveness of its respective overall product offering, the various company and industry reports detailing the outcomes of the decision round are then generated. Company co-managers can access the results of the decision round 15 to 20 minutes after the decision deadline.

The Compelling Case for Incorporating Use of a Strategy Simulation

There are *three exceptionally important benefits* associated with using a competition-based simulation in strategy courses taken by seniors and MBA students:

- *A three-pronged text-case-simulation course model delivers significantly more teaching-learning power than the traditional text-case model.* Using *both* cases and a strategy simulation to drill students in thinking strategically and applying what they read in the text chapters is a stronger, more effective means of helping

them connect theory with practice and develop better business judgment. What cases do that a simulation cannot is give class members broad exposure to a variety of companies and industry situations and insight into the kinds of strategy-related problems managers face. But what a competition-based strategy simulation does far better than case analysis is thrust class members squarely into *an active, hands-on managerial role* where they are totally responsible for assessing market conditions, determining how to respond to the actions of competitors, forging a long-term direction and strategy for their company, and making all kinds of operating decisions. Because they are held fully accountable for their decisions and their company's performance, *co-managers are strongly motivated* to dig deeply into company operations, probe for ways to be more cost-efficient and competitive, and ferret out strategic moves and decisions calculated to boost company performance. *Consequently, incorporating both case assignments and a strategy simulation to develop the skills of class members in thinking strategically and applying the concepts and tools of strategic analysis turns out to be more pedagogically powerful than relying solely on case assignments—there's stronger retention of the lessons learned and better achievement of course learning objectives.*

To provide you with quantitative evidence of the learning that occurs with using *The Business Strategy Game* or *GLO-BUS*, there is a built-in Learning Assurance Report showing how well each class member performs on nine skills/learning measures versus tens of thousands of students worldwide who have completed the simulation in the past 12 months.

- *The competitive nature of a strategy simulation arouses positive energy and steps up the whole tempo of the course by a notch or two.* Nothing sparks class excitement quicker or better than the concerted efforts on the part of class members at each decision round to achieve a high industry ranking and avoid the perilous consequences of being outcompeted by other class members. Students really enjoy taking on the role of a manager, running their own company, crafting strategies, making all kinds of operating decisions, trying to outcompete rival companies, and getting immediate feedback on the resulting company performance. Lots of back-and-forth chatter occurs when the results of the latest simulation round become available and co-managers renew their quest for strategic moves and actions that will strengthen company performance. Co-managers become *emotionally invested* in running their company and figuring out what strategic moves to make to boost their company's performance. Interest levels climb. All this stimulates learning and causes students to see the practical relevance of the subject matter and the benefits of taking your course.

As soon as your students start to say "Wow! Not only is this fun but I am learning a lot," *which they will*, you have won the battle of engaging students in the subject matter and moved the value of taking your course to a much higher plateau in the business school curriculum. This translates into a *livelier, richer learning experience from a student perspective and better instructor-course evaluations.*

- *Use of a fully automated online simulation reduces the time instructors spend on course preparation, course administration, and grading.* Since the simulation exercise involves a 20- to 30-hour workload for student teams (roughly 2 hours per decision round times 10 to 12 rounds, plus optional assignments), simulation adopters often compensate by trimming the number of assigned cases from, say, 10 to 12 to perhaps 4 to 6. This significantly reduces the time instructors spend reading cases, studying teaching notes, and otherwise getting ready to lead class

discussion of a case or grade oral team presentations. Course preparation time is further cut because you can use several class days to have students meet in the computer lab to work on upcoming decision rounds or a three-year strategic plan (in lieu of lecturing on a chapter or covering an additional assigned case). Not only does use of a simulation permit assigning fewer cases, but it also permits you to eliminate at least one assignment that entails considerable grading on your part. Grading one less written case or essay exam or other written assignment saves enormous time. With *BSG* and *GLO-BUS*, grading is effortless and takes only minutes; once you enter percentage weights for each assignment in your online grade book, a suggested overall grade is calculated for you. You'll be pleasantly surprised—and quite pleased—at how little time it takes to gear up for and administer *The Business Strategy Game* or *GLO-BUS*.

In sum, incorporating use of a strategy simulation turns out to be a *win-win proposition for both students and instructors*. Moreover, a very convincing argument can be made that a competition-based strategy simulation is *the single most effective teaching/learning tool that instructors can employ to teach the discipline of business and competitive strategy, to make learning more enjoyable, and to promote better achievement of course learning objectives*.

A Bird's-Eye View of *The Business Strategy Game*

The setting for *The Business Strategy Game (BSG)* is the global athletic footwear industry (there can be little doubt in today's world that a globally competitive strategy simulation is *vastly superior* to a simulation with a domestic-only setting). Global market demand for footwear grows at the rate of 7 to 9 percent annually for the first five years and 5 to 7 percent annually for the second five years. However, market growth rates vary by geographic region—North America, Latin America, Europe-Africa, and Asia-Pacific.

Companies begin the simulation producing branded and private-label footwear in two plants, one in North America and one in Asia. They have the option to establish production facilities in Latin America and Europe-Africa, either by constructing new plants or by buying previously constructed plants that have been sold by competing companies. Company co-managers exercise control over production costs on the basis of the styling and quality they opt to manufacture, plant location (wages and incentive compensation vary from region to region), the use of best practices and Six Sigma programs to reduce the production of defective footwear and to boost worker productivity, and compensation practices.

All newly produced footwear is shipped in bulk containers to one of four geographic distribution centers. All sales in a geographic region are made from footwear inventories in that region's distribution center. Costs at the four regional distribution centers are a function of inventory storage costs, packing and shipping fees, import tariffs paid on incoming pairs shipped from foreign plants, and exchange rate impacts. At the start of the simulation, import tariffs average \$4 per pair in Europe-Africa, \$6 per pair in Latin America, and \$8 in the Asia-Pacific region. However, the Free Trade Treaty of the Americas allows tariff-free movement of footwear between North America and Latin America. Instructors have the option to alter tariffs as the game progresses.

Companies market their brand of athletic footwear to footwear retailers worldwide and to individuals buying online at the company's website. Each company's sales and market share in the branded footwear segments hinge on its competitiveness on 11 factors: attractive pricing, footwear styling and quality, product line breadth, advertising,

use of mail-in rebates, appeal of celebrities endorsing a company's brand, success in convincing footwear retailers to carry its brand, number of weeks it takes to fill retailer orders, effectiveness of a company's online sales effort at its website, and customer loyalty. Sales of private-label footwear hinge solely on being the low-price bidder.

All told, company co-managers make as many as 53 types of decisions each period that cut across production operations (up to 10 decisions per plant, with a maximum of four plants), plant capacity additions/sales/upgrades (up to 6 decisions per plant), worker compensation and training (3 decisions per plant), shipping (up to 8 decisions per plant), pricing and marketing (up to 10 decisions in four geographic regions), bids to sign celebrities (2 decision entries per bid), financing of company operations (up to 8 decisions), and corporate social responsibility and environmental sustainability (up to 6 decisions).

Each time company co-managers make a decision entry, an assortment of on-screen calculations instantly shows the projected effects on unit sales, revenues, market shares, unit costs, profit, earnings per share, ROE, and other operating statistics. The on-screen calculations help team members evaluate the relative merits of one decision entry versus another and put together a promising strategy.

Companies can employ any of the five generic competitive strategy options in selling branded footwear—low-cost leadership, differentiation, best-cost provider, focused low cost, and focused differentiation. They can pursue essentially the same strategy worldwide or craft slightly or very different strategies for the Europe-Africa, Asia-Pacific, Latin America, and North America markets. They can strive for competitive advantage based on more advertising, a wider selection of models, more appealing styling/quality, bigger rebates, and so on.

Any well-conceived, well-executed competitive approach is capable of succeeding, provided it is not overpowered by the strategies of competitors or defeated by the presence of too many copycat strategies that dilute its effectiveness. The challenge for each company's management team is to craft and execute a competitive strategy that produces good performance on five measures: earnings per share, return on equity investment, stock price appreciation, credit rating, and brand image.

All activity for *The Business Strategy Game* takes place at www.bsg-online.com.

A Bird's-Eye View of *GLO-BUS*

The industry setting for *GLO-BUS* is the digital camera industry. Global market demand grows at the rate of 8 to 10 percent annually for the first five years and 4 to 6 percent annually for the second five years. Retail sales of digital cameras are seasonal, with about 20 percent of consumer demand coming in each of the first three quarters of each calendar year and 40 percent coming during the big fourth-quarter retailing season.

Companies produce entry-level and upscale, multifeatured cameras of varying designs and quality in a Taiwan assembly facility and ship assembled cameras directly to retailers in North America, Asia-Pacific, Europe-Africa, and Latin America. All cameras are assembled as retail orders come in and are shipped immediately upon completion of the assembly process—companies maintain no finished-goods inventories, and all parts and components are delivered on a just-in-time basis (which eliminates the need to track inventories and simplifies the accounting for plant operations and costs). Company co-managers exercise control over production costs on the basis of the designs and components they specify for their cameras, workforce compensation and training, the length of warranties offered (which affects warranty costs), the

amount spent for technical support provided to buyers of the company's cameras, and their management of the assembly process.

Competition in each of the two product market segments (entry-level and multifeatured digital cameras) is based on 10 factors: price, camera performance and quality, number of quarterly sales promotions, length of promotions in weeks, size of the promotional discounts offered, advertising, number of camera models, size of the retail dealer network, warranty period, and amount/caliber of technical support provided to camera buyers. Low-cost leadership, differentiation strategies, best-cost provider strategies, and focus strategies are all viable competitive options. Rival companies can strive to be the clear market leader in either entry-level cameras or upscale multifeatured cameras or both. They can focus on one or two geographic regions or strive for geographic balance. They can pursue essentially the same strategy worldwide or craft slightly or very different strategies for the Europe-Africa, Asia-Pacific, Latin America, and North America markets. Just as with *The Business Strategy Game*, almost any well-conceived, well-executed competitive approach is capable of succeeding, *provided it is not overpowered by the strategies of competitors or defeated by the presence of too many copycat strategies that dilute its effectiveness.*

Company co-managers make 49 types of decisions each period, ranging from R&D, camera components, and camera performance (10 decisions) to production operations and worker compensation (15 decisions) to pricing and marketing (15 decisions) to the financing of company operations (4 decisions) to corporate social responsibility (5 decisions). *Each time participants make a decision entry, an assortment of on-screen calculations instantly shows the projected effects on unit sales, revenues, market shares, unit costs, profit, earnings per share, ROE, and other operating statistics. These on-screen calculations help team members evaluate the relative merits of one decision entry versus another and stitch the separate decisions into a cohesive and promising strategy.* Company performance is judged on five criteria: earnings per share, return on equity investment, stock price, credit rating, and brand image.

All activity for *GLO-BUS* occurs at www.glo-bus.com.

Administration and Operating Features of the Two Simulations

The Internet delivery and user-friendly designs of both *BSG* and *GLO-BUS* make them incredibly easy to administer, even for first-time users. And the menus and controls are so similar that you can readily switch between the two simulations or use one in your undergraduate class and the other in a graduate class. If you have not yet used either of the two simulations, you may find the following of particular interest:

- Setting up the simulation for your course is done online and takes about 10 to 15 minutes. Once setup is completed, no other administrative actions are required beyond those of moving participants to a different team (should the need arise) and monitoring the progress of the simulation (to whatever extent desired).
- Participant's Guides are delivered electronically to class members at the website—students can read the guide on their monitors or print out a copy, as they prefer.
- There are 2- to 4-minute Video Tutorials scattered throughout the software (including each decision screen and each page of each report) that provide on-demand guidance to class members who may be uncertain about how to proceed.
- Complementing the Video Tutorials are detailed and clearly written Help sections explaining “all there is to know” about (a) each decision entry and the relevant

cause-effect relationships, (b) the information on each page of the Industry Reports, and (c) the numbers presented in the Company Reports. *The Video Tutorials and the Help screens allow company co-managers to figure things out for themselves, thereby curbing the need for students to ask the instructor “how things work.”*

- Team members running the same company who are logged in simultaneously on different computers at different locations can click a button to enter Collaboration Mode, enabling them to work collaboratively from the same screen in viewing reports and making decision entries, and click a second button to enter Audio Mode, letting them talk to one another.
 - When in “Collaboration Mode,” each team member sees the same screen at the same time as all other team members who are logged in and have joined Collaboration Mode. If one team member chooses to view a particular decision screen, that same screen appears on the monitors for all team members in Collaboration Mode.
 - Each team member controls their own color-coded mouse pointer (with their first-name appearing in a color-coded box linked to their mouse pointer) and can make a decision entry or move the mouse to point to particular on-screen items.
 - A decision entry change made by one team member is seen by all, in real time, and all team members can immediately view the on-screen calculations that result from the new decision entry.
 - If one team member wishes to view a report page and clicks on the menu link to the desired report, that same report page will immediately appear for the other team members engaged in collaboration.
 - Use of Audio Mode capability requires that each team member work from a computer with a built-in microphone (if they want to be heard by their team members) and speakers (so they may hear their teammates) or else have a headset with a microphone that they can plug into their desktop or laptop. A headset is recommended for best results, but most laptops now are equipped with a built-in microphone and speakers that will support use of our new voice chat feature.
 - Real-time VoIP audio chat capability among team members who have entered both the Audio Mode and the Collaboration Mode is a tremendous boost in functionality that enables team members to go online simultaneously on computers at different locations and conveniently and effectively collaborate in running their simulation company.
 - In addition, instructors have the capability to join the online session of any company and speak with team members, thus circumventing the need for team members to arrange for and attend a meeting in the instructor’s office. Using the standard menu for administering a particular industry, instructors can connect with the company desirous of assistance. Instructors who wish not only to talk but also to enter Collaboration (highly recommended because all attendees are then viewing the same screen) have a red-colored mouse pointer linked to a red box labeled Instructor.

Without a doubt, the Collaboration and Voice-Chat capabilities are hugely valuable for students enrolled in online and distance-learning courses where meeting face-to-face is impractical or time-consuming. Likewise, the

instructors of online and distance-learning courses will appreciate having the capability to join the online meetings of particular company teams when their advice or assistance is requested.

- Both simulations are quite suitable for use in distance-learning or online courses (and are currently being used in such courses on numerous campuses).
- Participants and instructors are notified via e-mail when the results are ready (usually about 15 to 20 minutes after the decision round deadline specified by the instructor/game administrator).
- Following each decision round, participants are provided with a complete set of reports—a six-page Industry Report, a one-page Competitive Intelligence report for each geographic region that includes strategic group maps and bulleted lists of competitive strengths and weaknesses, and a set of Company Reports (income statement, balance sheet, cash flow statement, and assorted production, marketing, and cost statistics).
- Two “open-book” multiple-choice tests of 20 questions are built into each simulation. The quizzes, which you can require or not as you see fit, are taken online and automatically graded, with scores reported instantaneously to participants and automatically recorded in the instructor’s electronic grade book. Students are automatically provided with three sample questions for each test.
- Both simulations contain a three-year strategic plan option that you can assign. Scores on the plan are automatically recorded in the instructor’s online grade book.
- At the end of the simulation, you can have students complete online peer evaluations (again, the scores are automatically recorded in your online grade book).
- Both simulations have a Company Presentation feature that enables each team of company co-managers to easily prepare PowerPoint slides for use in describing their strategy and summarizing their company’s performance in a presentation to either the class, the instructor, or an “outside” board of directors.
- *A Learning Assurance Report provides you with hard data concerning how well your students performed vis-à-vis students playing the simulation worldwide over the past 12 months.* The report is based on nine measures of student proficiency, business know-how, and decision-making skill and can also be used in evaluating the extent to which your school’s academic curriculum produces the desired degree of student learning insofar as accreditation standards are concerned.

For more details on either simulation, please consult Section 2 of the Instructor’s Manual accompanying this text or register as an instructor at the simulation websites (www.bsg-online.com and www.glo-bus.com) to access even more comprehensive information. You should also consider signing up for one of the webinars that the simulation authors conduct several times each month (sometimes several times weekly) to demonstrate how the software works, walk you through the various features and menu options, and answer any questions. You have an open invitation to call the senior author of this text at (205) 722-9145 to arrange a personal demonstration or talk about how one of the simulations might work in one of your courses. We think you’ll be quite impressed with the cutting-edge capabilities that have been programmed into *The Business Strategy Game* and *GLO-BUS*, the simplicity with which both simulations can be administered, and their exceptionally tight connection to the text chapters, core concepts, and standard analytical tools.

RESOURCES AND SUPPORT MATERIALS FOR THE 20TH EDITION

For Students

Key Points Summaries At the end of each chapter is a synopsis of the core concepts, analytical tools, and other key points discussed in the chapter. These chapter-end synopses, along with the core concept definitions and margin notes scattered throughout each chapter, help students focus on basic strategy principles, digest the messages of each chapter, and prepare for tests.

Two Sets of Chapter-End Exercises Each chapter concludes with two sets of exercises. The *Assurance of Learning Exercises* can be used as the basis for class discussion, oral presentation assignments, short written reports, and substitutes for case assignments. The *Exercises for Simulation Participants* are designed expressly for use by adopters who have incorporated use of a simulation and want to go a step further in tightly and explicitly connecting the chapter content to the simulation company their students are running. The questions in both sets of exercises (along with those Illustration Capsules that qualify as “mini-cases”) can be used to round out the rest of a 75-minute class period should your lecture on a chapter last for only 50 minutes.

The Connect™ Management Web-Based Assignment and Assessment Platform Beginning with the 18th edition, we began taking advantage of the publisher’s innovative Connect™ assignment and assessment platform and created several features that simplify the task of assigning and grading three types of exercises for students:

- There are self-scoring chapter tests consisting of 20 to 25 multiple-choice questions that students can take to measure their grasp of the material presented in each of the 12 chapters.
- There are two author-developed Interactive Application exercises for each of the 12 chapters that drill students in the use and application of the concepts and tools of strategic analysis.
- The Connect™ platform also includes author-developed Interactive Application exercises for 14 of the 31 cases in this edition that require students to work through answers to a select number of the assignment questions for the case. These exercises have multiple components and can include calculating assorted financial ratios to assess a company’s financial performance and balance sheet strength, identifying a company’s strategy, doing five-forces and driving-forces analysis, doing a SWOT analysis, and recommending actions to improve company performance. The content of these case exercises is tailored to match the circumstances presented in each case, calling upon students to do whatever strategic thinking and strategic analysis are called for to arrive at pragmatic, analysis-based action recommendations for improving company performance.

All of the Connect™ exercises are automatically graded (with the exception of those exercise components that entail student entry of short-answer and/or essay answers), thereby simplifying the task of evaluating each class member’s performance

and monitoring the learning outcomes. The progress-tracking function built into the Connect™ Management system enables you to:

- View scored work immediately and track individual or group performance with assignment and grade reports.
- Access an instant view of student or class performance relative to learning objectives.
- Collect data and generate reports required by many accreditation organizations, such as AACSB.

LearnSmart and SmartBook™ LearnSmart is an adaptive study tool proven to strengthen memory recall, increase class retention, and boost grades. Students are able to study more efficiently because they are made aware of what they know and don't know. Real-time reports quickly identify the concepts that require more attention from individual students—or the entire class. SmartBook is the first and only adaptive reading experience designed to change the way students read and learn. It creates a personalized reading experience by highlighting the most impactful concepts a student needs to learn at that moment in time. As a student engages with SmartBook, the reading experience continuously adapts by highlighting content based on what the student knows and doesn't know. This ensures that the focus is on the content he or she needs to learn, while simultaneously promoting long-term retention of material. Use SmartBook's real-time reports to quickly identify the concepts that require more attention from individual students—or the entire class. The end result? Students are more engaged with course content, can better prioritize their time, and come to class ready to participate.

For Instructors

Instructor Library The Connect Management Instructor Library is your repository for additional resources to improve student engagement in and out of class. You can select and use any asset that enhances your lecture.

Instructor's Manual The accompanying IM contains:

- A section on suggestions for organizing and structuring your course.
- Sample syllabi and course outlines.
- A set of lecture notes on each chapter.
- Answers to the chapter-end Assurance of Learning Exercises.
- A copy of the test bank.
- A comprehensive case teaching note for each of the 31 cases. These teaching notes are filled with suggestions for using the case effectively, have very thorough, analysis-based answers to the suggested assignment questions for the case, and contain an epilogue detailing any important developments since the case was written.

Test Bank and EZ Test Online There is a test bank containing over 900 multiple-choice questions and short-answer/essay questions. It has been tagged with AACSB and Bloom's Taxonomy criteria. All of the test bank questions are also accessible within a computerized test bank powered by McGraw-Hill's flexible electronic

testing program, EZ Test Online (www.eztestonline.com). Using EZ Test Online allows you to create paper and online tests or quizzes. With EZ Test Online, instructors can select questions from multiple McGraw-Hill test banks or author their own and then either print the test for paper distribution or give it online.

PowerPoint Slides To facilitate delivery preparation of your lectures and to serve as chapter outlines, you'll have access to approximately 500 colorful and professional-looking slides displaying core concepts, analytical procedures, key points, and all the figures in the text chapters.

The Business Strategy Game and GLO-BUS Online Simulations Using one of the two companion simulations is a powerful and constructive way of emotionally connecting students to the subject matter of the course. We know of no more effective way to arouse the competitive energy of students and prepare them for the challenges of real-world business decision making than to have them match strategic wits with classmates in running a company in head-to-head competition for global market leadership.

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As always, we value your recommendations and thoughts about the book. Your comments regarding coverage and contents will be taken to heart, and we always are grateful for the time you take to call our attention to printing errors, deficiencies, and other shortcomings. Please e-mail us at athompso@cba.ua.edu, margaret.a.peteraf@tuck.dartmouth.edu, john.gamble@tamucc.edu, or astrickl@cba.ua.edu.

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Crafting and Executing Strategy

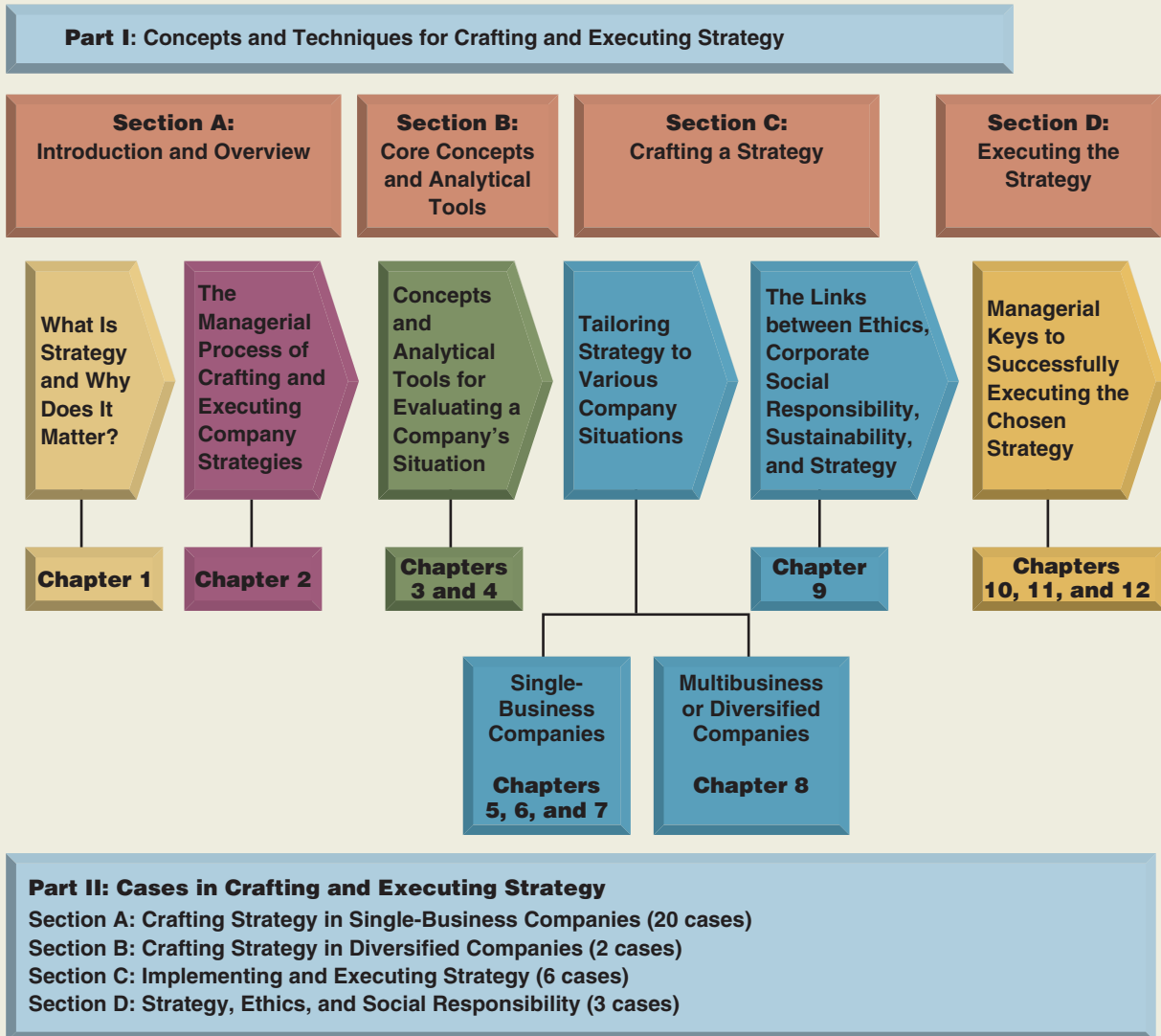
THE QUEST FOR COMPETITIVE ADVANTAGE

Concepts and Cases





Chapter Structure and Organization



CHAPTER 1

What Is Strategy and Why Is It Important?



Learning Objectives

THIS CHAPTER WILL HELP YOU UNDERSTAND:

- LO 1 What we mean by a company's *strategy*.
- LO 2 The concept of a *sustainable competitive advantage*.
- LO 3 The five most basic strategic approaches for setting a company apart from rivals and winning a sustainable competitive advantage.
- LO 4 That a company's strategy tends to evolve because of changing circumstances and ongoing efforts by management to improve the strategy.
- LO 5 Why it is important for a company to have a viable business model that outlines the company's customer value proposition and its profit formula.
- LO 6 The three tests of a winning strategy.

Learning Objectives are listed at the beginning of each chapter; corresponding numbered indicators in the margins show where learning objectives are covered in the text.

Illustration Capsules appear in boxes throughout each chapter to provide in-depth examples, connect the text presentation to real-world companies, and convincingly demonstrate "strategy in action." Some are appropriate for use as mini-cases.

ILLUSTRATION CAPSULE 9.4

TOMS's Well-Balanced Triple Bottom Line



Having sold over 2 million pairs of shoes worldwide, self-designated "Chief Shoe Giver" Blake Mycoskie founded TOMS on the principle of "One for One." Operating under the belief that "the way you shop can change the world," TOMS donates a pair of shoes to a child in need in over 50 different countries for every pair purchased. Each pair is made with sustainable materials that include organic canvas and recycled materials that minimize TOMS's ecological footprint. TOMS has been recognized with the Award for Corporate Excellence by the Office of the Secretary of State, while *Fortune* magazine has named Mycoskie to its "40 under 40" list.

Mycoskie credits much of TOMS's growth not to success in traditional avenues of advertising but, rather,

to the story behind the TOMS shoe as told by TOMS's customers. By focusing on the story behind its product and the importance of sustainable giving, TOMS generates brand awareness through motivated customers who share their feel-good purchases with friends and family. By utilizing user marketing rather than corporate marketing, TOMS successfully pitches a grassroots company-image and bundles a lifestyle with its product.

TOMS's environmental sustainability approach includes offering a line of vegan shoes, which contain no animal by-products, and maintaining its commitment to use earth and animal-friendly materials whenever possible. Its shoeboxes are made with 80 percent recycled waste and are printed with soy ink. Through these production considerations, TOMS caters to an environmentally conscious demographic with few established competitors and with loyal consumers who have helped TOMS experience sustained growth despite the global recession. From Shoe Giving Trips to employee training on the importance of environmental sustainability, TOMS aspires to offer its employees "more than a 9-to-5" job. This commitment to a worthwhile cause creates not only happier employees but also more autonomous and creative global citizens who work together to inspire change. By attaining economic growth through an emphasis on social justice and environmental sustainability, TOMS has maintained a well-balanced triple bottom line.

Note: Developed with Sean Zhang.

Source: Keynote statements by Blake Mycoskie and other information posted at www.toms.com.