STRATEGIC MANAGEMENT

AN INTEGRATED APPROACH

THEORY & CASES

CHARLES W. L. HILL

University of Washington - Foster School of Business

MELISSA A. SCHILLING

New York University - Stern School of Business

GARETH R. JONES



Australia • Brazil • Mexico • Singapore • United Kingdom • United States

Copyright 2020 Cengage Learning. All Rights Reserved. May not be copied, scanned, or duplicated, in whole or in part. Due to electronic rights, some third party content may be suppressed from the eBook and/or eChapter(s). Editorial review has deemed that any suppressed content does not materially affect the overall learning experience. Cengage Learning reserves the right to remove additional content at any time if subsequent rights restrictions require it.

BRIEF CONTENTS

PART ONE INTRODUCTION TO STRATEGIC MANAGEMENT

1	Strategic Leadership: Managing the Strategy-Making Process for Competitive		
2	Advantage External Analysis: The Identification of Opportunities and Threats	2 40	
PAI	RT TWO THE NATURE OF COMPETITIVE ADVANTAGE		
3 4	Internal Analysis: Resources and Competitive Advantage Competitive Advantage Through Functional-Level Strategies	76 107	
PAI	RT THREE STRATEGIES		
5 6 7 8	Business-Level Strategy Business-Level Strategy and the Industry Environment Strategy and Technology Strategy in the Global Environment	144 168 199 236	
9 10	9 Corporate-Level Strategy: Horizontal Integration, Vertical Integration, and Strategic Outsourcing		
	RT FOUR IMPLEMENTING STRATEGY		
11 12	Corporate Governance, Social Responsibility, and Ethics Implementing Strategy Through Organization	350 389	
PAI	RT FIVE CASES IN STRATEGIC MANAGEMENT	C-1	
Glossary Index		G-1 -1	

Copyright 2020 Cengage Learning. All Rights Reserved. May not be copied, scanned, or duplicated, in whole or in part. Due to electronic rights, some third party content may be suppressed from the eBook and/or eChapter(s). Editorial review has deemed that any suppressed content does not materially affect the overall learning experience. Cengage Learning reserves the right to remove additional content at any time if subsequent rights restrictions require it.

CONTENTS

Preface	xvi
Acknowledgments Dedication	xx xxiii
Dedication	XXIII

PART ONE INTRODUCTION TO STRATEGIC MANAGEMENT

Chapter 1	Strategic Leadership: Managing the Strategy-Making
	Process for Competitive Advantage

2

Opening Case: T-Mobile's Uncarrier Strategy 2

- 1-1 Overview 4
- 1-2 Strategic Leadership, Competitive Advantage, and Superior Performance 5
 - 1-2a Superior Performance 5
 - 1-2b Competitive Advantage and a Company's Business Model 7
 - 1-2c Industry Differences in Performance 8
 - 1-2d Performance in Nonprofit Enterprises 8

Strategy in Action 1.1: The Gates Foundation–Eradicating Malaria 9

- 1-3 Strategic Managers 10
 - 1-3a Corporate-Level Managers 10
 - 1-3b Business-Level Managers 12
 - 1-3c Functional-Level Managers 12
- 1-4 The Strategy-Making Process 12
 - 1-4a A Model of the Strategic Planning Process 13
 - 1-4b Mission Statement 13
- 1-5 Major Goals 17
 - 1-5a External Analysis 18
 - 1-5b Internal Analysis 18

Strategy in Action 1.2: The Evolution of Strategy at Time Inc. 19

- 1-5c SWOT Analysis and the Business Model 20
- 1-5d Strategy Implementation 21
- 1-5e The Feedback Loop 21
- 1-6 Strategy as an Emergent Process 22
 - 1-6a Strategy Making in an Unpredictable World 22
 - 1-6b Autonomous Action: Strategy Making by Lower-Level Managers 22
 - 1-6c Serendipity and Strategy 23
 - 1-6d Intended and Emergent Strategies 23

Strategy in Action 1.3: A Strategic Shift at Charles Schwab 24

- 1-7 Strategic Planning in Practice 26
 - 1-7a Scenario Planning 26
 - 1-7b Decentralized Planning 28
- 1-8 Strategic Decision Making 28
 - 1-8a Cognitive Biases and Strategic Decision Making 28
 - 1-8b Techniques for Improving Decision Making 30
- **1-9** Strategic Leadership 30
 - 1-9a Vision, Eloquence, and Consistency 31
 - 1-9b Articulation of the Business Model 31
 - 1-9c Commitment 31
 - 1-9d Being Well Informed 32
 - 1-9e Willingness to Delegate and Empower 32
 - 1-9f The Astute Use of Power 32
 - 1-9g Emotional Intelligence 33

Closing Case: The Rise of LuLulemon 35

Chapter 2 External Analysis: The Identification of Opportunities and Threats

Opening Case: Competition in the U.S. Airline Industry 40

- 2-1 Overview 42
- **2-2** Defining an Industry 42
- **2-3** Porter's Competitive Forces Model 43
 - 2-3a Risk of Entry by Potential Competitors 44

Strategy in Action 2.1: Circumventing Entry Barriers into the Soft Drink Industry 47

40

2-3b Rivalry Among Established Companies 48

Strategy in Action 2.2: Price Wars in the Breakfast Cereal Industry 50

- 2-3c The Bargaining Power of Buyers 51
- 2-3d The Bargaining Power of Suppliers 52
- 2-3e Substitute Products 53
- 2-3f Complementors 53
- 2-3g Summary: Why Industry Analysis Matters 54
- 2-4 Strategic Groups within Industries 55
 - 2-4a Implications of Strategic Groups 57
 - 2-4b The Role of Mobility Barriers 57
- 2-5 Industry Life-Cycle Analysis 58
 - 2-5a Embryonic Industries 58
 - 2-5b Growth Industries 59
 - 2-5c Industry Shakeout 60
 - 2-5d Mature Industries 61
 - 2-5e Declining Industries 61
 - 2-5f Summary 62
- 2-6 Limitations of Models for Industry Analysis 62
 - 2-6a Life-Cycle Issues 62
 - 2-6b Innovation and Change 62
 - 2-6c Company Differences 64

2-7 The Macroenvironment 65

- 2-7 a Macroeconomic Forces 65
- 2-7b Global Forces 66
- 2-7c Technological Forces 67
- 2-7d Demographic Forces 67
- 2-7e Social Forces 68
- 2-7f Political and Legal Forces 68

Closing Case: Competition in the U.S. Market for Wireless Telecommunications 70

PART TWO THE NATURE OF COMPETITIVE ADVANTAGE Internal Analysis: Resources and Competitive Advantage Chapter 3 76 Opening Case: Competitive Advantage at Nordstrom 76 **3-1** Overview 78 **3-2** Competitive Advantage 78 3-2a Distinctive Competencies 78 3-2b Resources 79 3-2c Resource Quality: The VRIO Framework 81 3-2d Resources and Sustained Competitive Advantage 82 **3-3** Value Creation and Profitability 85 3-4 The Value Chain 88 3-4a Primary Activities 89 Strategy in Action 3.1: Value Creation at Burberry 90 3-4b Support Activities 91 Strategy in Action 3.2: Competitive Advantage at Zara 92 3-4c Value-Chain Analysis: Implications 93 **3-5** The Building Blocks of Competitive Advantage 94 3-5a Efficiency 95 3-5b Quality as Excellence and Reliability 95 3-5c Innovation 97 3-5d Customer Responsiveness 97 **3-6** Analyzing Competitive Advantage and Profitability 98 3-6a Comparing Wal-Mart and Target 100 Closing Case: Southwest Airlines 104 Chapter 4 Competitive Advantage Through Functional-Level Strategies 107 Opening Case: Automation at Boeing 107 4-1 Overview 109 **4-2** Achieving Superior Efficiency 109 4-2a Efficiency and Economies of Scale 110 4-2b Efficiency and Learning Effects 111 Strategy in Action 4.1: Learning Effects in Cardiac Surgery 113 4-2c Efficiency and the Experience Curve 113 4-2d Efficiency, Flexible Production Systems, and Mass Customization 115

Copyright 2020 Cengage Learning. All Rights Reserved. May not be copied, scanned, or duplicated, in whole or in part. Due to electronic rights, some third party content may be suppressed from the eBook and/or eChapter(s). Editorial review has deemed that any suppressed content does not materially affect the overall learning experience. Cengage Learning reserves the right to remove additional content at any time if subsequent rights restrictions require it Strategy in Action 4.2: Pandora: Mass Customizing Internet Radio 117

- 4-2e Efficiency, Automation and Artificial Intelligence 118
- 4-2f Marketing and Efficiency 118
- 4-2g Materials Management, Just-in-Time Systems and Efficiency 120
- 4-2h Research and Development Strategy and Efficiency 121
- 4-2i Human Resource Strategy and Efficiency 121
- 4-2j Information Systems and Efficiency 123
- 4-2k Infrastructure and Efficiency 123
- 4-2| Summary 124
- **4-3** Achieving Superior Quality 125
 - 4-3a Attaining Superior Reliability 125
 - 4-3b Implementing Reliability Improvement Methodologies 126

Strategy in Action 4.3: General Electric's Six Sigma Quality Improvement Process 127

4-3c Improving Quality as Excellence 129

- 4-4 Achieving Superior Innovation 130
 - 4-4a The High Failure Rate of Innovation 131
 - 4-4b Reducing Innovation Failures 132
- 4-5 Achieving Superior Customer Responsiveness 134
 - 4-5a Focusing on the Customer 135
 - 4-5b Demonstrating Leadership 135
 - 4-5c Shaping Employee Attitudes 135
 - 4-5d Knowing Customer Needs 135
 - 4-5e Satisfying Customer Needs 136

Closing Case: Trouble at McDonald's 139

PART THREE STRATEGIES

Chapter 5 Business-Level Strategy

Opening Case: Reinventing The New York Times 144

- 5-1 Overview 146
- 5-2 Low Cost and Differentiation 146
 - 5-2a Lowering Costs 146
 - 5-2b Differentiation 147
 - 5-2c The Differentiation–Low-Cost Trade-off 149
 - 5-2d Value Innovation: Greater Differentiation at a Lower Cost 151

144

- Strategy in Action 5.1: IKEA: Value Innovation in Furniture Retailing 152
- 5-3 Who are Our Customers? Market Segmentation 153
 - 5-3a Three Approaches to Market Segmentation 153
 - 5-3b Market Segmentation, Costs and Revenues 154
- 5-4 Business-Level Strategy Choices 156

Strategy in Action 5.2: Microsoft Office Versus Google Apps 158

- 5-5 Business-Level Strategy, Industry, and Competitive Advantage 159
- 5-6 Implementing Business-Level Strategy 1605-6a Lowering Costs Through Functional Strategy and Organization 161

Copyright 2020 Cengage Learning. All Rights Reserved. May not be copied, scanned, or duplicated, in whole or in part. Due to electronic rights, some third party content may be suppressed from the eBook and/or eChapter(s). Editorial review has deemed that any suppressed content does not materially affect the overall learning experience. Cengage Learning reserves the right to remove additional content at any time if subsequent rights restrictions require it.

5-6b Differentiation Through Functional-Level Strategy and Organization 161 **5-7** Competing Differently: Blue Ocean Strategy 162 Closing Case: Virgin America 166

Chapter 6 Business-Level Strategy and the Industry Environment

168

199

Opening Case: The Rise of Internet Streaming Services and Decline in the Power of Cable Companies 168

6-1 Overview 170

- 6-2 Strategy in a Fragmented Industry 170
 - 6-2a Reasons for Fragmentation 170
 - 6-2b Consolidating a Fragmented Industry Through Value Innovation 171
 - 6-2c Chaining and Franchising 172
 - 6-2d Horizontal Mergers 173

6-3 Strategies in Embryonic and Growth Industries 174

- 6-3a The Changing Nature of Market Demand 175
- 6-3b Strategic Implications: Crossing the Chasm 178

6-3c Strategic Implications of Differences in Market Growth Rates 179

Strategy in Action 6.1: Crossing the Chasm in the Smartphone Market 180

6-4 Strategy in Mature Industries 182 6-4a Strategies to Deter Entry 183 6-4b Strategies to Manage Rivalry 185

Strategy in Action 6.2: Toyota Uses Market Development to Become the Global Leader 189

6-5 Strategies in Declining Industries 192 6-5a The Severity of Decline 192 6-5b Choosing a Strategy 193

Closing Case: Can Best Buy Survive the Rise of E-commerce? 196

Chapter 7 Strategy and Technology

Opening Case: Tencent and WeChat 199

7-1 Overview 201

7-2 Technical Standards and Format Wars 202

Strategy in Action 7.1: "Segment Zero" – A Serious Threat to Microsoft? 203

- 7-2a Examples of Standards 205
- 7-2b Benefits of Standards 206
- 7-2c Establishment of Standards 207
- 7-2d Network Effects, Positive Feedback, and Lockout 208
- **7-3** Strategies for Winning a Format War 212

7-3a Ensure a Supply of Complements 212

- 7-3b Leverage Killer Applications 212
- 7-3c Aggressive Pricing and Marketing 213

- 7-3d Cooperate with Competitors 214
- 7-3e License the Format 214
- 7-4 Costs in High-Technology Industries 215
 - 7-4a Comparative Cost Economics 215
 - 7-4b Strategic Significance 216

Strategy in Action 7.2: Lowering the Cost of Ultrasound Equipment Through Digitalization 217

- 7-5 Capturing First-Mover Advantages 218
 - 7-5a First-Mover Advantages 219
 - 7-5b First-Mover Disadvantages 220
 - 7-5c Strategies for Exploiting First-Mover Advantages 221
- 7-6 Technological Paradigm Shifts 224
 - 7-6a Paradigm Shifts and the Decline of Established Companies 225
 - 7-6b Strategic Implications for Established Companies 229
 - 7-6c Strategic Implications for New Entrants 230

Closing Case: Blu-ray versus HD-DVD and Streaming: Standards Battles in Video 232

Chapter 8 Strategy in the Global Environment

236

- Opening Case: Ford's Global Strategy 236
- 8-1 Overview 238
- 8-2 Global and National Environments 2388-2a The Globalization of Production and Markets 239

Strategy in Action 8.1: Making the Apple iPhone 240

8-2b National Competitive Advantage 242

- 8-3 Global Expansion, Profitability, and Profit Growth 245
 - 8-3a Expanding the Market: Leveraging Products 245
 - 8-3b Realizing Cost Economies from Global Volume 246
 - 8-3c Realizing Location Economies 246
 - 8-3d Leveraging the Competencies of Global Subsidiaries 247
- 8-4 Cost Pressures and Pressures for Local Responsiveness 248
 - 8-4a Pressures for Cost Reductions 249
 - 8-4b Pressures for Local Responsiveness 250
- 8-5 Choosing a Global Strategy 253
 - 8-5a Global Standardization Strategy 253
 - 8-5b Localization Strategy 254
 - 8-5c Transnational Strategy 255
 - 8-5d International Strategy 256
 - 8-5e Changes in Strategy over Time 257
- 8-6 The Choice of Entry Mode 258
 - 8-6a Exporting 258
 - 8-6b Licensing 259

Strategy in Action 8.2: Burberry Shifts its Strategy in Japan 261

- 8-6c Franchising 261
- 8-6d Joint Ventures 262
- 8-6e Wholly-Owned Subsidiaries 263
- 8-6f Choosing an Entry Strategy 264

8-7 Global Strategic Alliances 266 8-7a Advantages of Strategic Alliances 267 8-7b Disadvantages of Strategic Alliances 267 8-7c Making Strategic Alliances Work 268 Closing Case: The Globalization of Starbucks 272 Chapter 9 Corporate-Level Strategy: Horizontal Integration, 276 Vertical Integration, and Strategic Outsourcing Opening Case: Netflix in 2018 276 9-1 Overview 278 9-2 Corporate-Level Strategy and the Multibusiness Model 279 9-3 Horizontal Integration: Single-Industry Corporate Strategy 280 9-3a Benefits of Horizontal Integration 281 Strategy in Action 9.1: Wal-Mart's Expansion into Other Retail Formats 283 9-3b Problems with Horizontal Integration 285 9-4 Vertical Integration: Entering New Industries to Strengthen the "Core" Business Model 286 9-4a Increasing Profitability Through Vertical Integration 288 9-4b Problems with Vertical Integration 291 **9-5** Alternatives to Vertical Integration: Cooperative Relationships 293 9-5a Short-Term Contracts and Competitive Bidding 294 9-5b Strategic Alliances and Long-Term Contracting 294 9-5c Modularity and Platform Competition 295 9-5d Building Long-Term Cooperative Relationships 299 Strategy in Action 9.2: eBay's Changing Commitment to Its Sellers 300 9-6 Strategic Outsourcing 301 9-6a Benefits of Outsourcing 303 9-6b Risks of Outsourcing 304 Closing Case: The Proposed Merger of Comcast and Time Warner Cable 307 Chapter 10 Corporate-Level Strategy: Related and Unrelated Diversification 311 Opening Case: Google's acquisition of ITA Software 311 **10-1** Overview 313 **10-2** Increasing Profitability Through Diversification 314 10-2a Transferring Competencies Across Businesses 315 10-2b Leveraging Competencies to Create a New Business 316 10-2c Sharing Resources and Capabilities 316 10-2d Utilizing General Organizational Competencies 319 Strategy in Action 10.1: United Technologies Has an "ACE" in Its Pocket 321 **10-3** Two Types of Diversification 322 10-3a Related Diversification 323 10-3b Unrelated Diversification 323 **10-4** The Limits and Disadvantages of Diversification 325 10-4a Changes in the Industry or Company 325

- 10-4b Diversification for the Wrong Reasons 325
- 10-4c The Bureaucratic Costs of Diversification 327

Strategy in Action 10.2: How Bureaucratic Costs Rose Then Fell at Pfizer 329

- 10-5 Choosing a Strategy 330
 10-5a Related Versus Unrelated Diversification 330
 10-5b The Web of Corporate-Level Strategy 330
- 10-6 Entering New Industries: Internal New Ventures 332
 10-6a The Attractions of Internal New Venturing 332
 10-6b Pitfalls of New Ventures 332
 - 10-6c Guidelines for Successful Internal New Venturing 334
- **10-7** Entering New Industries: Acquisitions 335
 - 10-7a The Attraction of Acquisitions 336
 - 10-7b Acquisition Pitfalls 336
 - 10-7c Guidelines for Successful Acquisition 339
- **10-8** Entering New Industries: Joint Ventures 341 10-8a Restructuring 342
 - 10-8b Why Restructure? 342

Closing Case: LVMH: Getting Big While Staying Beautiful 345

PART FOUR IMPLEMENTING STRATEGY

Chapter 11 Corporate Governance, Social Responsibility, and Ethics 350

Opening Case: Volkswagen: From the "People's Car" to Dieselgate 350

- **11-1** Overview 355
- **11-2** Stakeholders and Corporate Performance 355
 - 11-2a Stakeholder Impact Analysis 357
 - 11-2b The Unique Role of Stockholders 357
 - 11-2c Profitability, Profit Growth, and Stakeholder Claims 358

Strategy in Action 11.1: Price Fixing at Sotheby's and Christie's 361

- 11-3 Agency Theory 361
 - 11-3a Principal–Agent Relationships 362
 - 11-3b The Agency Problem 362

Strategy in Action 11.2: Self-Dealing at Hollinger International Inc. 366

- 11-4 Governance Mechanisms 367
 - 11-4a The Board of Directors 367
 - 11-4b Stock-Based Compensation 369
 - 11-4c Financial Statements and Auditors 370
 - 11-4d The Takeover Constraint 371
 - 11-4e Governance Mechanisms Inside a Company 372
- **11-5** Ethics and Strategy 374
 - 11-5a Ethical Issues in Strategy 375
 - 11-5b The Roots of Unethical Behavior 378
 - 11-5c Behaving Ethically 379
- Closing Case: Starbucks: Taking a Stand on Social Issues 384

Chapter 12 Implementing Strategy Through Organization 389

Opening Case: Organization at Microsoft 389

12-1 Overview 391

- 12-2 Organizational Architecture 391
- **12-3** Organizational Structure 393

12-3a Centralization and Decentralization 393

Strategy in Action 12.1: FEMA and Hurricane Katrina 396

12-3b Tall Versus Flat Hierarchies 397

12-3c Structural Forms 399

- 12-3d Formal Integrating Mechanisms 403
- 12-3e Informal Integrating Mechanisms 405
- **12-4** Organization Controls and Incentives 407 12-4a Control Systems 407

Strategy in Action 12.2: Goal Setting and Controls at Nordstrom 409

12-4b Methods of Control 410

12-5 Organizational Culture 415

12-6 Organization Processes 417

Strategy in Action 12.3: Organizational Culture at Lincoln Electric 417

12-7 Implementing Strategy Through Organizational Architecture 418 12-7a Strategy and Organization in the Single-Business Enterprise 418

12-7b Strategy and Organization in the Multibusiness Enterprise 422

Closing Case: Organization Change at Google (Alphabet) 425

PART FIVE CASES IN STRATEGIC MANAGEMENT

Introduction: Analyzing a Case Study and Writing a Case Study Analysis C-4 What is Case Study Analysis? C-4 Analyzing a Case Study C-5 Writing a Case Study Analysis C-10 The Role of Financial Analysis in Case Study Analysis C-12 *Profit Ratios C-12 Liquidity Ratios C-13 Activity Ratios C-14 Leverage Ratios C-14 Shareholder-Return Ratios C-15 Cash Flow C-16* Conclusion C-16 Endnote C-17

Long Cases

Case 1: Trader Joe's in 2018 C-18

Case 2: Small Package Express Delivery Industry, 1973–2018 C-23

- Case 3: Airborne Express: The Underdog C-38
- Case 4: Charles Schwab C-50
- Case 5: Coca-Cola C-65
- Case 6: Uber in 2018 C-76
- Case 7: Dell Inc (A)-Going Private C-90
- Case 8: Dell Inc (B)—Transforming the Company C-100
- Case 9: Apple at Fourty C-106
- Case 10: Wal-Mart Stores C-122
- Case 11: Costco Wholesale Corporation in 2018 C-134
- Case 12: SpaceX: Disrupting the Space Industry C-144
- Case 13: Alibaba Group: The Rise of a Platform Giant C-151
- Case 14: Ending HIV? Sangamo and Gene Editing C-159
- Case 15: Tesla, Inc. in 2018 C-168
- Case 16: Chotukool: Challenges and Opportunities in Frugal Innovation C-181
- Case 17: IKEA in 2018: Furniture Retailer to the World C-184
- Case 18: General Electric C-193
- Case 19: 3M: The Innovation Engine C-204
- Case 20: Nike: The Sweatshop Debate 20 Years on C-219

Short Cases

- Case 21: How to Make Money in Newspaper Advertising C-226
- Case 22: A Battle for Dominance in Mobile Payments C-228
- Case 23: The Market for Large Commercial Jet Aircraft C-232
- Case 24: Verizon Wireless: Competitive Advantage C-234
- Case 25: Amazon.com: Competitive Advantage and Functional Strategy C-236
- Case 26: Nordstrom: Business-Level Strategy C-238
- Case 27: Procter & Gamble: Evolution of Global Strategy C-240

Case 28: JCB in India C-242 Case 29: Outsourcing and Vertical Integration at Apple C-244 Case 30: Citigroup: The Opportunities and Risks of Diversification C-246 Case 31: HP's Disastrous Acquisition of Autonomy C-249 Case 32: Organization at Apple C-251

Glossary G-1 Index I-1

Copyright 2020 Cengage Learning. All Rights Reserved. May not be copied, scanned, or duplicated, in whole or in part. Due to electronic rights, some third party content may be suppressed from the eBook and/or eChapter(s). Editorial review has deemed that any suppressed content does not materially affect the overall learning experience. Cengage Learning reserves the right to remove additional content at any time if subsequent rights restrictions require it.