

11TH EDITION

STRATEGIC MANAGEMENT

THEORY

CHARLES W. L. HILL

University of Washington – Foster School of Business

GARETH R. JONES

MELISSA A. SCHILLING

New York University – Stern School of Business



Brief Contents

PART ONE INTRODUCTION TO STRATEGIC MANAGEMENT

1	Strategic Leadership: Managing the Strategy-Making Process for Competitive Advantage	1
2	External Analysis: The Identification of Opportunities and Threats	43

PART TWO THE NATURE OF COMPETITIVE ADVANTAGE

3	Internal Analysis: Distinctive Competencies, Competitive Advantage, and Profitability	80
4	Building Competitive Advantage Through Functional-Level Strategies	116

PART THREE STRATEGIES

5	Business-Level Strategy	153
6	Business-Level Strategy and the Industry Environment	178
7	Strategy and Technology	210
8	Strategy in the Global Environment	246
9	Corporate-Level Strategy: Horizontal Integration, Vertical Integration, and Strategic Outsourcing	286
10	Corporate-Level Strategy: Related and Unrelated Diversification	318

PART FOUR IMPLEMENTING STRATEGY

11	Corporate Performance, Governance, and Business Ethics	359
12	Implementing Strategy in Companies That Compete in a Single Industry	395
13	Implementing Strategy in Companies That Compete Across Industries and Countries	439

Glossary	G-1
Index	I-1

Contents

Preface xix
Acknowledgements xxiii
Dedication xxvii

PART ONE INTRODUCTION TO STRATEGIC MANAGEMENT

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

 Opening Case 1

 Overview 3

 Strategic Leadership, Competitive Advantage, and Superior Performance 4

Superior Performance 5

Competitive Advantage and a Company's Business Model 6

Industry Differences in Performance 7

Performance in Nonprofit Enterprises 8

 Strategic Managers 9

Corporate-Level Managers 10

Business-Level Managers 10

Functional-Level Managers 11

 The Strategy-Making Process 11

A Model of the Strategic Planning Process 11

Mission Statement 12

 Major Goals 16

External Analysis 17

Internal Analysis 17

SWOT Analysis and the Business Model 17

 Strategy in Action 1.1: Strategic Analysis at Time Inc. 18

Strategy Implementation 19

The Feedback Loop 20

 Strategy as an Emergent Process 20

Strategy Making in an Unpredictable World 20

Autonomous Action: Strategy Making by Lower-Level Managers 21

 Strategy in Action 1.2: Starbucks' Music Business 21

Serendipity and Strategy 22

Intended and Emergent Strategies 22

	Strategy in Action 1.3: A Strategic Shift at Charles Schwab	23
	Strategic Planning in Practice	25
	<i>Scenario Planning</i>	25
	<i>Decentralized Planning</i>	26
	Strategic Decision Making	27
	<i>Cognitive Biases and Strategic Decision Making</i>	27
	<i>Techniques for Improving Decision Making</i>	29
	Strategic Leadership	29
	<i>Vision, Eloquence, and Consistency</i>	30
	<i>Articulation of the Business Model</i>	30
	<i>Commitment</i>	30
	<i>Being Well Informed</i>	31
	<i>Willingness to Delegate and Empower</i>	31
	<i>The Astute Use of Power</i>	32
	<i>Emotional Intelligence</i>	32
Chapter 2	External Analysis: The Identification of Opportunities and Threats	43
	Opening Case	43
	Overview	44
	Defining an Industry	45
	<i>Industry and Sector</i>	46
	<i>Industry and Market Segments</i>	47
	<i>Changing Industry Boundaries</i>	47
	Competitive Forces Model	47
	<i>Risk of Entry by Potential Competitors</i>	48
	<i>Rivalry Among Established Companies</i>	50
	Strategy in Action 2.1: Circumventing Entry Barriers into the Soft Drink Industry	51
	Strategy in Action 2.2: Price Wars in the Breakfast Cereal Industry	53
	<i>The Bargaining Power of Buyers</i>	55
	<i>The Bargaining Power of Suppliers</i>	56
	<i>Substitute Products</i>	58
	<i>Complementors</i>	58
	<i>Summary: Why Industry Analysis Matters</i>	59
	Strategic Groups Within Industries	60
	<i>Implications of Strategic Groups</i>	61
	<i>The Role of Mobility Barriers</i>	62
	Industry Life-Cycle Analysis	63
	<i>Embryonic Industries</i>	63
	<i>Growth Industries</i>	64
	<i>Industry Shakeout</i>	64
	<i>Mature Industries</i>	65
	<i>Declining Industries</i>	66
	<i>Summary</i>	66

Limitations of Models for Industry Analysis	67
<i>Life-Cycle Issues</i>	67
<i>Innovation and Change</i>	67
<i>Company Differences</i>	69
The Macroenvironment	69
<i>Macroeconomic Forces</i>	69
<i>Global Forces</i>	71
<i>Technological Forces</i>	71
<i>Demographic Forces</i>	72
<i>Social Forces</i>	72
<i>Political and Legal Forces</i>	72

PART TWO THE NATURE OF COMPETITIVE ADVANTAGE

Chapter 3	Internal Analysis: Distinctive Competencies, Competitive Advantage, and Profitability	80
	<i>Opening Case</i>	80
	Overview	82
	The Roots of Competitive Advantage	82
	<i>Distinctive Competencies</i>	83
	<i>Competitive Advantage, Value Creation, and Profitability</i>	85
	The Value Chain	89
	<i>Primary Activities</i>	89
	<i>Strategy in Action 3.1: Value Creation at Burberry</i>	91
	<i>Support Activities</i>	91
	<i>Strategy in Action 3.2: Competitive Advantage at Zara</i>	92
	The Building Blocks of Competitive Advantage	93
	<i>Efficiency</i>	93
	<i>Quality as Excellence and Reliability</i>	94
	<i>Innovation</i>	96
	<i>Customer Responsiveness</i>	96
	Business Models, the Value Chain, and Generic Distinctive Competencies	97
	Analyzing Competitive Advantage and Profitability	98
	The Durability of Competitive Advantage	103
	<i>Barriers to Imitation</i>	103
	<i>Capability of Competitors</i>	105
	<i>Industry Dynamism</i>	106
	<i>Summary</i>	106
	Avoiding Failure and Sustaining Competitive Advantage	106
	<i>Why Companies Fail</i>	106
	<i>Steps to Avoid Failure</i>	108
	<i>Strategy in Action 3.3: The Road to Ruin at DEC</i>	109

Chapter 4	Building Competitive Advantage Through Functional-Level Strategies	116
	Opening Case 116	
	Overview 117	
	Achieving Superior Efficiency 119	
	<i>Efficiency and Economies of Scale</i> 119	
	<i>Efficiency and Learning Effects</i> 120	
	Strategy in Action 4.1: Learning Effects in Cardiac Surgery 122	
	<i>Efficiency and the Experience Curve</i> 122	
	<i>Efficiency, Flexible Production Systems, and Mass Customization</i> 124	
	<i>Marketing and Efficiency</i> 125	
	Strategy in Action 4.2: Pandora: Mass Customizing Internet Radio 126	
	Materials Management, Just-in-Time Systems, and Efficiency 128	
	<i>R&D Strategy and Efficiency</i> 129	
	<i>Human Resource Strategy and Efficiency</i> 129	
	<i>Information Systems and Efficiency</i> 132	
	<i>Infrastructure and Efficiency</i> 132	
	<i>Summary</i> 133	
	Achieving Superior Quality 134	
	<i>Attaining Superior Reliability</i> 134	
	Strategy in Action 4.3: General Electric's Six Sigma Quality Improvement Process 135	
	<i>Implementing Reliability Improvement Methodologies</i> 136	
	<i>Improving Quality as Excellence</i> 138	
	Achieving Superior Innovation 139	
	<i>The High Failure Rate of Innovation</i> 140	
	<i>Reducing Innovation Failures</i> 141	
	Strategy in Action 4.4: Corning—learning from Innovation Failures 142	
	Achieving Superior Responsiveness to Customers 144	
	<i>Focusing on the Customer</i> 144	
	<i>Satisfying Customer Needs</i> 145	

PART THREE STRATEGIES

Chapter 5	Business-Level Strategy	153
	Opening Case 153	
	Overview 154	
	Low Cost and Differentiation 155	
	<i>Lowering Costs</i> 155	

	<ul style="list-style-type: none"> Strategy in Action 5.1: Low Costs at Southwest Airlines 156 Who are Our Customers? Market Segmentation 161 Business-Level Strategy Choices 164 Business-Level Strategy, Industry and Competitive Advantage 166 Strategy in Action 5.2: Microsoft Office versus Google Apps 167 Implementing Business-Level Strategy 168 Competing Differently: Searching for a Blue Ocean 171 	
Chapter 6	Business-Level Strategy and the Industry Environment	178
	<ul style="list-style-type: none"> Opening Case 178 Overview 179 Strategy in a Fragmented Industry 180 <ul style="list-style-type: none"> Reasons for Fragmentation 180 Consolidating a Fragmented Industry Through Value Innovation 181 Chaining and Franchising 182 Horizontal Mergers 183 Strategies in Embryonic and Growth Industries 184 <ul style="list-style-type: none"> The Changing Nature of Market Demand 185 Strategic Implications: Crossing the Chasm 188 Strategy in Action 6.1: Crossing the Chasm in the Smartphone Market 189 <ul style="list-style-type: none"> Strategic Implications of Differences in Market Growth Rates 190 Strategy in Mature Industries 191 <ul style="list-style-type: none"> Strategies to Deter Entry 192 Strategies to Manage Rivalry 194 Strategy in Action 6.2: Toyota Uses Market Development to Become the Global Leader 198 Strategy in Action 6.3: Non-Price Competition at Nike 199 Strategies in Declining Industries 201 <ul style="list-style-type: none"> The Severity of Decline 201 Choosing a Strategy 202 	
Chapter 7	Strategy and Technology	210
	<ul style="list-style-type: none"> Opening Case 210 Overview 211 Technical Standards and Format Wars 213 Strategy in Action 7.1: “Segment Zero”—A Serious Threat to Microsoft? 213 <ul style="list-style-type: none"> Examples of Standards 216 Benefits of Standards 217 	

<i>Establishment of Standards</i>	218
<i>Network Effects, Positive Feedback, and Lockout</i>	219
Strategies for Winning a Format War	222
<i>Ensure a Supply of Complements</i>	222
<i>Leverage Killer Applications</i>	222
<i>Aggressive Pricing and Marketing</i>	223
<i>Cooperate with Competitors</i>	223
<i>License the Format</i>	224
Costs in High-Technology Industries	224
<i>Comparative Cost Economics</i>	225
<i>Strategic Significance</i>	226
Strategy in Action 7.2: Lowering the Cost of Ultrasound	
Equipment Through Digitalization	227
Capturing First-Mover Advantages	227
<i>First-Mover Advantages</i>	229
<i>First-Mover Disadvantages</i>	229
<i>Strategies for Exploiting First-Mover Advantages</i>	230
Technological Paradigm Shifts	233
<i>Paradigm Shifts and the Decline of Established Companies</i>	234
Strategy in Action 7.3: Disruptive Technology in Mechanical	
Excavators	238
<i>Strategic Implications for Established Companies</i>	238
<i>Strategic Implications for New Entrants</i>	240

Chapter 8 Strategy in the Global Environment 246

Opening Case	246
Overview	247
The Global and National Environments	248
<i>The Globalization of Production and Markets</i>	248
<i>National Competitive Advantage</i>	250
Increasing Profitability and Profit Growth Through Global Expansion	253
<i>Expanding the Market: Leveraging Products</i>	253
<i>Realizing Cost Economies from Global Volume</i>	255
<i>Realizing Location Economies</i>	256
<i>Leveraging the Skills of Global Subsidiaries</i>	257
Cost Pressures and Pressures for Local Responsiveness	258
<i>Pressures for Cost Reductions</i>	259
<i>Pressures for Local Responsiveness</i>	259
Strategy in Action 8.1: Local Responsiveness at MTV	
Networks	260
Choosing a Global Strategy	261
<i>Global Standardization Strategy</i>	262
<i>Localization Strategy</i>	263
<i>Transnational Strategy</i>	264

	<i>International Strategy</i>	265
	<i>Changes in Strategy over Time</i>	265
	Strategy in Action 8.2: The Evolving Strategy of Coca-Cola	267
	The Choice of Entry Mode	268
	<i>Exporting</i>	268
	<i>Licensing</i>	269
	<i>Franchising</i>	270
	<i>Joint Ventures</i>	271
	<i>Wholly Owned Subsidiaries</i>	272
	<i>Choosing an Entry Strategy</i>	273
	Global Strategic Alliances	275
	<i>Advantages of Strategic Alliances</i>	275
	<i>Disadvantages of Strategic Alliances</i>	276
	<i>Making Strategic Alliances Work</i>	276
Chapter 9	Corporate-Level Strategy: Horizontal Integration, Vertical Integration and Strategic Outsourcing	286
	Opening Case	286
	Overview	287
	Corporate-Level Strategy and the Multibusiness Model	288
	Horizontal Integration: Single-Industry Corporate Strategy	289
	<i>Benefits of Horizontal Integration</i>	290
	Strategy in Action 9.1: Larry Ellison Wants Oracle to Become the Biggest and the Best	293
	<i>Problems with Horizontal Integration</i>	294
	Vertical Integration: Entering New Industries to Strengthen the “Core” Business Model	295
	<i>Increasing Profitability Through Vertical Integration</i>	297
	Strategy in Action 9.2: Specialized Assets and Vertical Integration in the Aluminum Industry	299
	<i>Problems with Vertical Integration</i>	301
	Alternatives to Vertical Integration: Cooperative Relationships	302
	<i>Short-Term Contracts and Competitive Bidding</i>	303
	<i>Strategic Alliances and Long-Term Contracting</i>	303
	Strategy in Action 9.3: Apple, Samsung, and Nokia Battle in the Smartphone Market	304
	<i>Building Long-Term Cooperative Relationships</i>	305
	Strategy in Action 9.4: Ebay’s Changing Commitment to Its Sellers	306
	Strategic Outsourcing	307
	Strategy in Action 9.5: Apple Tries to Protect Its New Products and the Workers Who Make Them	308
	<i>Benefits of Outsourcing</i>	310
	<i>Risks of Outsourcing</i>	311

Chapter 10	Corporate-Level Strategy: Related and Unrelated Diversification	318
	Opening Case	318
	Overview	322
	Increasing Profitability Through Diversification	322
	<i>Transferring Competencies Across Businesses</i>	323
	<i>Leveraging Competencies to Create a New Business</i>	324
	<i>Sharing Resources and Capabilities</i>	325
	<i>Using Product Bundling</i>	326
	<i>Utilizing General Organizational Competencies</i>	327
	Strategy in Action 10.1: United Technologies Has an “ACE” in Its Pocket	329
	Two Types of Diversification	331
	<i>Related Diversification</i>	331
	<i>Unrelated Diversification</i>	331
	The Limits and Disadvantages of Diversification	333
	<i>Changes in the Industry or Company</i>	333
	<i>Diversification for the Wrong Reasons</i>	334
	<i>The Bureaucratic Costs of Diversification</i>	335
	Strategy in Action 10.2: How Bureaucratic Costs Rose Then Fell at Pfizer	337
	Choosing a Strategy	338
	<i>Related Versus Unrelated Diversification</i>	338
	<i>The Web of Corporate-Level Strategy</i>	338
	Strategy in Action 10.3: Sony’s “Gaijin” CEO Is Changing the Company’s Strategies	340
	Entering New Industries: Internal New Ventures	341
	<i>The Attractions of Internal New Venturing</i>	341
	<i>Pitfalls of New Ventures</i>	342
	<i>Guidelines for Successful Internal New Venturing</i>	344
	Entering New Industries: Acquisitions	345
	<i>The Attraction of Acquisitions</i>	345
	<i>Acquisition Pitfalls</i>	346
	<i>Guidelines for Successful Acquisition</i>	348
	Entering New Industries: Joint Ventures	349
	<i>Restructuring</i>	350
	<i>Why Restructure?</i>	350

PART FOUR IMPLEMENTING STRATEGY

Chapter 11	Corporate Performance, Governance, and Business Ethics	359
	Opening Case	359
	Overview	361

Stakeholders and Corporate Performance	362
<i>Stakeholder Impact Analysis</i>	363
<i>The Unique Role of Stockholders</i>	363
<i>Profitability, Profit Growth, and Stakeholder Claims</i>	364
Strategy in Action 11.1: Price Fixing at Sotheby's and Christie's	366
Agency Theory	367
<i>Principal-Agent Relationships</i>	367
<i>The Agency Problem</i>	367
Strategy in Action 11.2: Self-Dealing at Hollinger International Inc.	371
Governance Mechanisms	372
<i>The Board of Directors</i>	372
<i>Stock-Based Compensation</i>	373
<i>Financial Statements and Auditors</i>	374
<i>The Takeover Constraint</i>	375
<i>Governance Mechanisms Inside a Company</i>	376
Ethics and Strategy	378
Strategy in Action 11.3: Nike—the Sweatshop Debate	379
<i>Ethical Issues in Strategy</i>	380
<i>The Roots of Unethical Behavior</i>	383
<i>Behaving Ethically</i>	384

Chapter 12 Implementing Strategy in Companies That Compete in a Single Industry 395

Opening Case	395
Overview	396
Implementing Strategy Through Organizational Design	397
Building Blocks of Organizational Structure	398
<i>Grouping Tasks, Functions, and Divisions</i>	399
<i>Allocating Authority and Responsibility</i>	399
Strategy in Action 12.1: Bob Iger Flattens Walt Disney	402
<i>Integration and Integrating Mechanisms</i>	403
Strategy in Action 12.2: Centralization and Decentralization at Union Pacific and Yahoo!	404
Strategic Control Systems	405
<i>Levels of Strategic Control</i>	407
<i>Types of Strategic Control Systems</i>	407
<i>Strategic Reward Systems</i>	410
Organizational Culture	410
<i>Culture and Strategic Leadership</i>	411
<i>Traits of Strong and Adaptive Corporate Cultures</i>	413
Building Distinctive Competencies at the Functional Level	414
<i>Functional Structure: Grouping by Function</i>	414
<i>The Role of Strategic Control</i>	415

<i>Developing Culture at the Functional Level</i>	416
<i>Functional Structure and Bureaucratic Costs</i>	418
<i>The Outsourcing Option</i>	419
Implementing Strategy in a Single Industry	419
<i>Implementing Cost Leadership</i>	421
<i>Implementing Differentiation</i>	421
<i>Product Structure: Implementing a Wide Product Line</i>	422
<i>Market Structure: Increasing Responsiveness to Customer Groups</i>	424
<i>Geographic Structure: Expanding by Location</i>	424
Strategy in Action 12.3: The HISD Moves from a Geographic to a Market Structure	426
<i>Matrix and Product-Team Structures: Competing in High-Tech Environments</i>	426
<i>Focusing on a Narrow Product Line</i>	429
Restructuring and Reengineering	430

Chapter 13 Implementing Strategy in Companies That Compete Across Industries and Countries

439

Opening Case	439
Overview	440
Corporate Strategy and the Multidivisional Structure	441
<i>Advantages of a Multidivisional Structure</i>	443
<i>Problems in Implementing a Multidivisional Structure</i>	444
Strategy in Action 13.1: Organizational Change at Avon	446
<i>Structure, Control, Culture, and Corporate-Level Strategy</i>	447
Implementing Strategy Across Countries	451
<i>The International Division</i>	451
<i>Worldwide Area Structure</i>	452
<i>Worldwide Product Divisional Structure</i>	454
<i>Global Matrix Structure</i>	455
Strategy in Action 13.2: Dow Chemical's Matrix Structure	457
Entry Mode and Implementation	458
<i>Internal New Venturing</i>	458
<i>Joint Ventures</i>	459
<i>Mergers and Acquisitions</i>	460

PART FIVE ANALYZING A CASE STUDY AND WRITING A CASE STUDY ANALYSIS

What is Case Study Analysis	C-2
Analyzing a Case Study	C-3
Writing A Case Study Analysis	C-8

The Role of Financial Analysis in Case Study Analysis C-9

Profit Ratios C-10

Liquidity Ratios C-11

Activity Ratios C-11

Leverage Ratios C-12

Shareholder-Return Ratios C-12

Cash Flow C-13

Conclusion C-14

Glossary G-1

Index I-1