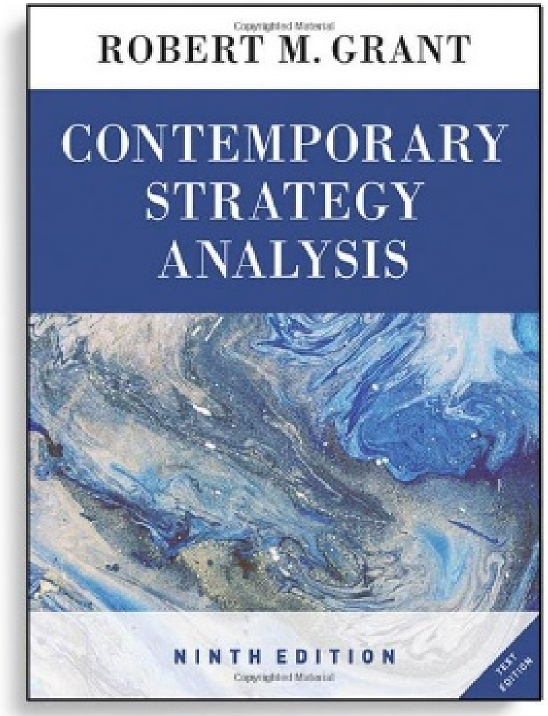
Chapter 4
Further Topics in Industry and Competitive Analysis



Further Topics in Industry and Competitive Analysis

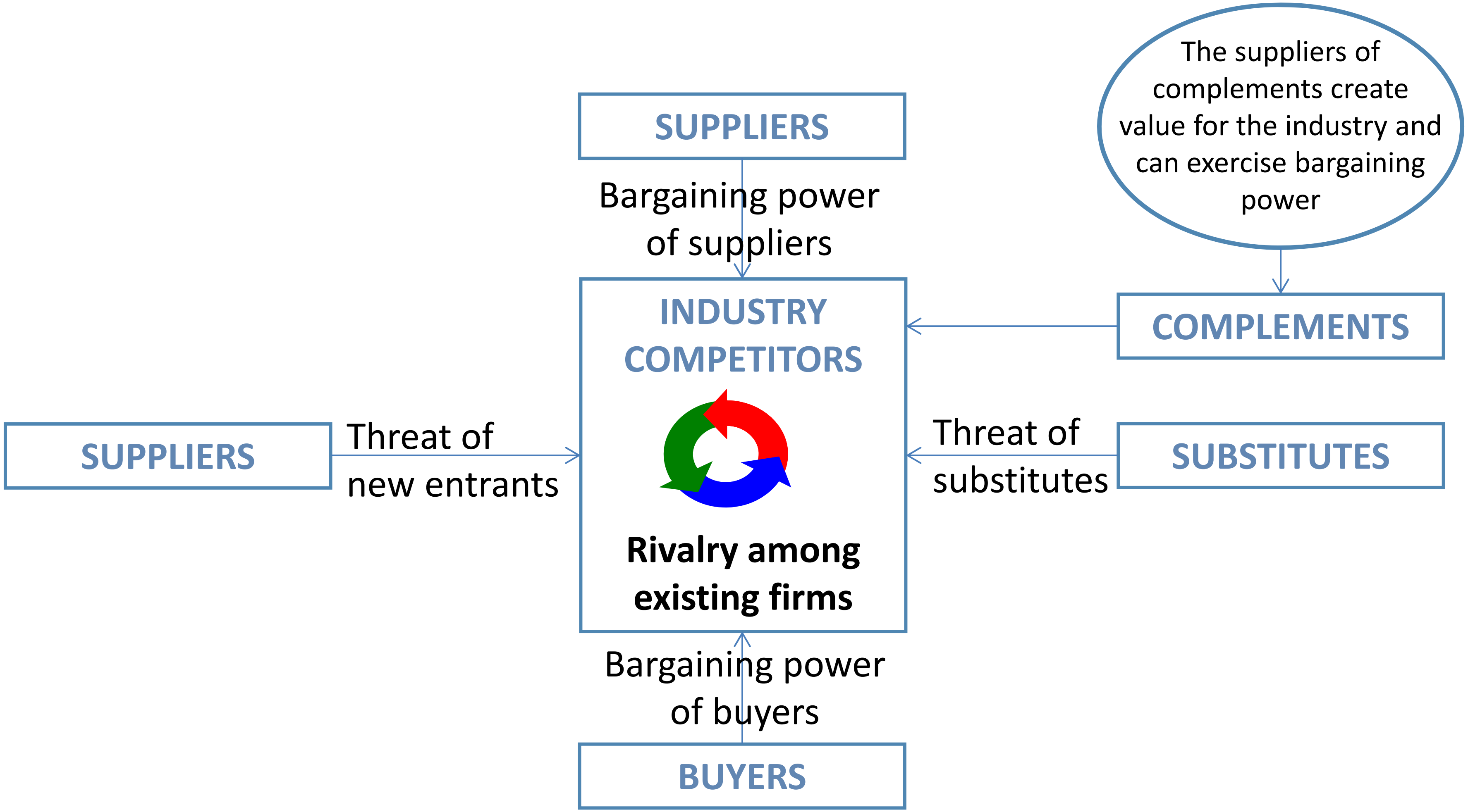
OUTLINE

- Extending 5-forces analysis
  - Does industry matter?
  - Complements
  - Dynamic competition
- Dynamic competition
  - “Schumpeterian” and “Hyper” competition
  - Game Theory (Nash Equilibrium)
  - Competitor Analysis
- Segmentation and strategic groups

Does Industry Matter?

	Percentage of variance in firms' return on assets explained by:		
	Industry effects (%)	Firm effects (%)	Unexplained variance (%)
Schmalensee (1985)	19.6	0.6	79.9
Rumelt (1991)	4.0	44.2	44.8
McGahan & Porter (1997)	18.7	31.7	48.4
Hawawini et al. (2003)	8.1	35.8	52.0
Roquebert et al. (1996)	10.2	55.0	32.0
Misangyi et al. (2006)	7.6	43.8	n/a

Five Forces or Six?
Introducing Complements



The Objectives of Industry Analysis

- Porter framework assumes:
  a) Industry structure drives competitive behaviour
  b) Industry structure is (fairly) stable
- But, competition also *changes* industry structure
  - **Schumpeterian Competition** – A "perennial gale of creative destruction" – market leaders over thrown by innovation
  - **Hypercompetition** – "Intense and rapid competition moves… continuously creating new competitive advantages and destroying existing competitive advantages
- Implication:
  - Within 5 forces framework
    INDUSTRY STRUCTURE → COMPETITIVE STRATEGY
  - Under dynamic competition
    COMPETITIVE STRATEGY → INDUSTRY STRUCTURE

The Contribution of Game Theory to Competitive Analysis

- Main value:
  1. Framing strategic decisions as interactions between competitors
  2. Predicting outcomes of competitive situations involving a few, evenly-matched players
- Some key concepts:
  1. **Competition** and **Cooperation** – Game theory can show conditions where cooperation is more advantageous than competition (**Prisoners' Dilemma**)
  2. **Deterrence** – Changing the payoffs in the game in order to deter a competitor from certain actions
  3. **Commitment** – Irrevocable deployments of resources that give credibility to threats
  4. **Signaling** – Communication to influence a competitor's decision

THE PRISONER'S DILEMMA

	B stays silent (cooperates)	B betrays A (defects)
A stays silent (cooperates)	Both serve 1 year	A serves 3 years, B goes free
A betrays B (defects)	A goes free, B serves 3 years	Both serve 2 years

- **Nash Equilibrium*** is the lower right cell
- **Cooperation** leads to more efficient outcome

The Contribution of Game Theory to Competitive Analysis

- Problems of Game Theory:
  - Useful in explaining past competitive behaviour – Weak in predicting future behaviour
  - Lack of an integrated general theory – Many different models; outcomes highly sensitive to small changes in assumptions

A Framework for Competitive Analysis

STRATEGY
How is the firm competing?

OBJECTIVES
What are competitor's current goals?
Is performance meeting their goals?
How are its goals likely to change?

ASSUMPTIONS
What assumptions does the competitor hold about the industry and itself?

RESOURCES & CAPABILITIES
What are the competitors' key strengths and weaknesses?

PREDICTIONS

- What strategy changes will the competitor initiate?
- How will the competitor respond to our strategic initiatives?

Segmentation Analysis: The Principal Stages

1. Identify key variables and categories
   - Identify segmentation variables
   - Reduce to 2 or 3 variables
   - Identify discrete categories for each vriable
2. Construct a segmentation matrix
3. Analyze segment attractiveness
4. Identify KSFs in each segment
5. Analyze benefits of broad vs. narrow scope
   - Potential for economics of scope across segments
   - Similarity of KSFs
   - Product differentiation benefits of segment focus

The Basis for Segmentation: The Characteristics of buyers and products

- Opportunities for Differentiation
  - Characteristics of the Buyers
    - Industrial Buyers
      - Size
      - Technical sophistication
      - OEM/replacement
    - Household Buyers
      - Demographics
      - Lifestyle
      - Purchase occasion
    - Distribution Channel
      - Size
      - Distributor/broker
      - Exclusive/nonexclusive
      - General/special list
    - Geographic Location
  - Characteristics of the Product
    - Physical size
    - Price level
    - Product features
    - Technology design
    - Inputs used (e.g. raw materials)
    - Performance characteristics
    - Pre-sales and post-sales service

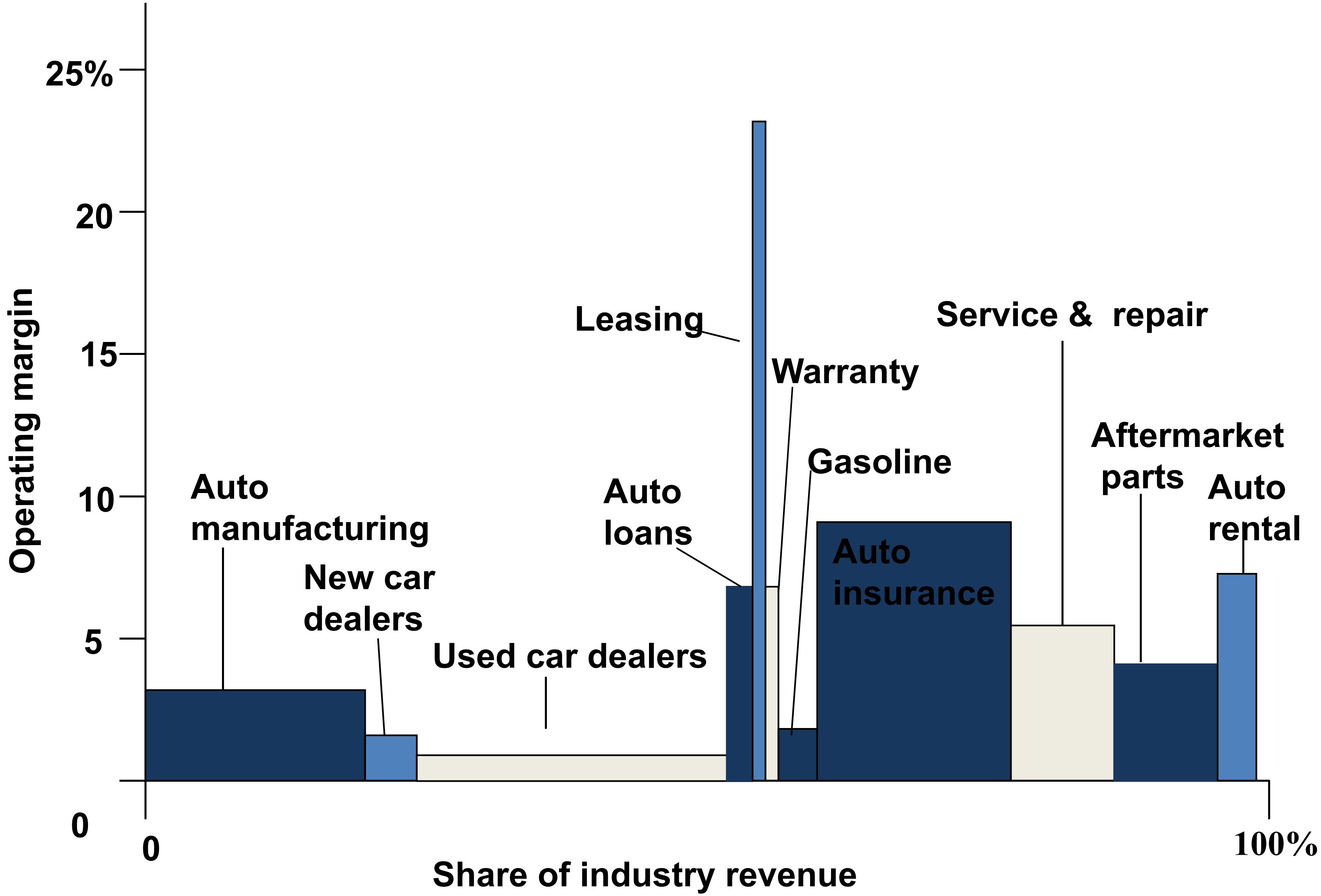
Segmenting the World Automobile Market

REGIONS

PRODUCTS

	North America	Latin America	W. Europe	E. Europe	East Asia	South Asia	Pacific	Africa/ Middle East
Luxury cars								
Large family cars								
Mid-size family cars								
Compact family cars								
Mini cars								
Sports cars								
SUVs								
Multi-purpose vehicles								
Pickup trucks								
Hybrid cars								
Electric cars								

Vertical Segmentation & Industry Profit Pools: The US Auto Industry



Segmentation & Key Success Factors: The US Bicycle Market

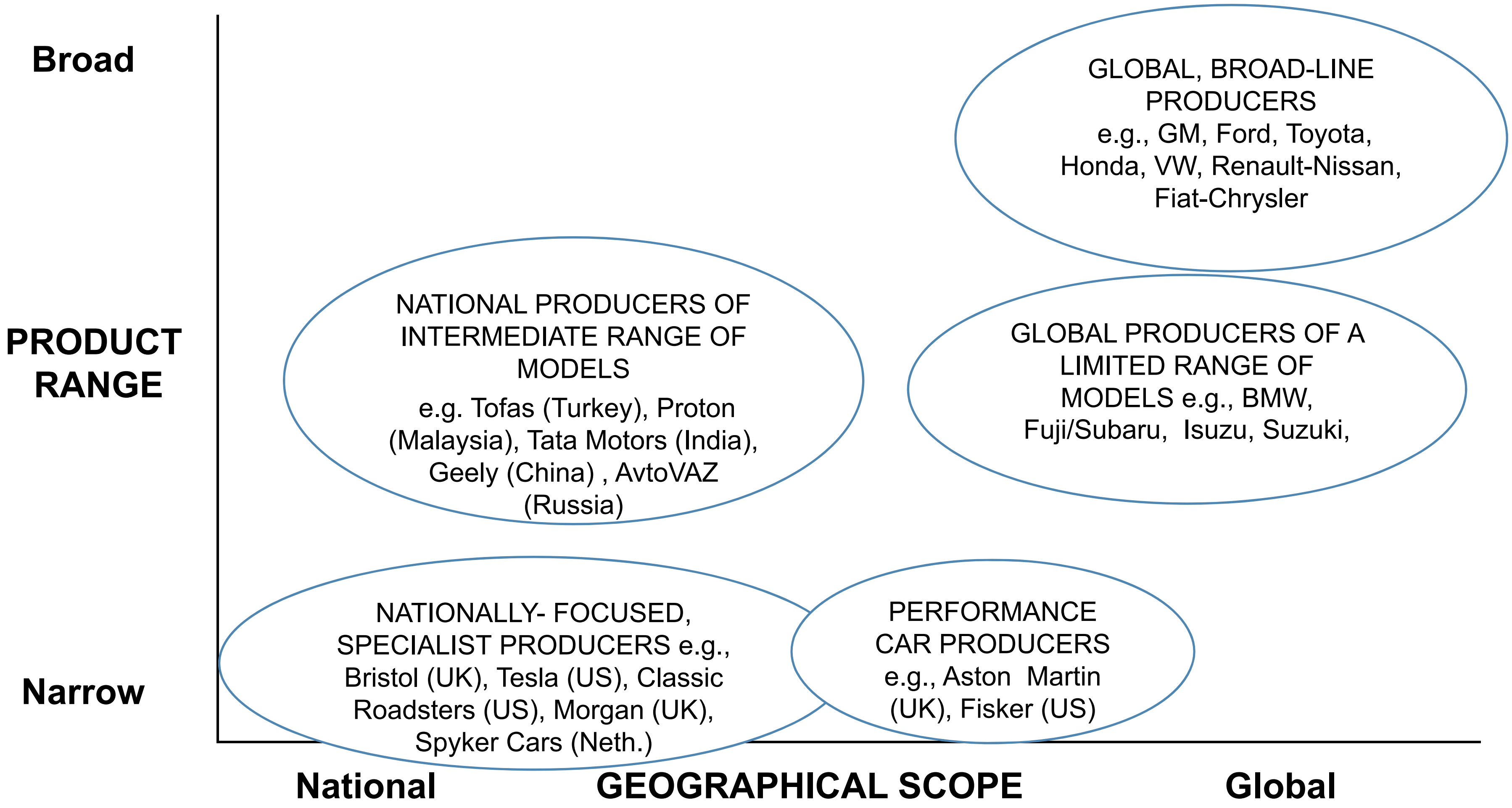
Segment	Key Success Factors
Low price bicycles sold primarily through department and discount stores, mainly under the retailer's own brand	Low cost through global sourcing of components and low wage assembly Supply contract with major retailer *Leading competitors*: Assemblers in Taiwan & China and a few US manufacturers
Medium-priced bicycles sold mainly under manufacturer's brand; distributed through soecialist cycle stores	Cost efficiency through Iscale and low wage costs Reputation for quality Good dealer reputation International marketing and & distribution *Leading competitors*: Raleigh, Peugeot, Fuji
High-priced bicycles for enthusiasts	Quality components and assembly Design innovation – e.g. less weight/wind resistance Reputation (e.g. success in racing) Strong dealer relations
Children's bicycles/tricycles sold through discount stores and toy stores	Similar to low price bicycle segment

Strategic Group Analysis

- A **strategic group** is a group of firms in an industry that follow the same or similar strategies

- Identifying strategic groups:
  - o Identifying principal strategic variables which distinguish firms
  - o Position each firm in relation to these variables
  - o Identify clusters

Strategic Group Within the World Automobile Industry



Strategic Groups Within the World Petroleum Industry