

Cost leadership and differentiation strategies

[Business](#), [Strategic Management](#)



In the competitive market industries of category of domestic, international or global have very competitive rivalry. Cost leadership and differentiation strategies are commonly used strategic management dimensions in the literature. Eg: German's Automotive, Tesco supermarket, IKEA. Competitive Strategy: It is the way by which firms choose to accomplish and hold their competitive advantage. Regarding competitive strategy Porter stated that "taking offence or defensive actions to create a defensible position in an industry, to cope with competitive forces and thereby yield a superior return for the firm". Companies have established different approaches to competitive strategy, as per the crisis companies should apply respective strategy. The basic of generic strategy:

Porter stated that company's strength is divided into two attributes: cost advantage and differentiation. By applying these attributes in a broad and narrow focus, three generic strategies result: cost leadership, differentiation and focus. They do not represent any industry nor they are specific to any company. Diagram 1: (Porter, 1980) Normally means "pursue a quality approach". Enables a price premium to be charged for the quality difference. Normally means "pursue a quality approach". Enables a price premium to be charged for the quality difference.

Concentrate on one or a small number of market segments. Can be differentiation or cost leadership. Concentrate on one or a small number of market segments. Can be differentiation or cost leadership. Porter initially advised Firms to avoid attempting both Strategies - Stuck in the Middle - as out and out differentiators and cost leaders will tend to be more competitive.

The success of Japanese (and other) firms with JIT, Kaizen and TQM techniques appears to provide evidence contrary to this view.

Cost Leadership aim requires strong focus on supply side as oppose to demand side of market - with high level competitor orientation (Day & Wendley, 1988). Cost Leadership strategy used by companies must benchmark them in a profitable position in the market place. As per Porter (1980), efficient cost leadership strategy minimizes cost in areas like R&D, Services, Sales and Advertising. In Japan, Toyota Company has successfully implemented cost leadership strategy with increased efficiency (Schonberger, 1994) which is a different factor make up in this strategy when compared to the western countries. Allen & Helms, 2001) Differentiation Strategy - The generic of differentiation strategy can be based upon design and brand image, distribution & so forth (Frambach. Et al. 2003). It involves by creating a place in the market that is realized as being different in the industry and has the capability to endure for a long run (Porter, 1980). The effectiveness of strategy depends on competitive offering to customers (Slater & Olson, 2001) with unique product for varied customer groups. This is with the aim to create minimum price of product in order to develop satisfaction andloyalty.

A firm with differentiation strategy creates superior characteristics in terms of image, reputation, reliability andequality(Dean & Evans, 1994; Sashi and Stern, 1995). This creates qualitative difference in products & service, engaged in advertising programs, marketing techniques with premium prices (Miller, 1986). According to Acquaah and Yasai - Ardekani (2006). Firms with

competitive strategies has advantage over their rivals as they realized how unique their products and services are.

The differentiation strategy has been successfully implemented in France, Sweden, Canada with companies having advantage of Financial and technology resources, human capital and modern management (Aulakh et al, 2000) Focus Porter defined focus as one of the generic strategies but later on mentioned it as moderator of cost leadership and differentiation strategy, Companies which apply this strategy normally focus on the market where there are less competition. (Pearson, 1999). Firms use this strategy to stress on a specific positioning in the market and so it offers quality and specialized products for that position.

Therefore sometimes focus strategy is referred as niche strategy (Lynch, 2003). This strategy allows the firm the possibility to charge a premium price for its specialized products. Ferrari and Rolls - Royce are examples of company using such strategy. The only problem with the strategy is that niche characteristic is not sufficient to justify company's attention. Stuck in the middle - When a company fails to make a choice between the strategies then it is implied that the company is stuck in the middle. Thus affecting its profitability and resulting poor financial performance. (Peter, 1980)

The Porter Generic competitive Strategies (1980, 1985) can't be given excessive prominence. Competitive forces (Allen and Helms, 2006; Miller, 1992; Spanos, et al. , 2004) has been termed " hybrid, mixed, integrated or combination strategies. (Kim. Et al. , 2004; Spanos, et al. , 2004). They combine both low cost and differentiation elements (Gopalakrishna and Subramanian, 2001; Proff, 2000). A combination of cost leadership and

<https://assignbuster.com/cost-leadership-and-differentiation-strategies/>

differentiation strategies should be distinguish from ' stuck in the middle' where firm fails to successfully pursue both. (Acquaah & Yasai - Ardekani, 2006).

A combination or hybrid strategy has been proved to be viable and profitable (Kim et al. , 2004; Miller & Dess, 1993; Wright et al. , 1991). Firms pursuing combined strategy achieved higher performance than the other firms which apply single strategy. Combined strategy also helps the firm to minimize their vulnerability due to reliance on cost - based advantages only (Yasai - Ardekani & Nystrom, 1996). This hybrid strategy success depends on ability to deliver enhanced benefit to customers with low price and sufficient margins to reinvestment. Tesco Supermarket is following same the same strategy (Strategy Explorer, 2010)

Cost Leadership Strategy: The cost leadership strategy is the basis for long - run compare to price competition. Price competition is easily duplicated (Porter, 1980; Ellis & Kelly, 1992). In retail business cost reduction must be exploited which minimizes cost throughout value chain activities. Important issues in retail business are related with cost of goods sold. (COGS). Large retail business achieve more easily cost leadership due to more power supplier to secure low procurement prices for purchased goods (Ellis & Kelley, 1992; Anderer, 1997).

Datuk Tony Fernandez as CEO of AirAsia Berhad said " Before business can grow it needs to have its cost under control, efficient and profitable and also it must create value". AirAsia leader of LCC in Malaysia, Thailand and Indonesia will face competition from existing and new players and it need to make consideration & more stressed for the point of becoming the low cost

<https://assignbuster.com/cost-leadership-and-differentiation-strategies/>

carrier in the airline industries. Differentiation Strategy: It emphasis several dimensions such as image, gain customer loyalty, innovation and level of service (Kim et al. , 2004) by generating differences n product through intensive marketing & image management (Miller 1988) and creating products which are innovative, dependable, durable, and serviceable (Beal & Yasai - Ardekani, 2000)

The implementation of combination of Cost Leadership and Differentiation Strategy (Hybrid Strategy): This new hybrid strategy may become even more important and more popular as Global competition increase. With generic strategy company improve their ability to adapt quickenvironmentchanges and learn new skills and technologies involving customer's value with products at low cost compare to competitor's products. Cost leadership enables the company to charge the lowest competitive price and achieving competitive advantage by delivering value to customers based on both product features and low price.

Competitive strategy is not only feasible but generates superior incremental performance result in multiple sources of competitive advantage. This will generate superior performance over the inability to success. The success of Japanese companies such as Toyota, Canon and Honda are best examples of cost leadership and differentiation strategies. (Ishikura, 1983). Porter's Generic Strategies in Hospitality Industry: 1. Cost Leadership Strategy: Hotelier such as Fairfield Inns, Etap offer services which are basics. Thus by doing so, they keep the cost at minimum and attract lot of market segment. . Differentiation Strategy: Chain of hotels such as Marriott and Hilton apply this strategy by providing guests with high quality and special service and

experience. 3. Focus Strategy: Four Seasons only stress on elite guests and Burj Al Arab hotel only target guests such as royal families, celebrities, and rich industrialists. Five Forces Analysis: Porter developed this model as a framework to understand the profitability about the industry.

Successful organization adopts a combination of competitive aspect to build a hybrid strategy. i. e. Design and low cost, quality and price . Only competing on price is not good enough (Daan Assens's Learning , 2010). Cost leadership and differentiation strategies are very successful in much different kind of industries, for developing, transition and developed economics. Cost leadership, Differentiation and hybrid strategies have been successfully applied for very broad range of products and services from retail products to luxury products.