Advanced Marketing Management

An International Business Perspective

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In relation to the Indian software industry, most firms in the Bangalore area experience fierce competition. The competition about future customers is not just with local firms, but also with firms outside Bangalore and multinational companies such as IBM and Accenture. Competition has resulted in a pressure on firms to deliver quality products and services, but also to be cost-effective. It has also encouraged firms to seek international certifications, with a rating in software development. Today, the Bangalore area has the world's highest concentration of companies with the so-called CMM-SEI (Carnegie Mellon University's Software Engineering Institute) Level 5 certification (the highest quality rating).

Government

According to Porter's diamond model, governments can influence and be influenced by each of the four main factors. Governments can play a powerful role in encouraging the development of industries within their own borders that will assume global positions. Governments finance and construct infrastructure, providing roads, airports, education and health care, and can support use of alternative energy (e.g. wind turbines) or other environmental systems that affect factors of production.

In relation to the Indian software industry, the federal government in Delhi had already targeted software as a growth area in the 1970s, because of its high skill requirements and labour intensity. Through the 1970s and 1980s, the industry was mainly dominated by public-sector companies like CMC. In 1984, the government started liberalizing industrial and investment policies, which gave access to IT companies from abroad (e.g. Texas Instruments). One of the new initiatives was also setting up 'technology parks', e.g. the Software Technology Park (STP) in Bangalore. The liberation policy continued throughout the 1980s and 1990s. In 1988, the National Association of Software and Service Companies (NASSCOM) was formed. NASSCOM is an association of IT firms, which acts as a catalyst for industry growth by supporting IT research and education in India. In 1999, the Ministry of Information Technology was set up to coordinate the IT initiatives at government, academic and business levels. Thus Bangalore's success in becoming a software hub was contributed to by the state government's active role in the early and later stages of the industry's evolution.

Chance

According to Porter's diamond, national/regional competitiveness may also be triggered by random events.

When we look at the history of most industries we also see the role played by chance. Perhaps the most important instance of chance involves the question of who comes up with a major new idea first. For reasons having little to do with economics, entrepreneurs will typically start their new operations in their home countries. Once the industry begins in a given country, scale and clustering effects can cement the industry's position in that country.

In relation to the development of competitiveness of the Indian software industry (especially in Bangalore) two essential events can be identified:

1. the Y2K problems (described earlier), which created an increased demand for services of Indian software firms;
2. the collapse of the dotcom boom in 2001 in the US and Europe, resulting in a search for ways to cut costs by outsourcing software functions to India.

From the firm's point of view, the last two variables, chance and government, can be regarded as exogenous variables that the firm must adjust to. Alternatively, the government may be considered susceptible through lobbying, interest organizations and mass media.

In summary, we have identified six factors that influence the location of global industries: factors of production, home demand, the location of supporting industries, the internal structure of the domestic industry, chance and government. We have also suggested that these factors are interconnected. As industries evolve, their dependence on particular locations may also change. For example, the shift in users of semiconductors from the military to the electronics industry has had a profound effect on the shape of the national diamond in that industry. To the extent that governments and firms recognize the source of any locational advantages they have, they will be better able to both exploit those differences and anticipate their shifts.

In relation to the software industry in India (Bangalore), which was used throughout the diamond model, the following conclusions may be arrived at (Nair *et al.*, 2007):

- The software industry in Bangalore started off by serving not only its domestic customers but also the demanding North American customers. Also the rivals for software firms tend not to be so much local but global.
- The support needed for software services is much less sophisticated than for manufacturing. For the manufacturing sector it is also important to have access to a well-functioning physical infrastructure (transport, logistics, etc.), which is not necessary for the software industry where most of the logistics can be done over the internet. That is one of the reasons why Bangalore's software industry created international competitiveness but the manufacturing sector did not.
- The software industry is very much dependent on advanced and well-educated human resources as the key factor input.

While the Bangalore-based firms started off at the low end of the value chain (performing coding work for the Y2K problem) they have continuously moved in the direction of delivering more value-added services in emerging areas.

The 'double diamond' and 'multiple diamond' framework

Double diamond
The international competitiveness of an industry in a country is not only dependent on its home country diamond conditions but also on those of trading partners.

A key limitation of Porter's (1990) diamond model is its main focus on solely home country conditions (Rugman *et al.*, 2012). The **double diamond** framework addresses this concern. Rugman and D'Cruz (1993) suggested that the international competitiveness of Canadian firms depended not only on their home country diamond conditions but also on those of their trading partner, the US. Consequently, the sources of a firm's international competitive advantage are not only limited to the home country advantages, according to Porter's single diamond model, but they can also be achieved by sensing and developing competitive advantages in relationship with multiple 'diamonds' in several host countries.

4.3 Competition analysis in an industry

The next step in understanding the firm's competitiveness is to look at the competitive arena in an industry, which is the top box in the diamond model (see Figure 4.1).

One of the most useful frameworks for analysing the competitive structure was developed by Porter. Porter (1980) suggested that competition in an industry is rooted in its underlying economic structure and goes beyond the behaviour of current competitors. The state of competition depends upon five basic competitive forces, as shown in Figure 4.1. Together these factors determine the ultimate profit potential in an industry, where profit is measured in terms of long-run return on invested capital. The profit potential will differ from industry to industry.

To make things clearer we need to define a number of key terms. An *industry* is a group of firms that offer a product or class of products that are close substitutes for each other. Examples are the car industry and the pharmaceutical industry (Kotler, 1997, p. 230). A *market* is a set of actual and potential buyers of a product and sellers. A distinction will be made between industry and market level, as we assume that the industry may contain several different markets. This is why the outer box in Figure 4.1 is designated 'industry level' and the inner box 'market level'.

Porter's five-forces model
The state of competition and profit potential in an industry depends on five basic competitive forces: new entrants, suppliers, buyers, substitutes and market competitors.

Thus the *industry level* (**Porter's five-forces model**) consists of all types of actors (new entrants, suppliers, substitutes, buyers and market competitors) that have a potential or current interest in the industry.

The *market level* consists of actors with a current interest in the market, i.e., buyers and sellers (market competitors). In Section 4.4 (value chain analysis) this market level will be further elaborated on, as the buyers' perceived value of different competitor offerings will be discussed.

Marketing myopia
The failure of a company to define its organisational purpose from a broad consumer orientation.

Although division into the above-mentioned two levels is appropriate for this approach, Levitt (1960) pointed out the danger of '**marketing myopia**', where the seller defines the competition field (i.e. the market) too narrowly. For example, European luxury car manufacturers showed this myopia with their focus on each other rather than on the Japanese mass manufacturers, who were new entrants into the luxury car market.

The goal of competition analysis is to find a position in industry where the company can best defend itself against the five forces, or can influence them in its favour. Knowledge of these underlying pressures highlights the critical strengths and weaknesses of the company, shows its position in the industry, and clarifies areas where strategy changes yield the greatest payoff. Structure analysis is fundamental for formulating competitive strategy.

Each of the five forces in the Porter model in turn comprises a number of elements that combine to determine the strength of each force, and its effect on the degree of competition. Dobbs (2014) provide practitioners and students with a practical and highly recommended set of templates for applying Porter's five forces framework for industry analysis. Each of the five forces is now discussed.

Market competitors

The intensity of rivalry between existing competitors in the market depends on a number of factors:

- *The concentration of the industry*. Numerous competitors of equal size will lead to more intense rivalry. There will be less rivalry when a clear leader (at least 50 per cent larger than the second) exists with a large cost advantage.
- *Rate of market growth*. Slow growth will tend towards greater rivalry.
- *Structure of costs*. High fixed costs encourage price cutting to fill capacity.
- *Degree of differentiation*. Commodity products encourage rivalry, while highly differentiated products, which are hard to copy, are associated with less intense rivalry.
- *Switching costs*. When switching costs are high because the product is specialized, the customer has invested a lot of resources in learning how to use the product or has made tailor-made investments that are worthless with other products and suppliers (high asset specificity), rivalry is reduced.
- *Exit barriers*. When barriers to leaving a market are high due to such factors as lack of opportunities elsewhere, high vertical integration, emotional barriers or the high cost of closing down plant, rivalry will be more intense than when exit barriers are low.

Firms need to be careful not to spoil a situation of competitive stability. They need to balance their own position against the well-being of the industry as a whole. For example, an intense price or promotional war may gain a few percentage points in market share, yet

lead to an overall fall in long-run industry profitability as competitors respond to these moves. It is sometimes better to protect industry structure than to follow short-term self-interest.

Suppliers

The cost of raw materials and components can have a major bearing on a firm's profitability. The higher the bargaining power of suppliers, the higher the costs. The bargaining power of suppliers will be higher in the following circumstances:

- Supply is dominated by few companies and they are more concentrated than the industry they sell to.
- Their products are unique or differentiated, or they have built up switching costs.
- They are not obliged to contend with other products for sale to the industry.
- They pose a credible threat of integrating forwards into the industry's business.
- Buyers do not threaten to integrate backwards into supply.
- The market is not an important customer to the supplier group.

A firm can reduce the bargaining power of suppliers by seeking new sources of supply, threatening to integrate backwards into supply and designing standardized components so that many suppliers are capable of producing them.

Buyers

The bargaining power of buyers is higher in the following circumstances:

- Buyers are concentrated and/or purchase in large volumes.
- Buyers pose a credible threat of integrating backwards to manufacture the industry's product.
- Products they purchase are standard or undifferentiated.
- There are many suppliers (sellers) of the product.
- Buyers earn low profits, which create a great incentive to lower purchasing costs.
- The industry's product is unimportant to the quality of the buyer's products, but price is very important.

Firms in the industry can attempt to lower buyer power by increasing the number of buyers they sell to, threatening to integrate forward into the buyer's industry and producing highly valued, differentiated products. In supermarket retailing, the brand leader normally achieves the highest profitability, partly because being number one means that supermarkets need to stock the brand, thereby reducing buyer power in price negotiations.

Customers who purchase the product but are not the end user (such as original equipment manufacturers [OEMs] or distributors) can be analysed in the same way as other buyers. Non-end-customers can gain significant bargaining power when they can influence the purchasing decision of customers downstream (Porter, 2008). Over the years, ingredient supplier DuPont has created enormous clout by advertising its Teflon brand not only to the manufacturers of cooking equipment, but also to downstream end-customers (households).

Substitutes

The presence of substitute products can reduce industry attractiveness and profitability because they put a constraint on price levels.

If the industry is successful and earning high profits, it is more likely that competitors will enter the market via substitute products in order to obtain a share of the potential profits available. The threat of substitute products depends on the following factors:

- the buyer's willingness to substitute;
- the relative price and performance of substitutes;
- the costs of switching to substitutes.

The threat of substitute products can be lowered by building up switching costs. These costs may be psychological. Examples are the creation of strong, distinctive brand personalities, and maintaining a price differential commensurate with perceived customer values.

New entrants

New entrants can serve to increase the degree of competition in an industry. In turn, the threat of new entrants is largely a function of the extent to which barriers to entry exist in the market. Some key factors affecting these entry barriers include the following:

- economies of scale;
- product differentiation and brand identity, which give existing firms customer loyalty;
- capital requirements in production;
- switching costs – the cost of switching from one supplier to another;
- access to distribution channels.

Because high barriers to entry can make even a potentially lucrative market unattractive (or even impossible) to enter for new competitors, the marketing planner should not take a passive approach but should actively pursue ways of raising barriers to new competitors.

High promotional and R&D expenditures and clearly communicated retaliatory actions to entry are some methods of raising barriers. Some managerial actions can unwittingly lower barriers. For example, new product designs that dramatically lower manufacturing costs can make entry by newcomers easier.

Strategic groups

Strategic group
A group of firms (or strategic business units, or brands) operating within an industry where the firms (or strategic business units, or brands) within the group compete for the same group of customers (segment), using similar market-related strategies.

A **strategic group** can be defined as a group of companies (or strategic business units, or brands) operating within an industry where the firms (or strategic business units, or brands) within the group compete for the same group of customers (segment), using similar market-related strategies. An industry could have only one strategic group if all the firms followed essentially the same strategy. At the other extreme, each firm could be a different strategic group.

Companies in different strategic groups compete for a different group of customers using strategies that are different from those of other strategic groups. So different strategic groups do not compete with each other, as they are pursuing different groups of customers.

Strategic group analysis is then a technique used to provide management with information about the firm's position in the market and a tool to identify their direct competitors. The five-forces industry analysis will form the first step in this process (Porter, 1980). After having identified the forces, the major competitors in the industry based on competitive variables will also be outlined. Competitors will then be divided into strategic groups based on similarities in strategies and competitive positions. For this purpose, Porter's three generic strategies (low cost, differentiation and focus) can be used (Porter, 1985).

For example, in the car industry, consumers who buy low-priced brands, such as Suzuki, Kia or Hyundai, buy them because they are inexpensive (low-cost strategy), while

those who buy a Toyota Camry or Honda Accord, say (differentiation strategy), are willing to pay a higher price for a car that is bigger, has more features/options, is more reliable, and so on. Finally, people who buy a Rolls-Royce or Jaguar (focus strategy) are willing to pay a fortune for something that is unique and prestigious.

Often a two-dimensional grid is made to position firms along an industry's two most important dimensions in order to distinguish direct rivals (those with similar strategies or business models) from indirect rivals. Firms may try to shift to a more favourably situated group, and how hard such a move proves to be will depend on whether entry barriers for the target strategic group are high or low.

The collaborative five-sources model

Porter's original model is based on the hypothesis that the competitive advantage of the firm is best developed in a very competitive market with intense rivalry relations.

The five-forces framework thus provides an analysis for considering how to squeeze the maximum competitive gain out of the context in which the business is located – or how to minimize the prospect of being squeezed by it – on the five competitive dimensions that it confronts.

Over the past decade, however, an alternative school (e.g. Reve, 1990; Kanter, 1994; Burton, 1995) has emerged which emphasizes the positive role of cooperative (rather than competitive) arrangements between industry participants, and the consequent importance of what Kanter (1994) has termed 'collaborative advantage' as a foundation of superior business performance.

An all-or-nothing choice between a single-minded striving for either competitive or collaborative advantage would, however, be a false one. The real strategic choice problem that all businesses face is where (and how much) to collaborate, and where (and how intensely) to act competitively.

Put another way, the basic questions that firms must deal with in respect of these matters are as follows:

- choosing the combination of competitive and collaborative strategies that are appropriate in the various dimensions of the industry environment of the firm;
- blending the two elements together so that they interact in a mutually consistent and reinforcing (and not counterproductive) manner;
- in this way, optimizing the firm's overall position, drawing upon the foundation and utilization of both collaborative and competitive advantage.

This points to the imperative in the contemporary context of complementing the competitive strategy model with a sister framework that focuses on the assessment of collaborative advantage and strategy. Such a complementary analysis, which is called the *five-sources framework* (Burton, 1995), is outlined below.

Five-sources model
Corresponding to Porter's five competitive forces, there are also five potential sources for building collaborative advantages together with the firm's surrounding actors.

Corresponding to the array of five competitive forces that surround a company – as elaborated in Porter's treatment – there are also five potential sources for the building of collaborative advantage in the industrial environments of the firm (the **five-sources model**). These sources are listed in Table 4.1.

In order to forge an effective and coherent business strategy, a firm must evaluate and formulate its collaborative and competitive policies side by side. It should do this for two purposes:

1. to achieve the appropriate balance between collaboration and competition in each dimension of its industry environment (e.g. relations with suppliers, policies towards customers/channels);
2. to integrate them in a way that avoids potential clashes and possibly destructive inconsistencies between them.