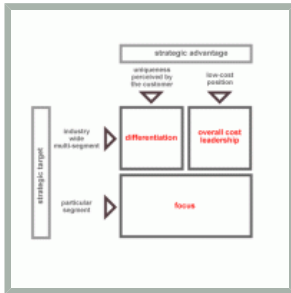


## three generic strategies



### characteristics

author:	Porter, Michael E.
country:	United States
period:	1980
type:	model
role:	consultant and manager
activity:	design, plan and implement
topic:	strategic management
abstr. level:	environment
perspective:	living
status:	final
module:	classics I
comments:	2

### description:

Michael Porter regarded the selection of a defensible position within an industry as the end result of a competitive strategic analysis. He argued that successful, profitable companies generally choose to compete on either low costs or by differentiating their products to meet specific customer needs. Although these two strategic options are mutually exclusive, he added a third category of firms as niche players that serve a specific market or product segment. Porter's three generic strategies are:

#### 1. COST LEADERSHIP

pursue lower costs in a broad target market;

#### 2. DIFFERENTIATION

deliver differentiated products and services to a broad target market;

#### 3. FOCUS

either pursue lowest cost or deliver differentiated products to a specific niche market.

Porter emphasized the mutual exclusivity of cost leadership and differentiation based on his observation that companies risk getting 'stuck in the middle' where competitors surpass them both on cost and superior product offerings. The distinction between the two options applies as well to his 3. focus strategy.

The industry's character determines the range of effective strategies. In a commodity market, only costs matter. In economic terms, this means " *perfect competition* ". The haute couture business, on the other hand, is driven solely by differentiation. Price is not a factor in a customer's purchase decision. Most industries tend to be mixed where one cost leader flourishes and opportunity exists for multiple differentiators.

Porter proposed a three stage analysis to determine and execute a competitive strategy:

1. analyse and choose the industry in which to compete (five forces);
2. analyse and choose the organisation's competitive strategy (generic strategies);
3. implement the strategy by managing the firm's activities (value chain analysis).

A firm's position must be modified when the relationship between the five forces in the industry change.

### assets:

 drivers of profitability  
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 four principal diagnosis components  
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 three generic strategies  
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### pros:

- Porter's generic strategies captured the tension between cost and differentiation. Organisations normally operate with a higher cost base when they produce and sell a premium product that customers highly value. His model showed that differentiation is as effective a strategy as cost leadership.
- No best strategy exists. Choosing a strategic position depends on time and circumstance. Implementation must be consistent once a position has been selected.
- Porter based his model on Chandler's assumption that 'structure follows strategy'. Organisations require different sets of structural traits to accommodate either a low cost or a differentiation strategy. The selection of a generic strategy provides direction to management and staff that helps them acquire internal consistency between management style, reward system, recruiting policy, etc.

### cons:

- The model applies best to large and established companies. Porter directed his analysis primarily on large multinationals with multiple strategic business units. Although the ideas behind the model still hold for smaller organisations, the tools are too heavy and all encompassing to provide valuable insight for them.
- Porter stressed the importance of choosing one generic strategy and following it through. In the late 70's, Porter saw too many US companies 'stuck in the middle' and unable to compete on a global scale. However, current opinion among strategy theorists holds that the generic strategies should not be treated as absolutes, but as a continuum. The objective of a strategy process is to find strategic positions where the widest gap exists between relative cost and the level of differentiation. An organisation then provides customers the most features at lower cost than its competitors.
- The Value Chain is used to analyse a firm's position in relation to its direct competitors with the assumption that rivalry drives profitability. This excludes other assumptions such as customer bonding

in Alexander Hax's delta model.

- Porter stated that competitive strategic analysis needs to happen on an ongoing basis. Mintzberg argued that real strategy is fuzzy at best. Even when a quantitative/economic change in the industry's conditions is detected, the reaction is frequently too late to realign the company. Most change occurs bottom-up, intuitively and creatively, and can be detected early using soft data rather than hard data.

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