

Question Paper

Business Policy & Strategy (MB311) : July 2004

Section A : Basic Concepts (30 Marks)

- This section consists of questions with serial number 1 - 30.
- Answer all questions.
- Each question carries one mark.
- Maximum time for answering Section A is 30 Minutes.

1. Which of the following control reflects the need to thoroughly reconsider the firm's basic strategy based on a sudden unexpected event?

- (a) Implementation control (b) Special alert control
(c) Premise control (d) Operational control
(e) Strategic surveillance.

[< Answer >](#)

2. The reasons for a company to go in for divestitures is

- (a) The company might want to increase its market share
(b) The assets of divested company are interfering with profitable operation of the seller
(c) The subsidiary might be losing money
(d) Both (b) and (c) above
(e) Both (a) and (c) above.

[< Answer >](#)

3. Which of the following management tools lays emphasis on the improvement of given business operation or a process through the exploitation of 'best practices'?

- (a) Reengineering (b) Reverse engineering
(c) Balanced Scorecard (d) Benchmarking
(e) None of the above.

[< Answer >](#)

4. The merger between Merck, a large manufacturer of pharmaceuticals and Medco, a large distributor of pharmaceuticals is a type of

- (a) Spin-off (b) Sell-off (c) Conglomerate merger
(d) Market Extension Merger (e) Vertical Merger.

[< Answer >](#)

5. The difference between a merger and a joint venture is

- (a) There is no profit sharing in joint ventures while in mergers partners share their profits
(b) In joint venture when two firms combine there is no organizational autonomy left between them while it is not so in the case of mergers
(c) When two firms go for a joint venture they maintain their separate legal entity whereas it is not the case with merger
(d) Joint venture is for unforeseeable future which is not the case with mergers
(e) In joint venture there is no expectation of profit.

[< Answer >](#)

6. Which of the following statements is **true** about a standstill agreement?

- (a) A standstill agreement is a voluntary contract in which the stockholder who is bought out, agrees to abstain from making further investments in the target company for a specified period of time
(b) A standstill agreement is a voluntary contract in which the stockholder who is bought out, agrees to make further investments in the target company for a specified period of time
(c) A standstill agreement is a forced contract in which the stockholder who is bought out, agrees to abstain from making further investments in the target company for a specified period of time
(d) A standstill agreement is a forced contract in which the stockholder who is bought out agrees to make further investments in the target company for a specified period of time
(e) All of the above.

[< Answer >](#)

7. Which of the following represents a difference between equity carve-out and a spin-off?

- (a) In an equity carve-out shares in the holding company are transferred to the subsidiary company and in a spin-off the vice-versa happens
(b) In equity carve-out the proportion of debt increases whereas in spin-offs, the proportion of debt comes down

[< Answer >](#)

- (c) In an equity carve-out a certain proportion of the shares in subsidiary company is offered for sale to general public while in spin-off a company distributes its shares on a pro-rata basis to the shareholders
- (d) In equity carve-out shares are re-purchased by the general public at a price below the market value while in a spin-off the shares are repurchased at a price above the market price
- (e) In equity carve-out the leverage ratio of the firm increases while it decreases in a spin-off.
8. Which of the following budgets is a statement that presents the financial plan for each department during the budget period? [< Answer >](#)
- (a) Capital budget (b) Expenditure budget
(c) Revenue budget (d) Cash budget
(e) Marketing budget.
9. Which of these, according to Porter, is **not** a support activity in a manufacturing firm's value chain? [< Answer >](#)
- (a) Firm infrastructure (b) Marketing and sales
(c) Human resource management (d) Procurement
(e) Service.
10. Firms usually source raw material from external suppliers and process them to produce the desired product. However, some firms may attempt to produce the raw material or some components on their own. For example, Levi's manufactures the cloth required for making jeans. Which of the following best describes this strategy? [< Answer >](#)
- (a) Integration (b) Horizontal integration
(c) Backward integration (d) Diversification
(e) Forward integration.
11. Which of the following ratios measures how effectively a firm is using its resources? [< Answer >](#)
- (a) Liquidity ratios (b) Activity ratios
(c) Profitability ratios (d) Leverage ratios
(e) None of the above.
12. Which of the following is **not** a step in operational control systems? [< Answer >](#)
- (a) Set standards of performance (b) Measure past performance
(c) Identify deviations from standards (d) Initiate corrective action
(e) Measure actual performance.
13. Which of the following factors is **not** considered in determining the industry attractiveness as per the GE Nine-cell planning grid? [< Answer >](#)
- (a) Entry and exit barriers (b) Economies of scale
(c) Knowledge of customers and markets (d) Caliber of management
(e) Industry profitability.
14. The connections between the way one value activity is performed and the cost of performance of another activity are known as [< Answer >](#)
- (a) Explicit Knowledge (b) Tacit Knowledge
(c) Linkages (d) Respected Activities
(e) Value Chain.
15. The collection of beliefs, expectations, and values learned and shared by a corporation's members and transmitted from one generation of employees to another is known as [< Answer >](#)
- (a) Cultural Integration (b) Cultural Intensity
(c) Corporate Culture (d) Corporate Integration
(e) Corporate Identity.
16. In the process of licensing, the party or firm that sells the right to use its intellectual property to another firm is known as? [< Answer >](#)
- (a) Franchisor (b) Licensor (c) Exporter (d) Dealer (e) Importer.
17. A leader who uses coercive power and manipulation to attain personal goals is called [< Answer >](#)

- (a) Phantom Leader
(b) Catalyst
(c) Strategic Leader
(d) Machiavellianist (e) Democratic Leader

18. Which of the following variables is/are related to rivalry among existing firms? [< Answer >](#)
- I. Access to distribution channels. II. Alternative suppliers.
III. Alternative buyers. IV. Product differentiation.
V. Amount of fixed costs.
- (a) Only (I) above (b) Only (II) above
(c) Both (II) and (III) above (d) Both (III) and (IV) above
(e) Both (I) and (V) above.
19. Which of the following describes a company's product, market and technological areas of thrust, and reflects the values and priorities of the strategic decision makers? [< Answer >](#)
- (a) Company's Profile (b) Company's Mission
(c) Company's Objective (d) Company's Strategy
(e) Company's Vision.
20. In which mode of strategic decision-making is strategy formulation confined to owner promoters? [< Answer >](#)
- (a) Entrepreneurial mode (b) Adaptive mode
(c) Planning mode (d) Receptive mode
(e) Intuitive mode.
21. In which of the following structures are functional and product forms combined simultaneously at the same level of the organization? [< Answer >](#)
- (a) Divisional structure (b) Functional structure (c) Simple structure
(d) Matrix structure (e) Geographic structure.
22. A firm's external environment includes a remote sector and an immediate task sector. Which of the following factors are included in the remote sector? [< Answer >](#)
- (a) Political, technological, economic and social
(b) Political, union activity, economic and technological
(c) State government, production, social and economic
(d) Mission, company profile and competition
(e) All of the above.
23. Which of the following is/are the key feature(s) for distinguishing annual objectives from long-term objectives? [< Answer >](#)
- (a) Time frame (b) Focus (c) Specificity
(d) Measurement (e) All of the above.
24. An industry in which no firm has a large market share and each firm serves only a small piece of the total market in competition with others is known as [< Answer >](#)
- (a) Multidomestic (b) Fragmented (c) Global (d) Transnational
(e) International industries.
25. Which of these is **not** an appropriate Question Mark division strategy for a product in the BCG Matrix? [< Answer >](#)
- (a) Product development (b) Divestiture
(c) Market penetration diversification (d) Conglomerate
(e) Innovation.
26. Which component in a mission statement represents an organization's basic beliefs, values, aspirations and ethical priorities? [< Answer >](#)
- (a) Philosophy (b) Self-concept
(c) Concern for public image (d) Culture
(e) Technology.
27. Establishing long-term objectives and strategies is part of [< Answer >](#)
- [\(a\) Strategy formulation](#) [\(b\) Strategy implementation](#) [\(c\) Strategy](#)

evaluation (d) Environmental scanning (e) Developing a business mission.

[< Answer >](#)

28. Managers play a key role in the decision-making system of the business. Which of the following **does not** come under the decisional roles category?

(a) Negotiator (b) Resource allocator (c) Entrepreneur(d) Leader (e) Disturbance handler.

[< Answer >](#)

29. What is the meaning of the advice to firms to "stick to the knitting"?

(a) Never pursue diversification strategies
(b) Focus on efficiency rather than effectiveness
(c) Do not stray too far from the firm's basic areas of competence
(d) Use a focus strategy whenever possible
(e) Both (a) and (b) above.

[< Answer >](#)

30. Which of the following does **not** support the contingency approach to strategic choice?

(a) A downturn in the economy (b) A labour strike(c) A technological break through (d) Change in firm's management(e) Shortage of critical material.

END OF SECTION A

Section B : Caselets (50 Marks)

- This section consists of questions with serial number 1 – 7.
- Answer **all** questions.
- Marks are indicated against each question.
- Detailed explanations should form part of your answer.
- Do not spend more than 110 - 120 minutes on Section B.

Caselet 1

Read the caselet carefully and answer the following questions:

1. Escorts Motors and Yamaha Motors entered into a joint venture to manufacture and market motorcycles in India. What was the rationale behind this joint venture and what synergies were expected out of it?
(7 marks) < Answer >
2. In May 2000, Escorts took the decision to sell off 24% stake in the joint venture. In May 2001, Yamaha Motors struck a deal with Escorts for acquiring the latter's remaining 26% shareholding in YMEL for Rs. 700 million. The deal marked Escort's exit from the joint venture. Why do you think Escorts exited from the joint venture?
(8 marks) < Answer >

In 1985, Yamaha Motor Company (Yamaha Motors) entered into a technical support agreement with Escorts Limited (Escorts), and started local production of Yamaha motorcycles. In 1995, Yamaha and Escorts signed another contract, establishing Escorts Yamaha Motor Ltd. (EYML) to manufacture and market motorcycles in India. Each company invested 50% of the capital for the Indian motorcycle venture.

The joint venture manufactured Rajdoot motorcycles at Faridabad and the RX and four-stroke YBX series at Surajpur. EYML had the largest countrywide network of over 500 dealers, supported by a wide base of sales & service outlets and spare parts stockists. Anil Nanda, chairman, EYML, said the Surajpur and Faridabad facilities would be modernized and upgraded with a Rs. 3.75 billion budget. With the additional investments, volumes were expected to go up from 300,000 units in 1996 to 500,000 units by the year 2000. Sales turnover too was projected to rise from Rs. 9 billion, (including exports of Rs. 1.2 billion) to Rs. 20 billion (including exports of Rs. 3 billion) over the same period.

In 1999, EYML closed down its moped manufacturing facility and discontinued production of its two existing brands due to lack of adequate demand. The company decided to concentrate fully on its motorcycle production. Company sources said that EYML decided to discontinue the production as earning was low from moped business. Against a 5% growth recorded by the moped segment in 1998-99, sales of EYML mopeds declined by 17.7%. Its market share also declined from 1.9% in 1997-98 to 1.5% in 1998-99.

In April 2000, Escorts announced that it was likely to sell around 20% stake in EYML to Yamaha Motors. On April 24, 2000, Rajan Nanda, Chairman of Escorts, the flagship of the Rs. 35 billion Escorts group held board meeting of Escorts Limited (Escorts). At the meeting, Nanda informed the directors that, subject to the board's approval, Yamaha Motors could be given a majority stake in the joint venture company. The Japanese two-wheeler major had offered to buy an additional 24% stake in EYML from Escorts at Rs. 200 per share. The deal would add Rs. 2.3 billion to Escorts' coffers. The announcement seemed to have been well accepted by the board. In late April 2000, the board of Escorts approved the proposal to divest 24% equity.

For the Escorts board, such announcements were not new. In a little over a year, Escorts had offloaded substantial chunks of its equity in three joint ventures to its overseas partners. It all started in 1999 when Escorts sold one-third of its shares in the construction equipment company Escorts JCB to JCB of the United Kingdom for Rs. 490 billion. This brought its stake down from 60% to 40%. Next came the turn of Hughes Escorts Communication, a 51:49 joint venture between Hughes Communications of the United States and Escorts. In December 1999, Escorts offloaded 23% of its stake to Hughes for Rs. 750 million. This brought its shareholding in the company to 26%. Escorts would thus become a minority shareholder in EYML. However, an official said that Escorts' holding in the joint venture would not be less than 26% and it would not exit from the joint venture. Said Nanda, "I have no intentions of selling off the entire stake to Yamaha. Escorts will retain the 26 per cent stake we now hold in the venture." With the change in the equity pattern, Yamaha Motors would control the management of the joint venture. Commented Nanda, "We have always believed that business relationships are driven by the value added by each partner. We have decided that it would be appropriate for Yamaha Motors, as the technology provider, to take the lead role in the business."

This was the second such exercise undertaken by Nanda since 1995 when he took over the reins of the company from

his father, Har Prashad Nanda as chairman of the group. Nanda identified four thrust areas for Escorts-agri-business, telecom, software and healthcare. The idea behind giving Yamaha Motors the majority stake in the joint venture was to focus more on the four thrust areas. Escorts would now concentrate on agri-business, telecom and healthcare. Escorts' exit from the joint venture seemed to be a well-planned move. The group had already moved out of businesses where it believed it did not have a sustainable advantage.

Escorts would now focus on four core businesses: agribusiness (tractors), telecom services (cellular telephony), IT and Internet services and healthcare services (cardiac healthcare). However analysts were skeptical about Escorts' success in these areas. One analyst said, "It's been almost 12-18 months since it identified these as core businesses, and Escorts is still grappling with the new economy initiatives." Escorts was planning to acquire a controlling stake in at least two circles – Madhya Pradesh and Gujarat. Escotel Mobile Communications, a 50:50 joint venture between Escorts and First Pacific of Hongkong, had earlier lost out on two acquisitions to Skycell in Chennai and Essar Cellphone in Delhi, as its bids were too low.

In May 2000, EYML was renamed Yamaha Motors Escorts Ltd (YMEL) following Escorts decision to sell off 24% stake. In May 2001, Yamaha Motors struck a deal with Escorts for acquiring the latter's 26% shareholding in YMEL for Rs. 700 million. The deal marked Escort's exit from the joint venture. Yamaha Motors would now hold 100% stake in the company.

With the change in management, Yamaha Motors was expected to build global capabilities, bring in new technology and offer a wide range of cost effective quality products. All this was expected to give them an edge over competitors. The company would also have the additional benefit of enlarging its scale of operations for manufacturing and supplying products worldwide. On its part, Escorts would continue to provide a stronger base for manufacturing facilities, a countrywide dealership network and skilled manpower.

Yamaha Motors was also working to regain its lost market position. From being number two in 1996, it had slipped to the fourth position in 2001. In December 2000, Yamaha Motors launched Crux-a four-stroke bike. By mid 2001, Crux had already sold 33,000 units. In December 2001, Yamaha Motors had a 14% share in the Indian market which improved marginally in March 2002, to 15%. As a part of marketing strategy, the company planned to introduce one new model each year and was working on one such model.

Caselet 2

Read the caselet carefully and answer the following questions:

3. Mallech Sen Gupta has given lot of importance to procurement division, control systems and organizational structure and further spent huge amount on training salesforce. Identify the above activities in the context of value chain and explain how these activities help Pioneer Electronics Ltd. deliver value to the customers?
(8 marks) < Answer >
4. Pioneer Electronics Ltd. entered into tie-ups with different companies with regard to supply of product designs. What are the advantages Pioneer Electronics Ltd. is going to get by having long-term agreement with different companies with regard to supply of product designs? Explain in detail.
(8 marks) < Answer >

By 2003, with revenues of around Rs. 160 crores, Pioneer Electronics Ltd. had established itself as a leading local manufacturer of consumer electronics and electrical goods in India. The company used to supply certain parts of TV, refrigerator and air-conditioners to various players in the industry apart from selling finished products directly in the market. With the increasing popularity of the company's products the CEO of the company, Mallech Sen Gupta (Mallech) planned to foray into new markets.

Pioneer Electronics Ltd. was established in 1977 by Rakesh Sen Gupta (Rakesh), father of present CEO Mallech. Before, starting his own venture, Rakesh, who was an engineer, worked as technical expert in various organizations. After working in various organizations for considerable time, he decided to start his own venture. Initially, he started a small plant in Pune. He decided upon Pune because it was strategically located. During the initial days Rakesh did not have enough funds. So he took loan of Rs. 25 lakhs from bank, borrowed Rs. 9 lakhs from his father-in-law and put Rs. 12 lakhs on his own. The venture started with an initial capital investment of Rs. 46 lakhs. The company initially concentrated on manufacturing certain parts of electronic goods. However, credit sales increased the fund lock, which had a heavy impact on the company. The company struggled to pay the bank loans.

In early 1980s, there was spurt in the number of suppliers. With growing market for electronic items in India, many players entered the market. Most of the buyers of the company had multiple suppliers and the buyers uses to give order to the suppliers who quoted less price. Therefore, in order to get orders, Pioneer Electronics Ltd. was forced to quote lower price than its competitors to get order. This price cut had further eaten away the revenues of the firm.

In 1986, Mallech, after completing his graduation in management, joined Pioneer Electronics Ltd. Mallech understood

the operations of the business very quickly. In one of his strategic discussions with his father, he said, "Time has come for us to bring in certain changes. Further, we need to increase the production level of our factory to avail the benefits of economies of scale."

"I agree with you. But, what about the purchasers. Even if you produce, buyers need to buy our products. So, we need to produce according to the demand existing in the market," said Rakesh.

"There is much more potential for TVs with the advent of cable network. The growth in upper middle class segment will lead to much more market demand in the coming years. To tap this potential we need to expand our production and produce goods at much more cheaper price. Even growing competition in the market is making big players to outsource certain activities like spare parts development etc. So, our buyer count is also going to increase. Still if there is slack in off take of our products, we ourselves will assemble the parts and sell the products. Anyway, we are manufacturing majority of the parts required for TV except picture tubes," said Mallesh.

"But that requires lot of funds. Further for selling goods, we need to have good distribution network," said Rakesh.

"Things will take care of itself with time," replied Mallesh.

In 1988, Pioneer Electronics Ltd. opened a new manufacturing plant in Hyderabad. The company also started cost cutting exercise and organizational restructuring. The company reduced the manpower and decided to leave the relatively low value adding manufacturing processes to suppliers. The entire manufacturing process was streamlined by bringing in much more professionalism in procurement division. Mallesh restructured the materials management division and it resulted in cost reduction. This was possible by controlling the flow of goods from Pioneer Electronics Ltd.'s suppliers. By restructuring its relations with suppliers, the company was able to get quality products from its suppliers at a competitive price. The company started to build a long-term relationship with suppliers by involving the suppliers right from the product planning stage. Each supplier was assessed periodically through company audits. The company created categories of preferred suppliers and supplier partners. All suppliers were also expected to do their own quality testing and the company only conducted random checks. The company even started having tie-ups with various marketing agencies to market its products.

In spite of all these measures, the company was not able to generate much profit. In early 1990s, the revenue of the company increased marginally. Though the company did not have a premium brand tag still consumers felt that they were getting value for the money. However, the company's markets were limited to Maharashtra, Andhra Pradesh and Karnataka. In early 1990s, there was an increase in company's revenues. However, from 1995 onwards, there was a drop in sales. Analysts attributed the reduction in revenue to poor after sales service. They found that though the company's products were cheaper when compared with competitors products, still consumers were hesitant to buy as the after sales service was bad. After much analysis, Mallesh found that the consumers include after sales service while ascertaining the value of the product at the time of purchase. Therefore, he started providing training to the sales personnel of the marketing agencies that worked for his company with regard to after sales service, though the company needed to spend heavily for the training. Further, he had an agreement with those agencies to provide after sales service.

Mallesh found that the company had diversified into too many businesses, which was affecting the efficiency of the company. Therefore, he dismantled several home appliance products and concentrated more on TVs and air-conditioners. Mallesh realized that with growing business, there was need for significant investment in R&D. So, Pioneer Electronics Ltd. entered into a tie-up with other related companies with regard to supply of product designs. This helped the company significantly as it was able to release new models into the market periodically.

By late 1990s, there was rapid growth in revenues. In 2001, the company started its own marketing & service division. However, the company did not discard its existing understanding with marketing agencies. Instead, the company's own marketing & service division will strengthen the existing force of marketing agencies. Mallesh realized that the process of adding value was a continuous process. Therefore, he formed a team, which specifically looks into value addition to the product by identifying various value activities of the products.

Caselet 3

Read the caselet carefully and answer the following questions:

5. By definition, a multinational firm extends its operations beyond its home country. The success of a multinational can be determined on the basis of different criteria like profits, market share, and reputation. Would you call the Tata group a successful multinational? Justify your answer.

(7 marks) < Answer >

6. Developing core competencies in marketing, sales and distribution is the key to entering foreign markets. Discuss the ways in which the Tata group can develop core competencies and acquire competitive advantages. What difficulties is it likely to face in this respect?

(7 marks) < Answer >

7. Do you think the Indian government is supporting aspiring multinationals like the Tatas, Birlas, and Ranbaxy? Do you think their Indian origin will be an asset or a liability when entering overseas markets?

(5 marks) < Answer >

In India, the Tatas are industry leaders in fields as diverse as automobiles, steel, publishing, textiles, tea, engineering, electronics and information technology. The group's annual turnover is in excess of US \$9 billion. Prior to 1991, Tata Sons, the holding company, held minor stakes of less than 26%, not sufficient for formal control in most of the companies of the group. With the opening of India's economy in 1991, Tatas hiked their stake to prevent their companies from becoming takeover targets for MNCs. With intense competition from MNCs, the Tatas could not continue to be No.1 in all the businesses they owned. Companies like Voltas, Rallis and Forbes Gokak, which were once regarded blue chip companies turned into loss-making companies. Voltas, though initially an engineering company, gradually turned its focus to consumer products like air conditioners, refrigerators, etc. Of the 80 Tata companies, less than ten accounted for 70% of the total sales of the group. The Tata group started divesting FMCG businesses like soaps and detergents (Tomco), cosmetics (Lakme), and Pharma (Merind), which were loss making concerns.

In the mid 1990s Tata International Ltd., the international business development arm of the Tata Group, intensified its efforts to globalize the Group's core businesses. According to the Golden Super Star Trading House status, the company exports a range of quality products and services to over 100 countries and facilitated the import of goods, services and technologies for Group companies. Tata International currently has offices and wholly-owned subsidiaries in various countries like Africa, South East Asia and UAE which promote international trade and the globalization of the Group's businesses.

While the Tata group focuses on the export of automobiles, steel and tea, Tata International concentrates on the export of leather and leather products from India. Through its locations in India and abroad, the company sources a wide range of products for exports: products such as mining equipment, machinery, consumables, automotive components, ferro alloys and minerals, bicycles and bicycle parts, agricultural machinery, electrical and electronic products, agro commodities and textile garments.

Tata International is responsible for 1.5 per cent of all exports from India. It has a 9 per cent share of the finished leather exports from India. Its leather business includes the manufacturing and marketing of finished leather and high-fashion leather articles like shoes, garments and accessories for the upper end markets of the European Union, USA and the Far East. It has a leather unit at Dewas in central India, which is the largest leather finishing unit in India and among the top three worldwide. Tata also manages a tannery in China and sources its hides and skins globally.

Tata's international operations involves executing turnkey contracts for transmission lines and supplies. Tata acts as a facilitator for the bulk import of a wide range of products such as fuel, capital goods, solvents, chemicals and drugs.

The company's global network includes wholly-owned subsidiaries in South Africa, Zambia, Zimbabwe, Namibia, Mozambique, Uganda, Tanzania, Ghana, UAE and Hong Kong; and offices in Thailand, Bangladesh, Oman, Cyprus, Russia, UK and China. The company complements its global marketing and sourcing capability through the associates of the Tata group in USA, Europe and Singapore. Its global operations include the marketing and distribution of steel products, ferro alloys, and automobiles; the setting up of automotive assembly and service centres; and running a five-star hotel. Procurement and vendor development in India is undertaken with assistance from the group's local offices.

END OF SECTION B

Section C : Applied Theory (20 Marks)

- This section consists of questions with serial number 8 - 9.
- Answer **all** questions.
- Marks are indicated against each question.
- Do not spend more than 25 -30 minutes on section C.

8. Strategic control focuses on monitoring and evaluating the strategic management process to ensure that it functions in right direction. Discuss the various types of strategic controls used in the organization.

(10 marks) < Answer >

9. Nissan, the Japanese automaker, had identified that its US sales are coming down. The quality and design of its cars were not up to the standards of other Japanese companies, such as Honda, Mazda and Toyota. Recognizing the problem Nissan introduced a newly designed mid-sized car, which was based on cost-leadership strategy. The company has decided not to increase the size of its car and hence would keep its cost and price low. The cost of

Nissan Altimo was \$14,000, well below the sticker price of \$19,000 of Toyota Camry and Honda Accord. Explain the advantages enjoyed by Nissan as a cost leader and problems to be faced, if any.

(10 marks) < Answer >

END OF SECTION C

END OF QUESTION PAPER

Suggested Answers

Business Policy & Strategy (MB311) : July 2004

Section A : Basic Concepts

1. Answer : (b) [< TOP >](#)

Reason : Special alert control reflects the need to thoroughly reconsider the firm's basic strategy based on a sudden unexpected event.(a) Implementation control determines whether or not the overall strategy should be changed in light of the unfolding events and results associated with incremental steps and actions that implement the overall strategy.(c)Premise control helps to check systematically and continuously whether or not the premises set during the planning and implementation are still valid.(d) Operational control are concerned with "steering" the company's future direction and they are concerned with provide action controls.(e) Strategic surveillance is designed to monitor a broad range of events inside and outside the company that are likely to threaten the course of a firm's strategy.
2. Answer : (d) [< TOP >](#)

Reason : rationale behind divestitures.

Discussion: Option (d) is correct. There are two major reasons for divestitures they are, first, the subsidiary might be losing money and secondly, the assets of divested company are interfering with profitable operation of the seller. Therefore, the subsidiary is creating a negative synergy with the parent company as the parent company is not able to realize is potential value due to the presence of subsidiary company. So, the parent company divests the subsidiary.

Option (a) is false as divestiture might or might not lead to market share expansion.
3. Answer : (d) [< TOP >](#)

Reason : Benchmarking lays emphasis on the improvement of given business operation or a process through the exploitation of 'best practices'.
4. Answer : (e) [< TOP >](#)

Reason : The type of Merger

Discussion: The correct answer is answer is (e). In vertical merger two firms are merged along the value-chain, for instance, manufacturer merging with a supplier. Vertical mergers are often used as a way to gain a competitive advantage within the marketplace. Therefore, merger between Merck and Medco is an example of vertical merger.

Option a) is wrong as spin-off is associated with controlled subsidiaries. The objective of spin-offs is to divest a part of the business, which does not fit with the company's major business area.

Option b) is wrong because sell-offs includes the commonly used strategies to exit businesses and to deploy corporate assets by returning cash or non-cash assets through special dividends to shareholders.

Option c) is wrong because conglomerate mergers involve merger between firms engaged in unrelated types of business activity. The basic purpose of such combination is utilization of financial resources. Option d) is wrong as in market extension merger as the name suggest, the objective is to expand the markets unlike that in vertical merger where objective is to gain competitive advantage within the market
5. Answer : (c) [< TOP >](#)

Reason : The difference between merger and joint venture

Discussion: Option c) is correct. In a merger, two (or more) separate corporations (organizations) come together to form one legal entity. There are several legal ways to implement a merger, but regardless of how it is done, the result is one corporation (organization), not the two (or more) that existed previously. This is not the case with a joint venture. Two (or more) organizations can establish a joint venture — project, program, organization, etc. — together, and jointly administer and govern it, while still maintaining their own organizational autonomy. With a joint venture, the partnering corporations (organizations) remain separate.

Option a) is not correct as in both joint venture and mergers profit sharing aspects between the partners are present.

Option b) is incorrect as when two companies go for a joint venture they maintain their separate legal identity. On the other hand when two companies go for a merger there is no organizational autonomy left.

Option d) is incorrect. Mergers are for unforeseeable future and not joint ventures.

Option e) is incorrect as both mergers and joint venture is undertaken for profit.

The characteristic features of Joint ventures are: -

In joint venture when two firms combine there is no organizational autonomy left between them while it is not so in the case of mergers.

When two firms go for a joint venture they maintain their separate legal entity whereas it is not the case with merger.

Joint venture is for unforeseeable future which is not the case with mergers

In joint venture there is no expectation of profit as it is established to fulfill a particular goal while mergers are profit oriented.

6. Answer : (a)

[<TOP >](#)

Reason : A standstill agreement is a voluntary contract in which the stockholder who is bought out, agrees to abstain from making further investments in the target company for a specified period of time. All other option are not correct.

7. Answer : (c)

[<TOP >](#)

Reason : The difference between equity carve-out and spin-offs.

Discussion: The correct option is (c). In a equity carve-out certain proportion of the subsidiary's shares are offered to the general public, bringing an infusion of cash to the parent company without the loss of control. However in a spin-off a company distributes all the shares of its own subsidiaries to its own shareholders on pro-rata basis.

Option a) is false as in equity carve-out shares of an wholly owned are offered to the general public and not transferred to any subsidiary. However, in spin-off the shares of subsidiary are distributed to its own shareholders and not to public in general.

Option b) is incorrect as the management policy affects the change of debt in the company.

Option d) is incorrect as in an equity carve-out shares of a wholly owned are offered to the general public and in spin-offs shares of subsidiary are distributed to its own shareholders and not to public in general.

Option e) is incorrect as there is no effect on the leverage ratio be it either in equity carve-out or spin-offs.

8. Answer : (b)

[<TOP >](#)

Reason : Expenditure budgets is a statement that presents the financial plan for each department during the budget period.

9. Answer : (b)

[<TOP >](#)

Reason : According to Porter, marketing and sales is **not** a support activity in a manufacturing firm's value chain.(a) A company's infrastructure is the final support activity as it is considered to be very important because it has to do with the company wide context within which all other value creation activities take place.(c) Human resource management is also a support activity that can help an enterprise create more value. This human resource function gives an idea regarding the right mix of skilled people to perform value creation activities effectively.(d) Procurement is the support activity which helps in the production process and adds to value creation (e) The service function plays a major role in providing after sales service and

support.

10. Answer : (c) [< TOP >](#)
Reason : Levi's manufacturing the cloth required for making jeans, the process is termed as backward integration which takes place when a firm assumes a function previously provided by a supplier.
11. Answer : (b) [< TOP >](#)
Reason : Activity ratios measure how effectively a firm is using its resources I, e to say this reflects a firm's efficiency in resource utilization.(a) Liquidity ratios measures a firm's capacity to meet its short-term financial obligations.(c) Profitability ratios provide a firm's overall economic performance. (d) Leverage ratios indicate a firm's financial risk.
12. Answer : (b) [< TOP >](#)
Reason : Operational controls are concerned with providing action controls. Operation control systems exist because operating managers need control methods appropriate to their level of strategy implementations. These provide post-action evaluation and control over short time periods. Operational control must take the following four steps in order to be effective I,e set standards of performance, Measure actual performance, identify deviations from standards and initiate corrective action or adjustment. Hence, measuring past performance is not a step in operational control systems.
13. Answer : (a) [< TOP >](#)
Reason : GE matrix takes two factors into consideration – Business strength and industry attractiveness. Exit and entry barriers is considered in determining the business strength and not the industry attractiveness. Hence the correct answer is (a).
14. Answer : (b) [< TOP >](#)
Reason : According to Porter, marketing and sales is not a support activity in a manufacturing firm's value chain.(a) A company's infrastructure is the final support activity as it is considered to be very important because it has to do with the company wide context within which all other value creation activities take place.(c) Human resource management is also a support activity that can help an enterprise create more value. This human resource function gives an idea regarding the right mix of skilled people to perform value creation activities effectively.(d) Procurement is the support activity which helps in the production process and adds to value creation (e) The service function plays a major role in providing after sales service and support.
15. Answer : (c) [< TOP >](#)
Reason : The collection of beliefs, expectations, and values learned and shared by a corporation's members and transmitted from one generation of employees to another is known as the corporate culture.
16. Answer : (b) [< TOP >](#)
Reason : Licensing is a means of entering a foreign market. In the process the party or firm that sells the right to use its intellectual property to another firm is called Licensor. (a)A franchisor is a firm that allows an independent entrepreneur or organization to operate a business under its name. (c) Exporter is a person or an entity who sells goods to another country for the purpose of trade.(d) . Dealer is a person who is involved in mere buying and selling of goods.(e) Importer is a person or an entity who bring in or introduce goods from a foreign country for the purpose of trade.
17. Answer : (d) [< TOP >](#)
Reason : Phantom is a board of directors having low degree of involvement in strategic management where it never knows what to do. On the other hand a catalyst is a board having high involvement in strategic management and takes a leading role in establishing and modifying the mission, objectives, strategy and policies. Strategic leader is one who gives direction to his subordinates with a long-term vision, which he shares with them. Democratic leader takes into consideration the suggestions by his subordinates in arriving at any decision. He follows a participative style of management. A machiavellianist is one who uses coercive power to achieve his personal goals.
18. Answer : (e) [< TOP >](#)
Reason : Access to distribution channels is a cause of rivalry among existing firms as the channels are limited and all the players are vying for the given distribution channels. Amount of fixed

costs also leads to rivalry among existing firms as the proportion of fixed costs in the cost structure (i.e. operating leverage) decides the responsiveness of the firms to business risks. Existence of alternative suppliers, buyers and product differentiation leads to reduction in rivalry among existing firms.

19. Answer : (b) [<TOP>](#)
Reason : The mission statement is enduring statement of instruction of an organization; it refers to the philosophy of business in order to build the image of the company by activities currently pursued by the organization and its future status. While, Vision statement describes the aspiration for the future , but without specifying the means to achieve those desired ends.
20. Answer : (a) [<TOP>](#)
Reason : In the entrepreneurial mode of strategic decision-making, strategy formulation is confined to owner promoters. The owner promoters then delegate their vision / mission to the organizational hierarchy for implementation.
21. Answer : (d) [<TOP>](#)
Reason : Matrix structures are functional and product forms combined simultaneously at the same level of the organization.(a) Divisional structure is a type of departmentalization in which positions are grouped according to similarity of products, services or markets. The Divisional structure does not promote specialization of labor (b) Functional structure is a type of departmentalization in which positions are grouped according to their main functional area or specialized area.(c) In simple structure all the strategic and operating decisions are under the control of the owner-manager(e)Geographic structure is a form of divisional structure involving divisions designed to serve different geographic areas.
22. Answer : (a) [<TOP>](#)
Reason : The remote environment is composed of a set of forces that originate beyond and usually irrespective of any single firm's operating situation- that is, political, economic, social, technological. It presents opportunities, threats and constraints for the firm, while the organization rarely exerts any meaningful reciprocal influence. All other options are not correct.
23. Answer : (e) [<TOP>](#)
Reason : An annual objective must be clearly linked to one or more long-term objectives of the business's grand strategy. However, to accomplish this (a) Time frame (b) focus(c) specificity (d) measurement are the four dimensions required to distinguish annual objectives from long-term objectives.
24. Answer : (b) [<TOP>](#)
Reason : In a fragmented industry, no firm has a large market share and each firm serves only a small piece of the total market in competition with others. Hence it is difficult for any single company to have a dominant position in the market A multi-domestic industry is one in which the competition within the competition within the industry is essentially segmented from country to country. A global industry is one in which competition within the industry crosses national borders. International industries can be characterized along a continuum from multi-domestic to global. Transnational are organizations, which operates in different continents.
25. Answer : (d) [<TOP>](#)
Reason : Conglomerate diversification is **not** an appropriate Question Mark division strategy in a BCG Matrix, as the viable strategy for question mark business would be to divest the weaker businesses and invest heavily in high potential businesses to turn them into stars in the near future.(a)(b)(c)(e) Product development, divestiture, market penetration and innovation does form the appropriate strategy in the question mark division in a BCG matrix.
26. Answer : (a) [<TOP>](#)
Reason : Philosophy component in a mission statement represents an organization's basic beliefs, values, aspirations, and ethical priorities.(b) In a competitive environment, finding a place requires a firm to realistically evaluate its own strengths and weakness as a competitor. The idea that the organization must know itself is the essence of the term self concept.(c) Public image is the representation or the image attributed to a business based on certain qualities by the environment in which it is operating(d) Culture is the customary ways of thinking and behaving by a particular population or society. (e) Technology is the knowledge, tools, equipment and work techniques used by an organization in delivering its product or service.

27. Answer : (a) [<TOP>](#)
Reason : Strategy formulation establishes long-term objectives and strategies.
28. Answer : (d) [<TOP>](#)
Reason : Decisional roles includes the role of an entrepreneur, disturbance handler, resource allocator and negotiator. The role of leadership is not included in decisional role but is included in interpersonal role.
29. Answer : (c) [<TOP>](#)
Reason : “Stick to the knitting” advice conveys the message that firms should pursue growth strategies in the business that they are familiar with, and not stray too far from the firm's basic areas of competence
30. Answer : (d) [<TOP>](#)
Reason : Change in firms management does not support the contingency approach to strategic choice.

Section B : Caselets

1. In 1985, Yamaha Motor Company (Yamaha Motors) entered into a technical support agreement with Escorts Limited (Escorts), and started local production of Yamaha motorcycles. In 1995, Yamaha and Escorts signed another contract, establishing Escorts Yamaha Motor Ltd. (EYML) to manufacture and market motorcycles in India. Each company invested 50% of the capital for the Indian motorcycle venture.

The joint venture was expected to result in many synergies. Yamaha Motors was expected to build global capabilities, bring in new technology and offer a wide range of cost effective quality products. All this was expected to give Escorts an edge over its competitors. The company would also have the additional benefit of increasing its scale of operations by manufacturing and supplying products worldwide. On its part, Escorts would continue to provide a stronger base for manufacturing facilities, a countrywide dealership network and skilled manpower.

EYML had the largest countrywide network of over 500 dealers, supported by a wide base of sales & service outlets and spare parts stockists. Anil Nanda, chairman, EYML, said the Surajpur and Faridabad facilities would be modernized and upgraded with Rs. 3.75 billion budget. With the additional investments, volumes were expected to go up from 300,000 units in 1996 to 500,000 units by the year 2000. Sales turnover too was projected to rise from Rs. 9 billion, (including exports of Rs 1.2 billion) to Rs. 20 billion (including exports of Rs. 3 billion) over the same period.

[< TOP >](#)

2. Escorts planned to use the funds it generated from its equity divestment in the erstwhile EYML to bring down its dependence on loan funds. Escorts sold off its entire stake in the joint venture so that it could focus on new economy businesses and get out of low growth areas. Escorts would now focus on four core businesses: agribusiness (tractors), telecom services (cellular telephony), IT and Internet services and healthcare services (cardiac healthcare). Of all its old economy businesses, only tractors was doing well. Naturally, Escorts retained this business. After pulling out of the joint venture, Escorts planned to invest in new areas. By divesting its stake in EYML, Escorts could raise cash to fund its acquisition of telecom circles. Escorts was planning to acquire a controlling stake in at least two circles – Madhya Pradesh and Gujarat. Escotel Mobile Communications, a 50:50 joint venture between Escorts and First Pacific of Hongkong, had earlier lost out on two acquisitions to Skycell in Chennai and Essar Cellphone in Delhi, as its bids were too low.

[< TOP >](#)

3. A value chain is a linked set of value creating activities beginning with basic raw materials coming from suppliers, moving on to a series of value added activities involved in producing and marketing a product or service, and ending with the distributors getting the final goods into the hands of the ultimate consumer. The value activities can be divided into primary activities and supporting activities. The primary activities include research and development, production, marketing and sales and services. The supporting activities include firm infrastructure, human resource management, technology development and procurement.

Mallesh Sen Gupta has given lot of importance to procurement division, control systems and organizational structure and further spent huge amount on training salesforce. All these activities fall under supporting activities. Support activities provide inputs to the primary activities and include activities like materials management. The materials management function, for example, controls the transmission of physical materials through out the value chain, from procurement to production and distribution. The value creation here depends upon the efficiency with which the material management is carried out. Thus, Pioneer Electronics Ltd. is able to provide the right mix of goods to consumers, which increases the perception of value that consumers associate with it. Similarly, the human resource function also adds value to an enterprise ensuring the right mix of skilled people to perform value creating activities effectively. Therefore, training was provided for salesforce. A company's infrastructure performs the most important supporting function. Therefore, the company's infrastructure is important because it provides the basic framework within which all the other value creating activities take place. Organization structure, control systems and the culture of the company together comprise the infrastructure of an organization. Therefore, Mallesh shaped the infrastructure of Pioneer Electronics Ltd., and with it, the performance of all other

value creating activities that take place within the company. Therefore, by giving importance to supporting activities, Pioneer Electronics Ltd. would be able to provide value to its customers.

[< TOP >](#)

4. Pioneer Electronics Ltd. can pursue the benefits by entering into long-term agreements or coalitions to gain certain advantages. Tie-ups related to technology licenses, supply agreements, joint ventures, and marketing agreements are formed with a long-term orientation. Through tie-ups, Pioneer Electronics Ltd. gets an opportunity to share its activities without entering new industry segments, geographic areas, or related industries. The coalition also bestows the cost and differentiation advantages of vertical linkages without the firm having to go in for vertical integration. This type of arrangement is beneficial because it does not involve coordination problems that are a characteristic of vertical integration. These coalitions involve long-term relationships, and a firm might find it easier to deal with its coalition partner than another independent firm. However, entering into an agreement is a laborious and time consuming process, which might involve many compromises and thus can nullify the advantages expected of the coalition. By sharing activities with marketing agencies with regard to after sales service, Pioneer Electronics Ltd. could be able to provide better services without incurring much cost.

[< TOP >](#)

5. A firm may be called a successful multinational when:

- Overseas operations are not limited to marketing and distribution but include value addition activities.
- Revenues from international operations account for a significant percentage of the total revenues of the firm.
- The company's brand has an international reputation and consumers worldwide consider the firm's products/services reliable and trustworthy.

Tata scores relatively low on these parameters compared to world renowned multinationals like GE, Unilever, Philips, etc. So, Tata has to go a long way in creating a place for itself in the international market.

[< TOP >](#)

6. Tata's core competency lies in steel-related technology and products. It can obtain new competitive advantages by forming strategic alliances with leading MNCs known for cutting-edge technologies. Tata has taken the right step in opting out of some of the activities which were merely adding on to its portfolio without any significant contribution to the group's revenues. It should identify the activities that can be given a high growth thrust and those that it can add to its portfolio, while eliminating unrelated activities. It needs to promote a unified Tata brand to be used by all the companies of the Group companies. It may also have to consolidate its focus, develop a corporate mission, recast corporate priorities and resource allocation, and reorganize its corporate structure.

The difficulties or threats that Tata faces in working towards these ends come chiefly from the entry of MNCs into the previously protected Indian market. Strong and cash-rich MNCs are entering the Indian market and buying out small competitors. The new takeover code has made such acquisitions much easier than in the past. This has led to the consolidation and strengthening of Tata's competitors. MNCs, either on their own or through partnerships with domestic firms, have entered several industries. Even in areas of Tata's core competency, small Indian firms in alliance with MNCs pose tough competition to Tata. The advanced technology and the brand power of MNCs are serious threats to companies of the Tata Group. The MNCs are experienced in leveraging their management and marketing expertise and global reputation to capture global markets.

In the days of economic protection, Tata and many other Indian firms which enjoyed protection, became used to domestic standards and business practices. As the Indian market is vast and there were very few players in each industry, they did not feel the need to explore new markets. Therefore their exposure to global standards and competition was very limited. Those firms that did venture into foreign markets, even to a limited extent, were exceptions. With the entry of MNCs in the Indian market, global standards and levels of competition have been brought to India. Many Indian firms are struggling to maintain their position in the domestic market. They are not able to focus on overseas expansion despite the opening up of several markets that were closed until recently.

[< TOP >](#)

7. The government has taken some steps to encourage Indian firms going overseas, especially in the IT sector where Indian firms are doing well. One incentive is income tax exemption for 100% export oriented units, STPs and EPZs. There has been an easing of norms on overseas investment. Indian firms are now permitted to invest \$100 million overseas, and are permitted investments in joint ventures abroad by market purchases without prior approval upto 50 percent of their net worth. This has made overseas acquisitions easier for firms attempting to expand their operations internationally.

The Indian origin of a product is most often a liability for firms because of the poor image of Indian products in

international markets. It may take time for Indian firms to change this image by delivering products which are of high quality and which incorporate advanced technology.

[< TOP >](#)

Section C: Applied Theory

8. ESTABLISHING STRATEGIC CONTROLS

Strategic control focuses on monitoring and evaluating the strategic management process to ensure that it functions in the right direction. In other words, strategic control is concerned with tracking the strategy as it is being implemented, detecting problems or changes in underlying premises, and making necessary adjustments. The purpose of strategic control is to answer the questions such as:

- Are the organization's internal strengths still holding good?
- Are its internal weaknesses still present?
- Has the organization added other internal strengths?
- Does it have other weakness?
- Are the organization's threats still existing and are there any new threats?
- Are the decisions consistent with the organizational policy?
- Are these sufficient resources to achieve the objectives?
- Are the organizational vision, mission and objectives appropriate to the changing environment?

Thus, strategic control provides feedback about the various steps of strategic management. It enables management to find out whether the strategic management processes are appropriate, compatible and functioning in the desirable direction. Sometimes, strategic control may initiate changes in objectives as well. The four basic types of strategic controls are:

1. Premise control
2. Implementation control
3. Strategic surveillance
4. Special alert control

These four types of strategic controls are discussed below. The nature of these four strategic control is summarized

1. Premise Control

Every strategy is based on predicted conditions or assumptions. These predictions or assumptions are referred to as planning premises, and a firm's strategy is designed around these predicted conditions. Premise control helps to check systematically and continuously whether or not the premises set during the planning and implementation process are still valid. If a premise is not longer valid, than the strategy may have to be changed. Premises are primarily concerned with two types of factors. They are:

- **Environmental Factors:** Environmental factors exercise considerable influence over the success of a strategy. Example of environmental factors are inflation, technology, interest rate, government regulation, demographic/social changes, etc. A company has little or no control over such factors and strategies are usually based on key premises about these factors.
- **Industry Factors:** Industry factors affect the performance of companies in a given industry. A few such factors about which strategic assumptions could be made are competitors, suppliers, substitutes barriers to entry, etc. These factors differ among industries, so a company should be aware of the factors that influence success in its particular industry.

Various premises are made about numerous industry and environmental variables. Tracking every premise is unnecessary, expensive and time consuming. So managers should select only those premises that are likely to change and those that would have a major impact on the company and its strategy. After key premises are identified, they should be monitored, and responsibility should be assigned to the persons/departments who are qualified sources of information. Also, premises should be updated(new predications) based on updated information. Finally, key areas of the strategy that are likely to be influenced by the predicted changes should be identified. This is done so that adjustments necessitated by a revised premise can be determined and initiated. For example, senior managers should be alerted about changes in a competitor's pricing policies in order to determine whether the revised pricing or other strategy adjustments are necessary or not. In the same

way managers have to be alerted about technological changes like the development of the web, which enable many companies to market their products internationally without even knowing their customer. Such strategic directions enabled these companies to gain a competitive advantage over their competitors.

2. Implementation Control

The action phase of strategic management is located in a series of steps, programs and moves undertaken over a period of time to implement the strategy. In this phase, programs are undertaken, people are added or reassigned, and resources are mobilized. In other words, managers convert broad strategic plans into concrete actions and results for specific units and individuals as they go about implementing the strategy. These actions take place over an intended period of time designed to achieve long-term objectives.

The strategic control undertaken within the context is known as implementation control. Implementation control determines whether or not the overall strategy should be changed in light of the unfolding events and results associated with incremental steps and actions that implement the overall strategy. There are two types of implementation control: monitoring strategic thrusts and milestone reviews.

- **Monitoring Strategic Thrusts:** Implementing broad strategies involves undertaking several new strategic projects that represent part of what needs to be done if the overall strategy is to be accomplished. Through these projects or thrusts, managers can obtain feedback that help determine whether the overall strategy is progressing as planned or whether it needs to be adjusted or changed
- **Milestone Reviews:** Managers often identify the critical milestones that will occur over the time period when the strategy is being implemented. These milestones may be critical events or major resource allocations. In such cases, a milestone review involves a full –scale reassessment of the strategy and the advisability of continuing or refocusing the direction of the company. Thus, the critical purpose of a milestone review is to undertake a through review of a firm’s strategy so as to control the company’s future.

3. Strategic Surveillance

Strategic surveillance is designed to monitor a broad range of events inside and outside the company that are likely to threaten the course of a firm’s strategy. The basic idea is that some form of general monitoring of multiple information sources should be encouraged. The specific intent of strategic surveillance is to uncover important, Yet unanticipated information. It must be kept unfocussed as much as possible and should be designed as a loose “ environment scanning” activity. Trade magazines, trade conferences, intended and unintended observations are all examples of sources of strategic surveillance. Thus, the purpose of strategic surveillance is to provide an ongoing vigilance of daily operations so as to uncover information they may prove relevant to the firm’s strategy.

4. Special Alert Control

A special alert control reflects that need to thoroughly reconsider the firm’s basic strategy based on a sudden, unexpected event. Such an occurrence should trigger an immediate and intense reassessment of the company’s strategy and its current strategic situation. Many firms develop crisis teams to handle the initial response and coordination needed when faced with unforeseen occurrences. Sometime, when unforeseen occurrences have an immediate effect on the firm’s strategy, companies develop contingency plans along with crisis teams to respond to such circumstances.

[< TOP >](#)

9. By pursuing a strategy of cost leadership, Nissan concentrates upon achieving the lowest costs of production and distribution so that it has the capability of setting its prices at a lower level than its competitors. This strategy suggests that only one company in the industry can achieve a sustainable competitive advantage in this way.

A point to be emphasized here is that pursuing a cost leadership strategy does not merely mean that the company is competing through lower prices. Rather, the idea is that the cost leader will charge industry average prices but with lower costs, and hence will enjoy higher profits.

A cost leadership strategy will only be effective under the following circumstances:

Where the cost leader’s products or services are perceived by the customer as being on par with its competitor’s offerings. If this does not happen, a cost leader will be forced to discount prices well below its competitors to gain sales. This will nullify the benefits of its favorable cost position.

Where there is little or no differentiation between competitors’ offerings.

Advantages

- The advantages of a cost leadership position are:
- The cost leader is protected from industry competitors by its cost advantage
- Lower costs also mean that it will be less affected than its competitors by increases in the prices of

inputs if there are powerful suppliers

- The cost leader will be less affected by a fall in the prices it can charge for its products if there are powerful buyers.
- Since cost leaders usually have a big market share, they purchase in relatively large quantities, thus increasing their bargaining power over suppliers
- If substitute products start to come into the market, the cost leader can reduce its prices to compete with them and retain its market share
- The cost leaders cost advantage constitutes a barrier to entry, because other companies are unable to enter the industry and match the leaders' costs or prices.
- The cost leader is therefore relatively safe as long as it can maintain its cost advantage with price being a key for a significant number of buyers.
- The way in which Nissan developed its mid sized car, the Altima, provides a good illustration of a company that decides to pursue a cost-leadership strategy.

Disadvantages

A firm pursuing a cost leadership strategy cannot be sure of its leadership position because of the following reasons:

- The principal dangers of the cost leadership approach lurk in the competitor's ability to find ways to produce at a lower cost and beat the cost leader at its own game.
- If technological change makes experience-curve economies obsolete, new companies will apply lower cost techniques that give them a cost advantage over the cost leader. Competitors may also draw a cost advantage from labor-cost savings.

The competitors' ability to imitate the cost leaders' methods easily is another threat to the cost leadership strategy. The cost leadership strategy in itself carries a risk, I.e in its single-minded desire to reduce costs; it may lose sight of changes in customer tastes. This will drastically affect the demand for a product.

[< TOP >](#)

[< TOP OF THE DOCUMENT >](#)