

UNIVERSITA' DEGLI STUDI DI MILANO-BICOCCA

Facoltà di Economia

**Dottorato di ricerca in “Economia aziendale, management ed
economia del territorio**

Ciclo XXV



**STRATEGIC MANAGEMENT: SOUTH AFRICAN
WINE INDUSTRY**

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Anno Accademico 2011-2012

*E' necessario imparare a lottare
anche quando non rimane alcuna speranza.*

(S. Pertini)

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INTRODUCTION AND STUDY

The technological development competition and other economic indicators, drive the company to find a new ways for effective management. This maybe overcoming the rigidity of classical theories and creating new analytical models, which change the context of the industrial landscape.

Cost management was used and developed to answer a few of these innovation needs, based on a clear precondition: to support and improve the management over the use of resources both quantitatively and qualitatively. The values, income and other components of the system become a final synthesis of a complex set of decisions, actions and elementary operations, under an organizational structure. The cost management has the advantage of operating on two sides: on one side, it seeks to remedy the deficiencies of traditional systems, on the other it propose improvement routes, by addressing a customer focused strategy. The logic of cost management influences management control system.

The studies of organization and strategy of the company, along with cost analysis studied, help us to identify the development processes of operating business. In this sense, the loss of effectiveness of the hierarchical-functional models by the scientific management and the control systems, confirm the evolution. Otherwise the strategic cost management is an approach to management accounting that emphasizes issues and strategic problems. The economic-financial information are used to developed strategies as a way to achieve a competitive advantage, it aims to reduce costs in the long term, when these are considered significant for the company.

Gap analysis is a central part of the teleological approach to change where dissatisfaction with the current state is expressed as differences between the present

situation and a desired future state, which drives strategies for closing the gap. These differences might represent any number of structural or performance characteristics and are reflected as a gap between the present and the future that forms the basis for the change program. The analysis involves identifying who needs to be changed, what needs to be changed, and how (the strategy) the change might be accomplished. A checkpoint is also frequently included for evaluating the feasibility of being able to close the gap, which might result in altering the desired state to one more attainable. Tactics for closing the gap include: lengthening the time frame for accomplishing this goal, reducing the scope of the change, reallocating resources to achieve goals, and obtaining new resources.

The management of a company changes following the production strategies and the various needs customers. The key to understanding, analyzing and recommending the logic and the dynamics of the company, is represented precisely by the strategic process, namely from all the activities and operations that across the company, transform the resources into results.

This paper expand on prior management accounting change research by presenting evidence from wineries in South Africa. I will try to understand how the strategic choices, may be different from one country to another. We analyze the wineries under three different strategic profiles that will be briefly mentioned and discussed in more detail later.

Identifying three different strategic aspects will try to understand, for each of these, what factors are most influence and how we can influence the life of the company.

There are three different kinds of strategy, which inform to study the company and to understand what the decisions to be taken are. These are Corporate Strategy, Business Strategy and Functional Strategy with cava all levels of the organization of a company decision making:

1. Corporate strategy

Is concerned with the overall purpose and scope of the business to meet stakeholder expectations. This is a crucial level since it is heavily influenced by investors in the business and acts to guide strategic decision-making throughout the business. Corporate strategy is often stated explicitly in a "mission statement".

- What are the markets where it should compete and in what kind of activities are involved these markets? (market; scope)?
- How can the company have better performance than its competitors? (Competitive advantage)?
- What external, environmental factors affect the businesses' ability to compete? (Environment)?
- What are the products that can be better for the company to maintain or create the own competitive advantage? (Products)?

2. Business strategy

It is concerned more with how a business competes successfully in a particular market. It concerns strategic decisions about choice of products, meeting needs of customers, gaining advantage over competitors, exploiting or creating new opportunities.

What resources (skills, assets, financial planning, relationships, internal technical competence and facilities) are required in order to be able to compete? (resources/ budget)?

To learn the concepts and techniques related to the provision and analysis of financial information, we take advantage of strategic cost management theory. A sophisticated understanding of a firm's cost structure can go a long way in the search for sustainable competitive advantage¹.

¹ Implementing Strategy – Lawrence G. Hrebiniak; William F. Joyce

Cost analysis traditionally is viewed as the process of assessing the financial impact of alternative managerial decision; the strategic elements became more conscious, explicit and formal.

Strategic cost management is an umbrella term used to define a form of analysis used primarily in manufacturing-based operations². This type of executive level analysis tries to combine some of the concepts from business cost management techniques and management accounting with the more traditional corporate to strategic management concepts.

The reason it is an umbrella term is because it involves three different types of business analysis techniques; namely cost driver analysis, strategic positioning analysis and value chain analysis.

The fact that it incorporates three different analysis techniques adds to the complexity of the process, their operational choices and their product roadmap. But this should be seen as providing much richer results and more in-depth analysis of the manufacturing environment.

The Business strategy is founded on three pillars.

Pillar 1: Cost driver analysis

Cost driver analysis is concerned with determining what the actual drivers of activity costs are within your operations. Business cost management analysis may pinpoint that indirect costs such as maintenance actually driven by the number of machines or activities being performed per hour by your operations.

This has a bearing on strategic cost management since cost drivers can actually be determined by both structural cost drivers and executional cost drivers.

Structural cost drivers relate to strategic management choices that drive costs. From this perspective there are at least five strategic choices by the firm regarding its underlying cost driver position for any given product group:

² Implementing Strategy – Lawrence G. Hrebiniak; William F. Joyce

- *Scale*. How big an investment to make in manufacturing, in R&D and marketing resources.
- *Scope*. Degree of vertical integration (Horizontal integration is more related to scale).
- *Experience*. How many times in the past the firm has already done what it is doing again.
- *Technology*. What process technologies are used at each step of the firm's value chain.
- *Complexity*. How wide a line or product of services to offer to customers.

What is more useful in a strategic sense is to explain cost position in terms of structural choices that shape the firm's competitive position; not all the strategic drivers are equally important, but (more than one) of them are very probably very important in every case.

For each cost driver there is a particular cost analysis framework that is critical to understanding the positioning of a firm. Being a well-trained cost analyst requires knowledge of these various frameworks.

Executional cost drivers relate to the actual operational processes and norms within operation. The effective use of staff, process layouts, just-in-time processes, etc. all have a bearing on the cost of executing activities within the firm. The list of basic executional drivers includes at least the following³:

- Work force involvement (participation) – the concept of work force commitment to continual improvement.
- Total quality management (beliefs and achievement regarding product and process quality).
- Capacity Utilization – (given the scale choices on plant construction).
- Plant layout efficacy – (how efficient, against current norms, is the layout?).
- Product Configuration – (Is the design or formulation effective?).

³ Strategic Cost Management – John K. Shank; Vijay Govindarajan

- Exploiting linkages with Suppliers/Customers, per the firm's value chain.

These types of business cost management techniques and analysis approaches are nothing new.

Pillar 2: Strategic positioning analysis

Strategic positioning analysis is an approach for researching what future environments might be like in their internal corporate structure as well as they external environment and determining the choice of business strategies to get from current situation to these desirable goals.

Some of the questions these types of strategic management concepts are trying to answer include:

- What are the opportunities and threats you can perceive in the current economic climate?
- What is the future economic landscape like for your products, market and business?
- What is the current state of your business?
- How could the company be roughly positioned in the future landscape?
- What systems need to be instigated in order to attain this future position?

Analysis starts with establishing what trends you can perceive. This means working out what technological/business opportunities or customer segments are altering which could turn into tomorrow's big earners. This becomes important to strategic cost management since investment in new technologies or risky new ventures can be highly risky.

Analysis of the status-quo often involves using some fairly standard strategic management tools such as:

- SWOT analysis – Strengths and weaknesses within your firm; opportunities and threats within the external competitive market.

- Product/market matrix - Establishing what new markets, product changes, product lines or market variations could prove profitable.
- Portfolio analysis – Establishing which of your projects are potential cash cows, stars, question mark or dogs.

The meat of strategic positioning analysis is deciding what strategies to choose for attaining specific goals or pursuing specific trends. To achieve this many companies consider stabilizing certain technologies, growing the company in specific areas or technologies, shrinking operations in specific technologies/products/markets or even doing a complete turnaround on ventures.

This also has a bearing on their innovation strategy, business development strategy, business intelligence strategy, communication strategy. There is a strategic cost management element associated with each decision you make which will have a bearing on the structural and executional costs.

In particular business cost management analysis will have to be completed to see how changes in their strategic direction are going to affect marketing plans, production plans, research work, personnel requirements, organizational structure, operational procedures, purchasing decisions, logistics, quality and public relations.

Pillar 3: Value chain analysis

Value chain analysis is an approach used to determine the series of activities involved in creating and building value within your operations. It requires a systematic approach to examining each different element in our primary activities as well as support activities.

The operations of the organization may be split out into both primaries as well as support activities.

Primary activities: Inbound logistics, operations, outbound logistics, marketing & sales and service.

Support activities: Procurement, technology development, human resources management and firm infrastructure.

These have a bearing on strategic cost management since all of these activities have a bearing on operational, structural and executional costs. By making strategic decisions around our value chain we can actually determine the level of these costs.

There is overlap between these three different types of strategic cost management analysis techniques which can all relate back to our executional, structural and organizational costs. Each type of analysis is aimed at establishing where cost benefits can be achieved through strategic choices we make within the firm.

This is not a fine science but requires careful analysis of how strategic management concepts provide positive or adverse reactions to each element of your value chain, positioning decisions and cost drivers. The art in doing this is working out strategies which have the most preferential cost benefits.

In this research we analyzed only the first and the second pillar, deepening the second one in the third part, the case study.

3. Functional Strategy

Is concerned with how each part of the business is organized to deliver the corporate and business-unit level strategic direction. Operational strategy therefore focuses on issues of resources, processes, people etc.

Once higher level corporate and business strategies are developed, management need to formulate and implement strategies for each functional area. For effective implementation, strategists have to provide direction to functional managers regarding the plans and policies to be adopted. In fact, the effectiveness of strategic management depends critically on the manner in which strategies are implemented. Strategy of one functional area can't be looked at in isolation, because it is the extent to which all the functional tasks are interwoven that determines the effectiveness of the major strategy.

Functional area strategy such as marketing, financial, production and Human Resource are based on the functional capabilities of an organization. For each functional area, first the major sub areas are identified and then for each of these sub functional areas, contents of functional strategies, important factors, and their importance in the process of strategy implementation is identified.

In terms of the levels of strategy formulation, functional strategies operate below the SBU or business-level strategies. Within functional strategies there might be several sub-functional areas. Functional strategies are made within the higher level strategies and guidelines therein that are set at higher levels of an organization. Functional managers need guidance from the business strategy in order to make decisions. Operational plans tell the functional managers what has to be done while policies state how the plans are to be implemented.

Major strategies need to be translated to lower levels to give holistic strategic direction to an organization. Functional strategies provide details to business strategy & govern as to how key activities of the business will be managed. Functional strategies play two important roles.

Firstly, they provide support to the overall business strategy. Secondly, they spell out as to how functional managers will work so as to ensure better performance in their respective functional areas. The reasons why functional strategies are really important and needed for business can be enumerated as follows:

The development of functional strategies is aimed at making the strategies-formulated at the top management level-practically feasible at the functional level.

Functional strategies facilitate flow of strategic decisions to the different parts of an organization.

They act as a basis for controlling activities in the different functional areas of business.

The time spent by functional managers in decision-making is reduced as plans lay down.

4. Research

The “strategy gap,” as this group of missing steps is called in this research, is real and exists within most organizations. Often unseen, the gap is a threat to the future performance—and even survival—of an organization and is guaranteed to impact the efficiency and effectiveness of senior executives and their management team. Organizations must plan and start executing that plan today if they expect to achieve their objectives sometime in the future. Yet surveys indicate that this just is not happening.

Without the ability to achieve objectives, executives and managers become mere bystanders in an organization where performance—or non-performance—“just happens.”

What is it about the strategic planning process and its execution that fails? Why do systems so frequently fail to live up to management’s expectations? These are crucial questions that need to be answered if the strategy gap is to be avoided.

The notion of competitive advantage understands the outcome of a strategy that enables the company to occupy and maintain a position favorably in the markets where it operates. This translates into a return higher than the average of actual and potential competitors.

The main objective and mandatory for any company is to create value, it follows that the value itself must be addressed and aligned with the strategic choices of the company. Most of these choices belong to the sphere of competitive strategy, in the sense that affect the conditions necessary for obtaining competitive advantages and the resulting revenue streams and value. Since the process of value creation inevitably by obtaining a competitive advantage, try to understand the determinants of the latter thus assumes central importance.

The goal of this study is to identify this gap, and the answer at to this question analyzing not all the company but specifically the wineries. The choice about this kind of firm comes of the desire to compare two different markets. How culture, consumer behavior, or your target markets affect these choices? Will explore the three level

strategies that have been previously discussed, and analyze the strengths and weak point for each of these. This work will divide in two parts: the first is a literature, the second is an analysis of the South African wineries.

The problem that we want to analyze and understand is “Why” and “How” the strategies that exist at various organizational levels are changing and how they increase or decrease competitive advantage. This research analyzes the strategic process of companies to understand where it and where it wants to be. The research studies the behavior not of the all company but only of the winery. The aim of the research is to find ways of enhancing and management consolidation and branding in the South Africa wine industry. It sought to identify what needs to be in place to develop competitive the South African wine industries.

Wine business has been dominated through most of the 20TH century by Western Europe. “Old Word” countries such as Italy accounted for the majority of grapes and wines produced. Most of the consumption was also concentrated in these markets since wine was considered part of the traditional way of life. In the last decade, rising “New World” wine countries such as Australia, USA, New Zealand and South Africa have been challenging the stronghold of the traditional producers⁴.

This study adopt a multiple case study approach based on a detailed fieldwork: a face to face interview and a questionnaire will be submitted some wineries in South Africa.

Strategic plans typically have a structure that makes them easy to follow. Most start by stating the purpose of the organization, which is usually followed by documenting the long- and short-term goals and the plans for achieving these goals. However, the terminology contained within these plans often varies between organizations, and the words have different meanings.

In the context of this research, these definitions will be used:

- ***Vision***: A concise statement of the organization’s reason for existing;

⁴ Orth, Lockshin, and d’Hauteville, 2007

- **Goals:** Broad statements describing the targeted direction;
- **Objectives:** Quantifications of objectives for a designated period of time;
- **Strategies:** Statements of how objectives will be achieved and the major methods to be used;
- **Tactics:** Specific action steps that map out how each strategy will be implemented.
- **Key Performance Indicators:** Measures of performance that show progress of each tactic in reaching the goals.

Part 1

Strategic management

In evaluating the business prospects of the company, managers must ask themselves three key questions: what is the current situation of the company? Where we want to go? How should we do to achieve this? To give a complete answer to the first question must assess the conditions and pressures competitive within the industry, the performance and position of the current market, its capacities and strengths in terms of resources, and its weaknesses in a competitive manner.

The definition of the objectives to be achieved requires some decisions on which direction to take: whether and under which new groups of customers or new needs of consumers, seek, what we should aspire to positions of market and what changes are needed. Planning the route to achieve its goals puts managers in the position of having to develop and choose strategic choices can able to lead the company in the desired direction to increase its turnover and to improve its financial and market performance.

Increasingly important to firm success, strategy is concerned with making choices among two or more alternatives. As we noted, when choosing a strategy, the firm decides to pursue one course of actions instead of the others. The choices are influenced by opportunities and threats in the firm's external environment as well as the nature and quality of the resources, capabilities, and core competencies in its internal organization.

The fundamental objective of using any type of strategies is to gain strategic competitiveness and earn above-average returns. Strategies are purposeful, precede to

taking of actions to which they apply, and demonstrate a shared understanding of the firm's vision and mission.

An effectively formulated strategy marshals, integrates, and allocates the firm's resources, capabilities, and competencies so that it will be properly aligned with its external environment. A properly developed strategy also rationalized the firm's vision and mission along with the actions taken to achieve them. Information about a host of variables including markets, customers, technology, worldwide finance, and the changing world economy must be collected and analyzed to properly form and use strategies. In the final analysis, sound strategic choices that reduce uncertainty regarding outcomes are the foundation for building successful strategies.

Every firm must form and use a business-level strategy. However, every firm may not use all the strategies – corporate-level, merger and acquisition, international, and cooperative. A firm competing in a single-product market area in a single geographic location does not need a corporate-level strategy to deals with product diversity or an international strategy to deal with geographic diversity. In contrast, a diversified firm will use one of the corporate-level strategies as well as a separate business-level strategy for each product market area in which it competes.

I want to examine the corporate level strategies, that is concerned with determining the business in which the company intends to compete as well as how to manage its different business. In the next chapter I inspect the business-level strategy that describes the actions a firms decides to take in order to exploit its competitive advantage over rivals. A company competing in a single product market has but one business-level strategy while a diversified firm competing in multiple product markets forms a business-level strategy for each of its business. In the next part I analyzed the functional strategy, the strategy of single internal business functions.

Chapter 1

Concept of strategic management

This section aims to provide a brief overview of the main features and purported benefits of strategic management and sets out some ideas, principles and terms that capture the essence of what mainstream academics and managers commonly describe as constituting strategic management.

Strategic management remains a concept that is difficult to define. Nevertheless, a review of the literature does provide a degree of consensus about several key characteristics such as decision-making and the long-term clarification and specification of objectives that together present a coherent model of strategic management.

Chandler, for example, emphasized that the determination of long-term goals and objectives as being central to strategic management. Also, he identified the capacity to decide courses of action and allocate the resources necessary to achieve them, as being crucial to the overall strategic process. Consequently, Chandler (1962) defined strategic management as "...the determination of the basic long-term goals and objectives of an enterprise, and the adoption of courses of action and the allocation of resources necessary for carrying out these goals"⁵.

The objective of the cost analysis in the Management accounting view, articulated by Simons et al. (1954) who coined three phrases to capture the essence: "Score Keeping", "problem solving" and "attention direction". These three roles are not seen as varying across firms depending on strategic context, the relevance of the related cost analysis tools also is not seen to vary across the firm. If agreement could be

⁵ A. Chandler; *Strategy and Structure: Chapters in the History of the American Industrial Enterprise*

reached that why we do management accounting differs in important ways depending on the basic strategic thrust.

Even, if management accounting in most companies today is still heavily involved with conventional tasks, it is important to realize that this focus need not be true in the future. Management accounting can adapt to the real business needs of the firm, if those needs are articulated.⁶

Strategic management offers other tangible benefits, such as an enhanced awareness of external threats, an improved understanding of competitors' strategies, increased employee productivity, reduced resistance to change, and a clearer understanding of performance reward relationships. Strategic management enhances the problem prevention capabilities of organizations because it promotes interaction among managers at all divisional and functional levels (Greeniey 1986:106). Interaction can enable companies to turn on their managers and employees by nurturing them, sharing organizational objectives with them, empowering them to help improve the product or service, and recognizing their contributions. More companies today fail as a result of change. That is, companies either fail to respond to changes in their environment or they fail to create change. Strategic management is a method by which companies can become more competitive and increase their chance of survival.

All firms, including wineries, use the strategic management process (see Figure 1), as the base for the commitments, decisions, and actions they will take when pursuing strategic competitiveness and above-averages terms.

⁶J. Shank, V. Govindarajan "Strategic cost Management" Chapter 1

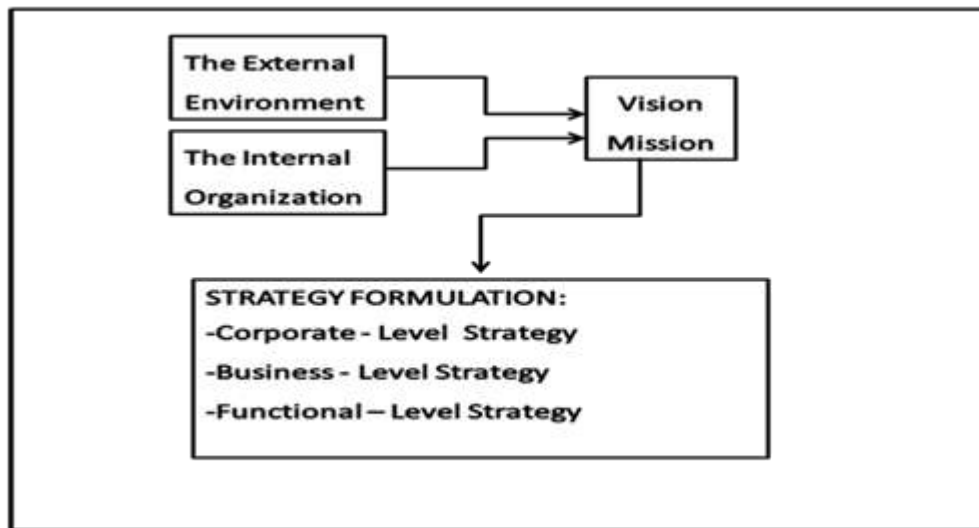


Figure 1 The strategic management process

The strategic management process is the full set of commitments, decision and actions required for a company to achieve strategic competitiveness and earn above-averages returns.

Strategic competitiveness is achieved when a firm successfully formulates and implements a value-creating strategy.

Strategy is an integrated and coordinated set of commitments and actions designed to achieve a specific goal, and designed to exploit core competencies. Strategy is all about gaining (or being prepared to gain) a position of advantage over adversaries or best exploiting emerging possibilities. As there is always an element of uncertainty about future, strategy is more about a set of options (“strategic choices”) than a fixed plan. So, we can say that the strategy is a set of business decisions that the company pursues to coordinate and manage its activities.

When choosing a strategy, firms make choices among competing alternatives as the pathway for deciding how they will pursue strategic competitiveness⁷. In this sense, the chosen strategy indicates what the firm *will do* as well as what the firm *will not do*.

⁷ J. McGregor, 2009, Smart management for tough times, Business week, March 2012

As a firm has a competitive advantage when it implements a strategy competitors are unable to duplicate or find too costly to try to imitate⁸. A company can be sure that its strategy is a competitive strategy only after competitors' effort to duplicate its strategy have ceased or failed. Is important that a firm understand that there isn't a permanent competitive advantage, the speed with which competitor are useful to acquire the skills needed to duplicate the benefits of a firm's value creating strategy determines how long the competitive advantage will last.

The first step in the strategic management process is to analyze its external environment and internal organization to determinate its resource, capabilities and core competencies⁹.

With this kind of information, the firm is ready to develops its vision and mission and formulates one or more strategies. To implements its strategies, the firms takes actions towards achieving strategic competitiveness and above-averages returns. Effective strategic actions that take a place in the context of carefully integrated strategy formulation and implementation efforts result in positive outcomes. This dynamic strategic management process must be maintained as ever-changing markets and competitive structures are coordinated with a firm's continuously evolving strategic inputs¹⁰.

In this research, I use the strategic management process to explain what wineries do to achieve strategic competitiveness. I want to explain/demonstrate why some winery consistently achieve competitive success while others fail to do so.

Is important for understand the strategic management process the reality of global competition, like a critical part of that, and the influences firm' performance. Indeed, learning how to successfully compete in the globalized world is one of the most significant challenges for firms competing in the current century.

⁸ H. R. Greve, 2009, Bigger and safer: The diffusion of competitive advantage, Strategic management journal.

⁹ The source of its "strategic inputs"

¹⁰ T. R. Crook, D. J. Ketchen, 2008, Strategic resources and performance: a meta-analysis, Strategic management journal.

The competitive landscape

This challenging landscape is being created primarily by the emergence of a global economy, globalization resulting from that economy, and technological changes.

The emergence of a global economy and technology, specifically rapid technological change, are the two primary drivers of hypercompetitive environments and the nature of today's competitive landscape.

There are some characteristics of the current competitive landscape that are noteworthy. Conventional sources of competitive advantage such as economies of scale and huge advertising budgets are not as effective as they once were in terms of helping firms earn to strategic competitiveness. Managers must adopt a new mind-set that values flexibility, speed, innovation, integration, and the challenges that evolve from constantly changing conditions.

Hypercompetition is a term often used to capture the realities of the competitive landscape. Under conditions of Hypercompetition, assumptions of market stability are replaced by notions of inherent instability and change; Hypercompetition results from the dynamics of strategic maneuvering among global and innovative combatants. It is a condition of rapidly escalating competition based on price-quality positioning, competition to create new know-how and established product or geographic markets. In a hypercompetitive market, firms often aggressively challenge their competitors in the hopes of improving their competitive position and ultimately their performance.

The global economy

A global economy is one in which goods, services, people, skills and ideas move freely across geographic borders. Relatively unfettered by artificial constraints, such as tariffs, the global economy significantly expands and complicates a firm's competitive environment¹¹. Interesting opportunities and challenges are associated with the emergence of the global economy.

¹¹ S.H. Lee, 2009, Flexibility in internationalization: is it valuable during an economic crisis? Strategic

Globalization is the increasing economic interdependence among countries and their organizations as reflected the flow of goods and services, financial capital, and knowledge across country borders. Globalization is a product of a large number of firms competing against one another in an increasing number of global economies.

In globalized markets and industries, financial capital might be obtained in one national market and used to buy raw materials in another one. Manufacturing equipment bought from a third national market can then be used to produce products that are sold in yet a fourth market. Thus, globalization increases the range of opportunities for companies competing in the current competitive landscape¹².

Additionally, highly globalized firms must anticipate ever-increasing complexity in their operations as goods, services, people and so forth move freely across geographic borders and throughout different economic market.

So, entry into international markets, even for a firm with a substantial experience in the global economy, requires effective use of the strategic management process. It is also important to note that even though global markets are an attractive strategic option for some companies, they are not the only source of strategic competitiveness. In fact, for most companies it is critical to remain committed to and strategically competitive in both domestic and international markets by staying attuned to technological opportunities and potential competitive disruptions that innovations create¹³.

Technology and technological changes

Technology-related trends and conditions can be places into three categories: technology diffusion and disruptive technologies, the information age, and increasing knowledge intensity. Through these categories, technology is significantly altering the nature of competition and contributing to unstable competitive environments as a result of doing so.

¹² E. Thornton, 2009, The new rules, Businessweek, January 19, 30-34.

¹³ R.D. Ireland & J. W. Webb, 2007, Strategic entrepreneurship: creating competitive advantage, through streams of innovation.

1.1 The strategic orientation

At the core of every decision and strategic process of all economic organizations must be identified a strategic orientation that allows you to define fully the business vision of the entrepreneur or the management of reference.

In many cases, the non-coherent strategic choice of baseline, or attitude of the management is not adequately responsive to key business variables, such as strategies or resources, have resulted in resounding failures, in recent times, to contribute to the difficulty of the choices of a good strategic background came the economic crisis, which has with him a very strong factor of unpredictability that makes the choices even more difficult and delicate, increasing the risk of irreparable errors.

You can assume four variables that make up the guidelines:

1. The field of activity;
2. The time horizon;
3. The development of dimension;
4. The development of quality.

1) The field of activity

This is a very important factor, because the organization and in particular entrepreneur or manager must carefully choose which path to take on the type of task. They must also decide whether or not to do something about the economic implications arising from financial policies associated with it. Is configured in this way, an analysis of the real options of investment, in which there are careful studies arising from the most important developments in financial theories in recent years. The principle of choosing an investment firm or another is based on the dichotomy resulting from use or not to enter into a new field of activity and profits that may arise, of course, if you opt for an investment that is not entirely consistent with the core of the business may create doubts about the largest shareholders, who will decide to support the project only with solid arguments on the degree of competition reached by new entrants.

The decision to build or not an investment is also linked to its implementation, with a flexible approach, in fact, during the organization and subsequent translation into business reality, dividing the work into several phases to better assess the costs and benefits. In fact, lately the approach companies use a stage-gate product development, where each phase is subject to careful analysis and evaluation of various kinds before moving on to the next one, and in this way you can then better evaluate a project and change or block their execution before the end. Wanting to observe new trends, one can say how the companies currently pay much attention to enterprise scalability, aimed at a willingness of the company to increase the size of the assets and/or replicate it elsewhere in case you have strong growth prospects, the which will ensure a guarantee of survival over time.

There are may be some strategic formulations, along with the tools to assess options, make it possible to find the most information and thus establish the economic value created for shareholders.

So the strategy allows you to better manage growth options and flexibility:

- *growth options*: the company initials make small investments in various business opportunities for its future, but does not create constraints with any of these;
- *flexibility options*: they develop projects and systems "flexible", that is, which are able to adapt to different situations potential in the future, and therefore there will of flexible manufacturing systems which working on a single production line will carry out the various versions of the product set business plans.

Even projects, as mentioned above for investments will be structured in stages and therefore have growth options and flexibility, preventing any kind of constraint arising from the integral development of a project. In fact, if you were to see that in the early stages of production and placing on the market, with the "beta", the products will not achieve the targets set, can be blocked, and with their projects.

For growth options, you have to remember three possible options:

- Investment in platforms are the investments that create products or basic technologies which, if properly structured, can provide great opportunities for business side flanking the core technology, resulting in great creations of value;
- Strategic Alliances and Joint Ventures: This is joint investments, including small and medium sized, with 2 or more undertakings which generate new strategies for creating value and competitive advantage of cost and differentiation;
- Organizational skills: they are a very important factor since it may offer potential opportunities to create competitive advantages from better products, sometimes unique, and diversification. Often the high professional skills of a company, after the entry into the market of their products, they can improve the quality standards of their competitors, or even more egregious cases and recent, create a new market.

2) The time horizon

It is a very important variable of the strategic background by virtue of the survival of the organization, many companies, with actions driven by short-term strategies, at times, undermine the solidity of the company for the simple pursuit of short-term profit. Of course, each company will have a time horizon focusing on the short or long term, defining specific behaviors strategic plans in terms of:

- A- Target corporate profit;
- B- Relationships / interrelationships with stakeholders;
- C- Business succession;
- D- Reorganization / restructuring.

A) Target corporate profit

Among the variables of the time horizon, the bottom line is configured as a main objective for the firm's survival.

Profit is intended for the positive difference of revenue earned on the costs that can be distributed among the owners of the company, its maximization is the main objective, but to be realistically implemented should be well planned. In fact, a prerequisite for the maximization is to be clear as to achieve and maintain economic relations company (net income, ROS, ROE, ROI, ROA) to measure business performance perfectly. Corporate profitability can be measured by the return on equity business that is divided into two types:

- Return on capital can be defined as a return of investors to the use of his capital;
- Income statement intended as a surplus generated by the business available after they have been paid all the components of capital, including capital. It is the best way to measure the company's performance, and can also be called economic rent.

To better measure the income statement, various methods have been studied, the most common of which turns out to be nowadays the Economic Value Added (EVA) is operating income after tax (Net Operating Profit After Taxes) less the cost of capital, which is derived from the weighted average cost of capital (Weighted Average Cost of capital).

The choice of economic income also comes from some of the advantages of a financial nature and cost of the measurements:

- Managers, the removal tool for measuring the performance, must comply with the very strict parameters and maintain a degree of internal discipline once the business results and avoid damaging the positive results with corporate investment policies and then use of capital also outside, wrong ;
- we have a better view of the allocation of capital between the different business activities, since the presence of the index weighted cost of capital,

allows us to observe and evaluate the effects of the costs due to political capital intensive.

B) Relationships / interrelationships with stakeholders

In carrying out its activities, a company interacts with various subjects, such stakeholders, i.e. stakeholders, and those who are part of or have contact with a company modify its behavior according to their expectations and thus change the corporate strategy.

The companies, in their normal activities, creating value, the exchange with the social partners and more specifically: employees (wages and salaries), external financing (interest payments), the owners of real estate (revenues), the State (taxes) and the owners of the company (profits and dividends per share). In addition to monetary exchange entities, companies create value for customers satisfaction in terms of purchase of the product, obtaining the trust if the product will be deemed valid; doing so companies can benefit from the surplus of the consumer, that is, their willingness to pay a higher price for a higher quality product with better services. It can be argued that companies should try to maintain a balance between the interests of the various stakeholders, trying to mediate the various requests received avoiding conflicts and the positions taken by a very strong category or another.

Historically, there are several guidelines were in balance to maintain between the various stakeholders, are also conditioned by the internal regulations and geographical locations. Indeed, in English countries, there is a strong shareholder capitalism, where both administrators and the rest of the organization are aimed to maximize profits for the owners. However, in other European countries, regulations are more stringent and require companies to discuss and consider the interests of employees, the State and also other companies, forcing all companies to mutual respect. It has been seen in recent years as policies oriented toward capitalism very strong and valid without controls have led to disastrous situations from the financial point of view, all due to bad choices of shareholders who, pressing the top and corporate collusion

with the directors, chased easy financial gains with short-term strategies, consuming the company in which they were stakeholders.

C) Business succession

In decisions on the strategic business, an entrepreneur must also include how to handle the succession. In fact, being in many cases the founder, the company will feel like one of his creatures and may be tempted not to think about the future, a clear sign of a strategy for the short to medium term. Companies, by their nature, follow the principle of continuity if the market conditions allow and this is guaranteed by all those who have a role of engine of business. All those who interact with the company, starting from owners, administrators move up to the employees, have an interest in knowing what the future of the company, especially in view of changes at the top for guarantees of continuity.

The size of the company is a very important factor to consider in succession, as the number of subjects that are part of the organization is very high and as a result, corporate governance bodies will have to deal with special situations:

- Insert the heirs in management positions and directly from the company at the time of taste, without being tempted to place their children in positions where they would express well their potential. Are widespread cases of important positions in society occupied by persons inadequate or insufficiently prepared, with a lot of heavy consequences from the point of view of the solidity company, which is put at risk by incorrect choices;
- the subdivision of shares, the size of which in this case plays a key role: grants of shares to the heirs of the founder can conserve the property of the company. This mode of allocation of shares in the company shows a master and myopic vision than large companies often have a share of stock on the market for trade;
- the granting of compensation: should be commensurate with the activities. It often happens that they are bestowed fees, whatever their activity, or in the

worst cases, compensation is not at all reflecting the actual activity carried out within the company.

Especially in cases of short-term strategies, employees with short-term contracts will try to get the most from the organization in the short term, or until the end of their contract, this strategy management to hire people for short periods of time is very negative because it is not at all aimed at a long-term perspective, it will develop alternatives and suitable replacements in personnel. There are very important studies which have shown that young managers, but also managers and employees, they need a period of "break-in" before being able to create value for the company, in fact, the senior being those who will give him the way to work, will give their "heirs" the basis for the company to grow. Had the basics, and thanks to their new knowledge, the new generation will be able, if conditions permit, to improve the products / services of the companies in which they operate, allowing firms to survive and grow in the market.

Strategies for succession should be oriented to ensure good continuity of the company in the future, above all, must be considered as the basic entry in the company of qualified managers, strong leadership and the future cost containment.

D) Corporate restructuring

In succession, as well as changes to senior management and intermediate levels, there are often corporate restructuring. These operations are very important for business organizations because it may allow the achievement of a greater competitive strength of the enterprise.

Of course, forecasts of corporate restructuring must be provided and planned for a long-term horizon, as will also be linked to the objectives of profit. The major corporate restructuring transactions relate to investments to be made after careful evaluation of which can increase profits, you should not seek easy money in the short term, because it does not guarantee the continuity of the results and may cause damage to corporate stability.

Another area in which they can, and in fact you often, restructuring, is the staff. The area of the staff is perhaps one of the most important and sensitive to business restructuring in the company's consolidated balance will change in some cases by the turnover. In addition, thanks to the laws of the various states, it must meet any agreements with the trade unions, with regard to redundancies and regulations on social security benefits, in recent times, is a very treated by the press, due to the effects of crisis, which has hit very hard business. It has been noted in fact that corporate restructuring, where they were possible, led strategies aimed at seeking more of short-term profits at the expense of the staff, many companies have preferred to rely on the instruments provided for in the legislation, such as layoffs or similar trying to contain internal costs. This choice is very wrong, especially since denotes a lack of strategies to launch the company in temporary crisis, preferring to get small short-term gains than to seek a raise competitive for the future. It should also be noted that the current situation is very unpredictable, and it allows you to have a clear vision of the future Circulation that could have the market in the medium term, given the situation, companies are very careful in planning future actions .

Last but not least in importance, must also be involved in restructuring the research and development, and training. This company is very important because it is one in which all projects are developed and the ideas that are then transformed into products to be made and placed on the market. The best choice you can make an entrepreneur, but also a society, is to allocate many resources to this line of business since, if the products are successful, will allow you to have good long-term implications. It is an area that does not show the company almost never results in the short term, because it takes time to study the variables in which we will move: market conditions, consumer desires, engineering costs and product development and for advice. And it is its weight in terms of cost and the door to be affected by corporate restructuring because sometimes you do not recognize their importance, especially for long-term strategies. When there is a tendency towards short-term strategies, research and development suffer a cut very decided preference for short-term profits in order to maintain corporate profits. These actions, especially in recent times, have the effect of

return or otherwise to maintain the profitability of the company, but at the price of a loss of competitiveness in the future.

So in corporate restructuring and raising, research and development must be fully provided by the companies, if they are not in serious trouble, because they represent a good way to achieve profitability in the medium term and ensure the survival of the company, of course, the development will be very well designed and supported by investment and appropriate staff to avoid worsening the situation even worse products.

3) The develop of dimension

It is an important element of the strategic orientation of the bottom, in regard to the size that will have the company in the market. Means not only the actual size of the plants, the company has the capacity to grow in the market or at least to maintain its presence and say his name.

Dimensional development is often associated with the positive factor of the growth of the company, because if a company is not growing, you do not think that will have no chance to survive in the market. It is not always true, since there are in the business world who have decided to maintain a size not very big, but they have large margins and continue their activities. For growth also means its propensity to expand its product portfolio, that is not to focus too closely, developing the business side of the core support. In broadening its offer, the company can follow two main roads:

- Create products that have the same characteristics as the main one, but vary in size and potential. In this way it is possible to employ the same plants of the main product, by applying small modifications to adapt production. So the company can not incur costs resulting from the purchase of new equipment for the production of other goods, focusing and improving those that represent their core business. Accessories and support may be sold, subject to commercial agreements with the parent company, other specialized companies which, having a greater know-how about this range of

products they will carry these products at a lower cost because of their experience in the field, trying to still maintain a good standard of quality.

- Opt for a production that goes from its base product to accessories, it therefore being of a single article, and thereby increase the number of installations for the production of accessories, also integrating the field of marketing, controlling in this way a large part of the supply chain. This strategy appears to be in most cases more expensive than the previous one in that the design and implementation of the company's major assets other than those involving higher costs for the company to expand the facilities.

Of course, the whole production will remain within our company, and will be checked carefully before being marketed, the decision not to outsource technology accessories could respond to a strategy of trying to maintain quality and knowledge inside the 'company. In fact, the outsourcing of some phases of the production as a risk for businesses to "spread" of a part of the technology portfolio that has helped to create the product and potentially create new competitors. Lately a great closure to the dissemination of know-how has become impossible, given the development of technology and the level of imitation that has been reached in some areas, the only way to contain this phenomenon is to impose a block to the service support for users of unauthorized products, although this could backfire.

These two policies for growth, more towards the creation of more products similar to each other and outsourcing of some production phases, while the other in wanting to maintain its identity against the trends of the market, it must have a base of medium-long term because these are decisions that lead effects after a while 'time.

We have to consider also the possibility that the company will grow, that is considered a growth induced by the simple desire to increase the size of your company or let everything happen physiologically.

In the first case, when the growth is "pushed" by the entrepreneur or from the direction, regardless of the ability to increase strength, denotes a frantic search for

visibility regardless of the conditions corporate. The search for greater visibility resulting from a higher dimension, in the majority of cases that were analyzed showed how sometimes very questionable choices have been made, also from the point of view of consistency. In fact, to increase the size of their company skills are required from the management point of view and experience that require time, which cannot be certainly be obtained without adequate studies. But also the desire to reduce the risk by excessive fragmentation can be counterproductive as it will have higher costs from Spin-offs and therefore even if the company will increase its size could become "a giant with feet of clay."

In the second case, allowing the company to grow "physiologically", apply strategies for medium to long term, while maintaining the internal balance. This choice of business expansion is much more consistent than the last, because you decide to observe the trend of the market and then take action to meet the demands of customers, in addition, from the point of view of competition, do not try to be the strongest in regardless of its strength, but study all the players in the market and therefore plan the best choice to survive and eventually grow. In fact, the corporate stability is achieved only after time, and so it should be good times less good, especially in recent times, and once the situation stabilizes, made good profits, you can start to increase the size of your company, through acquisitions and vertical integration in order to have a lower cost both upstream and downstream of the value chain. This phase is very delicate, because right now you have to choose how to work well, especially in the cases listed first:

- Additions should be well studied and analyzed, in that, while reducing competition in the market, the risk of improper acquisition is to shoulder unnecessary costs, which would make the financial statements, undermining stability in the face of substantial size little ;
- The vertical integration upstream of the value chain, through the acquisition of companies specializing in raw materials, downstream with the absorption of businesses for sale or franchise must be made after careful study of the costs.

Even if they enable the parent company to increase its size on the supply chain, we have to consider the cost factor internal vs. external ones, since it is advisable to use this expansion strategy only when the costs of outsourcing are greater integration, mainly due to the "intermediate steps".

A physiological growth is preferable for companies to preserve the integrity of the organization and ensure their survival in the long term. At the expense of a very rapid and sometimes strong, but that can hide dangers wrong strategic choices, the achievement of one dimensional development of all respect must be done gradually and in small steps. Just so you can carefully assess the market conditions, the development potential offered by actors and threats of competitors, failing to respond perfectly to any external input.

Lately, business expansions are very small, as the crisis has weakened some firms, such as having precarious financial position prefer to at least try to keep the acquired market positions.

4) The development of quality

It is an important factor in the strategic background and is also very delicate because the quality has the characteristic of being subjective.

In addition, the qualitative development of the company does not apply only to products sold, but also to the whole organization of production, thus extending the concept of quality and then talking to business excellence. This has occurred mainly with large groups such as Benetton and Luxottica, but achieving a balance in the factors of production of the products, together with a way of working very orderly and coordinated, means that there are cases of entrepreneurial excellence among small companies.

This is a choice that can be made by a company in good economic conditions, since they operate at a higher level compared to the standard, involves incurring very high costs; ultimately, to reduce much of the cost of production starting from raw materials, many companies have relocated their facilities in countries with labor costs

and raw materials minors. Recognition of excellence for a company is not certified by specific regulations, such as for health care facilities, but builds on the success that is able to obtain on the market, thanks to the guidance of the proprietor or management.

1.2 The strategic planning

The importance of strategic planning is relative high in a build unit mission and may be necessary because the company's overall strategic plan must encompass all of its businesses in order to effectively balance cash flow, while it is relative low in a harvest strategy, this happens because when the environment is uncertain the strategic plan process is especially important. Management needs to give much thought to how to cope with the uncertainties and usually requires a longer-range view of planning than is possible in the annual budget; if the environment is stable, there may be a strategic planning process or only a broad-brush strategic plan.

Strategic planning has become exceptionally important in management circles today, it includes those activities that engage defining the organization's mission, setting its objectives, analyzing the external and internal environment of the organization, and developing and selecting strategies to enable it to operate successfully in its environment¹⁴. Strategic planning starts with a clear understanding of the organizational mission. Secondly, organizational objectives must be established so that strategic alternatives are available to achieve those objectives. This step entails examining the organization's strengths and weaknesses, forecasting the future environment, and so on. Finally, to complete the planning process, strategic choices are made.

The concept of business planning from a certain point of view, has been extended by another concept: that of strategy. We have defined the strategy as a system of choices on the resources to be used and actions to be taken so that the company can achieve its goals. Now, if the business planning is the set of decisions taken by the management to take actions aimed at achieving the objectives¹⁵, strategic planning

¹⁴ Rowe et al. 1989:12

¹⁵ "Planning is the conscious determination of action and related developments needed to achieve the objective:

"takes into account the close relationship between the company and external environment with which it is in mutual dependence."¹⁶ From these statements it is clear the company's dynamism and its vital link with the outside world. In practice, strategic planning there is the link between strategy and business planning process. This concept is best explained by Chung¹⁷:

"Strategic planning involves more than just formulating action plans; it introduces strategic thinking into the planning process. When managers think strategically they ask themselves the following questions:

- a) What is our business? What should be in?*
- b) Who are our customers, and what do they want?*
- c) Who are our competitors? What are their strengths and limitations?*
- d) What is our competitive strength? How should we use our resources to gain a competitive edge?*
- e) What major changes are occurring in our environments? How will these changes affect our businesses?"*

In the definition above are taken into account all the elements necessary to undertake a proper strategic planning process and the elements of strategy. Strategic planning involves mainly the higher levels of the organization company, who carry out coordination tasks, since they provide more information than the other hierarchical levels, and most importantly, have the authority to give innovative ways. Once you know the strategies, they must be distributed within the business organization, in such a way that they are shared and that all the holding can operate to achieve common ends established by management. This distribution takes the form of the strategic planning process.

therefore, planning is decision" da Harold Koontz, a preliminary Statement of principal of Planning and control, journal of management academy - 1985

¹⁶ Bastia P., sistemi di pianificazione e controllo, Il Mulino, 2001

¹⁷ Chung, Management, critical factors, 1987

Business planning function has then to be a tool to support of management so that they can make informed strategic decisions. Lorange¹⁸ analyzes the role of planning based on four aspects:

- · Allocation of scarce corporate resources (financial, technological and human resources) to liable to make a strategic decision;
- · Support the company in the process of adaptation to the threats and opportunities from the environment, identification of alternatives, effective harmonization strategic relationship with the environment;
- · Coordination of strategic line with the strengths and weaknesses the company (internal analysis of the company);
- · Management development through a system of learning from the results of strategic decisions made in the past, and will reinforce the skills and competencies.

There is, however, worth noting that in the past the use of formal tools of planning has been repeatedly criticized for using incorrect it has been done, and today, however, there is a tendency increasingly to re-evaluate the formalization of the strategy as long as you put the right attention on how to plan.

Particular attention to the formalization of the planning has been given by School of Management Science, among which we find authors such as Anthony, Lorange, Hax, Chandler and Ansoff. According to this line of the entrepreneur is a rational being, a homo economicus, who identified the objectives, choosing among the range of possible alternatives that allows it to achieve maximum overall utility. Within these theories if they are developed of the other, in particular that research that outlined in the Operation and supported the formal processes of exploitation strategy, i.e. the planning. Planning, therefore, becomes an important tool dissemination strategy for the following reasons:

- Provides the framework for the application of analytical tools;

¹⁸ Lorange P., Pianificazione strategica, Mc-Graw Hill, 1990

- Shows the process of formation of the strategies;
- Is a tool for communication strategy, enabling the spread of information and objectives throughout the organization;
- Is a process of organizational learning;
- Allows the efficient allocation of corporate resources;
- Is a method of structured analysis;
- Is a tool to support strategic decisions;
- Enables continuous improvement through control of the progressive implementation the strategy and the elimination of any errors you (self-correction);
- Simulates problem solving.

1.3 The strategic management process

There is no one universally accepted way of practicing strategic management.

Different authors use different models. However, in most cases, authors refer to strategic management as a process that includes the various aspects of strategy formulation, implementation and evaluation and control. The purpose of this section is to provide a brief overview of the strategic management process. As was stated earlier, strategic management is a comprehensive approach to management aimed at helping organizations achieve strategic objectives. Basically, strategic management can be broken down into three phases: strategic planning or formulation, strategy implementation and strategic control¹⁹. The figure shows the basic components of strategic management, which includes not only the planning process but the implementation and control phases as well. Although the steps in strategic management process are separate and consecutive, it is important to note that considerable overlap among the steps exists. Additionally, multidirectional arrows in the figure illustrate the

¹⁹ Götze and Mikus 1999:10 and Megginson et al. 1992:198

importance of good communication and feedback throughout the strategic management process.

Strategy development and execution is grounded in the broad range of business decisions and competitive moves management pursues in order to optimize successful performance consistent with its strategic plan's goals, objectives and business initiatives. A strategic plan is the output that comes through the strategic management process and discipline that involves a team approach encompassing all functional areas within a business. Strategic planning is the foundation activity within the strategic management process that helps produce the organization's strategic plan. The strategic plan reflects a company's choice of actions among numerous alternative courses of action. The strategic plan supports and directs management's attention toward implementing a unified and measured approach to the completion of its intended business, market and strategic results.

Crafting and implementing strategy should be core to every business and include all functional areas within the business. How well a strategic plan is executed has a direct influence on how successful a company will be in achieving its maximum potential. Execution of a powerful strategic plan through the strategic management process is both a proven recipe for business success and a reflection of excellent management.

There are five interrelated tasks associated with the strategic management process.

1. Defining what business the company is in today and where it is going. This is done through the formulation of a strategic vision; where the organization is headed, coupled with what the organization's purpose or mission is today.
2. Establishing strategic objectives and performance targets.
3. Formulating a strategy to achieve the strategic objectives and targeted results.
4. Implementing and executing the chosen strategic plan.

5. Evaluating ongoing strategic plan performance in conjunction with new business, market and strategic developments. Initiate appropriate adjustments and corrective actions for both short and long-term goals, objectives and strategies as a function of actual experience, dynamic environmental conditions, current thinking, new ideas, perceived risks, and potential opportunities.

The following models reflect the key elements associated with strategic planning and the strategic management process.

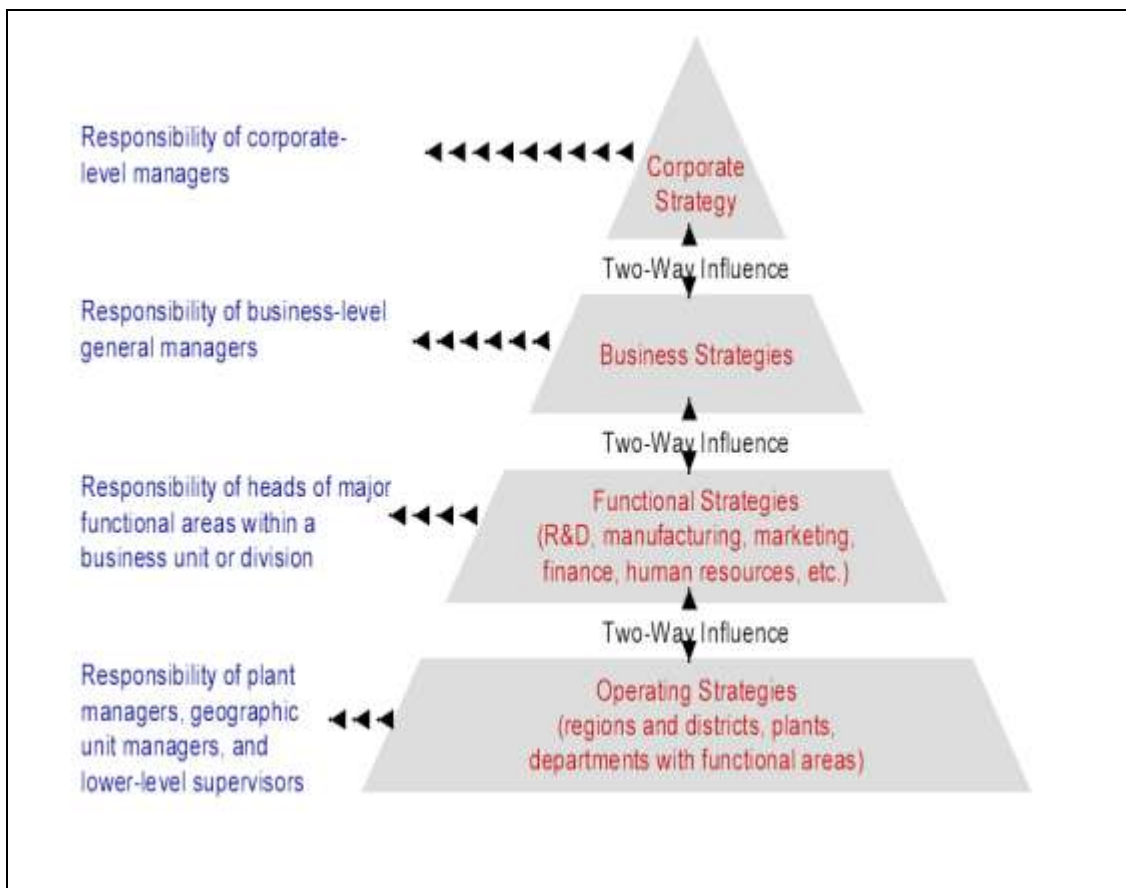


Figure 2 THE ENTERPRISE STRATEGY PIRAMID

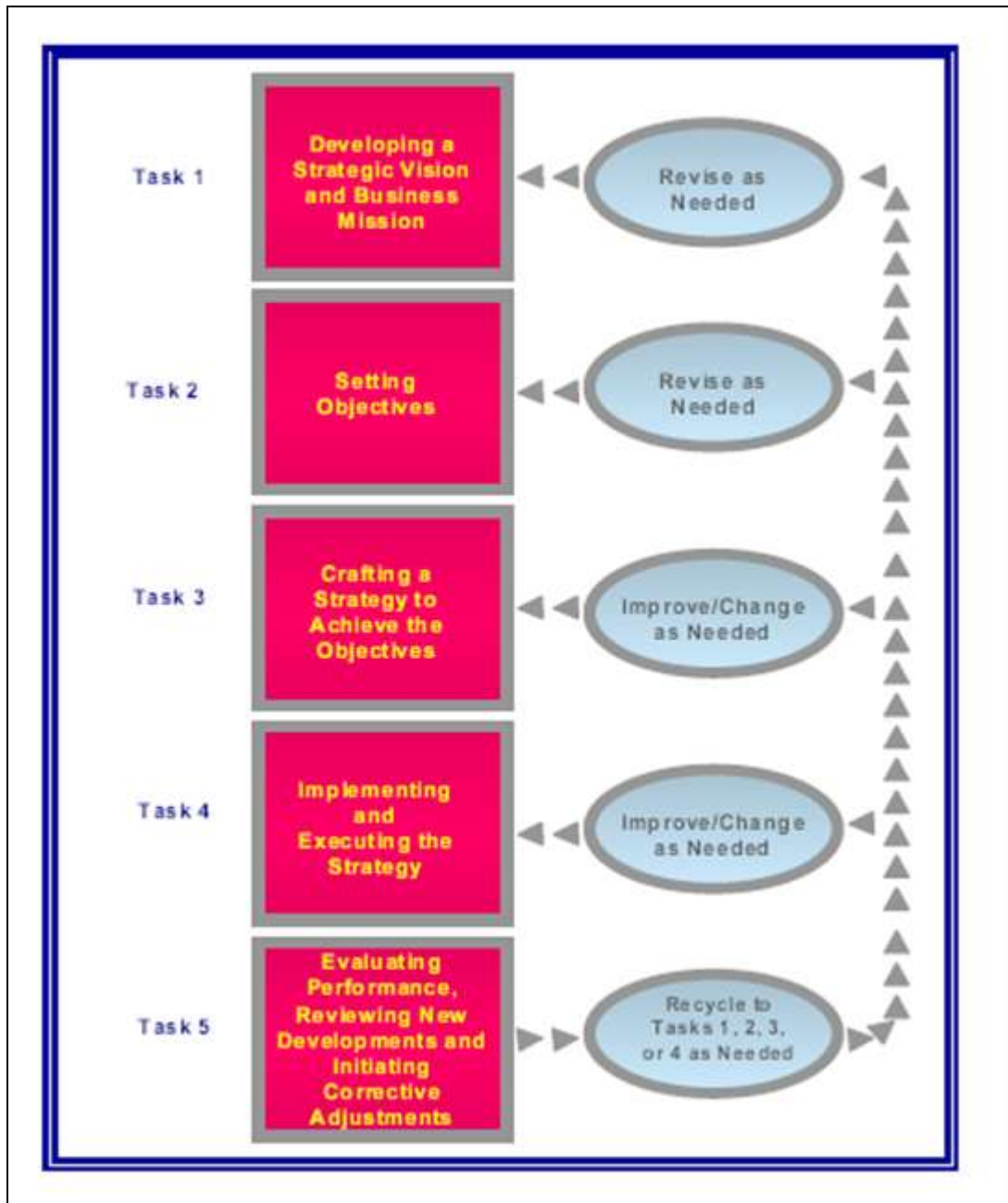


Figura 3 THE FIVE TASKS OF STRATEGIC MANAGEMENT

1) Defining the business

Defining the business as it currently is and as it will be in the future is a necessary first step in establishing a meaningful direction and developmental path for the organization. Management's view of what the organization seeks to do and to

become over the long-term is the organization's strategic mission. The strategic mission broadly charts the future course of the organization. Since decisions about long-term direction fall squarely upon the shoulders of senior officers, the strategic mission nearly always reflects the personal vision and thinking of top-level managers.

2) Establishing strategic objectives

Specific performance targets are needed in all areas affecting the survival and success of a company, and they are needed at all levels of management, from the corporate level on down deep into the organization's structure. The act of establishing formal objectives not only converts the direction an organization is headed into specific performance targets to be achieved but also guards against drift, aimless activity, confusion over what to accomplish and loss of purpose. Both short-run and long-run objectives are needed.

The strategic objectives for the organization as a whole should at a minimum specify: the market position and competitive standing the organization aims to achieve, annual profitability targets, key financial and operating results to be achieved through the organization's chosen activities, and any other milestone by which strategic success is measured. Because performance objectives are needed up and down the organization, the objective-setting task of strategic management involves all managers; each must identify what their area's contribution to strategic success will be and then establish concrete, measurable performance targets.

3) Formulating the strategy

This component of strategic management brings in the critical issue of just how the targeted results are to be accomplished. While objectives are the "end product", the strategy is the "means" of achieving them. The task of formulating the strategy entails taking into account all of the relevant aspects of the organization's internal and external situation and coming up with a detailed action plan for achieving the targeted short-run and long-run results. Strategy is a blueprint of all the important entrepreneurial,

competitive and functional area actions that are to be taken in pursuing organizational objectives and positioning the organization for sustained success.

The definition of strategy is “a statement of how what resources are going to be used to take advantage of which opportunities to minimize which threats to produce a desired result”. This definition points toward the issues that strategy must address:

1. *How to respond to changing conditions* specifically, what to do about shifting customer needs and emerging industry trends, which new opportunities to pursue, how to defend against competitive pressures and other externally imposed threats, and how to strengthen the mix of the firm's activities by doing more of some things and less of others.
2. *How to allocate resources* over the organization's various business units, divisions, and functional departments making decisions that steer capital investment and human resources in behind the chosen strategic plan is always critical; some kind of strategy-supportive guidelines for resource allocation have to exist.
3. *How to compete* in each one of the industries in which the organization participates decisions about how to develop customer appeal, to position the firm against rivals, to emphasize some products and de-emphasize others, and to meet specific competitive threats are always integral to competitive survival and the achievement of a defensible competitive advantage.
4. Within each line of business of the organization, *what actions and approaches to take in each of the major functional areas and operating departments* to create a unified and more powerful strategic effort throughout the business unit. Obviously, the different functional and operating level strategies ought to be coordinated rather than be allowed to go off on independent courses; they need to support the creation of a sustainable competitive advantage.

4) Strategy implementation and execution

Putting the strategy into place and getting individuals and organizational subunits to go all out in executing their part of the strategic plan successfully is essentially an administrative task. This implies several managerial challenges, such as:

- Building an organization capable of carrying out the strategic plan;
- Developing strategy-supportive budgets and programs;
- Linking the motivation and reward structure directly to achieving the targeted results;
- Creating an organizational culture that is in tune with strategy in every success-causing respect;
- Developing an information and reporting system to track and control the progress of strategy implementation;
- Installing policies and procedures that facilitate strategy implementation.

Developing an action agenda for implementing and executing the strategy involved managers at all levels, deciding on answers to the question “What is required for us to implement our part of the overall strategic plan and how can we best get it done?” doing this task well means scrutinizing virtually every operating activity to see what actions can be taken to improve strategy execution and to instill strategy-supportive practices and behavior. The administrative tasks of implementing and executing the strategy involve a process of moving incrementally and deliberately to create a variety of “fits” that bring an organization’s conduct of its internal operations into good alignment with strategy.

A number to fits are thus needed:

- Between strategy and the internal organizational structure;
- Between strategy and organizational skills/technical know-how/operating capabilities;
- Between strategy and the allocation of budgets and staff size;

- Between strategy and the organization's systems of reward and incentives;
- Between strategy and internal policies, practices and procedures;
- Between strategy and the internal organizational atmosphere (as determined by the values and beliefs shared by managers and employees, the philosophies and decision-making styles of top managers, and other factors that make up the organization's personality and culture).

5) Evaluating strategic performance and making corrective adjustments

Neither strategy formulation nor strategy implementation is a once-and-for-all-time task. In both cases, circumstances arise which make corrective adjustments desirable. Strategy may need to be modified because it is not working well or because changing conditions make fine-tuning, or even major overhaul, necessary. Even a good strategy can be improved, and it requires no great argument to see that changes in industry and competitive conditions, the emergence of new opportunities or threats, new executive leadership, a reordering of objectives, and the like can all make a change in strategy desirable. Likewise, with strategy implementation there will be times when one or another aspect of implementation does not go as well as planned, making adjustments necessary.

And changing internal conditions, as well as experiences with current strategy execution, can drive different or improved implementation approaches. Testing out new ideas and learning what works and what doesn't through trial and error is common. Thus, it is always a compulsory task for managers to monitor both how well the chosen strategy is working and how well implementation is proceeding, making corrective adjustments whenever better ways of doing things can be supported. The function of strategic management is ongoing, not something to be done once and then neglected.

The process of strategic management

Because each component of strategic management entails judging whether to continue with things as they are or to make changes, *the task of managing strategy is a*

dynamic process - all strategic decisions are subject to future modification. Changes in the organization's situation and ups and downs in financial performance are constant drivers of strategic adjustments. A model of the strategic management process is shown in Figure.

The first three components, in combination, give direction to the enterprise, establish the directional map for strategic action, and, in effect, define what is called an organization's *strategic plan*. The fourth component is easily the most complicated and challenging one because it involves not only deciding on but also undertaking the administrative actions needed to convert the strategic plan into results; indeed, orchestrating the execution of strategy is probably 5 to 10 times more time consuming than is formulating the strategic plan. The fifth component, evaluating strategic performance and making corrective adjustments, is both the end and the beginning of the strategic management cycle. The march of external and internal events guarantees that the time will come for making revisions in the four previous components. Most of the time, revisions will be of the fine-tuning variety, but occasions for major overhaul in one or more components arise – sometimes because of significant external developments and sometimes because of sharply sliding financial performance.

While defining the business, establishing strategic objectives, formulating a strategy, implementing and executing the strategic plan, and evaluating performance accurately portray the conceptual elements in managing an enterprise's strategy, the process is not quite so cleanly divided and neatly performed in actual practice.

First, managers do not necessarily, or even usually, go through the sequence in rigorous lockstep fashion. Moreover, the boundaries between the components are sometimes hard to distinguish in practice: establishing a strategic mission shades into setting objectives for the organization to achieve (both involve direction-setting); objective-setting shades into considering whether and how strategies can be formulated to achieve them; and deciding on a strategy is nearly always entangled in discussion about the direction the organization needs to take and the position it should try to assume.

Second, the tasks involved in strategic management are never isolated from everything else that falls within a manager's purview. Strategy has to be formulated and implemented in the midst of a managerial schedule that is fragmented with appointments, meetings, paperwork deadlines, unexpected problems, and momentary crises. It is incorrect to construe the job of managing strategy as the exclusive task of managers, even though it may well be the most important function they perform where organizational success or failure is concerned.

Third, the demands that strategy management puts on the manager's time are irregular. Strategic issues, new opportunities, and bright ideas about strategy or its implementation do not appear according to some ordered timetable; they have to be dealt with whenever they arise.

Finally, formulating and implementing strategy must be regarded as something that is *ongoing* and that *evolves*. What qualifies as a high-performance strategy today is sooner or later rendered stale by events unfolding both inside and outside the company. The task of "strategizing" can never therefore be a one-time exercise. While the "whats" of an organization's strategic mission and long-term strategic objectives, once established, usually present fairly stable targets to shoot for, the "hows" of strategy evolve regularly in response to changes in an organization's internal situation and external environment. As a consequence, finetuning- type changes in strategic plans, and an occasional major change in strategic thrust, are normal and expected (big strategy changes, however, cannot be made often). The need to keep strategy in tune with an organization's changing situation makes the strategic management process dynamic and means that the prevailing strategy is rarely the result of a single comprehensive analysis. Strategic decisions are made over a period of time, not all at once; moreover, previous decisions are modified and decisions to initiate new strategic moves are forthcoming from time to time. Much of the time strategy evolves in a fairly orderly manner, but sometimes the strategy is crisis-driven, forcing a number of big strategic decisions to be made rapidly.

Similarly, strategy implementation is the product of incremental improvements, internal fine-tuning, the pooling effect of many administrative decisions, and gradual

adjustments in the actions and behavior of both managerial subordinates and employees. Implementation is not something that can be made to happen overnight. The transition from the old strategy to executing the new strategy takes time; normally, the larger the degree of strategic change, the more time it takes for the new methods of implementation to take hold.

1.4 The external environmental

Before an organization can set realistic objectives and establish strategies, it must determine its present status.

The general environment is composed of dimension in the broader society that influence an industry and the firms within it. We group these dimensions into seven environmental *segments*: demographic, economic, political/legal, sociocultural, technological, global and physical.

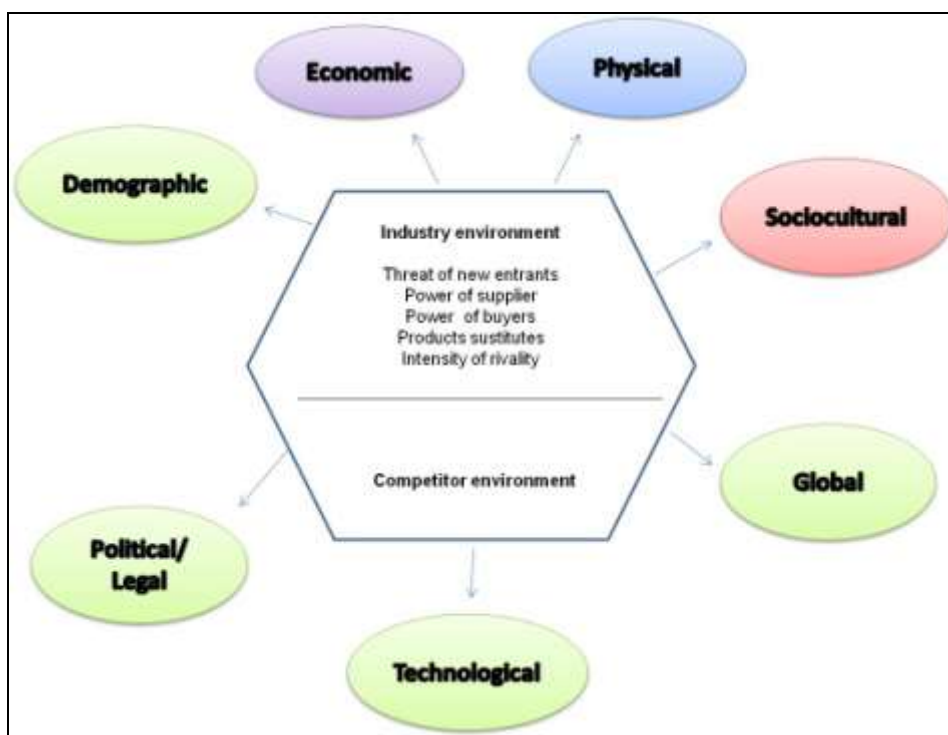


Figure 4 The external environment

Examples of *elements* analyzed in each of these segments are show in Table.

DEMOGRAPHIC SEGMENT	<ul style="list-style-type: none"> • Population size • Age structure • Geographic distribution 	<ul style="list-style-type: none"> • Ethnic mix • Income distribution
ECONOMIC SEGMENT	<ul style="list-style-type: none"> • Inflation rate • Interest rate • Trade deficits or surpluses • Budgets deficit or surpluses 	<ul style="list-style-type: none"> • Personal savings rates • Business savings rates • Gross domestic product
POLITICAL/LEGAL SEGMENT	<ul style="list-style-type: none"> • Antitrust laws • Taxation laws • Deregulations philosophies 	<ul style="list-style-type: none"> • Labor training laws • Educational philosophies and policies
SOCIOCULTURAL SEGMENT	<ul style="list-style-type: none"> • Women in the workforce • Workforce diversity • Attitudes about the quality of the work life 	<ul style="list-style-type: none"> • Shifts in work and career preferences • Shifts in preferences regarding product and service characteristics
TECHNOLOGICAL SEGMENT	<ul style="list-style-type: none"> • Product innovations • Applications of knowledge 	<ul style="list-style-type: none"> • Focus of private and government-supported R&D expenditures • New communications technologies
GLOBAL SEGMENT	<ul style="list-style-type: none"> • Important political events • Critical global markets 	<ul style="list-style-type: none"> • Newly industrialized countries • Different cultural and institutional attributes
PHYSICAL ENVIRONMENTAL SEGMENT	<ul style="list-style-type: none"> • Energy consumption • Practices used to develop energy sources • Renewable energy efforts • Minimizing a firm's environmental footprint 	<ul style="list-style-type: none"> • Availability of water as a resource • Producing environmentally friendly product

Table 1 The general environment: Segments and Elements

Because firm cannot directly control the segments of their external environment, successful ones learn how to gather the information needed to understand all segments and their implications for selecting and implementing the firm's strategies.

The external environmental analysis is also part of the process of answering the question "*Where are we now*"? It includes those factors that may influence the success of the organization but are external to and not under the total control of the organization. Developing an awareness of the present and future external environment enables the organization to respond more effectively to change. The external environmental analysis is performed to identify the external opportunities and threats. The firm also must know its own capabilities and limitations in order to select the opportunities that it can pursue

with a higher probability of success. The external environment has two aspects: the macro-environment that affects all firms and a micro-environment that affects only the firms in a particular industry. Developing an industry profile is an important element in understanding present environmental conditions. An industry profile answers questions about key areas of a particular industry. Some of the areas that might be examined are marketing practices, market structure, financial condition, competition, operating conditions, and production techniques. The industry environment is also influenced by forces outside the industry itself.

An organization not only must analysis its present environmental conditions but also must forecast its future environment. Establishing objectives and strategies is much easier under stable environmental conditions. However, establishing objectives and strategies is more realistic when forecasting is made. Regardless of the strong possibility of error, to be successful organizations should forecast their future environment. Forecasting is concerned with assessing the impact of many forces (political, economic, social, and technological forces) on an organization. It also focuses on developing an understanding of the expected future for the most important issues and trends.

The industry environment is the set of factors that directly influences a firm and its competitive actions and responses: the threat of new entrants, the power of suppliers, the power of buyers, the threat of product substitutes, and the intensity of rival among competitors. In total the interactions among these five forces determinate an industry's profit potential; in turn, the industry's profit potential influences the choices each firms makes about its strategy actions. The challenge for a firm is to locate a position within an industry where it can favorably influence the five factors or where it can successfully defend against their influence.

How companies gather and interpreter information about their competitors is called *competitors analysis*. Understanding the firm's competitor environment complements the insights provided by studying the general and industry environments.

Analysis of the general environment is focused on environmental trends while an analysis of the industry environment is focused on the factors and conditions

influencing an industry's profitability potential and an analysis of competitors is focused on predicting competitors' actions, responses, and intentions. In combination, the results of these three analysis influence the firms' vision, mission and strategic actions.

The industry profile partially indicates the threats/opportunities for the organization based on its present and future industry environment. The external environmental analysis is designed to identify the key environmental forces that have influence on an organization and its industry. The present impact of these forces helps in identifying the threats/opportunities for the organization. Forecasting the future environmental forces identifies the key forces that are most likely to affect the organization and its threats/opportunities.

The internal strengths/weaknesses, coupled with the external opportunities/threats and a clear statement of mission, provide the basis for establishing objectives and strategies.

1.4.1. The external environment analysis

Most firms face internal environments that are highly turbulent, complex, and global (conditions that make interpreting those environments difficult). To cope with often ambiguous and incomplete environmental data and to increase understanding of the general environmental, firms engage in external environmental analysis. This analysis has four parts: scanning, monitoring, forecasting, and assessing (See table 2).

SCANNING	✓ Identifying early signals of environmental changes and trends
MONITORING	✓ Detecting meaning through ongoing observations of environmental changes and trends
FORECASTING	✓ Developing projections of anticipated outcomes based on monitored changes and trends
ASSESSING	✓ Determining the timing and importance of environmental changes and trends for firm's strategies and their management

Table 2 Components of the External Environmental Analysis

Identifying opportunities and threats is an important objective of studying the general environment. An **opportunity** is a condition in the general environment that if exploited effectively, helps a company achieve strategic competitiveness. A **threat** is a condition in the general environment that may hinder a company's efforts to achieve strategic competitiveness.

Firms use several source to analyzed the general environment, including a wide variety of printed materials²⁰, trade shows and suppliers, customers, and employees of public sector organizations. People in boundary-spanning positions can obtain a great deal of this type of information.

SCANNING

Scanning entails the study of all segments in the general environment. Through scanning, firms identify early signals of potential changes in the general environment and detect changes that are already under way. Scanning often reveals ambiguous, incomplete, or unconnected data and information. Thus, environmental scanning is challenging but critically important for firms, especially those competing in highly volatile environments. In additions, scanning activities must be aligned with the organizational context; a scanning system designed for a volatile environmental is inappropriate for a firm in a stable environment.

MONITORING

When monitoring, analysts observe environmental changes to see if an important trends is emerging from among those spotted through scanning. Critical to successful monitoring is the firm's ability to detect meaning in different environmental events and trends.

Effective monitoring requires the firm to identify important stakeholders as the foundation for serving their unique needs. Scanning and monitoring are particularly important when a firm competes in an industry with high technological uncertainty.

²⁰ Such as trade publications, newspapers, business publications, the results of academy research and public pools

FORECASTING

Scanning and monitoring are concerned with events and trends in the general environment at a point time. When forecasting, analysts develop feasible projections of what might happen, and how quickly, as a result of the changes and trends detected through scanning and monitoring. Forecasting events and outcomes accurately is challenging. Already in place, the trend of firms outsourcing call center work and logistics' activities to companies specializing in these activities appeared to accelerate as a result of the recent global crisis.

ASSESSING

The objective of assessing is to determinate the timing and significance of the effects of environmental changes and trends that have been identified. Through scanning, monitoring, and forecasting, analysts are able to understand the general environment. Going a step further, the intent of assessment is to specify the implications of that understanding. Without assessment, the firm is left with data that may be interesting but are of unknown competitive relevance. Even if formal assessment is inadequate, the appropriate interpretation of that information is important: *“Research found that how accurate senior executives are about their competitive environments is indeed less important for strategy and corresponding organizational changes than the way in which they interpret information is about their environments”*²¹.

1.4.2. Industry environments analysis

An industry is a group of firms producing products that are close substitute. The industry environment, compared with the general environment, has a more direct effect on the firm's strategic competitiveness and ability to earn above-average returns.

²¹ K. M. Sutcliffe & Weber, 2003, The high costo of accurate knowledg, Harvard Business Review

Analysis of the structure of the industry as a fundamental basis for the formulation of a strategy

Porter, in a line of continuity with previous economic / industrial dictates of environment dependence and those of Harvard who proposed to bring the success of companies at strategies able to valorizing the points of force in response to environmental stimuli, giving a great importance to the competitive space, but, however, in his analysis introduce of new dimensions, covering both the industrial sector as the strategic groups, which allow you to achieve a more organic definition of competitive space.

The starting point of Porter's teaching is that understanding the competitive external environment is a critical element of a successful strategy, and competitive strategy must connect the company to its reference environment, to make way for the realization of a satisfaction profit rate by the exploitation of those factors that determine the Company profitability within the sector or sectors in which it operates.

These factors, at the base of the success of a company, consist in:

- the level of attractiveness of the industrial sector of activity;
- the particular position taken by the company within the industry itself, which enables it to obtain an competitive advantage²².

This last point is the major innovation compared to previous studies on strategic positioning and is developed to become the hub off all development of the strategy process: the strategy is the pursuit of competitive advantage as a condition of success, aiming to establish a profitable and sustainable position against the forces that determine the competitors on an industry.

The fundamental basis for the formulation of a competitive strategy is so the analysis of industry structure: the knowledge competitive forces clarifies any strengths and weaknesses, brings out the opportunities and environmental threats, highlights the potential development paths of a business.

²² Porter M.E., Towards a dynamic theory of strategy, in: Strategic Management Journal, vol.12, 1991, p.95-117

Porter tends to repeat many of the classical assumptions of the economic industry, which indicate how the structure of the industry is driving the competitive behavior and determine its profitability, and how the choices strategic resulting from them are often in search of protected positions compared to the intensity of competition²³.

Porter, however, compared to previous studies on a strategic environment competitive, which often introduced systematic approaches, too loads of useful information is not always real, suggests something more innovative, because its main focus is on those factors vital to the enterprise, which directly influence the profitability performance.

The process of strategy is formulated from the analysis of the competitive environment in which the firm operates, as a result of the link between industry structure and profitability prospects, it follows that the analysis by sector gives the necessary elements to define in a concrete way the strategic path to pursue, according to the specific criterion of competitive advantage.

1.4.3. The model of five competitive force

The definition of industrial sector and its level of profitability (indicated by rate of return on capital over the cost of capital), are in fact determined by the interplay of five competitive forces, which assume different emphasis depending on the sectors²⁴.

They include three sources of "vertical" competition: new entry competitors, the threat of substitutes, the rivalry between the competitors present, and two sources of competition "horizontal": the contract power of customers and contract power of suppliers.

The influence of these five competitive forces determines the competition intensity and makes up the structure of the industry sector, in its once, subject to

²³ Porter M.E., *Come le forze competitive modellano la strategia*, in Porter M.E., Montgomery C. (a cura di), *Strategia*, Il Sole 24 ore Libri, Milano, 1993

²⁴ Porter M.E., *Come le forze competitive modellano la strategia*, in Porter M.E., Montgomery C. (a cura di), *Strategia*, op. cit.; Porter M.E., *La strategia competitiva. Analisi per le decisioni*, op. cit.

evolution and changing trends: even the same strategies of firms are able to induce changes on the structure sector, improving or worsening the profitability that comes with it.

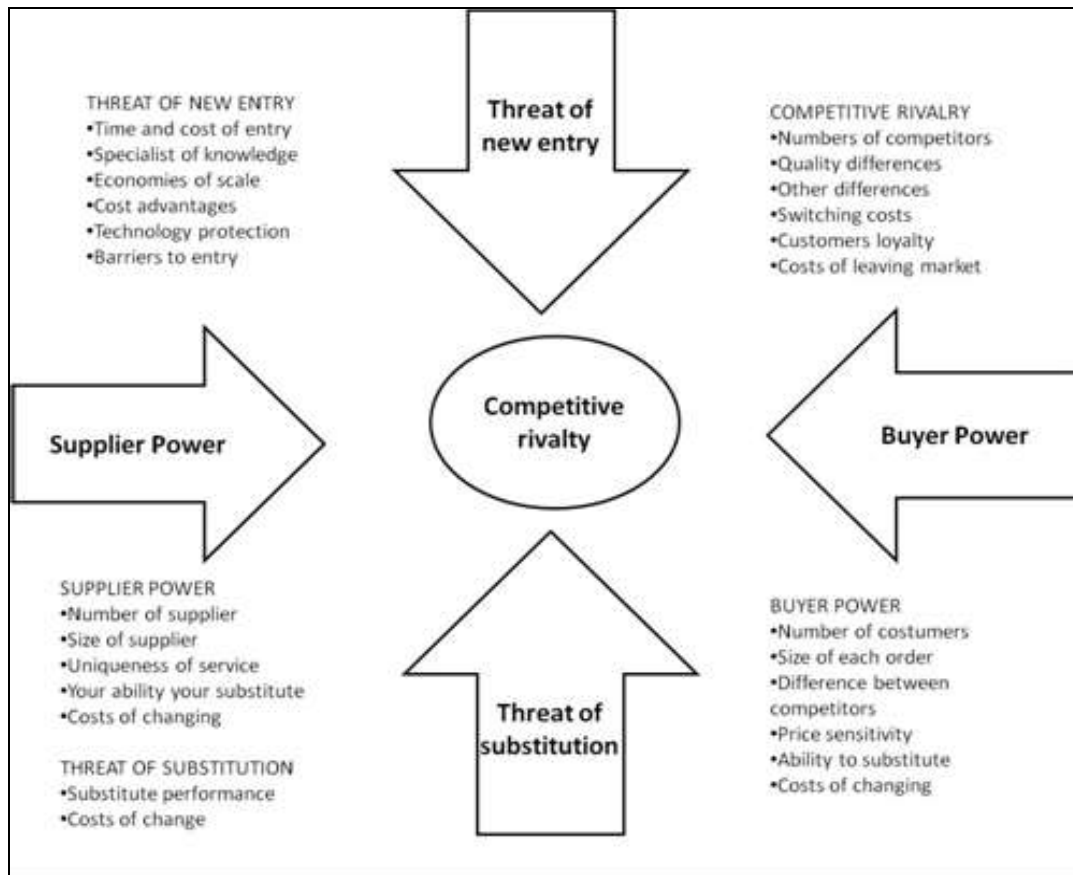


Figure 5 Porter M.E. The competitive advantage

Threat of new entry

The strategic question, fundamental for a company, is the how to address the necessary attention to any new, and sometimes unavoidable, entry.

In many sectors, new firms cannot enter under the same conditions those consolidated, but still can be a threat to which to defend themselves, it creates barriers to entry. The severity of threat depends on the height of entry barriers (which dictate to what point an industries can in the long term, benefit from the higher profits above the

competitive level) and by the liveliness of the reactions of competitors current that newcomers should expect.

- Possible key barriers to entry are²⁵:
- Economies of scale
- Capital / investment requirements
- Customer switching costs
- Access to industry distribution channels
- The likelihood of retaliation from existing industry players.

Competitive rivalry

The competitive behavior of firms in a sector, such as price manipulation, advertising battles, strategies for innovation and quality of service offered to customers, are aimed to increasing the share of market or to defend it from attacks by competitors.

Six structural factors determine the nature and intensity of competition between businesses²⁶:

- *The structure of competition* - for example, rivalry is more intense where there are many small or equally sized competitors; rivalry is less when an industry has a clear market leader;
- *The structure of industry costs* - for example, industries with high fixed costs encourage competitors to fill unused capacity by price cutting;
- *Degree of differentiation* - industries where products are commodities (e.g. steel, coal) have greater rivalry; industries where competitors can differentiate their products have less rivalry;

²⁵ Porter M.E., La strategia competitiva. Analisi per le decisioni, op. cit., p.15

²⁶ Porter M.E., La strategia competitiva. Analisi per le decisioni, op. cit., p.25

- *Switching costs* - rivalry is reduced where buyers have high switching costs - i.e. there is a significant cost associated with the decision to buy a product from an alternative supplier;
- *Strategic objectives* - when competitors are pursuing aggressive growth strategies, rivalry is more intense. Where competitors are "milking" profits in a mature industry, the degree of rivalry is less;
- *Exit barriers* - when barriers to leaving an industry are high (e.g. the cost of closing down factories) - then competitors tend to exhibit greater rivalry.

Threat of substitutes

The threats of substitutes are products that perform the same function for the same group of consumers, but are based on different technologies. Their existence implies a shift in consumer preferences if there is an increase in the price of the product, ie demand is elastic compared to the price.

The presence of substitute products can lower industry attractiveness and profitability because they limit price levels. The threat of substitute products depends on:

- Buyers' willingness to substitute
- The relative price and performance of substitutes
- The costs of switching to substitutes

The substitute products that deserve more attention from the strategic point of view are therefore those that evolve in the direction of better relations quality / price compared to that inherent in the product sector and those who come from areas that are profitable.

Bargaining power of suppliers

Suppliers are the businesses that supply materials & other products into the industry. Suppliers can use their bargaining power on business customers threatening to raise prices of supplies, reduce the quality of products or services, limit the quantities sold to each buyer. Suppliers can also compress very strong profitability of a company if the customer is unable to make sustained increases from affecting prices charged.

The cost of items bought from suppliers (e.g. raw materials, components) can have a significant impact on a company's profitability. If suppliers have high bargaining power over a company, then in theory the company's industry is less attractive. The bargaining power of suppliers will be high when:

- There are many buyers and few dominant suppliers;
- There are undifferentiated, highly valued products;
- Suppliers threaten to integrate forward into the industry (e.g. brand manufacturers threatening to set up their own retail outlets);
- Buyers do not threaten to integrate backwards into supply;
- The industry is not a key customer group to the suppliers.

Bargaining power of buyers

Buyers are the people / organizations who create demand in an industry, even the buyers are a competitive force, as they are can affect the potential profitability of an asset by pressing for price reductions, asking for a better quality of services and more favorable payment terms, even playing on the rivalry of supply companies.

- The bargaining power of buyers is greater when:
- There are few dominant buyers and many sellers in the industry;
- Products are standardized;
- Buyers threaten to integrate backward into the industry;

- Suppliers do not threaten to integrate forward into the buyer's industry;
- The industry is not a key supplying group for buyers.

The limit of the five competitive force

The five competitive forces model, developed by Porter, whose foundations reside in the paradigm "structure - conduct - performance" of the economy industry, has been widely used as a framework for the analysis of competition and to assess the degree of attractiveness of an industry. However, this model is not without its critics, which can be mainly traced to three factors²⁷:

1) the relationships between companies are not always characterized by strong juxtaposition.

The antagonism and confrontation do not necessarily represent the fact order to compete more effectively and widely, so they are common in the world business relationships based on respect, trust and cooperation between the companies: for example, the dissemination of strategic alliances, including joint ventures, licensing, venture capital investments, acquisitions in other forms of participation and collaboration, and the onset in these years of collaborative relationships and even partnerships with suppliers, while relations with customers have evolved by relations of force guidelines for customer satisfaction;

2) barriers to entry in an industry are often less important compared with distinct characteristics and difficult to imitate some companies, which effectively act as a deterrent to competition;

3) of the five competitive forces model has a static nature, as considers the structure of a sector as stable and determined from outside. This affects the intensity of competition which, in turn, influences the level of profitability of the sector.

²⁷ Grant R.M., *L'analisi strategica per le decisioni aziendali*, Il Mulino, Bologna, 1999, p.98-99; De Toni A., Tonchia S., *Pianificazione strategica e competenze aziendali*, in: *Economia e Management*, n.3, 1999, p.43-59; Hax A. C., Majluf N. S., *La gestione strategica dell'impresa*, a cura di Sicca L., Edizioni Scientifiche Italiane, Napoli, 1993, p. 69-70.

But competition is not bound by a process, which leaves unchanged the structure of an industry, but dynamic, amending and redesigned continuous structure of a sector, either deliberately through strategic corporate decisions and as a result of subsequent competitive interaction.

1.5 The internal environmental

An internal organizational analysis is designed to answer in part the question "Where are we now?" It is an evaluation of all relevant factors within the organization. In practice, a checklist of factors is used in performing an internal organizational analysis. A typical checklist might include the following factors: financial position, organizational structure, quantity and quality of personnel, product line, competitive position, condition of facilities and equipment, marketing capability, research and development capability, past objectives and strategies²⁸. Based on understanding of these areas, managers can determine their company's weaknesses or strengths vis-à-vis other companies.

Increasingly, those who analyze the firm's internal organization should use a globe mind-set to do so. A global mind-set is the ability to analyze, understand and manage (if in a managerial position) an internal organization in ways that are not dependent on the assumptions of a single country, culture or context. Because they are able to span artificial boundaries, those with a global mind-set recognize that their firms must possess resources and capabilities that allow understanding of and appropriate responses to competitive situations that are influence by country-specific factors and unique societal cultures. Firms populated with people having a global mind-set have a "key source of long-term competitive advantage in the global marketplace".

Finally, analysis of the firm's internal organization requires that evaluators examine the firm's portfolio of resources and the bundles of heterogeneous resources and capabilities managers have created. This perspective suggests that individual firms possess at least some resource and that other companies do not. Resource are the source

²⁸ Brauchlin and Wehrli 1991:62

of capabilities, some of which lead to the development of a firm's core competencies or its competitive advantages.

Understanding how to leverage the firm's unique bundle of resources and capabilities is a key outcome decision makers seek when analyzing the internal organization.

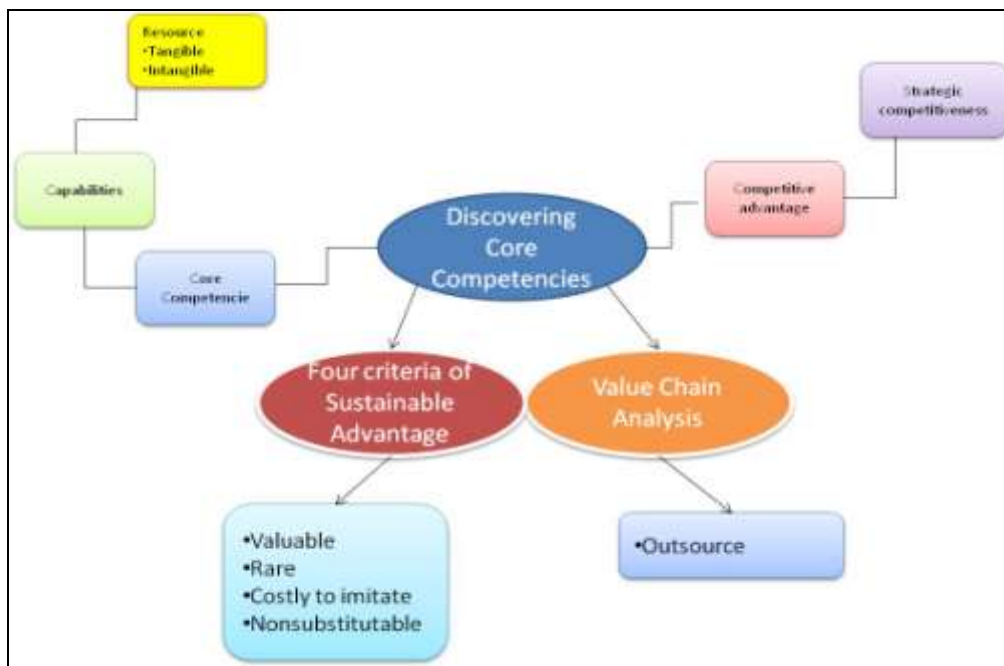


Figure 6 Components of internal Analysis leading to competitive advantage and strategic comepetitiveness

RESOURCES

Broad in scope, resources cover a spectrum of individual, social, and organizational phenomena²⁹. Typically, resources alone do not yield a competitive advantage.

In fact, a competitive advantage is generally based on the unique bundling of several resources. Some of a firm's resources are tangible while others are intangible.

²⁹ R.H. Lester, A. Hilmann, 2008, Former Government officials as outside directors: The role of Human and social capital, Academy of Management Journal.

Tangible resources are assets that can be observed and quantified; production equipment, manufacturing facilities, distribution centers, and formal reporting structures are examples of tangible resources. Intangible resources are assets that are rooted deeply in the firm's history and have accumulated over time. Because they are embedded in unique patterns of routines, intangible resources are relatively difficult for competitors to analyze and imitate. Knowledge, trust between managers and employees, managerial capabilities, organizational routines, scientific capabilities, the capacity for innovation, brand name, and the firm's reputations for its goods or services and how it interacts with people are intangible resources.

The four types of intangible resources are financial, organizational, physical, and technological (see Table 3). The three types of intangible resources are human, innovation, and reputational (see table 4).

FINANCIAL RESOURCES	<ul style="list-style-type: none">• The firm's borrowing capacity• The firm's ability to generate internal funds
ORGANIZATIONAL RESOURCES	<ul style="list-style-type: none">• The firm's formal reporting and structure and its formal planning, controlling, and coordinating systems
PHYSICAL RESOURCES	<ul style="list-style-type: none">• Sophistication and location of a firm's plant and equipment• Access to raw materials
TECHNOLOGICAL RESOURCES	<ul style="list-style-type: none">• Stock of technology, such as patent, trademarks, copyrights, and trade circle

Table 3 Tangible Resources

HUMAN RESOURCES	<ul style="list-style-type: none">• Knowledge• Trust• Managerial capabilities• Organizational routines
INNOVATION RESOURCES	<ul style="list-style-type: none">• Ideas• Scientific capabilities• Capacity to innovate
REPUTATIONAL RESOURCES	<ul style="list-style-type: none">• Reputation with costumers• Brand name• Perceptions of product quality, durability and reliability• Reputation with suppliers• For efficient, effective, supportive, and mutually beneficial interactions and relationships

Table 4 Intangible resources

CAPABILITIES

Capabilities exist when resources have been purposely integrated to achieve a specific task or set of tasks. These tasks range from human resource selection to product marketing and research and development activities. Critical to the building of competitive advantage, capabilities are often based on developing, carrying and exchanging information and knowledge through the firm's human capital. Client-specific capabilities often develop from repeated interactions with client and the learning about their needs that occurs. As a result, capabilities often evolve and develop over time.

As illustrated in Table 5, capabilities are often developed in specific functional areas (such as manufacturing, R&D, and marketing) or in part of functional area (e.g. advertising). Table, show a grouping of organizational functions and the capabilities that some companies are thought to possess in terms of all or parts of those functions.

FUNCTIONAL AREAS	CAPABILITIES
Distribution	Effective use of logistics management techniques
Human resources	Motivating, empowering, and retaining employees
Management information system	Effective and efficient control of inventories through point-of-purchase data collection methods
Marketing	Effective promotion of brand-name products Effective customers service Innovative merchandising
Management	Ability to envision the future of clothing Effective organizational structure
Manufacturing	Design and production skills yielding reliable products Product and design quality Miniaturization of components and products
Research & Development	Innovative technology Development of sophisticated elevator control solutions Rapid transformation of technology into new products and processes Digital technology

Table 5 Example of firm's capabilities

CORE COMPETENCIES

Core competencies are capabilities that serve as a source of competitive advantage for a firm over its rivals. Core competencies distinguish a company competitively and reflect its personality. Core competencies emerge over time through an organizational process of accumulating and learning how to deploy different resources and capabilities. As the capacity to take action, core competencies are “crown jewels of a company”, the activities the company performs especially well compared with competitors and through which the firms adds unique value to its goods or services over al long period time.

There are two tools that help a firms to identify and build their core competencies: the first consists of four specific criteria of sustainable competitive advantage that firms can use to determinate those capabilities that are core competencies. Because the capabilities shown in Table 5 have satisfied these four criteria, they are core competencies. The second tool is the value chain analysis. Firms use this tool to select the value creating competencies that should be maintained, upgraded, or developed and those that should be outsourced.

FOUR CRITERIA OF SUSTAINABLE COMPETITIVE ADVANTAGE

As show in table 6 capabilities that are valuable, rare, costly to imitate and no-substitutable. In turn, core competencies are sources of competitive advantage for the firms over its rivals. Capabilities failing to satisfy four criteria of sustainable competitive advantage are not core competencies, meaning that although every core competence is a capability, not every capabilities is a core competencies. In slightly different words, for a capability to be a core competence, it must be valuable and unique from a customer's point of view. For a competitive advantage to be sustainable, the core competence must be inimitable and no-substitutable by competitors.

Valuable Capabilities	Help a firm neutralize threats or exploit opportunities
Rare Capability	Are not possessed by many other
Costly-to-Imitate Capabilities	<ul style="list-style-type: none">• Historical: a unique and a valuable organizational culture or brand name• Ambiguous cause: The causes and uses of a competence are unclear• Social complexity: Interpersonal relationships, trust and friendship among managers, suppliers, and customers
Nonsubstitutable Capabilities	No strategic equivalent

Table 6 The four criteria of Sustainable Competitive Advantage

- Valuable: valuable capabilities allow the firm to exploit opportunities or neutralize threats in its external environment.
- Rare: rare are capabilities that few, if any, competitors possess.
- Costly to imitate: that are capabilities that other firm cannot easily develop. Capability that are costly to imitate are created because of one reason or a combination of three reason
- Nonsubstitutable: are capabilities that do not have strategic equivalents.

The second tool is the value chain analysis; firms use this tool to select the value-creating competencies that should be maintained, upgraded, or developed and those that should be outsourced. I speak about that in the next chapter, because I identify the value chain analysis, like one of the three pillar of the business-level of strategy.

1.6 The first step to make a strategy: Vision, Mission and objective

The managerial process of creating and executing the company's strategy consists of five stages connected one to each other:

1. *Development of a strategic vision and mission* that indicates the path to follow and the future direction of the company in terms of product, market, customers, and technology.
2. *Definition of objectives* that are also criteria for evaluation of performance and growth of the company.
3. *development of a strategy for achieving the objectives* in accordance with the strategic direction outlined by management.
4. Effective and efficient introduction and implementation of the strategy chosen.
5. Evaluations of performance and introduction of corrective measures.

The values, vision and mission statements identify what the business is and what it stands for, how it wants to be seen, and how it wants to go forward.

First Considerations: The values, vision and mission statements set the tone for not only the business plan, but also for your company. They define the path your company will follow and act as a guiding principle by which your company functions. Your values, vision and mission statements tell your reader what you and your business are all about — what your company stands for, what you believe in, and what you intend to achieve. Economy of words is critical. This doesn't necessarily mean that they should be short at the expense of effectiveness, but that each word should be powerful and meaningful. Be clear and concise and make it obvious what your company is attempting to do. Is there a difference between a values statement, a vision statement, and a mission statement? Yes, the differences are:

The **VALUES** define what your business stands for — they are your core rules.

Your **VISION** defines how you want your business to be seen externally — by clients, suppliers, investors and even competitors. It's what you constantly strive to attain, and it becomes your reason for being.

Your **MISSION** is what you intend to become or accomplish. It should be challenging but achievable. A well-written mission statement demonstrates that you understand your business, have defined your unique focus, and can articulate your objectives concisely to yourself and others.

The way to think of this is that the **VALUES** drive the **VISION** which in turn drives the **MISSION**.

Vision is a picture of what the firm wants to be and, in broad terms, what it wants to ultimately achieve³⁰. Thus, a vision statements articulates the ideal description of an organization and gives shape to its intended future. In other words, a vision statements

³⁰ R.D. Ireland, R.E. Hoskisson, & M. A. Hitt, 2009, Understanding business strategy.

point the firm in the direction of where it would eventually like to be in the years to come. Vision is a “big picture” thinking with passion that helps people *feel* what they are supposed to be doing in the organization. People feel what they are to do when their firm’s vision stretches and challenges people as well.

It is also important to note that vision statements reflect a firm’s value and aspirations and are intended to capture the heart and mind of each employee and, hopefully, many of its other stakeholders. A firm’s vision tends to be enduring while its mission can change in light of changing environmental conditions. A vision statement tends to be relatively short and concise, making it easily remembered.

As a firm’s most important and prominent strategic leader, the CEO is responsible for working with others to form the firm’s vision. Experience shows that the most effective vision statement results when the CEO involves a host of stakeholders to develop it³¹. In addition, to help the firm reach its desired future state, a vision statement should be clearly tied to the conditions in the firm’s external environment and internal organization.

Mission. Organizations cannot survive if they don’t know where they are going and what they are all about. For Wheelen and Hunger an organizational mission defines the fundamental, unique purpose that sets a company apart from other companies of its type and identifies the scope of the company's operations in terms of products (including services) offered and markets served.

In other words, mission statement describes an organization's purpose, its customers, its products (often in functional terms, that say what need or needs are being met), and its technology (that is, how it delivers its products or services). Thus, it is the purpose or reason for the organization's existence.

³¹ E.g., other top-level managers, employees working in different parts of the organization, suppliers and customers

The organizational purpose defines the activities that the organization performs or intends to perform and the kind of organization that is or intends to be. The mission statement tells who we are and what we do as well as what we'd like to become.

Mission statements should be sufficiently narrow to help the company determine its proper market niche³². One of the easiest ways to fail is to attempt to satisfy everyone. Because of the different characteristics of customers and geographic areas, and varying product preferences, a company attempting to satisfy a large group of diverse customers is forced to make compromise decisions in virtually every aspect of its pricing, product features, and service policies. Consequently, it finds itself failing to satisfy anyone completely. Other competitors are likely to move into the industry and develop plans that focus on narrow market niches. And the original company, in its attempt to retain a large, diverse market, frequently finds this market disappearing into small slices that are served by other companies with narrower focuses. In highlighting the importance of mission statements, Drucker argued that the mission statement defines the organization. He stated that *"...only a clear definition of the mission and the purpose of the organization makes possible clear and realistic business objectives"*.

The vision is the foundation for the firm's mission. A mission specifies the business or businesses in which the firm intends to compete and the customers it intends to serve.

The firm's mission is more concrete than its vision; however, like the vision, a mission should establish a firm's individuality and should be inspiring and relevant to all stakeholders. Together, vision and mission provide the foundation the firm needs to choose and implement one or more strategies. The probability of forming an effective mission increases when employees have a strong sense of the ethical standards that will guide their behaviors as their work to help the firm reach its vision. Thus, business ethics are vital part of a firm's discussions to decide what it wants to become (its vision) as well as who it intends to serve and how it desires to serve those individuals and group (its mission).

³² Megginson et al. 1992:203

Objectives. An organization without objectives is an organization without direction. Objectives are the end results, goals, or targets that all organizational activities seek to attain, they are an important part of planning process because they become the focal point for directing strategies. Although objectives can vary widely from organization to organization, normally they can be categorized as follow: profitability, service to customers, employee needs and well-being, social responsibility, and others. The following items provide potential areas for establishing long-term objectives for most organizations: profitability, markets, productivity, product, financial resources, physical facilities, research and innovation, organization structure and activities, human resources, customer services, social responsibility.

Generally, long-term objectives need to be established for every area of the organization where performance and results directly influence the survival and prosperity of the organization; long-term objectives must support and not be in conflict with the organization's mission. The long-term objectives should be clear, concise, and quantified whenever possible and should be detailed enough so that the organization's personnel can clearly understand what the organization intends to achieve. They should span all significant units or areas of the organization and not concentrate on just one area.

Objectives for different areas of the organization can serve as checks on each other, but should be reasonably consistent with each other. Finally, objectives should be dynamic in that they need to be reevaluated in light of changing conditions.

Organizational mission statements, policies, objectives, and strategy are not mutually exclusive components of strategic planning process. Rather, they are highly interdependent and inseparable. One cannot talk about attaining objectives without knowing the policies that must be followed. Similarly, a strategy cannot be determined without first knowing the objectives that are to be pursued and the policies that are to be followed. Furthermore, strategy implementation impacts upon the strategic planning process. The figure which shows the entire strategic management process as a series of sequential steps, should be considered merely as a method for analyzing the entire process and not as a step-by-step process that should be sequentially followed.

Chapter 2

Corporate level strategy

In recent years the term Corporate strategy has been widely adopted by management to describe the activities associated with the statement of an organization's overall goals or objective and the means by which they are to be achieved/fulfilled. In this chapter I want to introduce the corporate-level strategy, which are strategies firms use to *diversify* their operations from a single business competing in a single market into several product markets and, most commonly, into several businesses. Thus, a corporate-level strategy specifies actions a firm takes to gain a competitive advantage by selecting and managing a group of different businesses competing in different product markets.

Corporate-level strategy, which is concerned with deciding what businesses and national markets an enterprise should participate in. The business options are to focus on a single business; vertically integrate into adjacent businesses, forming a supply chain from raw materials to consumers; and diversify into other businesses. The national market options are to focus on the firm's home market or expand internationally. Corporate-level strategy also encompasses decisions about *how* to enter new businesses and markets—whether through acquisitions and mergers or by establishing new ventures. As always, the goal of management in pursuing these strategies is to boost the overall performance of the enterprise measured by profitability and profit growth.

Corporate-level strategies help companies select new strategic positioning – positions that are expected to increase the firm's value. We discuss several topics to examine corporate-level strategies, because customers are the foundation of successful corporate-level strategy and should never be taken for granted. In terms of customers

when selecting a corporate-level strategy the firm determines (1) who will be served, (2) what needs those target customers have that it will satisfy, and (3) how those needs will be satisfied.

How then are we to define corporate strategy? My own preference is for the sense associated with military usage (from which so many apparently new business ideas have been borrowed with little or no acknowledgement), namely, the achievement of a stated purpose through the utilization of available resources. In a business context I follow the definition proposed by Andrews (1971), namely: “*Corporate strategy is the pattern of major objectives, purposes, or goals, and essential policies and plans for achieving those goals, stated in such a way as to define what business the company is in or is to be in, and the kind of company it is or is to be*”.

Customers: Their relationship with corporate level strategies

Strategic competitiveness results only when the firm satisfies a group of customers by using its competitive advantage as the basis for competing in individual product markets. A key reason firms must satisfy customers with their corporate-level strategies is that returns earned from relationship with customers are the lifeblood of all organizations.

The most successful company try to find new ways to satisfy current customers and/or to meet the needs of new customers. Being able to do this can be even more difficult when firms and customers face challenging economic conditions; during such times, firms may decide to reduce their workforce to control costs.

Effectively managing relationships with customers

The firm’s relationship with its customers are strengthened when it delivers superior value to them. Strong interactive relationships with customers often provide the foundation for the firm’s efforts to profitably serve customers’ unique needs.

Customers loyalty has a positive relationship with profitability, however, more choices and easily accessible information about the functionality of firms’ products are creating increasingly sophisticated and knowledgeable customers, making it difficult to

earn their loyalty. A number of companies have become skilled at the art of *managing* all aspects of their relationship with their customers.

Reach, Richness and Affiliation

The *reach* dimension of relationship with customers is concerned with the firm's access and connection to customers. In general, firms seek to extend their reach, adding customers in the process of doing so.

Richness, the second dimension of a firms' relationship with customers, is concerned with the depth and detail of the two-way flow of information between the firm and the customer. The potential of the richness dimension to help the firm establish a competitive advantage in its relationship with customers leads many firms to offer online services in order to better manage information exchanges with their customers. Broader and deeper information based exchanges allow firms to better understand their customers and their needs. Such exchange also enable customers to become more knowledgeable about how the firm can satisfy them.

Affiliation, the third dimension, is concerned with facilitating useful interactions with customer. Viewing the world through the customer's eyes and constantly seeking ways to create more value for the customer have positive effects in terms of affiliation.

As I present next, effectively managing customer relationship (along the dimensions of reach, richness and affiliation) helps the firm answer questions related to the issue of *who*, *what*, and *how*.

Who: Determining the customers to serve

Deciding *who* the target customer is that the firm intends to serve with its corporate-level strategy is an important decision. Companies divide customers into group based on differences in the customers' needs to make this decision. Dividing customers into groups based on their needs is called market segmentation, which is a process that clusters people with similar needs into individual and identifiable groups.

Almost any identifiable human or organizational characteristic can be used to subdivide a market into segments that differ from one another on a given characteristic. Common characteristics on which customers' needs vary are illustrated in the Table 7.

CONSUMER MARKETS
Demographic factors (age, income, sex, etc.)
Socioeconomic factors (social class, stage in the family life cycle)
Geographic factors (cultural, regional and national differences)
Psychological factors (lifestyle, personality traits)
Consumptions patterns (heavy, moderate, and light user)
Perceptual factors (benefit segmentation, perceptual mapping)
INDUSTRIAL MARKETS
End-use segments (identified by SIC code)
Product segments (based on technological differences or production economics)
Geographic segments (define by boundaries between countries or by regional differences within them)
Common buying factor segments (cut across product market and geographic segments)
Customers size segments

Table 7 Basis for Customer Segmentation

What: determining with customer needs to satisfy

After the firm decide *who* it will serve, it must identify the targeted customer group's needs that its goods or services can satisfy. In a general sense, *needs (what)* are related to a product's benefit and features. Successful firms learn how to deliver to customers what they want and when they want it. Having close and frequent interactions with both current and potential customers helps the firm identify those individuals' and groups' current and future needs.

From a strategic perspective, a basic need of all customers is to buy products that create value for them. The generalized forms of value that goods or services provided

are either low cost with acceptable features or highly differentiated features with acceptable cost.

How: determining core competencies necessary to satisfy customer needs

After deciding *who* the firm will serve and specific *needs* of those customers, the firm is prepared to determine how to use its capabilities and competencies to develop products that can satisfy the needs of its target customers. Firms use core competencies (*how*) to implement value-creating strategies and thereby satisfy customers' needs. Only those firms with the capacity to incessantly improve, innovate, and upgrade their competencies can expect to meet and hopefully exceed customer's expectations across time.

Our discussion about customers shows that all organizations must use their capabilities and core competencies (the *how*) to satisfy the needs (the *what*) of the target group of costumers (the *who*) the firm has chosen to serve.

2.1 Corporate strategy and adding value

Large organizations that operate in highly dynamic and competitive markets face different types of pressure:

1. Pressure to reduce costs³³
2. Pressure to increase revenue³⁴
3. Pressure to increase market share

³³ Public and private sector have experienced significant pressure to bolster productivity while reducing their overall costs, both in regard to overhead and process costs. Initially, these pressures lead many companies to lay off significant percentages of their workforces or close departments in order to meet budgetary goals.

³⁴ Some authors offers six rules that owners and managers of smaller businesses can apply to become - or at least act like - a company and navigate past the cost-management trap to revenue-side management: Rule 1: Functionally satisfy at least the minimum; Rule 2: Don't compete on price; Rule 3: Drive expectation; Rule 4: Measures causes over outcomes; Rule 5: Critical change occurs once competitors start to follow the company's lead; Rule 6: Deep, sustainable strength takes time.

4. Pressure to be responsive to the markets in which they operate
5. Pressure to innovate and stay relevant³⁵
6. Pressure to satisfy shareholders and stakeholders
7. Pressure to transfer information, knowledge, and competencies among business units and functional areas.

In order to respond to some of these pressures, large H&T organizations need to pursue a low-cost strategy at a convenient location where they can benefit from economies of scale. Large H&T organizations may also need to adapt their product and service offerings to the conditions of local markets in order to be able to accommodate the differences between markets. Being able to strike a balance between these competing demands can be seen as a competitive advantage that adds value to the organization's portfolio. The intent is to create and maintain synergy among all business units and functional areas so the whole organization can collectively work together to achieve the corporate goals.

Ghoshal and Barlett (1990) presented frequently used typology to describe the multinational corporate strategy that encompasses the preceding competing demands. They identified four main strategies for the multinational corporations: international, multidomestic, global, and transnational outlines the key characteristics of these strategies.

The international strategy creates value through the transfer of core competencies and resources from home to host country markets. An organization pursuing an international strategy adopts a decentralized approach to the management of its resources and capabilities outside the core to subsidiaries. In terms of product offerings and marketing, the local networks and competences are exploited, but there is limited adaptation to the local markets. International strategy is appropriate in those markets where although there is a need for local responsiveness it is not urgent. In contrast, a multidomestic strategy strives to achieve maximum local responsiveness.

³⁵ A brand to stay relevant can use four strategies: 1) Gain parity; 2) Leapfrog the innovation; 3) Reposition; 4) Stick your knitting.

Products and services are designed and developed according to the preferences of local customers. The cost of operations according to the expectations could be high, as multidomestic strategy requires leveraging local resources and competencies in each market. Business units are fully responsible and accountable for strategic and operating decisions, as they operate autonomously.

An organization pursuing a global strategy tends to centralize strategic and operating decisions at the corporate level (Ghoshal and Bartlett, 1990). This strategy also involves standardizing products and services as well as marketing activities in order to benefit from economies of scale. Its strengths are efficiencies of scale and cost advantages. Therefore, the strategy is appropriate when there is a need for cost reduction, and demand for local adaptation is low (Connelly et al., 2007). In the organizations where global strategy is pursued, there is a high degree of cooperation, resource, and competence sharing at the corporate level and learning from the centre (Connelly et al., 2007). Finally, the transnational strategy aims to strike a balance between lowering costs on one hand and being responsive to local demands on the other. Any organization pursuing this strategy, however, must reconcile conflicting goals: the demand for low cost, which requires global coordination, and the demand for local responsiveness, which requires flexibility and local control (Connelly et al., 2007). Attention is paid to managing integrative links between local companies as well as with the centre in order to resolve this conflict. There is a great deal of sharing knowledge and competences between headquarters and subsidiaries for the company's worldwide operation.

2.2 Strategies of corporate level strategy

Strategy must ensure the survival and prosperity of the company. So, the company must obtain a return on capital superior than its cost, what determines the ability of firm to earn such a rate of return?

There are two routes.

First, the company may locate in an industry where favorable conditions result in the industry earning a rate of return above the competitive level.

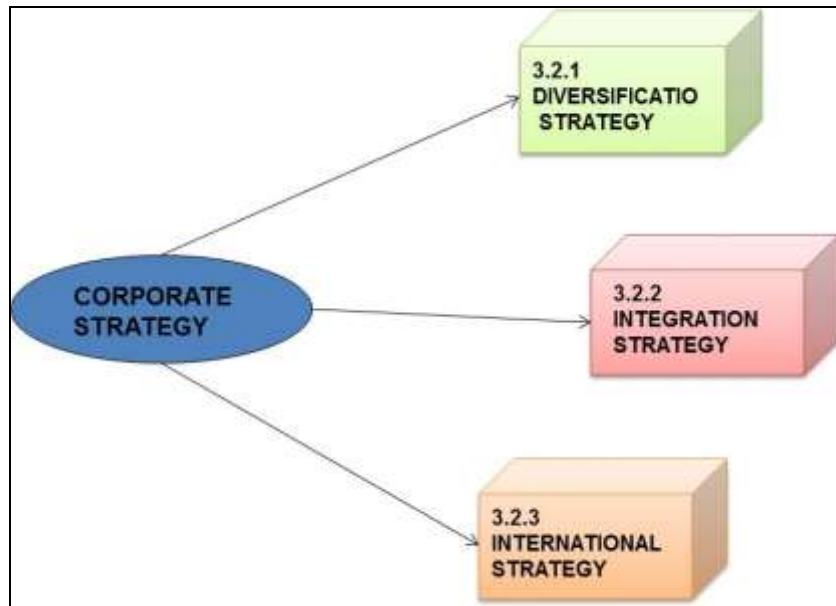
Second, the firm may attain a position of advantage in comparison to its competitors within an industry, allowing it to earn a return in excess of the industry average. These two source of superior performance define the two basic levels of strategy within an enterprise: corporate strategy, and functional strategy.

CORPORATE STRATEGY → define the scope of the firm in terms of the industries and markets in which it competes. Corporate strategy decisions include investments in diversification, vertical integration, acquisitions and new ventures; the allocations of resources between the different business of the firm; and disinvestment. Corporate strategy refers to the overarching strategy of the diversified firm. Such a corporate strategy answers the questions of in which businesses should we be in? and how does being in these business create a synergy and or add to the competitive advantage of the corporation as a whole.

Corporate strategy is the responsibility of the top management team, supported by corporate staff.

The corporate strategy is aimed at recent decisions of the company related to three fundamental aspects:

- the degree of diversification of the business, from which it must decide diversification strategies, also known as portfolio strategies;
- the degree of vertical integration, which are formulated in relation to vertical integration strategies or disintegration or outsourcing;
- The amplitude of the markets on which to operate, under which are formulated comprehensive strategies.



2.2.1 Diversification strategy

The content of the strategic portfolio of the company may affect the strategic business areas or just individual products. Portfolio selection aimed to identify the key areas in which to enter or leave is made within the scope of company strategy. Instead, the selection of the product portfolio in a strategic area comes within the ambit of the strategies or marketing policies. The strategic business areas, known simply SBA, may belong to different sectors within the industry or in different niches.

In essence, the diversification strategy must specify:

- if the company is to be only one-business therefore linked to the original activity;
- if the company is to be multi-business and therefore extend to different areas of business seizing strategic opportunities;
- if the company is to abandon the original business as in the declining phase.

DIVERSIFICATION

In the panorama of strategies most used by companies around the world highlights the diversification. The decision to diversify its strategic business areas and as a result the business activities is mainly due to the search for a higher value. The company's growth, outside of those who are the constraints that characterize a given area, is one of the most difficult choices between business strategies, and the entry into new sectors, if you do not have certain skills or the basis for a start 'attached to the core business activities, it might be very difficult to limit and achieve a destruction of corporate value very deep.

Diversification decisions involve considerations regarding the attractiveness of the area where you want to enter and possess sufficient expertise to achieve a good competitive advantage in the new sector. These are potential determinants of profit, which must be analyzed carefully by corporate executives who are concerned with strategies, trying to build up of the medium-and long-term effects that will have on the company.

The diversification's reason

In redefining the business priorities with regard to the objectives of value creation for companies, businesses, has always tried to get a sustained growth, associated with a reduced risk. The consistency of these objectives is not always agree with the policies of the shareholders, who often try to get the maximum profit from business, without moving towards new horizons production - trade and this trend is intensified in the last four years, mainly because of the economic crisis.

Renewed growth: diversification of its activities, and therefore the SBA (strategic business area), comes from the willingness of companies to exit the industry in which they operate for many years, thus avoiding a prison industry that would prevent them to renew the eyes of stakeholders. The time spent in a given sector mainly characterized by low growth and substantial inputs of liquidity is one of the key incentives for large companies trying to expand their portfolio of business activities, even in very different fields. Of course, starting a new business in a new sector requires

large cash flows: it is therefore very important not to dispose of, regardless, the productive branches of sectors with low growth, because they are the ones that allow you to have the resources necessary to development and growth of new SBA. Often search for easy profits by shareholders locks diversification strategies which do not guarantee safe and profits in the short term;

Reducing the risk: The diversification of activities aimed at reducing business risk, often carried out with the meeting of more sectors under a single ownership structure, may allow you to acquire a good cash flow, reducing the overall variability. However, the greatest interest to reduce the risk lies with managers over shareholders, who cannot invest in portfolios of financial assets and very different, they are able to reduce their exposure. The real advantage, which could have shareholders from the diversification of business activities, is when you are unable to diversify at a lower cost than that incurred by the shareholders on their investments. It is very unlikely to occur, because the transaction costs borne by shareholders are lower than those faced by companies: Legal, costs arising from bank loans and premium on shares (resulting from the acquisition of an independent enterprise).

Cost advantage, differentiation and disadvantages

The option to apply a diversifying strategy is to exploit fully the possibilities offered by the bonds between the different activities, which are often the main sources of competitive advantage from diversification. The links that allow you to get value from their creation are those arising mainly from the sharing of resources and responsibilities among the various activities in the firm. The diversification often gives the possibility of strengthening the market power of the undertaking which carried out, in parallel could consolidate this power and thus make the company much stronger against competitors.

- Economies of scope;
- Advantages internalization of transaction;
- The advantage of the parent company;
- The diversification of the business as a system of internal market.

The three principles of diversification strategy

The selection of strategic business methodology is based on three principles:

- A. the life cycle of the strategic business;
- B. the attractiveness of the strategic business;
- C. portfolio analysis.

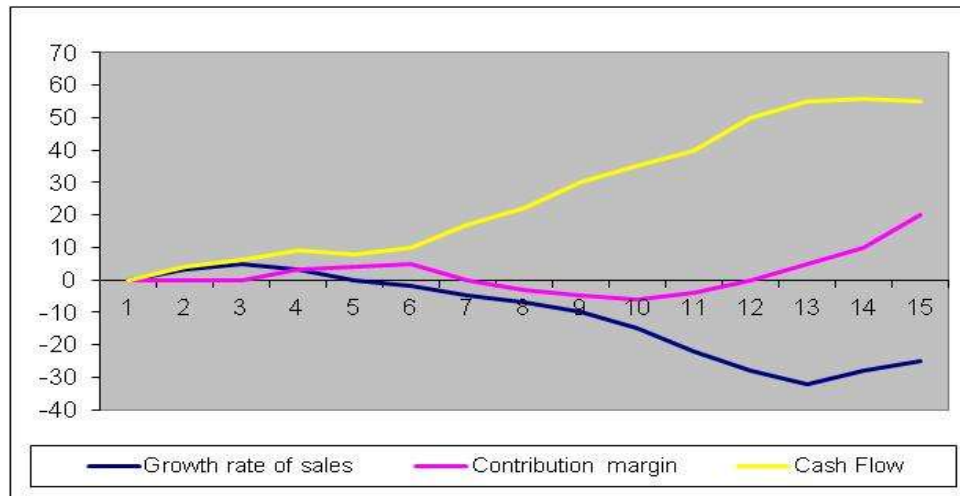
A. The life cycle of the strategic business³⁶

The selection of the portfolio of strategic business areas is based on the rate of development of the strategic business as it is reasonable to assume that it is strategically necessary: enter into strategic business areas with a high rate of development; exit strategic business areas with low or negative growth rates.

To determine the estimated rate of development can proceed by analyzing the life cycle of the strategic business, with the following modalities.

1. Shooting the financial statements of companies operating in the strategic area of business for a time interval of 3-5 years.
2. Are identified in these budgets, revenues, contribution margin and cash flow, when data are available.
3. It deflates values in order to bring all real-valued on the basis of the percentage of each year's inflation
4. It is calculated for each year the growth rate of sales, the contribution margin and cash flow deflated physically returning it on a graph.

³⁶ M. Saita, I fondamentali dell'economia aziendale e strategia aziendale, Giuffrè editore, 2010



In order to assess whether the strategic area of business is in a beginning stage, development, maturity or decline settle the ranges, such as for revenues:

- If the rate of development varies in the early years from 0 to 10% over the strategic area of business is in a phase of beginning;
- If ranges from 10 to 60% is in a stage of development;
- If in recent years ranges from 0 to 10% is in a stage of maturity;
- If in recent years is less than 0 is in a phase of decline.

The same procedure for the contribution margin and cash flow, where you can find trend reversals, such as a possible decline of revenues could pay a development cash flow. The analysis of the life cycle of the strategic business must be carried out for both the business areas of the company for both traditional business areas where there is a guideline or weak signals of interest for the company .

B. Attractiveness of the strategic area of business

The analysis of the life cycle is not sufficient to make the area attractive strategic business, because we must take into account a number of variables that despite a significant growth rate could make critical placement in a new strategic business area.

Should therefore provide an array of strategic attractiveness of the business based on five factors:

1. market factors, which take part in the data of the life cycle of the product;
2. competition;
3. financial economic factors;
4. macro-environmental factors;
5. technological factors.

Some of these factors can be measured in terms of absolute values (income) or percentages (growth rate of the market), other factors need to express a qualitative judgment (e.g. type of competitors).

In order to compare the attractiveness of different market areas it is necessary to establish a system of values by allowing scores to arrive at a judgment of attractiveness, based on five levels:

1. maximum attractiveness;
2. high attractiveness;
3. attractiveness media;
4. low attractiveness;
5. attractiveness nothing.

The choice of attractiveness factors may be different depending on the characteristics of the strategic business areas.

C. Portfolio Analysis: BCG Matrix

The matrix of the Boston Consulting Group (BCG), a leading consulting firm, are expected to be identified for each SBA, the rate of market growth and market share relative importance compared to the competitor.

A market share of 0.1, for example, indicates that our company sells that particular SAA on 10% of what sells the most important competitor, if the part were instead equal to 2 would mean that the firm makes sales of twice the leading competitor. To understand the relationship between growth rate and market share relative market builds a matrix which will be discussed in the chapter of business-level strategy.

2.2.2 The integration strategy

The strategy of integration involves business processes in which they must decide which business activities and which activities are part of the company's value chain must be carried out within the company, or should be outsourced, albeit with special cooperation agreements.

The degree of vertical integration: mainly business processes, especially in decisions about which activities in the value chain must be carried out within the economic organization and which are not. This is a very important topic for economic organizations, since the decision to integrate or less has a very strong connection with the costs both short, and long-term. The decision to invest in a way to integration of the value chain, from upstream to downstream of the production process must be carefully evaluated and approved in consultation with all stakeholders in business, just because of the investments that must be supported.

The integration allows for significant cost advantages and differentiation, together in the same market, but also a considerable element of risk attached to the internal costs if there were changes in the price of supplies, in fact, increased competitiveness expressed by suppliers outside would think to a de-backward integration. Then, you can add the bureaucratic costs arising out of dealings with customers, connected to the rigidities in related services, and therefore higher costs of internalization of services. Do not forget the presence of barriers to exit in case you opt for a de-integration of the group, in fact, the sale of equipment or disposal of businesses, especially in this period, it is very difficult given the costs involved. Even in the case of

outsourcing and outsourcing have costs resulting from exit barriers, particularly for services not related to the core business or high professional skills, which if they were kept within the organization would be very cost centers " heavy "and thus reduce the company's profits.

VERTICAL INTEGRATION

The search for a better performance by companies involves the critical choices, especially regarding the ability to change its configuration in production. It is the assessment of costs and benefits to be gained from the various activities that make up the value chain to determine the level of integration of the company. In the words of vertical integration is defined as "the internalization of a number of vertically related activities." The degree of integration is measured by the level of control exercised by the properties of the various stages of the value chain, from raw material processing to marketing. This level can be measured analytically by the ratio of the added value created by the company and its sales revenue: the greater the production carried out within the company, the lower the value of goods and services purchased in relation to turnover. At the level of income, this ratio results in a lower incidence of post regarding purchases in favor of the host, the value of activities carried out within the company.

Motivations and types of vertical integration

The interaction with the market by an enterprise, the management of its portfolio products and brands and relationships with all stakeholders involve a big commitment. The management of a large number of activities which are not part of the same economic organization leads to difficulties in the transmission of information, the management of which is vital for businesses of a certain size. Everything turns into higher costs of operating and managerial inefficiencies, which could be eliminated or at least reduced if you were to opt for an internalization of the various business activities. In addition to reducing costs, the integration of vertically related provides greater control by the company on several parts of the value chain, than companies that have opted for a choice to outsource some stages of production.

The strategy of vertical integration by a company is often used during its growth. In fact, in the years when a company increases its size, both in terms of "physical" or economic, the management of the company's growth should be the first objective of the company. The total control by the company of the activities that make up the value chain enables management to 360 °, thanks to which it is able to carefully evaluate all the components of cost. Another factor to consider is the protection from competitors, especially in the early stages of maturation of the company in the market. In fact, when a new competitor enters a new market in which there are other economic strongest, their first wish would be to get rid of the newcomer before it becomes strong. Consequently, the choice not to external contact for certain machining operations, supplies of semi-finished products (which will be achieved directly) may offer a greater level of protection³⁷.

The choice by the companies of the level of integration usually involves a choice of two-way integration, which scholars suggest using two terms:

Upstream integration: when the company "takes control and ownership of the production of its own components and other inputs." It is a type of integration that enables the company to control the suppliers of essential raw materials for the production.

Downstream integration: when a company "takes control and ownership of activities carried out in the final part of the value chain, or previously performed by its customers." Implementing this type of integration, the company decided to keep under control all the activities that are at the end of the value chain.

Advantages and disadvantages of integration

The implementation of a strategy that involves the vertical integration of some of the activities of the value chain or all involving balancing in the planning of costs and benefits that can be obtained. The sustainability of an integrative process is one of the

³⁷ The choice of the integration strategy as part of an economic entity, as well as decide whether to implement the early stages of the value chain, or in the past, passing through the choice of many activities internalize within their organization

evaluations more difficult to predict in the long run, especially in these times, precisely because of the instability present in the markets.

The main advantages achievable by the vertical integration strategy are:

- Barriers to competition
- Limiting the risks associated with investments in specialized facilities
- Protection of the quality of goods and services
- Internalization of markets
- Planning and coordination

ORIZONTAL INTEGRATION

The constant growth and development of a market involves the continuous updating of the corporate objectives, both a management and dimensional, to be related with the activities undertaken by competitors. From the dimensional point of view, as has been said in other contexts, businesses are always trying to win new market share, both through internal growth and through the acquisition of smaller competitors or low.

In terms of strategic policies, obtaining greater company size, time to have more market power than its competitors, is referred to as horizontal integration. It is defined as "a development strategy in which the activities of a company are expanded through the merger, acquisition or alliance with another company that performs the same activities." Then, using these three forms of business combinations, the new economic entity will be able to increase its product portfolio, expanding the recipients of its production. This will enable it to achieve a greater presence in the sector in which it operates, thanks to trade relations undertaken by companies before integration. Furthermore, the strategy of horizontal integration allows entry into new geographic markets with substantial barriers to entry which, however, present great opportunities for growth for the company. These decisions, in consultation with the company's internationalization strategies will enable the company to further expand its size, customer base and visibility worldwide.

Motivation of horizontal integration

The decision to expand its business size through the strategy of horizontal integration is a decision of great importance and impact on the management and operating company. Expanding the size of the company through the formation of a new party, the latter will be able to conquer new market segments, the first can not be reached because of the small size company. Moreover, it sometimes happens that integration between companies that make them complementary products within the same industry sector. In this way, the new economic entity will be able to compete on many portions of the market at the same time, thanks to the ability to exert a multiple production³⁸.

Finally, the implementation of a strategy of horizontal integration is linked to financial reasons internal and external to the company. Frequently greater size of the company allows to obtain tax benefits based on the number of workers, or more likely in the hands of an economic entity to facilitate the development of distressed areas. The increased size of the company then can take advantage of more opportunities both in terms of tax and social-economic development, resulting in an improvement in leverage in the event of success.

Advantages and disadvantages of horizontal integration

The application of a strategy of horizontal integration by a company, which aims to expand its market size and volume of business, as well as lead to a radical change in society, will provide a number of advantages to the new economic entity.

³⁸ With two companies implementing products complement each other, the new company will be able to complete its range of products. Not only that, in fact, the new set of skills and expertise, in addition to internal resources, will enable the development of new products, enabling the company to meet the needs of customers, established and potential. Due to the expansion of the product portfolio, together with the growth in size of the company, increase its market share. This will not be just the sum of shares held by various companies merged into a single economic organization, but at best, even bigger.

2.2.3 The internationalization strategy

The overall strategy or internationalization strategy is subsequently examined by considering some key issues such as:

- a) the advantage of global internationalization strategy;
- b) development strategies in international markets;
- c) the role of sectors in the process of internationalization;
- d) the Competitive Advantage of Nations.

a. The advantage of global-internationalization strategy

The advantages of internationalization strategies are varied, but two can be more readily apparent as they are based on two fundamental principles, as well recalls Levitt³⁹:

- the globalization of consumer preferences, caused by the strong impact of international publicity, increased communication (television, internet, etc.). Between the various countries of the world, and the further internationalization of people studying, working and traveling in other countries
- economies of scale arising from the possibility of production and distribution of products on international markets, just think of the automotive, finance, online, computer, books, etc..

In addition to these two basic principles, they do see the benefits of global strategies, Rispoli⁴⁰ recalls a number of other factors that have made it increasingly possible internationalization strategies of companies:

³⁹ T. LEVITT, *The globalization of markets*, in *Harvard business review*, maggio-giugno 1983

⁴⁰ M. RISPOLI, *Sviluppo dell'impresa e analisi strategica*, Il Mulino, Bologna, 1998

- dynamic of cultural factors, such as a tendency to world economic development, as well as consumer preferences have already been mentioned;
- factors related to communication technologies (networks, Internet, websites, etc.).
- reduction of protectionist barriers, and consolidation of international trade agreements (WTO, EU, NAFTA, EFTA, ASEAN, etc.).
- logistical factors that allow a more rapid transport of goods and persons;
- financial factors, resulting from the globalization of capital markets and the reduction in Europe of national currencies;
- factors relating to the acquisition of raw materials, human resources, technology and know-how;
- competitive factors various markets in search of new markets more favorable.

b. Development strategies

Development strategies in foreign markets may involve choices regarding the geographical location of production and the mode of entry in international markets⁴¹.

a) The geographical location of production.

The geographic location of production can cover the entire value chain or individual activities in the value chain. In the first case, the factors that affect the localization strategy are:

- the existence of inputs that allow cost advantage or differentiation;
- specificity of the competitive advantage, it is possible to localize other countries those activities that allow, in any case, the maintenance of the

⁴¹R.M. GRANT, *op. cit.*, pag. 417.

competitive advantages already existing holding, transferability of assets, some assets are difficult to export because of high transport costs.

In the second case, it is possible to locate in foreign countries only in certain activities of the value chain;

b) Modes of entry into international markets

The mode of entry in foreign markets can take place with trade or direct investment. The traditional business relationships can be direct export by the customer or through indirect channels, represented by officials or agents overseas. Fall in trade relations traditional formulas even more sophisticated, such as: the sale of trademarks under license in sectors characterized by high marketing skills;

- the transfer of technologies licensed for use in sectors with a high technological expertise and covered with a good legislation for the protection of industrial property rights (chemical, pharmaceutical, etc.).
- formulas franchise in the fashion industry, clothing, retail, dining, fast food, etc.

This option is implemented when the competitive advantage of the company is closely linked to the country of origin and therefore can not benefit from additional competitive advantages in other countries. More consistent with a strategy of globalization are direct investments, such as:

- joint ventures with local companies, usually designed to use the national commercial network;
- branches or real or only domestic companies with marketing, or marketing and production, or, at least, even research and development.

c. the role of sectors in the process of internationalization

Not all sectors enables companies to develop, in the same way, the process of internationalization, in fact, we can distinguish four types of domains with different degrees of trade and foreign direct investment.

The sectors that have high foreign direct investment and, at the same time, a high level of product marketing, are the so-called global sectors

The sectors that have high foreign direct investment, but poor marketing of products / services are management consulting, investment banking, fast food, etc.

The sectors that have high commercial and low direct investment are shipbuilding, aerospace, etc..

The sectors that have low propensity, are defined and protected areas are increasingly decreasing, because, in the past, protected areas were the banking, insurance, retail, telecommunications, energy, and today we are witnessing to a rapid growth of internationalization in these sectors .

d. The Competitive Advantage of Nations

The internationalization strategies, a key role is assumed by the competitive advantage of nations, well outlined by Porter⁴², which is based on three fundamental principles:

- the competitive advantage of a nation is derived from the performance of the national companies that, in turn, are influenced by cultural characteristics, management, resources and know-how of the country;
- In order to sustain a competitive advantage over time, nations must have a dynamic advantage, which should over time increase innovation, improve skills;
- the competitive strength of a nation is based, rather than on the natural resources of a country, the dynamic advantage, as demonstrated by Japan, which has managed to grow despite the presence of a cost of human resources and infrastructure high, and in lack of raw materials (although facilitated by a low cost of capital).

⁴² M.E. PORTER, *Il vantaggio competitivo delle nazioni*, Mondadori, Milano, 1991

Based on these principles, nations must, on the one hand to develop comparative advantage, which should produce those goods that can better utilize the resources of the country, the other side must point to a dynamic advantage. The comparative advantages of nations are easily identifiable in both tangible and intangible resources of a country.

MARKET EXPANSION

A company, during its activity, has the natural tendency to grow and increase its dimension both as regards the economic side both from the financial point of view of production. The strategic decision to increase its size mainly depends on the willingness of the management or the owners to try to increase or at least maintain a certain competitive advantage over its competitors, which often happens, however, is also due to decisions on related more to the prestige , regardless of management skills in the organization.

Growth's reasons

The achievement of certain corporate performance requires, at a certain point in the life of the company, that it can expand its business, then point to growth thanks to the good results achieved. The possession of the right mix of resources and skills, see economies of scale and scope, a good level of power to customers and suppliers, combined with a growth in prestige to attract more talented human capital are all competitive advantages that 'firm must be able to administer, and in which to invest, empirical studies have shown that the best performance is achieved by companies that have been able to manage their growth, investing in the resources and expertise to make it happen. Growth is then the common factor that drives companies to try to create more business value is pointing to the shareholders, but also to other stakeholders, of course, because of globalization, it had to make a virtue of necessity, in the sense that the 'openness to world markets must be well organized. Much attention should be stored in knowing how to manage growth, careful evaluation of the costs to be incurred resulting from an expansion of its production capacity, but also human resources, which are a significant cost component. In fact, an expansion in both domestic and international,

resulting in an increase in its physical dimension also the company will incur costs arising from new investments to increase production capacity. Statistical studies show that it is mainly small businesses who suffer most from the effects of the growth of their competitors, mainly because of the incumbents from the various countries of the world, thanks to their greater size are able to exploit the economies of scale and perfection purpose.

Having decided on the growth strategy, the resulting expansion of the size of its market and, paths that can be taken are 2: internal growth and by acquisitions. The internal growth is considered by many scholars and proven by empirical evidence, the initial strategic decision to increase its production, and then expand its market. This is mainly to implement new activities based on the resources owned by the company: human resources, financial and technological resources and expertise. It is therefore to create business value through investment in new plant, machinery and other tangible assets, to increase the number of products to be placed in the market and then try to increase the level of competition. Besides the increase in production capacity in order to maintain market share, you can use a strategy of diversification, as written above, where there is a tendency towards the entry into markets other than those of the core business. Of course, diversification is intended as a conglomerate, ie buy smaller companies, to invest on them, implementing the skills that have made us the market leader and thus revive the activities together.

The second form of growth that companies can choose to expand their market growth through acquisitions. This type of growth mainly includes mergers and acquisitions, strategic alliances and production, licensing, franchising, and all other types of agreements that allow alliances aimed at winning more market share, which will be discussed later.

Forms of business concentration aforementioned fee in implementing them a certain degree of business integration descending, with implications in terms of strategic, organizational and financial. Greater integration (fusion), and the control by one company over the other, the higher the level of shared strategies and implications arising at various levels of the company. On the contrary, in the case of simple

commercial agreements, with a lower level of integration, these will not cause the requirement to share business lines, but simply to respect the contract predetermined. So depending on the degree of integration resulting from the agreements established there will be internal synergies in the management of business development, from research and development to commercialization of products.

GLOBALIZATION-INTERNATIONALIZATION

The vast majority of companies in the world, as they grow, they had to consider whether to expand their size coming from the territory of the country where they work, or not. The decision to grow more than the market in which they began, responds perfectly to meet the economic, but also competitive. In fact, the work in a trade with a saturated local market does not allow to have great growth opportunities, which could instead get entry into a new geographical area.

When it comes to internationalization "a company decides to expand its activities beyond national borders through trade or direct investment on the place." The decision to undertake this growth strategy must be carefully considered because of the potential for growth that can be obtained, both in terms of profits, and market share from which derives the achievement of a competitive advantage over competitors in the long run.

The strong economic growth of recent years has led to the creation of a large transaction network in the world, which was followed by the globalization of economic activity. This has facilitated the exchange of goods and services worldwide between businesses and consumers, making them closer and able to interact with lower transaction costs.

Models of internationalization

Once you make the decision to enter a foreign market, a company or a group are faced with two possibilities:

1. trade through the sale and transfer of goods and services from the country where the company operates, or has production plants, where she decided to start her business;
2. direct investment with the construction of production facilities or the acquisition of productive activities in the country where we operate, deciding whether to make only some stages of production or act as an active commercially.

The decision by the company to exit its territory is not always dictated by the search for a new market in which to increase their profits, but also expand its portfolio of resources and expertise. Usually, large corporations are opting for the choice of creating production facilities in countries in order to better serve local markets, reducing transaction costs. The geographic location of production is the key stage in the decision to pursue a strategy of internationalization.

After evaluating the best geographical location in terms of profit opportunities, costs and benefits can be acquired at the level of know-how, a company must analyze the effects of these decisions will have on the value chain. Frequently, businesses, instead of transferring the entire value chain in a foreign country, they tend to fragment, assessing the benefits. It is mainly a partial outsourcing of activities, which allows the creation of several stages of production, often the first or at least the intermediate ones, in countries with labor costs or raw materials lower. The areas where it is most widely used this strategy are the clothing and consumer electronics, in which raw materials or basic components of the products are available at lower prices. Another factor to consider is the cost in terms of coordination of the various activities spread around the world. These are mainly transport costs of goods and higher inventory for safety margins, to which must be added the cost of the time, a crucial factor in many types of businesses. The only type of policy production can eliminate these costs is the just-in-time, which requires the proximity of different enterprises. So the possibility of fragmenting the value chain through careful assessments of an economic, but also cultural and social, which the company should be careful. It is not only the factors having an impact in the short term but in the long term. In fact, with the passage of time,

the social conditions of the place where the corporation has decided to expand its business, could change to improve conditions for workers. If the opening of a factory was linked to agreements with a fundamentalist regime, and this was reversed, the costs of any renegotiations have to be taken by the company.

Chapter 3

Business level strategy

Business-level strategy is an integrated and coordinated set of commitments and actions the firm uses to gain a competitive advantage by exploiting core competencies in specific product markets. Business-level strategy indicates the choices the firm has made about how it intends to compete in individual product markets. The choices are important because long-term performance is linked to a firm's strategies. Given the complexity of successfully competing in the global economy, the choices about how the firm will compete can be difficult.

Every firm chooses at least one business-level strategy; thus it is the *core* strategy – the strategy that the firm forms to describe how it intends to compete in a product market.

STRATEGIC POSITIONING OF A BUSINESS-LEVEL STRATEGY

The role of accounting information within a business is to facilitate the development and implementation of business strategy. It is explicit attention to the strategic management context distinguishes SCM from managerial accounting.

Many factors jointly influence the management control process in a company. Researchers have attempted to examine these factors by applying what is called “*contingency theory*”, where is a behavioral theory that claims that there is no single best way to design organizational structures. The best way of organizing e.g. a company, is, however, contingent upon the internal and external situation of the

company. The contingency approach to organizational design tailors the design of the company to the sources of environmental uncertainties faced by the organization.

The point is to design an organizational structure that can handle uncertainties in the environment effectively and efficiently.

We have identified important factors that influence the design of control system, some of them being size, environment, technology, interdependence and strategies. Strategies differ in different types of organization, and controls should be tailored to the requirements of specific strategies.

The logic for linking controls to strategy is based on the following line of thinking:

- ✓ For effective execution, different strategies require different task priorities; different Key success factors; and different skills, perspective and behaviors.
- ✓ Control systems are measurement systems that influence that behavior of those people whose activities are being measured.
- ✓ Thus, a continuing concern in the design of control systems should be whether the behavior induced by the system is the one that is consistent with the strategy⁴³.
- ✓ Thus, a business unit's strategy depends upon two interrelated aspects: (A) its mission or goals, and (B) the way the business unit chooses to compete in its industry to accomplish its goals – the business unit's competitive advantage.

Business unit strategy

There are three different kind of missions that a business unit's can adopt:

⁴³ Journal of Cost Management 6, 3, (1992) pp. 14-25

Build. This mission implies a goal of increased market share, even at the expense of short-term earnings and cash flow. A business unit following this mission is expected to be a net user of cash in that the cash from its current operations would usually be insufficient to meet its capital investment needs.

Hold. This strategic mission is geared to the protection of the business unit's market share and competitive position. The cash outflows for a business unit following the mission would usually be more or less equal to cash inflow.

Harvest. This mission implies a goal of maximizing short-term earnings and cash flow, even at the expense of market share. A business unit following such a mission would be a net supplier of cash.

Business unit mission

The planning and control requirements of business units pursuing different strategies are quite different. As noted earlier, the mission for ongoing business units could be build, hold or harvest. These missions constitute a continuum, with pure build at one end and pure harvest at the other end. For effective implementation, there should be congruence between the mission chosen and the type of controls used. Develop the control - mission fit using the following line of reasoning⁴⁴.

The mission of the business unit influences the uncertainties that its general managers face and the short term versus long term tradeoffs that he or she makes. Management control systems can be systematically varied to help motivate the manager to cope effectively with uncertainty and make appropriate short-term versus long-term tradeoffs. Thus, different missions often require systematically different management control systems⁴⁵.

⁴⁴ This section draws from some research focused on strategy implementation issues at the business unit level. Govindarjan – Fisher – Hall – Simons.

⁴⁵ Strategic cost management – J.K. Shank & V. Govindarjan – chapter 6

Mission and uncertainty

Build units tend to face a great environmental uncertainty than the harvest units. Build strategies typically are undertaken in the growth stage of the product life-cycle, whereas harvest strategies typically are undertaken in the mature/decline stage of the product life-cycle.

The uncertainty faced by a build business unit is also greater because one of its objectives is to increase market share; the build strategy puts a business unit into greater conflicts with its competitors than does a harvest strategy. Competitors' actions are likely to be unpredictable and thus contribute to the uncertainty faced by build business units. Both on the input and output sides, build managers tend to be more dependent on external individuals and organizations than do harvest managers. Environment uncertainty can be increased because build business unit are often in new and evolving industries. The experience of build managers in their industries is likely to be less than that of their counterparts in established business. This inexperience also contributes to the greater uncertainty faced by managers of build units in dealing with external constituencies⁴⁶.

Mission and time sprain

The choice of build versus harvest strategies has implication for short-time versus long-time profit tradeoffs. The share-building strategies include some actions aimed at establishing market leadership, but sometimes they depress short-term profits. So, many short-term decision, do not result in profit until some future period, whereas the harvest strategies maximize short-term profit.

The purpose of a Business-Level Strategy

The purpose of a business level strategy is to create differences between the firm's position and those its competitors. To position itself differently from competitors,

⁴⁶ Strategic cost management – J.K. Shank & V. Govindarjan – chapter 6

a firm must decide whether it intends to *perform activities differently* or to *perform different activities*. In fact, “choosing to perform activities differently or to perform different activities than rivals” is the essence of business-level strategy. Thus, the firm’s business-level strategy is a deliberate choice about how it will perform the value chain’s primary and support activities to create unique value. Indeed, in the complex twenty-first-century competitive landscape, successful use of a business-level strategy results only when the firm learns how to integrate the activities it performs in ways that create superior value for customers.

Fit among activities is a key to the sustainability of competitive advantage for all firms; as M. Porter comments, “*Strategic fit among many activities is fundamental not only to competitive advantage but also to the sustainability of that advantage. it is harder for a rival to match an array of interlocked activities than it is merely to imitate a particular sales-force approach, match a process technology, or replicate a set of product features. Positions built on systems of activities are far more sustainable than those built on individual activities*”.

3.1 Types of Business – Level Strategy

Firms choose from among four business-level strategies to establish and defend their desired strategic position against competitors: *cost leadership, focus/niche differentiation, cost leadership, focus/niche differentiation*.

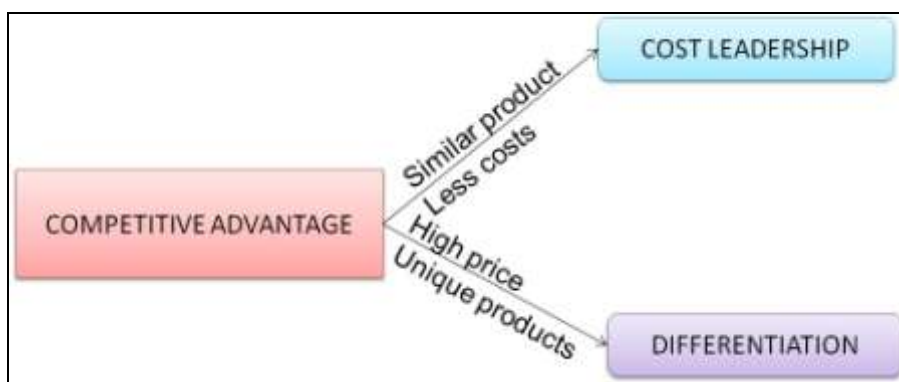


Figure 7 Sources of competitive advantage

Each business-level strategy helps the firm to establish and exploit a particular competitive advantage within a particular competitive scope. How firms integrate the activities they perform within each different business-level strategy demonstrates how they differ from one another.

When selecting a business-level strategy, firms evaluate two types of potential competitive advantage: *“lower cost than rivals, or the ability to differentiate and command a premium price that exceeds the extra cost of doing so”*. Having lower cost derives from the firm’s ability to perform activities differently than rivals; being able to differentiate indicates the firm’s capacity to perform different (and valuable) activities. Thus, based on the nature and quality of its internal resources, capabilities, and core competencies, a firm seeks to form either a cost competitive advantage or a uniqueness competitive advantage as the basis for implementing its business-level strategy.

Two types of competitive scopes are broad target and narrow target. Firms serving a broad target market seek to use their competitive advantage on an industry-wide basis. A narrow competitive scope means that the firm intends to serve the needs of a narrow target customer group. With focused strategies, the firm *“select a segment or group of segments in the industry and tailors its strategy to serving them to the exclusion of others”*. Buyers with special needs and buyers located in specific geographic regions are examples of narrow target customer group. As shown in Figure, a firm could also strive to develop a combined cost/uniqueness competitive advantage as the foundation for serving a target customer group that is larger than a narrow segment but not as comprehensive as a broad customer group. In this instance, the firm uses the integrated cost leadership/differentiation strategy.

None of the four business-level strategies shown in the picture is inherently or universally superior to the others. The effectiveness of each strategy is contingent both on the opportunities and threats in a firm’s external environment and on the strengths and weaknesses derived from the firm’s resource portfolio. It is critical, therefore, for the firm to select a business-level strategy that is based on a match between the opportunities and the threats in its external environment and the strengths of its internal organization as shown by its core competencies.

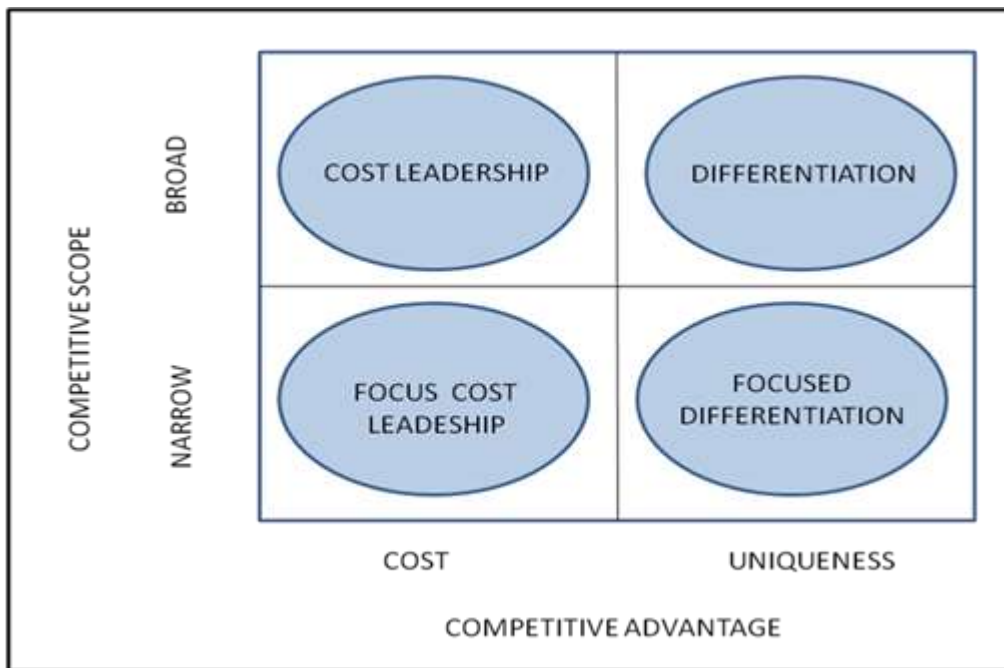


Figure 8 The Porter strategy

Cost leadership strategy

The cost leadership strategy is an integrated set of actions taken to produce goods or services with features that are acceptable to customers at the lowest cost, relative to that of competitors. Firms using the cost leadership strategy commonly sell standardized goods or services (but with competitive levels of differentiation) to the industry's most typical customers. Process innovations, which are newly designed production and distribution methods and techniques that allow the firm to operate more efficiently, are critical to successful use of the cost leadership strategy. Cost leader's goods or services must have competitive levels of differentiation that create value for customers.

This category of strategy seeks to improve efficiency and control costs throughout the organization's supply chain. It is pursued by organizations which strive to be the lowest cost producers in an industry, through approaches such as economies of scale of production, learning curve effects, tight cost control, and cost minimization in areas, for example, R&D, services, sales force, or advertising (Porter 1998b:35). They

compete with each other in areas such as process technology, raw material input costs and capacity utilization. Organizations that operate in this category usually sell a standard product (Picot and Scheuble 2000:242). While cost leaders may be the cheapest producers in their market, they cannot ignore the basis of differentiation. If the consumer perceives that the leader's product is not comparable to its competitors then a cost leader may be forced to discount its price even further to ensure the sale. The main risk for organizations that decide to compete in this category is that there can only be one cost leader and competition can intensify, leading to a price war where no one wins (Porter 1998b:45).

With this strategy, the objective is to become the lowest-cost producer in the industry. Many (perhaps all) market segments in the industry are supplied with the emphasis placed minimizing costs. If the achieved selling price can at least equal (or near) the average for the market, then the lowest-cost producer will (in theory) enjoy the best profits. This strategy is usually associated with large-scale businesses offering "standard" products with relatively little differentiation that are perfectly acceptable to the majority of customers. Occasionally, a low-cost leader will also discount its product to maximize sales, particularly if it has a significant cost advantage over the competition and, in doing so, it can further increase its market share.

The cost advantage also represents an effective defense against the five competitive forces:

- with respect to competitors the company can better resist a possible price war, being able to make a profit even at a price level that competition is the minimum practicable;
- customers, however strong, cannot drive down the price below that charged by the competitor who has the best position;
- low costs defend the company by increases imposed by suppliers;
- Finally, the low costs are also a barrier against the entry of any new competitors and a good protection against substitute products.

In general, an advantage of cost protects companies against five competitive forces because they are less efficient than its rivals suffer the first shots of the competitive struggle.

Differentiation Strategy

The differentiation strategy is an integrated set of actions taken to produce goods or service (at an acceptable cost) that customers perceive as being different in ways that are important to them.

While cost leaders serve a typical customer in an industry, differentiators target customers for whom value is created by the manner in which the firm's products differ from those produced and marketed by competitors. Product innovation, which is "the result of bringing to life a new way to solve the customer's problem – through a new product or service development – that benefits both the customer and the sponsoring company" is critical to successful use of the differentiation strategy. Firms must be able to produce differentiated products at competitive costs to reduce upward pressure on the price that customers pay. When a product's differentiated features are produced at noncompetitive costs, the price for the product can exceed what the firms target customers are willing to pay. When the firm has a thorough understanding of what its target customers value, the relative importance they attach to the satisfaction of different needs, and for what they are willing to pay a premium, the differentiation strategy can be effective in helping it earn above-average returns. Through the differentiation strategy, the firm produces nonstandardized (that is unique) products for customers who value differentiated features more than they value low cost.

According to this strategy the company seeks to differentiate itself from its rivals by achieving a degree of uniqueness that is valued by many customer segments. The company can charge a price premium, where the premium achieved is more than the costs incurred, leading to higher than average margins. Organizations that pursue this strategy design their products to possess one or a number of the attributes which are of value to the customer and which make their products "stand out" from their

competitors. Characteristics that are common for organizations operating in this category are that they have higher than average profit margin due to being unique in the market and will continuously be updating their products to ensure that they are in touch with the needs of their customers.

This category differs from the cost leader category, since there can be more than one successful differentiation strategy within a market if there are a number of attributes that are widely valued by the buyer. Organizations have succeeded in differentiating their products through improving quality, better after-sales services and more reliable delivery as well as through increasing the functionality (Porter 1998b:38). The majority of organizations chose to operate within this category.

Improves the position of the differentiation against five competitive forces, such as cost leadership, but it does so different because:

- compared with direct competitors, differentiation reduces substitutability product, customer loyalty increases, decreases sensitivity to price;
- increased customer loyalty due to the entry of new competitors becomes more difficult;
- the higher margin increases the firm's ability to absorb increases imposed by any supplier with strong bargaining power;
- the distinctive features of the product and customer loyalty also constitute a defense against substitute products.

Focus/Niche Strategy

The focus strategy is an integrated set of actions taken to produced goods or services that serve the needs of a particular competitive segment. Thus, firm use a focus strategy when they utilize their core competencies to serve the needs of a particular industry segment or niche to the exclusion of others. Examples of specific market segments that can be targeted by a focus strategy include (1) a particular buyer group (e.g., youths or senior citizen), (2) a different segment of a product line (e.g., products

for professional painters or the do-it-yourself group), (3) a different geographic market (e.g., northern or southern Italy).

In the focus strategy, a business aims to differentiate within just one or a small number of target market segments. The special customer needs of the segment mean that there are opportunities to provide products that are clearly different from competitors who may be targeting a broader group of customers. The important issue for any business adopting this strategy is to ensure that customers really do have different needs and wants - in other words that there is a valid basis for differentiation - and that existing competitor products are not meeting those needs and wants.

Here a business seeks a lower-cost advantage in just one or a small number of market segments. The product will be basic - perhaps a similar product to the higher-priced and featured market leader, but acceptable to sufficient consumers. Such products are often called "me-too's".

The focus strategy concentrates on a narrowly defined segment of the market (market niche), and attempts to make its organization the market leader within this niche (Porter 1998a:15).

The segment may be a particular group of customers, a specific geographic area, or a certain part of the product or service line (Rowe et al. 1989:156). The rationale is that by specialization the organization can serve the market segment more effectively than can competitors who attempt to cover the entire market (Dess and Miller 1994:68). The focus strategy still relies on a cost leadership or a differentiation strategy, or perhaps both, to establish a strong position within the particular market segment, or niche.

The differentiation within a focus strategy can occur by exploiting differences in the special needs or wants of a buyer in a specific market segment and tailoring products to the specialized needs of the market segment. In cost focus strategy, the organization strives to exploit differences in cost behavior of specific market segments. It can be based on finding a distinct group of customers whose needs are slightly below average. Costs are saved by meeting their needs specifically and avoiding unnecessary

additional costs (Thompson 1993:216). Organizations in this category have adopted the opinion that "It is better to be a big fish in a small pond, rather than a minor swimming with whales". Some risks of focus strategies include imitation and changes in the target segments. Furthermore, the success will encourage other organizations into the market niche. This increases competition and tightens margins since the market available is not large enough to be financially viable (Porter 1998b:46). Finally, other focusers may be able to carve out sub-segments that they can serve even better.

This strategy may involve both the acquisition of the variation is cost advantage, or both, simultaneously, provided only to the segment on which the firm concentrates its efforts. In particular:

- through a strategy of focusing on the costs the company is seeking efficiency higher than that of competitors exploiting economies of scale that may have been overlooked by larger competitors size;
- through a strategy of focusing the company on the differentiation exploits the specific needs of the segment by differentiating the product or service from competitors who may have chosen to serve in the strategy wider group of customers. This strategy is successful if the needs of targets chosen are significantly different than those of broader market.

3.2 Pillar 1: Cost driver analysis

Accountants usually define cost as a resource consumed or foregone that give up opportunity to achieve a specific objective. It is usually measured as the monetary amount that must be paid to acquire goods and services⁴⁷. All costs incurred by an organization result from activities that are pursued by the organization. "Know your organization's costs" is an essential theme for any manager. Thus, cost concepts are applicable only if they influence a decision, and cost data are relevant only if they are useful to a cost concept. It is well known in an industry that a company can manage

⁴⁷ (Horngren et al. 2000:28)

what it can measure. Unfortunately, some companies may not identify their costs precisely; determining how costs behave and best cost structure. Managers need to understand how costs behave and what cost structure is to make informed decisions about products, processes, and resources, to plan, and to evaluate performance.

What does it mean to say an organization understands its costs? It means that the organization's managers can predict, with some clarity, how costs will respond to management's actions. In other words, it means managers can predict how cost will change, if at all, when they direct the organization to do something differently than it is being done today. To say an organization understands its costs implies that managers understand the underlying cause-and-effect relationship between the work of the organization and the costs of the organization.

Cost drivers is a characteristic of an activity or event that causes that activity or event to incur costs and can be more or less under a firm's control. In other words, factors that causally affect costs (over a given time span) are called cost drivers. That is, a cause-and-effect relationship exists between a change in the level of activity and a change in the level of the total costs of that cost object.

Some companies, especially those following the cost leadership strategy, use cost management to maintain or improve their competitive position. Cost management requires a good understanding of how the total cost of an object changes as the cost drivers change. It is well-recognized now that costs are driven not only by output volume and its related measures such as direct labor hours or machine hours, but also by non-volume related output variables that result from the diversity of company's product lines and complexity of its production process. That is why many companies have transformed their traditional cost management systems into, for example, activity-based cost management systems. In addition, in today's competitive business environment, to achieve a major cost advantage, an organization must focus not only on traditional cost drivers but also on strategic cost drivers. Strategic cost drivers determine the long-run cost position of a company. They explain the differences that exist in unit costs across companies of the same industry. For example, economies of scale will give larger companies a major strategic cost advantage. Technology affects the way activities are

performed and the mix of resources (materials, machinery, and human resources) that are used to carry out those activities. Technology determines the competitive advantage of a company if it has a significant role in determining the relative cost or differentiation position.

Cost drivers – strategic views

The new conditions of the business environment caused the considerable changes in the cost structures of companies in the last third of the 20th century. These changes have resulted in higher overhead rates; investment in machinery and services has reduced direct labor costs and simultaneously increased overhead costs. These transactions engage exchanges of the materials and/or information necessary to move production along but not directly result in physical products. Rather, these transactions are responsible for aspects of the "bundle of goods" that customers purchase - such aspects as on-time delivery, quality, variety, and improved design⁴⁸. Therefore, there are different cost drivers, which stem not only from the production transactions but also from other transactions of the company.

There have been some significant changes in the life-cycle costs, adding together at cost structure change. Upstream costs (such as design and development) and downstream costs (such as marketing, selling, distribution and servicing) have become important parts of the total lifecycle costs of the product. Thus, the firm's cost position is frequently affected by activities that are performed within its value chain and activities with the value chains of suppliers and customers. Therefore, it is important to identify and analyze cost drivers across the entire value chain.

In this context, Porter introduced his system of cost drivers to exceed the strong production orientation of the traditional views of cost drivers.

Porter concentrates on the strategic level, he emphasized that the value activities the firm performs in opposing in an industry consequence in the performance of a company's costs and its relative cost position and he used the value chain as a basic idea

⁴⁸ (Miller and Vollman 1985:144).

in his considerations about cost drivers. Consequently, cost advantage results if the company obtains a lower cumulative cost of performing value activities than its competitors. The performance of a company's costs and its relative cost position depend on a number of structural factors that influence cost. Porter has identified several major factors that affect costs. The cost drivers that Porter has identified are briefly reviewed below.

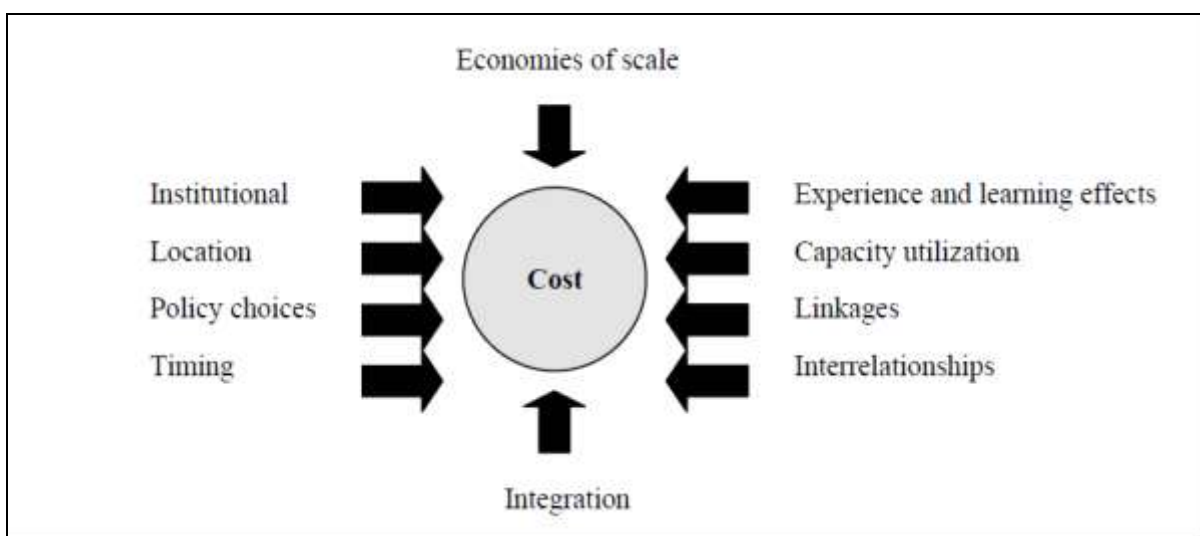


Figure 9 Cost drivers according to Porter

A) Economies of scale

They are maybe an effective cost driver in many industries. The costs of the activities are frequently affected by economies or diseconomies of scale. Porter stated that scale economies happen from some principal sources. Economies of scale can trunk from efficiencies in the actual operation of an activity at higher scale as well as from less than proportional increases in the overhead needed to support an activity as it grows. There are, however, limits to scale economies, for example, size can bring with it added complexity, which itself can lead to diseconomies. In some cases, a company may be reluctance to fully exploit economies of scale because of product differentiation; where customer preferences are differentiated, firms may find that the price premium of

targeting a single segment with a differentiated product outweighs the higher cost of small volume production. In addition, economies of scale can lead to inflexibility; scale efficient production is likely to involve highly specialized labor and equipment, which tends to be inflexible. In a dynamic environment, very large firms may have greater difficulties than smaller units in adjusting to fluctuations in demand and changes in technology, input prices, and customer preferences. The scale sensitivity of activities is different, for example, R&D activities, national advertising activities, and infrastructure activities of the firm are typically more scale-sensitive than activities such as procurement and sales force operations because their costs are heavily fixed no matter what the firm's scale is⁴⁹. However, economies (and diseconomies) of scale can be found to some extent in every value activity of a company such as purchasing, R&D, and advertising.

Economies of scale are the possibility to carry out, because of the larger size of the company, some activities that generate value with:

- Lower costs, thereby resulting in a cost advantage;
- Greater differentiation than its competitors, thereby obtaining an advantage of differentiation.

Cost advantages in economies of scale

The economies of scale can give rise to cost advantages such as:

- - Possibility to recoup research costs of higher production volumes (only the large international pharmaceutical companies can afford to do a research drug);
- - Possibility to amortize the cost of advertising on higher sales volumes (only companies operating throughout the country can afford to advertise on national TV channels);
- - Lower proportion of fixed costs.

⁴⁹ Porter 1998a:71

Advantages of differentiation in the economies of scale

Economies of scale can also give rise to advantages of differentiation when they allow to perform tasks that, in the case of small size, they could not play. So, for example, only large companies car rental (Hertz, Maggiore, Avis, etc..) May allow the return of the car rented in any city in the country, thanks to a network is very comprehensive. The same service delivery cannot be made by many other car rental firms smaller.

The same example can apply to shipping companies, thanks to a higher dimension can make shipments all over the country.

The sustainability of competitive advantages in economies of scale

Economies of scale will highly sustainable competitive advantage over time, as the time to switch from medium to large in size, from domestic and global markets, are very long. Therefore, the economy of scale represents a high barrier to entry for companies if they want to enter the industry, have to absorb or long or high costs to achieve optimal dimensions of scale.

A strategy to quickly create, over time, economies of scale, is represented by the acquisition or mergers with other companies in the same sector, resulting in very high costs.

B) Experience and learning effects

Further cost reductions may be achieved through learning and experience effects. Porter used the term learning to compass all types of cost reduction that result from improving know-how and procedures independent of scale. However, learning refers to increase in efficiency that is possible at a given level of scale through having performed the necessary tasks many times before. Was in the 1960s that Boston Consulting Group extended the recognized production learning curve further than manufacturing and looked at increased efficiency that was possible in marketing, advertising and selling and other aspect of the business, through experience. This judgment suggests that companies with larger market share will, by definition, have a

cost advantage through experience, assuming all companies are operating on the same experience curve. The experience curve as an explanation of costs has come under increasing scrutiny recently. However, the principal font of experience-based cost reduction is learning by personnel and activities, because it can reduce cost over time by many systematic ways. Learning occurs both at the individuals level and at the activities level, thus, the measures of learning are different. Porter stated that a suitable measure of learning expresses the systematic ways of learning that explain the fall in costs over the time in a value activity.

Finally, Porter indicated that the popular measure of the rate of learning is cumulative firm volume - it has many benefits, however, it hides other rates of learning in value activity and is not a suitable representative of the learning in many activities of the company. Thus, understanding the systematic ways of learning in each activity and identifying the best measure of learning rate may be necessary for a firm to achieve cost reductions through learning.

Learning is the ability to play, thanks to a better knowledge of the business, some activities that generate value with:

- Lower costs, thereby resulting in a cost advantage;
- Greater differentiation than its competitors, thereby obtaining an advantage of differentiation.

A definition of learning is not easy, but some rules, generally applicable, may be mentioned, such as:

→ Learning is often made up of many small improvements;

→ Learning has a relapse rate, or may give rise to advantages of cost and differentiation, very variable, in relation:

- the industry in which the entity operates (for example, is very high in consulting firms, to be lower in manufacturing);
- generating activities of value (for example, is very high in research and development, to be lower in the marketing and sales);

Cost advantages resulting from learning

Learning can help you get easily demonstrable cost advantages when introducing innovations. Thus, for example, a change in the organizational structures or in the planning of production, or in the design of the products, in the initial phase hardly allows cost reductions. Only later, after the staff has learned of the innovative changes, it is possible to achieve lower costs.

Advantages of differentiation resulting from learning

Learning allows you to realize the benefits of differentiation only if you can maintain exclusivity over its competitors. This exclusivity can be obtained in various ways such as, for example:

- The protection of know-how through patents;
- Customization of plant and equipment purchased from outside, with modifications within the company;
- The residence of the employees in the company with a high learning;
- Introduction of confidentiality clauses in employment contracts in order to avoid leaks, and possibly control of the publications of the employees.

How to increase the learning:

Learning can be increased by a careful analysis of competitors, giving up forms of pride to presumptions of superiority. The competitor analysis in order to improve learning can take place via:

- Improving the value chain of competitors;
- Removal of individual components of the product competitors (reverse engineering);
- Analysis of patents by competitors;
- Interviews with suppliers.

Sustainability of learning

The competitive advantages that result from learning are usually quite sustainable in time, to the extent that can be prevented leakage of know-how.

C) Capacity utilization

It has captured considerable attention in the literature. Determining the right level of capacity is one of the most challenging tasks facing managers. Capacity utilization has been shown to have a major impact on unit cost. Over the short and medium term, plant capacity is more or less fixed, and variations in output are associated with variations in capacity utilization. During periods of low demand, plant capacity is underutilized, this raises unit costs because fixed costs must be spread over fewer units of production. On the other hand, during periods of peak demand, output may be pushed beyond the normal full-capacity operation. In this case, the unit costs may increase due to overtime pay, premiums for night and weekend shifts, increased defects, and higher maintenance costs. Therefore, Porter argued that capacity utilization at a certain point in time is a function of seasonal, cyclical and other demand or supply fluctuations, which have no influence on the competitive position of a company, and rather capacity utilization over the entire cycle is the correct cost driver. Finally, capacity utilization as cost driver is conditional on environmental conditions and competitor behavior especially competitor investment behavior and on the other hand on the company itself through principal decisions in areas such as marketing and product selection.

The model of the production capacity utilization should not be confused with the degree of capacity utilization, because the production capacities can be used with different modes that allow the maximum exploitation, regardless of the average level of utilization. So, for example, if you take into consideration the sales force, the model of capacity utilization in the choice between commission paid to agents and sellers salaried.

The choice of the seller's employees, in the case of new products, new areas of sales, will increase the revenue per capita, provided the cost of the seller, so you are using the best resource Seller's employees, as it increases its profitability; If I Had chosen a sales network represented by agents paid on commission, any increase in sales volumes, the range of products, the sales region do not result in greater profitability, as the cost of the agent is usually proportional to the turnover.

Competitive Advantages in the model of capacity utilization

The model of the production capacity utilization almost always involves cost benefits and advantages of differentiation resulting from the possibility to produce and sell for maximizing the production capacity and reducing downtime in production. The strategies implemented to achieve these benefits are different in nature and below we remember those who have been most successful:

- Lower prices during the low season, in order to maintain production levels or dispose of stocks.
- Special promotions balances during periods of crisis or out of season;
- Decentralization of machining contractors for excess demand;
- Looking for customers with a stable demand or cyclical than seasonal demand;
- Sale of competitors to fluctuating market segments that prevent exploitation of the productive capacities and subsequent withdrawal from market segments;
- Acquisition of subsidiaries in other countries with needs cyclically as opposed.

Sustainability of the model of capacity utilization

The many ideas to use productive capacity, while being very innovative, however, are always quickly receivable from external competitors, and then easily imitated. For this reason, the sustainability of the model of the production capacity utilization is very low.

D) Linkages

A further set of cost drivers are linkages. No function or activity can be fully understood on its own; nor can costs be evaluated in such isolation. The cost incurred by most activities is significantly affected by those activities that link with it. Porter described two types of linkages; internal linkages among the activities of value chain and external linkages with suppliers and channels. Internal linkages concern the activities of value chain that have an effect on the costs. These linkages exist between direct and indirect activities, They occur also between alternative activities that achieve the target objectives such as advertising and direct sales. Porter explained that changing the way of performing one of the linked activities may not only has an impact on the cost of another activity but also has an impact on the total cost of the linked activities. This requires coordination and optimization of linked activities. Better coordination of linked activities.

Linkages exist not only among value chain activities but also between a firm's activities, suppliers, and channels. External linkages with suppliers of factors inputs or distributors of the firm's final products can affect the costs of a firm's activities. For example, frequent supplier shipments can reduce a firm's inventory needs, appropriate packaging of supplier products can lower handling cost, and supplier inspection can remove the need for incoming inspection.

As with internal linkages, Porter stated that external linkages with suppliers and channels can lower cost or enhance differentiation by improving coordination and joint optimization between a firm's activities and the value chains of suppliers and channels.

The value chain can be analyzed within the company through value-generating activities, or outside the company, under the different links in the value chain, represented by the suppliers, the sales channels, customers. Therefore, it is possible to identify the determinants of costs and determinants of differentiation in both internal links in the value chain, is in the connections with the outer rings of the value chain, so called 'vertical connections.

Internal Connections

It can achieve cost benefits by increasing the costs of a value-generating activities, in order to reduce to an extent more than proportional costs of another activity generating value; for example, increasing the costs of control and testing activities in the production , we reduce the costs of external defects in the technical assistance given to customer service. You can also get the benefits of differentiation by seeking closer and faster connections in the value chain, so, for example, you may have delivery times quicker than the competitors by acting upstream of the process of outbound logistics, management orders more timely and more frequent visits to customers by the sellers to acquire orders.

Connections vertical

You can have cost advantages with better connections with the outer rings of the value chain. So, for example, may have higher purchase costs of raw materials by imposing a system of quality control at the supplier and eliminating the costs of inspection and testing of raw materials within the company. You can also have advantages of differentiation with the outer rings of the value chain with improved liaison with suppliers, for example, by requiring the supplier to an exclusive supply. In addition, the best connections with the sales channels (retailers, distributors) could lead to joint promotional actions, better training of staff working in the sales channels, a partnership investment business (advertising, hiring vendors, vehicles, etc..) carried by the channels.

Sustainability of links

The sustainability of the competitive advantages of the links both internal and vertical, is remarkably high, because:

- For internal connections between the value generating activities is difficult to detect by competitors;
- For vertical linkages with suppliers and customers, time and organizational efforts for the implementation and management are very high.

E) Interrelationships

The relationships of mutual dependence between one business and other parts of a company's operations affect costs. Porter stated that the most important type of possible interrelationships among business units is tangible interrelationships; arising from opportunities to share activities in the value chain among related business units due to the presence of common suppliers, customers, technologies, and other factors. Business units that can share a sales force.

Another type of interrelationship, he termed intangible interrelationships; involving the transference of generic skills or know-how to similar but separate value activities in many business (e.g. using cost reduction expertise gained in one division may lower cost in others). The third type of interrelationships, sharing know-how between separate activities. This form of interrelationships can affect the costs if the activities are similar and if the know-how is significant to improving the efficiency of the activity. In this case sharing the generic skill represents transferring the successful results of learning from one activity to another. In summary, interrelationships with other strategic business units in the overall corporate portfolio can help to share experience and gain economies of scale in functional activities, such as marketing, research and development, quality control, ordering and purchasing.

Businesses can frequently reduce their costs if they share them with other business units. They can sometimes achieve the same effect by transferring knowledge within the group to other strategic business units who share similar technology or problems. Awareness of this potential means of reducing costs might influence a firm's decisions.

The interrelationships differ from the links since they assume that, within the company, there are many businesses that use the same value generating activities. In this case you have a competitive advantage against competitors monobusiness or with a smaller number of business. The sustainability of this competitive advantage is high because the time to build multi-business activities are very long.

F) Degree of integration

Vertical integration involves ownership or control of inputs to the firm's processes or the channels of product distribution. When a firm tries to gain ownership or control of its inputs called "backward integration" or its outputs called "forward integration". Degree of vertical integration in a value activity can influence its cost.

Decisions on integration, e.g. contracting out delivery and/or service, also affect costs. Similarly, the decision to make or buy components can have major cost implications. Therefore, integration can affect costs through many ways, for example, forward integration gives a firm control over sales and distribution channels, which can help in avoiding costs of using market, such as procurement and transportation costs. Backward integration gives a firm more control over cost, availability, and quality of the raw materials that go into its present products or services, thus, a firm can avoid suppliers with considerable bargaining power. In addition, some companies use integration in hopes of benefiting from the economies of scale - they result in lower overall costs and thus increased profits.

However, companies should be cautious when adopt vertical integration because it can raise costs, for example, through creating inflexibility, bringing activities in-house that suppliers can perform more cheaply, and undermining incentives for efficiency because the relationship with the supplying unit becomes captive. Porter argued that integration may lower cost, raise cost, or has no effect on cost – this depends on the activities and purchased inputs involved. A company should decide the potential benefits of integration and de-integration for each important activity.

G) Timing

During the last years, timing has gained more significance for the costs of value activity. Porter argued that the cost of a value activity often reflects timing. Timing, though not always controllable, can lead to cost advantages. There are a number of occasions when the "first mover" in an industry can gain significant cost advantages. If they move quickly into volume production, they may have influence on costs through

learning, scale, etc. However, the advantage does not always rest with the first mover. Sometimes there are significant advances in the technology or product design that a later entrant can exploit. The first mover may either be unwilling to spend heavily again so soon, or simply not have money to do so.

Thus, Porter emphasized that the role of timing in cost position of the company may depend on timing with respect to the business cycle or market conditions than on timing in absolute terms. Timing may lead to either sustainable cost advantage or a short-term cost advantage.

The time factor is the competitive advantage of both cost and differentiation, resulting from:

Be the first to go on the market

The advantages to be the first to go on the market can be summarized thus:

- Advantages of lower initial costs as suppliers have not yet understood the importance of the business;
- Access to preferred suppliers with any conditions of any party;
- Better geographical location (think of Benetton stores located in city centers);
- Acquisition of patents before the competition;
- The benefits of learning from the staff;
- Maintenance of the benefit over time through acquisition of major customers.

Do not be the first to leave a market.

The advantages not to be the first to go on the market can be summarized thus:

- Lower cost of launching and publicizing of novelty;
- Purchase of equipment at a later date, and probably the most modern;

- Knowledge of the value chain of the competitor and can mimic the positive aspects and avoid the negative ones;
- Use of younger staff, and probably less expensive or staff already prepared stealing competitors.

H) Polity choices

The cost of a value activity is always affected by policy choices a company makes - they may be influenced by other cost drivers. Many of the decisions taken within a company are based on discretionary policies. It is not easy to get these decisions right and it is often necessary to modify them in the light of their effects on cost and differentiation. They also need to be modified as the circumstances within which the strategic business unit operates evolve. The extent to which a company should, or should not adopt/maintain any of these policies needs to be considered carefully.

Policy choices have implications for costs, they also affect the actual and perceived uniqueness of the product to the customer. The general rules are to reduce costs on factors which will not significantly affect valued uniqueness, avoid frills if they do not serve to differentiate significantly, and invest in technology to achieve low-cost process automation and low-cost product design (fewer parts can make for easier and cheaper assembly). Although policy choices play an independent role in determining the cost of value activities, they also may be affected by other cost drivers. Thus, accountants should not ignore the impact of policy choices on the cost in cost analysis. Also, a company should make a detailed examination of each activity to identify and recognize the extent to which the explicit and implicit policy choices determine the cost.

I) Location and institutional factors

The final two cost drivers identified by Porter in his plan are location and institutional factors. The first one that can affect its cost is the geographic location of a value activity. It can stem from many factors and may be treated as a separate cost

drivers. Location has always been an important factors in costs, it can affect costs through many ways, like the cost of labor or tax rates. In addition location has an important influence on logistical cost. Thus, it is also necessary to identify the impact of location on the cost and recognize opportunities for reducing costs by establishing new patterns of location of facilities relative to each other. The second one, institutional factors such as the regulations imposed by the government, that can have important effects on a firm's ability to produce economically.

There are many ways in which a company can look for reduce costs. In trying to became a cost leader in an industry, first, a company should be conscious that there can only be one cost leader, and second, that there are many ways in which this position can be attacked (for example using different cost drivers).

Cost advantages can be between the most difficult to sustain and defend in front of heavy and determined competition. Porter argue that most of the factors listed above as cost drivers could also be used as "uniqueness drivers" if the firm is seeking to differentiate itself from its competitors.

Porter draws attention to the fact that the cost behavior of a value activity may be influenced by many cost drivers. While one cost driver may have the great impact on the cost of a value activity, there are several drivers often interact to determine the cost. Thus, a company must try to quantify the relationship between cost drivers and the cost of a value activity. For example, a company should estimate for each activity the slope of the scale or learning curve, the policy choices that have the greatest impact on cost, the cost advantage or disadvantage of timing, and so on for each driver. Although the process of quantification of cost drivers is difficult, it is necessary to determine the relative significance of each cost driver. In addition, it can help a company to estimate its relative cost position in comparison with competitors.

Porter argued that there are interaction relationships between cost drivers. On the one hand, cost drivers may reinforce each other in influencing cost. The list of cost drivers by Porter has made an important contribution to the research of the cost drivers, he has presented one attempt to create a comprehensive list of cost drivers particularly long-term drivers through using the value chain as a basic idea.

Despite that fact, some cost drivers in his list represent strongly aggregated drivers such as policy choices and another subdivision such as location. In addition, Porter explained functional connections between cost drivers and the costs as well as the mutual interdependence among cost drivers as a general theme. Altogether, the list of cost drivers by Porter is a landmark and a useful for further works about cost drivers. Thus, Shank and Govindarajan evaluated the attempt of Porter asserting that Porter attempted to create a comprehensive list of cost drivers but his attempt is more important than his list. They emphasized that in strategic management literature better lists exist such as Riley. Thus, the list of cost drivers by Shank and Govindarajan (1993) is discussed below.

Shank and Govindarajan (1993:151) emphasized that the notion of cost is driven by volume has no strategic significance. If a company in some way can double its throughput, can it achieve cost advantage? There are too many instances of companies in which average cost goes up, not down, as volume grows. Also, if the output volume is the necessary answer to cost leadership, some companies may encounter some difficulties in competing against other companies. In addition, bigger size may not mean lower cost, in some industries, for example, the processed pasta business, and milk-processing industry, some companies dominated the market through small regional plants. But if the volume is an uninteresting answer to the question of what drives costs and has no strategic significance, what cost drivers are more useful in a strategic sense to explain cost position of the firm.

Within this context, Shank and Govindarajan (1993) presented their list of cost drivers. In their work, they argued that the basic concept of strategic cost drivers is to get away from the notion that volume drives cost. In strategic cost management, cost is caused by a multitude of factors that are related to each other in complex ways. Identifying and analyzing these factors mean best explaining the changing relationship between these factors and costs over time and therefore understanding the cost behavior and cost structure of a company. Shank and Govindarajan (1993) focused on the concept of cost drivers after Riley (1987). They broke the list of cost drivers into two categories.

The first category is called "structural" cost drivers are relate to business strategic choices about an organization's underlying economic structure, and deals with the following strategic choices:

- Scale: How big an investment to make in facilities for research and development, manufacturing and marketing?
- Scope: Degree of vertical integration. Horizontal integration is related to scale.
- Experience: How many times in the past, the firm has already done what it is doing now?
- Technology: What process technologies are used at each step of the firm value chain? (State of the Art).
- Complexity: How wide a line of products or services to offer to the customers.

Each structural driver involves choices by the firm that drive product cost. Over the years, economists and strategists focused their attention to some of these structural drivers such as economies of scale, and experience and learning effects. Shank and Govindarajan emphasized that only experience and learning effects on the cost have drawn much interest from management accountants. In addition, complexity, as a structural variable, has received the most attention among accountants recently.

Structural cost drivers	Executional cost drivers
<ul style="list-style-type: none"> • Scale of investment in capacity • Degree of vertical integration • Experience • Technology: process technology employed • Complexity: breadth of product line 	<ul style="list-style-type: none"> • Workforce involvement • Total quality management • Utilization of capacity • Product design • Exploitation of external linkages • Plant layout efficiency

Figure 10 List of cost drivers according to Shank and Govindarajan (1993:20)

The second category of cost drivers is called "executional" cost drivers, are relate to the execution of the business activities, and that constitute determinants of a successful cost position. The most important executional cost drivers include:

- Workforce involvement (participation) - work force commitment to continuous improvement.
- Total quality management (beliefs and achievement regarding product and process quality).
- Capacity utilization (given the scale choice on plant location).
- Plant layout efficiency (how efficient against current norms, is the plant layout?).
- Product configuration (is the design or formulation effective?).
- Exploiting linkages with suppliers and /or customers, in the firm's value chain.

Executional cost drivers are determinants of a firm's cost position that hinge on its ability to execute successfully. They are linked to efficiency and the more cost drivers identified the more likely it is to improve satisfaction. In contrast, the structural cost drivers have no direct linkage with efficiency and the number of cost drivers identified does not demonstrate a link to improving satisfaction.

For each of the structural drivers, more is not always better (Shank and Govindarajan 1993:21). For example, there are diseconomies of scale, or scope, as well as economies. A more complex product line is not necessarily better or worse than a less complex line. In addition, too much experience can be as bad as too little in a dynamic environment. The insights from analysis based on structural drivers are too often old fashioned and while the consultant who performs a strategic cost analysis is gradually directing his attention on the executional cost drivers, the accountant from his side is still grasping the structural cost drivers (Shank and Govindarajan, 1993:22).

The structural and executional activities determine the nature and number of the daily activities performed in the company. If a company decides to manufacture more than one product at a plant, this structural choice will produce a need for scheduling, a product-level activity. Similarly, providing a plant layout defines the nature and extent of the materials handling activity. Although organizational activities determine operational activities, analysis of operational activities and cost drivers can be used to suggest strategic choices of organizational activities and cost drivers. For instance, the number of material moves as a measure of the materials moving activity by individual products suggests that resource spending can be reduced if the plant layout is redesigned to reduce the number of moves required.

Examples of some structural and executional activities with cost drivers are listed by category in Table below.

STRUCTURAL ACTIVITIES	STRUCTURAL COST DRIVERS
Plant Construction	Number of plants, scale, degree of work centralization
Employee Grouping	Number and type of work units
Complexity	Number of product lines, number of unique processes, number of unique parts, degree of complexity
Process selection and use	Types of process, experience of usage
EXECUTIONAL ACTIVITIES	EXECUTIONAL COST DRIVERS
Employee utilization	Degree of involvement
Quality service provision	Quality management approach
Operation of plan layout	Plant layout efficiency
Product design and manufacturing	Product configuratio

Table 8 Organizational activities and cost drivers

As illustrated in Table, a company activity can commonly be driven by more than one cost driver. For instance, the number of plants, scale and degree of

centralization all affect the cost of plant construction. Companies that have a commitment to a high degree of centralization may build larger plants, so that there are more physical concentration and more control. Similarly, complexity may be driven by the number of different products, number of specific processes and number of specific parts. Organizational drivers are factors that affect a company's long-term cost structure. This is understood by considering the various drivers shown in Table.

The structural drivers are the drivers of scale, scope, experience and complexity. For instance, economies and diseconomies of scale are well-known economic phenomena. An interesting characteristic of structural cost drivers is that more is not always better. Moreover, the efficiency level of a structural cost driver can change. For instance, changes in technology can affect the scale driver by changing the optimal size of a plant. In the baking industry, baking technology has eliminated economies of scale (in the form of mass baking) as a competitive advantage. Much smaller scale plants can now achieve the same level of efficiency once produced only by larger baking factories. Use of a nearby bakery is common in local districts.

Of more recent interest and emphasis are executional drivers. Considerable managerial effort is now exercised to improving how things are done in a company. Continuous improvement and its various dimensions (employee empowerment, total quality management, process value analysis, life-cycle assessment, etc.) are what executional efficiency is about. Staff costs decrease as the degree of employee involvement and empowerment increases. Employee involvement relates to a broader area of organizational culture, degree of participation, and commitment to the objective of continuous improvement.

Shank and Govindarajan (1993:22) emphasized that there is no clear agreement on the list of fundamental cost drivers. There are many studies that discussed different lists of cost drivers.

Whatever cost drivers on the list, the key ideas are as follows:

- For strategic cost management output volume is usually not the most useful factor or driver to understand the cause-and-effect relationship between cost and behavior or to explain the cost behavior.
- In a strategic sense, it is more useful to examine the structural and procedural activities and their cost drivers that may explain a cost position and shape the firm's competitive position.
- A company should be fully aware that cost drivers are not equally important all the time, but some are very probably very important in many cases.
- For each cost driver, there is a particular cost analysis framework that is critical to the understanding the positioning of the firm. Being a well-trained cost analyst is not enough; he or she requires knowledge of each framework.

Summarizing, the consideration of Shank and Govindarajan was to create a list of cost drivers. Their list of cost drivers includes only two categories: structural cost drivers and executional cost drivers and gives not enough attention to operational cost drivers as also in the list of cost drivers by Porter. Also, they neglected, as well as Porter study of the interdependence between the individual drivers. The effect of the cost drivers on the costs is only described through structural activities in the work of Porter and through structural and executional activities in the work of Shank and Govindarajan. Moreover, the list of Shank and Govindarajan lacks the aspect of timing, which was included by Porter and becomes more significant in a rapidly changing market with short life cycles and highly volatile demand.

3.3 Pillar 2: Strategic Positioning Analysis

Wondering how to analyze a company's strategic positioning? Here are a few tips to help you perform a strategic positioning analysis and identify which strategic position makes sense going forward.

Strategic positioning is similar to a high stakes chess game.

Strategic positioning is the positioning of an organization (unit) in the future, while taking into account the changing environment, plus the systematic realization of that positioning. The strategic positioning of an organization includes the devising of the desired future position of the organization on the basis of present and foreseeable developments, and the making of plans to realize that positioning. The strategic position methods is derived from the business world, the methods is aimed at ensuring the continuity of the organization. The strategy determinates the contents and the character of the organization's activities. Terms, such as survival, legitimacy, market positioning, relationship with environment and choice for a certain work area, come up in this context. Subject which have been developed reasonably well in literature on strategic management include: information collection techniques, analysis techniques and planning schemes. Not or hardly developed are methods for exploring the future.

The companies that dominate the marketplace are usually the ones that have planned to position themselves as a leader in a specific market segment or have risen to the fore by dominating a targeted value proposition. Strategic position analysis is vital for companies that are serious about remaining relevant with consumers. The methods for performing a strategic assessment vary, but there are several aspects that any strategic position audit simply can't ignore.

- Information collection (Internal and external) & and the Future
- Product performance: is a leading consideration in strategic positioning assessment. If your products are performing in a manner that is consistent with your strategic positioning, than you have done your job. But if your products are underperforming in your positioning category (e.g. price), then something is out of kilter and further analysis is required.
- Analysis: One can make an analysis of the strategic positioning by confronting the data of the internal and external research with each other.
- Core competencies: is your strategic positioning consistent with your company's core competencies? If your competencies have shifted, it's possible that your desired strategic position has become incompatible with

your business model and needs to be refocused to leverage the organization's business strengths.

- Choice of strategy: the positioning will be determinate.
- Resource allocation: strategic analysis must address the company's current resource allocation. It's particularly important to make sure your business's resource (people, equipments, supply, channels, etc) are capable of maintaining the position once you have secured it.
- Competitive & market pressures: external factors also play an important role in strategic position analysis. Competitive positioning and changing market conditions can dramatically affect the outcomes of your brand's strategic positioning efforts, even if your strategic position is already entrenched in the consumer consciousness.
- Implementation: the main thing of implementation is that, departing from the future positioning choice, theory is translated into what is to be done in order to realize that positioning.

To analyze the strategic positioning of a firm we can use different methods and analysis, in this research I chose to study the two principal: the SWOT ANALYSIS, and the PORTFOLIO APPROACH.

A) SWOT ANALYSIS

SWOT analysis is an analytical method, which is used to identify and categorize significant internal factors (i.e. strengths and weaknesses) and external factors (i.e. opportunities and threats) an organization faces.

SWOT analysis is an analytical method which is used to identify and categorize significant internal (Strengths and Weaknesses) and external (Opportunities and Threats) factors faced either in a particular arena, such as an organization, or a territory, such as a region, nation, or city.

It provides information that is helpful in matching the firms' resources and capabilities to the competitive environment in which it operates and is therefore an important contribution to the strategic planning process. It should not be viewed as a static method with emphasis solely on its output, but should be used as a dynamic part of the management and business development process.

SWOT analysis involves the collection and portrayal of information about internal and external factors that have, or may have, an impact on the evolution of an organization or business. It generally provides a list of an organization's Strengths and Weaknesses as indicated by an analysis of its resources and capabilities, plus a list of the Threats and Opportunities identified by an analysis of its environment. Strategic logic requires that the future pattern of actions to be taken should match strengths with opportunities ward off threats and seek to overcome weaknesses.

SWOT analysis is not necessarily a Foresight approach but can be a good starting point for the discussions in Foresight. Another possibility is matching your own strengths and weaknesses against different Foresight results. The different viewpoints can be a starting point for a discussion of the real threats and opportunities.

People directly involved in various hierarchical levels of decision making in an organization or business, or a wider sample of actors if the SWOT analysis concerns a whole region or nation. Representatives from a variety of stakeholders groups should be involved, as they would bring in the analysis their own particular perspectives. At least one expert in SWOT analysis should take part or moderate the process.

Drawing up Opportunity and Threat matrices encourages an assessment of the likely probability and impact any factor may have on the organization. A scoring system can be used to assign importance to factors. A factor with a high score on both 'probability of occurrence' and 'likely impact on the organization or business', would have to be one worthy of close attention and play a significant part in the development of a strategic plan. Similarly, Strengths and Weaknesses can be assessed against a scoring system that allows the factors to be identified according to their significance (i.e. major, minor, neutral) and level of importance (high, medium, low).

It is possible to represent this analysis in a Performance-Importance matrix that highlights those factors which are both important and in which performance of the organization/ business is low. It is towards these factors that strategy should be addressed. To be more specific, the set of questions that needs to be answered should be similar to the following:

Strengths

- What are your advantages?
- What do you do well?
- What relevant resources do you have access to?
- What do other people see as your strengths?

Consider this from your own point of view and from the point of view of the people you deal with. Don't be modest. Be realistic. If you are having any difficulty with this, try writing down a list of your organization's characteristics. Some of these will hopefully be strengths!

In looking at your strengths, think about them in relation to your competitors - for example, if all your competitors provide high quality products, then a high quality production process is not a strength in the market, it is a necessity.

Weaknesses

- What could you improve?
- What do you do badly?
- What should you avoid?

Again, consider this from an internal and external viewpoint: Do other people seem to perceive weaknesses that you do not see? Are your competitors doing any better than you? It is best to be realistic now, and face any unpleasant truths as soon as possible.

Opportunities

- Where are the good opportunities in front of you?

- What are the interesting trends you are aware of?

Useful opportunities can come from such things as:

- Changes in technology and markets on both a broad and narrow scale
- Changes in government policy related to your field
- Changes in social patterns, population profiles, lifestyles, etc.
- Local Events

A useful approach to looking at opportunities is to look at your strengths and ask yourself whether these open up any opportunities. Alternatively, look at your weaknesses and ask yourself whether you could open up opportunities by eliminating them.

Threats

- What obstacles do you face?
- What is your competition doing?
- Are the required specifications for your job, products or services changing?
- Is changing technology threatening your position?
- Do you have bad debt or cash-flow problems?
- Could any of your weaknesses seriously threaten your business?

<p>Strengths and Weaknesses</p>	<p>the internal environment: the situation inside the company or organization</p>	<p>for example, factors relating to products, pricing, costs, profitability, performance, quality, people, skills, adaptability, brands, services, reputation, processes, infrastructure, etc.</p>	<p>factors tend to be in the present</p>
<p>Opportunities and Threats</p>	<p>the external environment: the situation outside the company or organization</p>	<p>for example, factors relating to markets, sectors, audience, fashion, seasonality, trends, competition, economics, politics, society, culture, technology, environmental, media, law, etc.</p>	<p>factors tend to be in the future</p>

Table 9 Swot Analysis

Carrying out this analysis will often be illuminating - both in terms of pointing out what needs to be done, and in putting problems into perspective.

A SWOT analysis is based on hard facts. These can be time-consuming and costly to gather.

People are needed who have a good knowledge of the sector, region, area or country, etc. under analysis in the specific exercise. The main tangible output is a matrix presenting the most important strengths, weaknesses, opportunities and threats for the area, sector, region, country examined and aiming at giving a reasonable overview of major issues that can be taken into account when subsequently drawing up strategic plans for an organization.

The success of this method is mainly owed to its simplicity and its flexibility. Its implementation does not require technical knowledge and skills. SWOT analysis allows the synthesis and integration of various types of information which are generally known but still makes it possible to organize and synthesize recent information as well.

It is worth pointing out that whereas SWOT analysis is often not seen strictly speaking as a Foresight method, it is fruitful to consider it from this perspective. Indeed, Foresight is particularly useful for addressing the OT dimensions, whereas SWOT analyses often fail because of poor examination of OT (opportunities and threats).

A correlation is made between the internal factors, strengths and weaknesses of the organization, and the external factors, opportunities and threats. An effort can be made to exploit opportunities and overcome weaknesses and at the same time for the organization to protect itself from the threats of the external environment through the development of contingency plans.

The most common drawbacks of SWOT analysis are:

- The length of the lists of factors that have to be taken into account in the analysis;
- Lack of prioritization of factors, there being no requirement for their classification and evaluation;
- No suggestions for solving disagreements;
- No obligation to verify statements or aspects based on the data or the analysis;
- Analysis only at a single level (not multi-level analysis);

- No rational correlation with the implementation phases of the exercise.

Moreover, there are risks of:

- Inadequate definition of factors;
- Over-subjectivity in the generation of factors (compiler bias);
- The use of ambiguous and vague words and phrases

One has to be aware that this method is very commonly used by consulting firms and that for this reason some people in the public/quasi-public sector have an aversion to it.

A SWOT analysis could be performed in other contexts than those of an organization, for instance in the case of an individual facing major decisions such as professional orientation.

You should use SWOT analysis if:

- You need to identify the strengths and weaknesses of your organization, sector, area, region, country, etc;
- You need to identify what are the main threats and opportunities faced by your organization, sector, area, region, country, etc;
- You need to decide what are the most appropriate methods and tools to be used for the implementation of a foresight exercise.

SWOT analysis is a framework for analyzing your strengths and weaknesses, and the opportunities and threats you face.

This will help you to focus on your strengths, minimize weaknesses, and take the greatest possible advantage of opportunities available.

	strengths (internal)	weaknesses (internal)
opportunities (external)	<p>strengths/opportunities Obvious natural priorities</p> <p>Likely to produce greatest ROI (Return On Investment)</p> <p>Likely to be quickest and easiest to implement.</p> <p>Probably justifying immediate action-planning or feasibility study.</p> <p>Executive question: "If we are not already looking at these areas and prioritizing them, then why not?"</p>	<p>weaknesses/opportunities Potentially attractive options</p> <p>Likely to produce good returns if capability and implementation are viable.</p> <p>Potentially more exciting and stimulating and rewarding than S/O due to change, challenge, surprise tactics, and benefits from addressing and achieving improvements.</p> <p>Executive questions: "What's actually stopping us doing these things, provided they truly fit strategically and are realistic and substantial?"</p>
threats (external)	<p>strengths/threats</p> <p>Easy to defend and counter</p> <p>Only basic awareness, planning, and implementation required to meet these challenges.</p> <p>Investment in these issues is generally safe and necessary.</p> <p>Executive question: "Are we properly informed and organized to deal with these issues, and are we certain there are no hidden surprises?" - and - "Since we are strong here, can any of these threats be turned into opportunities?"</p>	<p>weaknesses/threats</p> <p>Potentially high risk</p> <p>Assessment of risk crucial.</p> <p>Where risk is low then we must ignore these issues and not be distracted by them.</p> <p>Where risk is high we must assess capability gaps and plan to defend/avert in very specific controlled ways.</p> <p>Executive question: "Have we accurately assessed the risks of these issues, and where the risks are high do we have specific controlled reliable plans to avoid/avert/defend?"</p>

Table 10 The 2x2 matrix model automatically suggests actions for issues arising from the SWOT analysis, according to four different categories

B) THE PORTFOLIO APPROACH

In today's world, the majority of H&T organizations offer more than only one product or service, and many serve more than one customer group. There are very good strategic reasons for this: Relying solely on one activity would expose the organization

to the risks of a potential downturn in an area of operations. Organizations with multiple product lines or business units must ask themselves how these various products and business units should be managed to boost overall performance.

One of the most popular aids to developing a corporate strategy that addresses the preceding issues in a multi-business H&T organization is portfolio analysis. Portfolio analysis puts the corporate headquarters into the role of an internal auditor. In portfolio analysis, top management views its product lines and business units as a series of investments that will have a return.

The product lines/business units form a portfolio of investments that top management constantly assesses to ensure the maximum return on invested money. Two of the most popular portfolio approaches are Boston Consulting Group (BCG) Matrix and the Directional Policy Matrix (GE-McKinsey).

BCG Growth-Share Matrix

The Boston Consulting Group (BCG) growth-share matrix was developed from Henderson's earlier work with experience curve effects which he applied as a purchasing agent at Westinghouse to help explain the link between increase experience and lower manufacturing costs. Although the phenomenon was not new it was Henderson who brought it to real prominence and demonstrated how it could be harnessed for purposes of strategic planning.

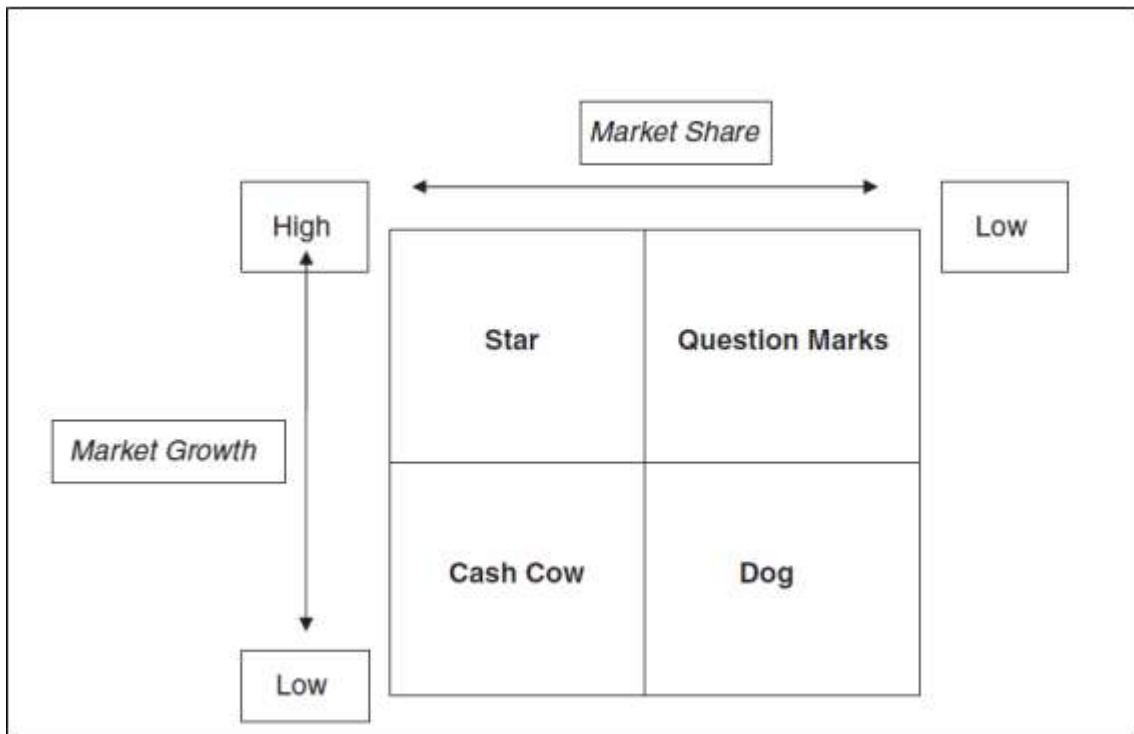


Figure 12 The BCG matrix

The BCG shows the simplest way to portray an organization's portfolio of investments. Each of an organization's product lines or business units is plotted on a matrix according to both the growth rate of the industry in which it competes and its relative market share. A unit's relative competitive position (market share) is defined as its market share in the industry divided by that of the largest other competitor. Relative market share is important because in a competitive environment, it is advantageous to be larger than your rivals. Market growth rate is important because markets that are growing rapidly offer more opportunities for sales than markets with lower growth rates. Overall, the matrix assumes that, other things being equal, a growing market is attractive. The BCG Growth-Share Matrix suggests that as a product moves through its life cycle, it is categorized into one of four types for the purpose of funding decisions:

Stars. The upper left quadrant represents those products or business units with high market shares operating in high-growth markets. The business units or products in this quadrant may be investing heavily to keep up with growth. However, since they

have high market shares, it is assumed that these products will have economies of scale and be able to generate large amounts of cash. Therefore, they are asserted that they will be cash neutral and considered as self-sufficient in terms of investment needs.

Cash cows. The lower left quadrant shows business units or products with a high market share in low-growth markets. Business units or products in this quadrant are mature, and it is assumed that lower levels of investment will be required. On the other hand, high market share means that the business unit should be profitable. They typically bring in far more money than is needed to maintain their market share.

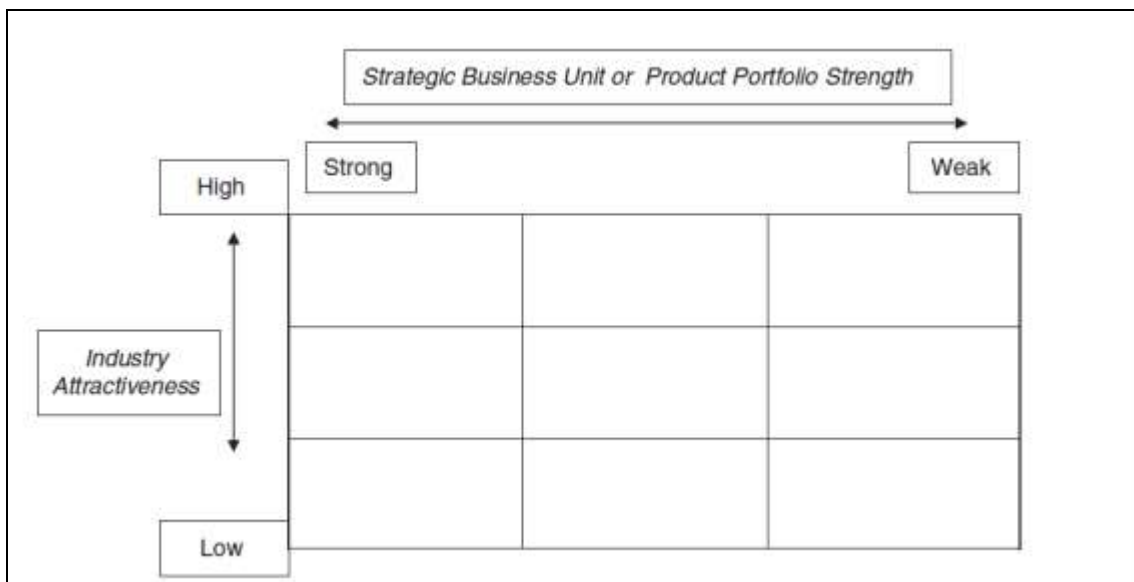
Question marks. Sometimes called “problem children” or “wildcats,” these are new products with the potential for success but that require much effort and resources for development. Their market shares are less dominant, as competition may be more aggressive. The market growth means that it is likely that considerable investment will still be required, and low market share will mean that such business units or products will have difficulty generating substantial cash. Hence, on this basis, these products are likely to be cash users.

Dogs. These products or business units have low market share, and since they are in an unattractive industry, they do not have the potential to bring in much cash. Dogs should be either sold off or managed carefully for the small amount of cash they can generate.

Another important aspect of the matrix is that it indicates likely cash flows associated with each quadrant/stage of the life-cycle. As noted earlier, *new products* in both stable and unstable markets tend to have a negative cash flow (costs exceeded revenue) due to the high costs of promoting and distributing the product, and the absence of any significant experience effects. In the *rapid growth* phase, successful firms tend to plough their profits back into the business to both grow and protect their position. As a result cash flow tends to be marginally negative or neutral. In *maturity*, the benefits of experience and stability accrue, and cash flow is invariably positive and provides funding to support new products in the earlier stage of their life-cycle. Finally, products in *declining markets* are usually portrayed as being in balance or negative in terms of cash flow.

The Directional Policy Matrix

The Directional Policy Matrix (GE-McKinsey) is another way to consider a portfolio of business. Originally developed by McKinsey & Co. consultants, this matrix categorizes business units or products into those with good prospects and those with poorer prospects. Specifically, it positions business units or products according to (1) how attractive the relevant market is in which they are operating and (2) the competitive strength of strategic business units in that market.



As depicted in Figure, the GE Business Matrix includes nine cells based on long-term industry attractiveness and business strength/competitive position. In contrast to the BCG matrix, it includes much more data in its two key factors than just business growth rate and market share. For example, at GE-McKinsey, industry attractiveness can be identified by the five forces analyses and it includes market growth rate and industry size, among other possible opportunities and threats. Business strength or competitive position includes market share as well as profitability and size, among other possible strengths and weaknesses. Wheelen and Hunger (2006) propose four steps to plot business units on the GE Business Screen:

1. Select criteria to rate the industry for each product line or business unit. Assess overall industry attractiveness for each product line or business unit on a scale from 1 (very unattractive) to 5 (very attractive).
2. Select the key factors needed for success in each product line or business unit. Assess business strength/competitive position for each product line or business unit on a scale of 1 (very weak) to 5 (very strong).
3. Plot each product lines or business unit's current position on a matrix like that depicted in Figure.
4. Plot the firm's future portfolio, assuming that present corporate and business strategies remain unchanged. Is there a performance gap between project and desired portfolios? If so, this gap should serve as a stimulus to review the organization's current mission, objectives, strategies, and policies.

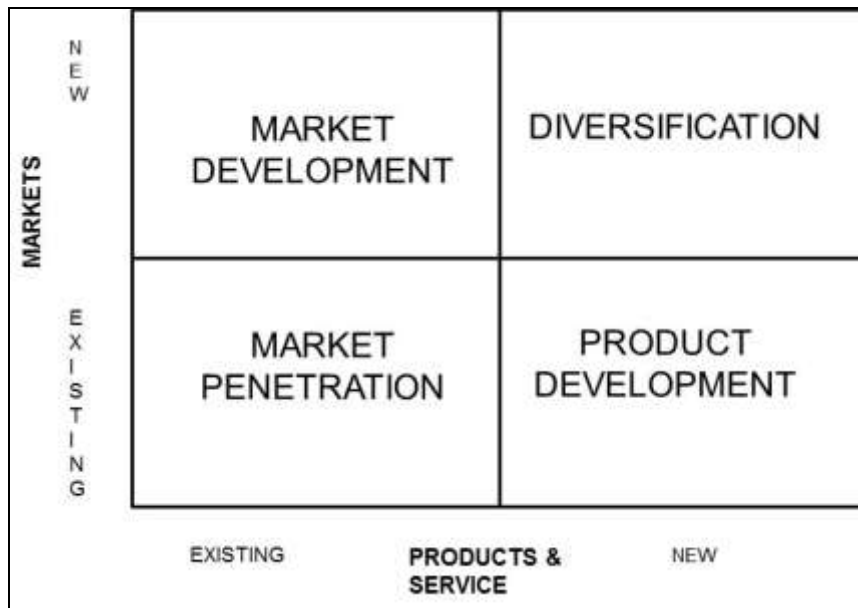
The Ansoff matrix

For a whole variety of reasons, there are times when as an individual or in business you want or need to expand or change your field or market. In business, you might need to achieve economies of scale, make more money for investors, or gain national or even global recognition of their brand. Having decided that you want to grow the business , you'll have hundreds of ideas about things you could do. For the business, this means new products, new markets, new channels, or new marketing campaigns.

Understanding the Tool

The Ansoff Matrix was first published in the Harvard Business Review in 1957, and has given generations of marketers and small business leaders a quick and simple way to develop a strategic approach to growth.

Sometimes called the Product/Market Expansion Grid, it shows four growth options for business formed by matching up existing and new products and services with existing and new markets, as shown in Figure below.



The Matrix essentially shows the risk that a particular strategy will expose you to, the idea being that each time you move into a new quadrant (horizontally or vertically) you increase risk.

The Corporate Ansoff Matrix

Looking at it from a business perspective, staying with your existing product in your existing market is a low risk option: You know the product works, and the market holds few surprises for you.

However, you expose yourself to a whole new level of risk either moving into a new market with an existing product, or developing a new product for an existing market. The market may turn out to have radically different needs and dynamics than you thought, or the new product may just not work or sell.

And by moving two quadrants and targeting a new market with a new product, you increase your risk to yet another level.

Use of the tool is straightforward: start by plotting the approaches you're considering on the matrix. The table below shows how you might classify different approaches.

<p style="text-align: center;">Market Development</p> <p>Here, you're targeting new markets, or new areas of the market. You're trying to sell more of the same things to different people. Here you might:</p> <ul style="list-style-type: none"> • Target different geographical markets at home or abroad • Use different sales channels, such as online or direct sales if you are currently selling through the trade • Target different groups of people, perhaps different age groups, genders or demographic profiles from your normal customers. 	<p style="text-align: center;">Diversification</p> <p>This strategy is risky: There's often little scope for using existing expertise or achieving economies of scale, because you are trying to sell completely different products or services to different customers</p> <p style="text-align: center;">Its main advantage is that, should one business suffer from adverse circumstances, the other is unlikely to be affected.</p>
<p style="text-align: center;">Market Penetration</p> <p>With this approach, you're trying to sell more of the same things to the same people. Here you might:</p> <ul style="list-style-type: none"> • Advertise, to encourage more people within your existing market to choose your product, or to use more of it • Introduce a loyalty scheme • Launch price or other special offer promotions • Increase your sales force activities, or • Buy a competitor company (particularly in mature markets) 	<p style="text-align: center;">Product Development</p> <p>Here, you're selling more things to the same people. Here you might:</p> <ul style="list-style-type: none"> • Extend your product by producing different variants, or packaging existing products in new ways • Develop related products or services (for example, a domestic plumbing company might add a tiling service – after all, if they're plumbing in a new kitchen, most likely tiling will be needed!) • In a service industry, increase your time to market, customer service levels, or quality.

Manage risk appropriately. For example, if you're switching from one quadrant to another, make sure:

- That you research the move carefully;
- That you build the capabilities needed to succeed in the new quadrant;
- That you've got plenty of resources to cover a possible thin period while you're developing and learning how to sell the new product, or are learning what makes the new market tick; and
- That you have firstly thought through what you have to do if things don't work out, and that failure won't "break" you.

Some marketers use a nine-box grid for a more sophisticated analysis. This adds "modified" products between existing and new ones, and "expanded" markets between existing and new ones. This is useful as it shows the difference between product extension and true product development, and also between market expansion and venturing into genuinely new markets (see Figure). However, be careful of the three "options" in grey, as they involve trying to do two things at once without the one benefit of a true diversification strategy (escaping a downturn in one product market).

	New	Market Development	Partial Diversification	Diversification
Markets	Expanded	Market Expansion	Limited Diversification	Partial Diversification
	Existing	Market Penetration	Product Extension	Product Development
		Existing	Modified	New
		Products & Services		

3.4 Pillar 3: Value Chain Analysis

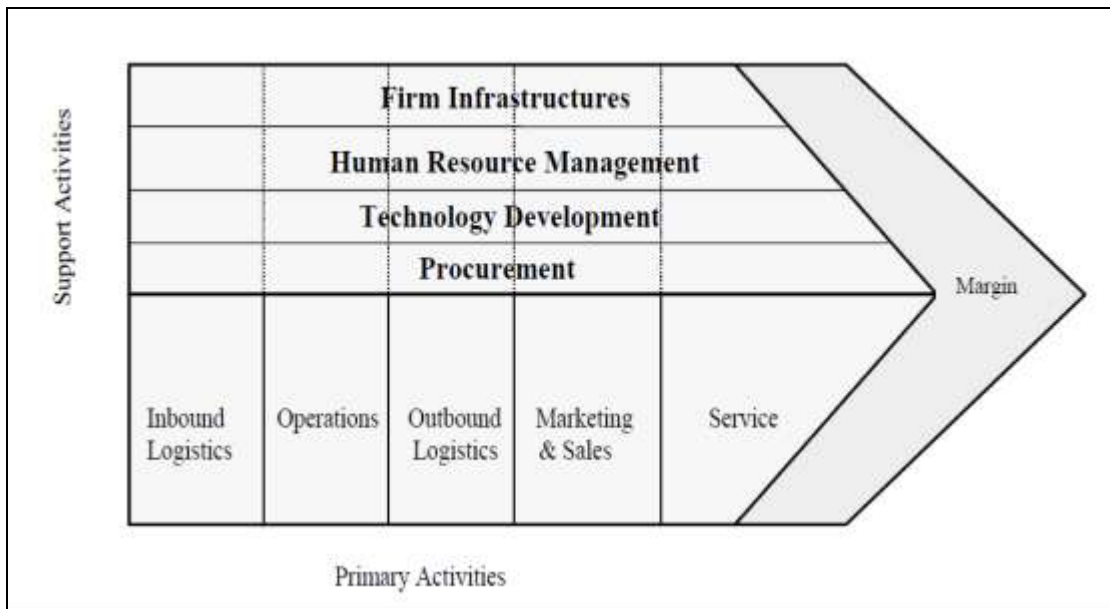
The idea of the value chain is based on the process view of companies, the idea of seeing a manufacturing (or service) company as a system, made up of subsystems each with inputs, transformation processes and outputs⁵⁰. Inputs, transformation processes, and outputs involve the acquisition and consumption of resources - money, labor, materials, equipment, buildings, land, management, etc.

Many companies engage in hundreds, even thousands, of activities in the process of converting inputs to outputs. A company cannot reduce costs and/or create value for customer by looking at its activities as a whole. Creating competitive advantage originates from many separate activities a company performs in designing, production, marketing, delivering, and supporting its products. Each of these activities can contribute to improve company's cost position and customer value. Examining all activities a company performs and how they interact is necessary for improving cost position and customer value, the value chain is a systematic way for doing so. Porter argued that the value chain approach, which involves disaggregating a company's operations into its strategically relevant activities, can be an important managerial tool to understand how value chain activities are performed, to identify what cost drivers of value chain activities are and the existing and potential opportunities for improving cost position and customer value.

The value chain describes the activities within and around a company, and relates them to an analysis of the competitive strength of the company. Therefore, it considers a systematic way to make a company able to evaluate which activity can add value to the products or services to its customers. Thus, this idea was built upon the insight that a company is more than a random compilation of machinery, equipment, people and money. Only if these things are arranged into systems and systematic activities it will become possible to produce something for which customers are willing to pay a price. While one can define or group the activities a company performs at

⁵⁰ Stabell and Fjeldstad 1998:416 and Dess and Picken 1999a:102

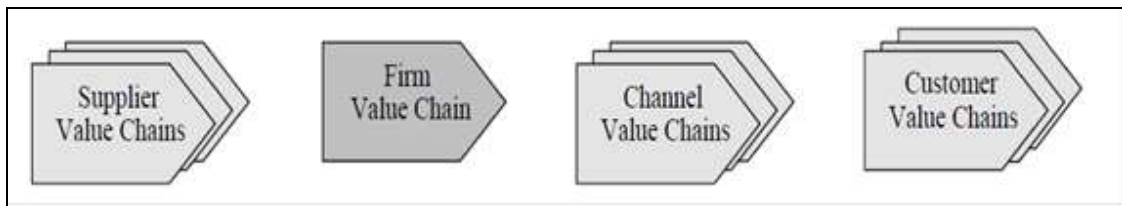
different levels of detail, the figure represents a common approach (Porter's value chain) to categorize such activities.



Porter distinguished between primary activities and support activities. Primary activities are directly involved in creating and bringing value to the customer. They deal with physical products. They can be grouped into five main areas: inbound logistics, operations, outbound logistics, marketing and sales, and service. Each of these primary activities is linked to support activities, which help to improve their effectiveness or efficiency. There are four main areas of support activities: procurement, technology development (including R&D), human resource management, and infrastructure (systems for planning, finance, quality, information management, etc.). As shown in the figure, the value chain contains the element of margin. The term "margin" implies that a company realizes a profit margin that depends on its ability to manage the linkages between all activities in the value chain. In other words, the company is able to deliver a product/service for which the customer is willing to pay more than the sum of the costs of all activities in the value chain. Porter explained that a company's value chain is embedded in a broader value system that provides inputs into the company and helps

transfer outputs to the ultimate consumer. The figure illustrates the value system for an industry. Within the whole value system, there is only a creation value of profit margin available. This is the difference of the final price the customer pays and the sum of all costs incurred with the production and delivery of the product/service.

It depends on the structure of the value system, how this margin spreads across the suppliers, producers, distributors, customers, and other elements of the value system (see Gadiesh and Gilbert 1998:149). Each member of the system will use its market position and negotiating power to get a higher proportion of this margin. Nevertheless, members of a value system can cooperate to improve their efficiency and to reduce their costs in order to achieve a higher total margin to the benefit of all of them.



As shown in the picture, suppliers have value chains that create and deliver the purchased inputs used in a company's chain. Suppliers not only deliver a product but also can influence the costs and performance within the company by many ways. In addition, many products pass through distribution channels on their way to the customer. The value chains of these channels perform additional activities that affect the customer, as well as influence the company's own activities. The linkages between a company and its suppliers and customers should be managed so that all parties benefit. Gaining and sustaining competitive advantage depends not only on understanding a company's value chain activities and the linkages between these activities, but also on recognizing and managing the relationships between the company and the value chains of its suppliers and customers. The value system and value chain are important tools for understanding how a company can position itself against its competitors. The value chain represents the interrelated value-creating activities inside the company.

These activities affect each other and cannot be treated in isolation. To achieve competitive advantage, cost management of value chain activities requires them to be managed and optimized together instead of viewing them as separate and independent cost centers. The idea in the value chain was to capture the fact that a company does a series of functions (e.g. operations, technology development, etc.). Analyzing how these functions are done relatively to their competitors can provide useful insights. On the other hand, the value system is the set of interdependent value chains all the way from the suppliers of raw materials to the end-user. To gain competitive advantage a company has to realize that the costs and benefits, i.e. values associated with the product, must be examined from the final consumer's point view. For a product to be competitive, it must pass through the whole value system efficiently.

To manage costs and make recommendations for building cost advantage, the company or even the business unit is a level to work at it; every business may be viewed as a chain of activities. It is obvious that the behavior of a company's costs and its cost position develop as the result of the value activities the company performs in competing in an industry (Porter 1998a:70). Therefore, effective cost management requires considering or examining costs within value activities carefully and in detail and not the cost of the company as a whole (Partridge and Perren 1994a:23).

Shank and Govindarajan (1993), Donelan and Kaplan (1998) and Blocher et al. (1999) stated that using value chain analysis for strategic cost management could help a company to assess and improve its strategic position by:

- Improving quality by providing better understanding of customer requirements when products are assembled from multiple input sources (e.g. cars, computers...).
- Providing a way to evaluate competitive cost position and thereby improving strategic positioning.
- Reducing time when there is a great deal of interdependency between the participants in a value chain.

- Reducing cost by focusing attention on areas needing cost reduction and by reconfiguring the value chain.

Using value chain analysis for strategic cost management comprises some stages or is predicated upon the fundamental methodology identified in the literature. Shank and Govindarajan (1993), Donelan and Kaplan (1998) and Blocher et al. (1999) stated that the principal stages of value chain analysis for strategic cost management are:

- Identify the value chain activities and disaggregate the firm into separate activities.
- Establish the relative importance of different activities in the total cost of the product.
- Compare costs by activity.
- Identify cost drivers.
- Identify linkages and interrelationships in the value chain.
- Identify opportunities for reducing costs and/or improving value.

Chapter 4

Functional level strategy

The functional strategies are the strategies set at the level of individual business functions. With this expression are the main specialized activities in which it articulates the organization: finance, marketing, production, research and development, personnel management. Define the functional strategies means setting goals specific to each function and define the actions to be taken to ensure that these objectives can be achieved. It is, as is obvious, of strategies that have a much narrower scope than the previous.

The functional strategy of a company is customized to specific industry and is used to back up other corporate and business strategy.

Functional Strategy makes you look at how are you going to implement the strategies and accomplish the goals of the organization, it is the final level of strategy developed by the major functional departments; these are action plans. They achieve the business strategies of the organization through the above departments. Functional Strategy harnesses the activities, skills and resources available, is primarily coordinates the functional areas of the corporate, so that each area upholds and contributes to individual business level strategy and to the overall corporate level strategy. This involves coordinating the various functions and operations needed to design, manufacture, delivery and support the product or service of each business within the organization. Functional Strategy is mainly concerned with -making efficient use of specialists with the functional area, integrating activities with functional area – coordinating advertising, promotion, and marketing resources in marketing, or purchasing, inventory control, and shipping in productions and operations, assuring that

the functional strategy mesh with the business level strategies and the corporate level strategies.

Timing is another area of importance in functional strategy. For instance, the advertisement of a new product for market introduction well ahead, planning the production schedule accordingly, purchase of raw material for production in time, delivery schedule to the distributors and retailers, all these have to be coordinated and timed in perfect unison. The Functional Strategy has shorter time duration to act in comparison to either business level or corporate level strategies. Responsibility to `accountability` is also easily fixed in Functional Strategy, because actions occur sooner and more easily attributed to the function than is possible at other levels of strategy. In this, lower level managers are more directly involved with the implementation of Functional Strategy.

Functional Strategy supports both market definition of the corporate strategy and also the market navigation of the business strategy as shown below.

When it comes to business and how it can ideally be decomposed, think of the main activities of the management. Are mainly marketing, finance, manufacturing, research and development, human resources. Each function has long-term goals to be achieved and then each function has a strategy. Together, coordinated by top management, contribute to achieving the objectives. It makes no sense to do lists between them. However, in the contemporary economy imposes strong competition to always put in the foreground the question: what expectations have potential buyers who want to serve? Consequently, the requirements of potential customers on the one hand and the advantages competitive the company can put in place to serve the other has a high priority in formulating strategies.

Once higher level corporate and business strategies are developed, management need to formulate and implement strategies for each functional area. Strategy of one functional area can not be looked at in isolation, because it is the extent to which all of the functional tasks are interwoven that determine the effectiveness of the major strategy.

For effective implementation, strategists have to provide direction to functional managers regarding the plans and policies to be adopted. In fact, the effectiveness of strategic management depends critically on the manner in which strategies are implemented.

Functional strategies provide details to business strategy & governs as to how key activities of the business will be managed. Functional strategies play two important roles. Firstly, they provide support to the overall business strategy. Secondly, they spell out as to how functional managers will work so as to ensure better performance in their respective functional areas.

Functional area strategy such as marketing, financial, production and Human Resource are based on the functional capabilities of an organization. For each functional area, first the major sub areas are identified and then for each of these sub functional areas, content of functional strategies, important factors, and their importance in the process of strategy implementation is identified.

In terms of the levels of strategy formulation, functional strategies operate below the SBU or business-level strategies. Within functional strategies there might be several sub-functional areas. Functional strategies, are made within the higher level strategies and guidelines therein that are set at higher levels of an organization. Functional managers need guidance from the business strategy in order to make decisions. Operational plans tell the functional managers what has to be done while policies state how the plans are to be implemented. Major strategies need to be translated to lower levels to give holistic strategic direction to an organization. The reasons why functional strategies are needed can be enumerated as follows:

- The development of functional strategies is aimed at making the strategies-formulated at the top management level-practically feasible at the functional level.
- Functional strategies facilitate flow of strategic decisions to the different parts of an organization.

- They act as basis for controlling activities in the different functional areas of business.
- The time spent by functional managers in decision-making is reduced as plans lay down clearly what is to be done and policies provide the discretionary framework within which decisions need to be taken.
- Functional strategies help in bringing harmony and coordination as they remain part of major strategies.
- Similar situations occurring in different functional areas are handled in a consistent manner by the functional managers.

Thus, strategies need to be segregated into viable functional plans and policies that are compatible with each other. In this way, strategies can be implemented by the functional managers. Environmental factors relevant to each functional area have an impact on the choice of functional strategies. Organizational strategies affect the choice of functional strategies.

However, the actual process of choice is influenced by objective as well as subjective factors. Functional strategies affect, and are affected by, the resource allocation decisions.

4.1 Marketing strategy formulation

Ordinary marketing is an activity performed by business organizations. However, it is not necessarily confined only to business enterprises. It is an activity that creates and sustains exchange relationships among those who are willing and able to buy and sell products, services, satisfaction and even ideas. In the present day for business, it is considered to be the activities related to identifying the needs of customers and taking such actions to satisfy them in return of some consideration. In marketing it is more important to do what is strategically right than what is immediately profitable.

The term marketing constitutes different processes, functions, exchanges and activities that create perceived value by satisfying needs of individuals. Marketing induces or helps in moving people closer to making a decision to purchase and facilitate a sale. Marketing in recent decades has assumed an astounding importance. It is an immediate cause and effect of rapid economic growth, globalization, technological up gradation, development of ever-increasing human needs and wants and increasing purchasing power.

A business organization faces countless marketing variables that affect the success or failure of strategy implementation. Some examples of marketing decisions that may require special attention are as follows:

- The kind of distribution network to be used. Whether to use exclusive dealerships or multiple channels of distribution.
- The amount and the extent of advertising. Whether to use heavy or light advertising. What should be the amount of advertising in print media, television or internet.
- Whether to limit or enhance the share of business done with a single or a few customer.
- Whether to be a price leader or a price follower.
- Whether to offer a complete or limited warranty.
- Whether to reward salespeople based on straight salary

4.1.1 Delivering value to customer

One of the most common reasons for the failure of a business venture, large or small, is its inability to deliver value to customers. The concept of value is one of those things that is both simple and complex. Simple because it only has three components; complex because it can only be defined by the customer, and can include tangible and

intangible concepts such as perceptions and opinions. This article is intentionally simplistic, so as to introduce the concepts in their most basic form.

1. **Understand that the first component of value is "utility."** It means that whatever you are delivering to your customer has to be fit for the purpose the customer will give to it. In essence, for any goods or service you deliver to a customer, having utility means that the customer can enhance the performance of their own assets, or remove some sort of constraint that prevents them from receiving more value from their assets.
2. **Know that the next component is "warranty."** It means that the goods or services that you deliver to your customer must be fit for use. The same concepts apply to all other goods and services. They have to be as available as the customer considers appropriate, provide the right capacity to meet the customer's demand, be as secure as the customer expects them to be and as continuous as is considered reasonable by the customer.
3. **Strive to identify and overcome the barriers of the customer's perceptions.** The easiest way to explain this is to think back to the day you bought your last automobile. Why did you pick that one? After all, all cars are the same — four wheels, chassis, engine, transmission, differential, body, seats, steering wheel, glass, seat belts, etc... Or are they? The job of the salesperson who wants to make the sale is to identify these perceptions and determine the best way to present the service — a car — in a way that will convince the customer that this is the vehicle that meets all of the requirements, real and perceived.
4. **The perceptions of the customer are what makes or breaks the transaction that exchanges value for money.** For example, most people would not pay \$100 for a can of corned beef, right? However, put a person in a situation where that person has not eaten for days and that's all to be found, and that person will exchange anything of value for that

food. The art of selling boils down to finding what the customer wants that they consider to be of value, and convincing them that what you have for sale will deliver that value.

5. **Remember that strategy and marketing are two different concepts.**

- Strategy is about **deciding** what you will offer that is of value to potential customers, how that value will be delivered, and how you will convince the customer that the value the customer wants should be obtained from you. In short, it's about defining the **value proposition**.
- Marketing is about **communicating** the strategy and value proposition to a customer in a way that will make them want to buy the service or goods from you.

6. **Pursue positive returns.** Where does money come into play in all of this? The customer must perceive that the total value of the service is higher than its cost, and produces a positive return. The return can be tangible (as in a positive Return on Investment) or intangible (as in an increase in the reputation of the customer's brand, or the goodwill of the customer's customers). Keep in mind that sometimes intangible returns can be much more valuable than tangible ones!

4.1.2 Positioning

The goal of positioning is to define the location of "space" that the product must take in the strategic choice and in the mind of the consumer.

In fact, "Positioning is what you do to the mind of the potential customer, not really doing anything to the product itself. This does not mean that the position does not change. Often it entails. But the changes made in the name, the price and the packaging is not any way constitute changes in the product. They are usually the changes "cosmetic" performed for the purpose of ensuring a profitable position in the consumer's

mind. "The basic approach of positioning is not to create something new and different, but to manipulate what is already present in the mind, it has retained the connections that already exist. The analysis then allows positioning on the one hand to identify and clarify the critical character of the product and other information to form the basis for a more precise formulation of pricing, product, distribution and communication.

Starting from the assumption that the product generally expresses a set of utilities and benefits that relate to the needs of various kinds can be identified several variables that can be used for positioning a product. In this sense, Valdani (1995) identifies nine criteria, used individually or jointly guide the decisions of placement of a product by a company. These criteria are:

- 1) Product Attributes: The criterion more intuitive and perhaps more used in the positioning strategy a product is based on its specific characteristics differentiating (characteristics technical, technological innovation, speed, power, accessories, etc.). The problem with this approach is able to identify an attribute very important for the market or a segment thereof, that has not already been promoted by a rival.
- 2) My invisible positioning based mainly on specific tangible product can be vulnerable to change and innovation. The use and development of resources invisible can be so effective to support and strengthen its strategy of positioning. A resource such as an invisible technology leadership, the image of the brand, reputation for quality, the ability of management, is mainly based on information and knowledge and invaluable importance in contributing to the positioning of the product.
- 3) Benefits sought by customers: More generally effective criterion is based on the product positioning than the benefits / advantages and its ability to provide a solution to the problems or meet specific consumer needs. A rational benefit is structurally related to an attribute of the product and should be integrated in the decision-making rational purchase. The psychological benefit, consequential to the process of formation of the

attitudes of the buyer, is related to perceptions relating to the purchase, consumption or use of the brand.

- 4) Price: The price can have a significant role in the positioning of the product. It is an important piece of information, which was positively related to quality.
- 5) Opportunities to use: Many products can be placed instead to specific occasions of use or particular moods. This criterion may be appropriate and beneficial in the case of consumer products where it is often necessary to characterize an acceptability social or a particular state of mind to correlate occasions.
- 6) Potential Users: The product can also be positioned with respect to a specific group of users. This positioning is effective because it combines the strategy of product differentiation in the market segmentation.
- 7) Opinion leaders: A character or a character opinion leaders in the world entertainment can sometimes be used to create associations with a brand to compete to place it strategically.
- 8) Direct placement: Place a product directly against another product is a viable criterion for grouped in an "implicit or explicit" to compare two competing products.
- 9) Country of origin effect: Another way to position effectively a product is to create an association with a specific country in order to assert an image of quality or specific expertise.

4.1.3 Marketing Mix

Marketing mix forms an important part of overall competitive marketing strategy. The marketing mix is the set of controllable marketing variables that the firm blends to produce the response it wants in the target market. The marketing mix consists

of everything that the firm can do to influence the demand for its product. These variables are often referred to as the “4 P.” The 4 P stand for product, price, place and promotion. An effective marketing program blends all of the marketing mix elements into a coordinated program designed to achieve the company’s marketing objectives by delivering value to consumers. The 4 P are from a marketer’s angle. When translated to buyers angle they may be termed as 4 C. Product may be referred as customer solution, price as customer cost, place as convenience and promotion as communication.

Product

Product stands for the “goods-and-service” combination the company offers to the target market. Strategies are needed for managing existing product over time adding new ones and dropping failed products. Strategic decisions must also be made regarding branding, packaging and other product features such as warranties.

Products and markets are infinitely dynamic. An organization has to capture such dynamics through a set of policies and strategies. Some products have consistent customer demand over long period of time while others have short and fleeting life spans. There are products that have wide range of quality and workmanship and these also change over time. There are industrial or consumer products, essentials or luxury products, durables or perishables. Products can be differentiated on the basis of size, shape, colour, packaging, brand names, after-sales service and so on. Organizations seek to hammer into customers’ minds that their products are different from others. It does not matter whether the differentiation is real or imaginary. Quite often the differentiation is psychological rather than physical. It is enough if customers are persuaded to believe that the marketers product is different from others.

Organizations formalize product differentiation through christening ‘brand names’ to their respective products. These are generally reinforced with legal sanction and protection. Brands enable customers to identify the product and the organization behind it. The products’ and even firms’ image is built around brand through

advertising and other promotional strategies. Customers tend to develop strong brand loyalty for a particular product over a period of time.

Price

Price stands for the amount of money customers have to pay to obtain the product. Necessary strategies pertain to the location of the customers, price flexibility, related items within a product line and terms of sale. The price of a product is its composite expression of its value and utility to the customer, its demand, quality, reliability, safety, the competition it faces, the desired profit and so on.

In an industry there would be organizations with low cost products and other organizations with high costs. The low cost organizations may adopt aggressive pricing strategy as they enjoy more freedom of action in respect of their prices. They may also afford selective increase in costs to push their sales. Theoretically, organizations may also adopt cost plus pricing wherein a margin is added to the cost of the product to determine its price. However, in the competitive environment such an approach may not be feasible. More and more companies of today have to accept the market price with minor deviations and work towards their costs. They reduce their cost in order to maintain their profitability.

For a new product pricing strategies for entering a market needs to be designed. In pricing a really new product at least three objectives must be kept in mind.

- (a) Making the product acceptable to the customers.
- (b) Producing a reasonable margin over cost.
- (c) Achieving a market that helps in developing market share.

For a new product an organization may either choose to skim or penetrate the market. In skimming prices are set at a very high level. The product is directed to those buyers who are relatively price insensitive but sensitive to the novelty of the new product. For example call rates of mobile telephony were set very high initially. Even the incoming calls were charged. Since the initial off take of the product is low, high

price, in a way, helps in rationing of supply in favour of those who can afford it. In penetration firm keeps a temptingly low price for a new product which itself is selling point. A very large number of the potential consumer may be able to afford and willing to try the product.

Place

Place stands for company activities that make the product available to target consumers. One of the most basic marketing decision is choosing the most appropriate marketing channel. Strategies should be taken for the management of channel(s) by which ownership of product is transferred from producers to customers and in many cases, the system(s) by which goods are moved from where they are produced from they are purchases by the final customers. Strategies applicable to the middleman such as wholesalers and retails must be designed.

The distribution policies of a company are important determinants of the functions of marketing. The decision to utilize a particular marketing channel or channels sets the pattern of operations of sales force. We will learn more about place when we study logistics later in this chapter.

Promotion

Promotion stands for activities that communicate the merits of the product and persuade target consumers to buy it. Strategies are needed to combine individual methods such as advertising, personal selling, and sales promotion into a coordinated campaign. In addition promotional strategies must be adjusted as a product move from an earlier stages from a later stage of its life.

Modern marketing is highly promotional oriented. Organizations strive to push their sales and market standing on a sustained basis and in a profitable manner under conditions of complex direct and indirect competitive situations. Promotion also acts as an impetus to marketing. It is simultaneously a communication, persuasion and conditioning process.

There are at least four major direct promotional methods or tools – personal selling, advertising, publicity and sales promotion. They are briefly explained as follows:

(i) Personal Selling: Personal selling is one of the oldest forms of promotion. It involves face-to-face interaction of sales force with the prospective customers and provides a high degree of personal attention to them. In personal selling, oral communication is made with potential buyers of a product with the intention of making a sale. It may initially focus on developing a relationship with the potential buyer, but end up with efforts for making a sale. Personal selling suffers from a very high costs as sales personnel are expensive. They can physically attend only one customer at a time. Thus it is not a cost-effective way of reaching a large number of people.

(ii) Advertising: Advertising is a non-personal, highly flexible and dynamic promotional method. The media for advertisings are several such as pamphlets, brochures, newspapers, magazines, hoardings, display boards, radio, television and internet. Choice of appropriate media is important for effectiveness of the message. The media may be local, regional, or national. The type of the message, copy, illustration are a matter of choice and creativity. Advertising may be directed towards consumers, middlemen or opinion leaders. Advertising is likely to succeed in promoting the sales of an organization but its effectiveness in respect to the expenditure can not be directly measured. Sales is a function of several variables out of which advertising is only one.

(iii) Publicity: Publicity is also a non-personal form of promotion similar to advertising. However, no payments are made to the media as in case of advertising. Organizations skillfully seek to promote themselves and their product without payment. Publicity is communication of a product, brand or business by placing information about it in the media without paying for the time or media space directly. Thus it is way of reaching customers with negligible cost. Basic tools for publicity are press releases, press conferences, reports, stories, and internet releases. These releases must be of interest to the public.

(iv) Sales promotion: Sales promotion is an omnibus term that includes all activities that are undertaken to promote the business but are not specifically included

under personal selling, advertising or publicity. Activities like discounts, contests, money refunds, installments, kiosks, exhibitions and fairs constitute sales promotion. All these are meant to give a boost to the sales. Sales promotion done periodically may help in getting a larger market share to an organization.

4.2 Financial Strategy Formulation

The financial strategies of an organization are related to several finance/accounting concepts considered to be central to strategy implementation. These are: acquiring needed capital/sources of fund, developing projected financial statements/budgets, management/ usage of funds, and evaluating the worth of a business. Strategists need to formulate strategies in these areas so that they are implemented. Some examples of decisions that may require finance/accounting policies are:

- To raise capital with short-term debt, long-term debt, preferred stock, or common stock.
- To lease or buy fixed assets.
- To determine an appropriate dividend payout ratio.
- To extend the time of accounts receivable.
- To establish a certain percentage discount on accounts within a specified period of time.
- To determine the amount of cash that should be kept on hand.

Acquiring capital to implement strategies / sources of funds

Successful strategy implementation often requires additional capital. Besides net profit from operations and the sale of assets, two basic sources of capital for an organization are debt and equity. Determining an appropriate mix of debt and equity in a firm's capital structure can be vital to successful strategy implementation.

Theoretically, an enterprise should have enough debt in its capital structure to boost its return on investment by applying debt to products and projects earning more than the cost of the debt. In low earning periods, too much debt in the capital structure of an organization can endanger stockholders' return and jeopardize company survival. Fixed debt obligations generally must be met, regardless of circumstances. This does not mean that stock issuances are always better than debt for raising capital. Some special stock is issued to finance strategy implementation, ownership and control of the enterprise are diluted. This can be a serious concern in today's business environment of hostile takeovers, mergers, and acquisitions. The major factors regarding which strategies have to be made are: capital structure; procurement of capital and working capital borrowings; reserves and surplus as sources of funds; and relationship with lenders, banks and financial institutions. Strategies related to the sources of funds are important since they determine how financial resources will be made available for the implementation of strategies. Organizations have a range of alternatives regarding the sources of funds. While one company may rely on external borrowings, another may follow a policy of internal financing.

Projected financial statements / budgets

Projected (pro forma) financial statement analysis is a central strategy-implementation technique because it allows an organization to examine the expected results of various actions and approaches. This type of analysis can be used to forecast the impact of various implementation decisions (for example, to increase promotion expenditures by 50 percent to support a market-development strategy, to increase salaries by 25 percent to support a market-penetration strategy, to increase research and development expenditures by 70 percent to support product development, or to sell common stock to raise capital for diversification). Nearly all financial institutions require a projected financial statements whenever a business seeks capital. A pro forma income statement and balance sheet allow an organization to compute projected financial ratios under various strategy-implementation scenarios. When compared to prior years and to industry averages, financial ratios provide valuable insights into the feasibility of various strategy-implementation approaches.

Primarily as a result of the Enron collapse and accounting scandal, companies today are being much more diligent in preparing projected financial statements to "reasonably rather than too optimistically" project future expenses and earnings.

A financial budget is also a document that details how funds will be obtained and spent for a specified period of time. Annual budgets are most common, although the period of time for a budget can range from one day to more than ten years. Fundamentally, financial budgeting is a method for specifying what must be done to complete strategy implementation successfully.

Financial budgeting should not be thought of as a tool for limiting expenditures but rather as a method for obtaining the most productive and profitable use of an organization's resources. Financial budgets can be viewed as the planned allocation of a firm's resources based on forecasts of the future.

There are almost as many different types of financial budgets as there are types of organizations. Some common types of budgets include cash budgets, operating budgets, sales budgets, profit budgets, factory budgets, capital budgets, expense budgets, divisional budgets, variable budgets, flexible budgets, and fixed budgets. When an organization is experiencing financial difficulties, budgets are especially important in guiding strategy implementation.

Financial budgets have some limitations. First, budgetary programs can become so detailed that they are cumbersome and overly expensive. Over budgeting or under budgeting can cause problems. Second, financial budgets can become a substitute for objectives, A budget is a tool and not an end in itself. Third, budgets can hide inefficiencies if based solely on precedent rather than on periodic evaluation of circumstances and standards. Finally, budgets are sometimes used as instruments of tyranny that result in frustration, resentment, absenteeism, and high turnover. To minimize the effect of this last concern, managers should increase the participation of subordinates in preparing budgets.

4.3 Production Strategy Formulation

The strategy for production are related to the production system, operational planning and control, and research and development (R&D). The strategy adopted affects the nature of product/service, the markets to be served, and the manner in which the markets are to be served. All these collectively influence the operations system structure and objectives which are used to determine the operations plans and policies. Thus, a strategy of expansion through related diversification, for instance, will affect what products are offered to which market and how these markets are served. The operations system structure, which is concerned with the manufacturing/ service and supply/delivery system, and operations system objectives, which are related to customer service and resource utilization, both determine what operations, plans and policies are set.

Production System

The production system is concerned with the capacity, location, layout, product or service design, work systems, degree of automation, extent of vertical integration, and such factors. Strategies related to production system are significant as they deal with vital issues affecting the capability of the organisation to achieve its objectives. Strategy implementation would have to take into account the production system factors as they involve decisions which are long-term in nature and influence not only the operations capability of an organisation but also its ability to implement strategies and achieve objectives.

Operations Planning and Control

Strategies related to operations planning and control are concerned with aggregate production planning; materials supply; inventory, cost, and quality management; and maintenance of plant and equipment. Here, the aim of strategy implementation is to see how efficiently resources are utilized and in what manner the day-to-day operations can be managed in the light of long-term objectives.

Operations planning and control provides an example of an organizational activity that is aimed at translating the objectives into reality.

4.4 Logistics Strategy

Management of logistics is a process which integrates the flow of supplies into, through and out of an organization to achieve a level of service which ensures that the right materials are available at the right place, at the right time, of the right quality, and at the right cost. Organizations try to keep the cost of transporting materials as low as possible consistent with safe and reliable delivery.

Supply chain management helps in logistics and enables a company to have constant contact with its distribution team, which could consist of trucks, trains, or any other mode of transportation. Given the changes that affect logistics operations such as emerging technologies and industry initiatives, developing and using a formal logistics strategy is very important. For a business organization effective logistic strategy will involve raising and finding solutions to the following questions:

- Which sources of raw materials and components are available?
- How many manufacturing locations are there?
- What products are being made at each manufacturing location?
- What modes of transportation should be used for various products.
- What is the nature of distribution facilities?
- What is the nature of materials handling equipment possessed? Is it ideal?
- What is the method for deploying inventory in the logistics network?
- Should the business organization own the transport vehicles?

Improvement in logistics can results in savings in cost of doing business. These savings can also reveal in the profits of the company. Some examples of how logistics can help a business are as follows:

- Cost savings
- Reduced inventory
- Improved delivery time
- Customer satisfaction
- Competitive advantage

4.4.1 Supply Chain Management

The way businesses were conducted in the yesteryears is entirely different as they are conducted now. Today, organizations work in highly turbulent environment. There are several changes in business environment that have contributed to the development of supply chain networks. The technology has made impact on all spheres of business activities. Organizational systems have improved. Even the available infrastructure is improving.

Technological changes and reduction in information communication costs with increase in its speed has led to changes in coordination among the members of the supply chain network. Availability of newer technologies have resulted in creation of innovative products with shorter product life cycles.

Traditionally companies have been managing themselves by taking orders, buying supplies, manufacturing products and shipping them from their warehouses. Such organizations may lose out the businesses that strongly lay their focus on key areas of marketing, branding and delivering value to the customer and outsourcing the rest. Today organizations and individual customers have become more demanding. They desire customized products that are made according to their needs. They also aspire that these should be available at lower costs.

What is Supply Chain Management?

The term supply chain refers to the linkages between suppliers, manufacturers and customers. Supply chains involve all activities like sourcing and procurement of material, conversion, and logistics. Planning and control of supply chains are important components of its management. Naturally, management of supply chains include closely working with channel partners – suppliers, intermediaries, other service providers and customers. Supply chain management is defined as the process of planning, implementing, and controlling the supply chain operations. It is a cross-functional approach to managing the movement of raw materials into an organization and the movement of finished goods out of the organization toward the end-consumer who are to be satisfied as efficiently as possible. It encompasses all movement and storage of raw materials, work-in-process inventory, and finished goods from point-of-origin to point-of-consumption. Organizations are finding that they must rely on the chain to successfully compete in the global market. Modern organizations are striving to focus on core competencies and reduce their ownership of sources of raw materials and distribution channels. These functions can be outsourced to other business organizations that specialize in those activities and can perform in better and cost effective manner. In a way organizations in the supply chain do tasks according to their core-competencies. Working in the supply chain improve trust and collaboration amongst partners and thus improve flow and management of inventory.

Is logistic management same as supply chain management

Supply chain management is an extension of logistic management. However, there is difference between the two. Logistical activities typically include management of inbound and outbound goods, transportation, warehousing, handling of material, fulfilment of orders, inventory management, supply/demand planning. Although these activities also form part of Supply chain management, the latter has different components. Logistic management can be termed as one of its part that is related to planning, implementing, and controlling the movement and storage of goods, services and related information between the point of origin and the point of consumption.

Supply chain management includes more aspects apart from the logistics function. It is a tool of business transformation and involves delivering the right product at the right time to the right place and at the right price. It reduces costs of organizations and enhances customer service.

Implementing Supply Chain Management Systems

Successful implementing supply management systems requires a change from managing individual functions to integrating activities into key supply chain processes. It involves collaborative work between buyers and suppliers, joint product development, common systems and shared information. A key requirement for successfully implementing supply chain will be network of information sharing and management. The partners need to link together to share information through electronic data interchange and take decisions in timely manner.

Implementing and successfully running supply chain management system will involve:

1. Product development: Customers and suppliers must work together in the product development process. Right from the start the partners will have knowledge of all Involving all partners will help in shortening the life cycles. Products are developed and launched in shorter time and help organizations to remain competitive.

2. Procurement: Procurement requires careful resource planning, quality issues, identifying sources, negotiation, order placement, inbound transportation and storage. Organizations have to coordinate with suppliers in scheduling without interruptions. Suppliers are involved in planning the manufacturing process.

3. Manufacturing: Flexible manufacturing processes must be in place to respond to market changes. They should be adaptive to accommodate customization and changes in the taste and preferences. Manufacturing should be done on the basis of just-in-time (JIT) and minimum lot sizes. Changes in the manufacturing process be made to reduce manufacturing cycle.

4. Physical distribution: Delivery of final products to customers is the last position in a marketing channel. Availability of the products at the right place at right

time is important for each channel participant. Through physical distribution processes serving the customer become an integral part of marketing. Thus supply chain management links a marketing channel with customers.

5. Outsourcing: Outsourcing is not limited to the procurement of materials and components, but also include outsourcing of services that traditionally have been provided within an organization. The company will be able to focus on those activities where it has competency and everything else will be outsourced.

6. Customer services: Organizations through interfaces with the company's production and distribution operations develop customer relationships so as to satisfy them. They work with customer to determine mutually satisfying goals, establish and maintain relationships. This in turn help in producing positive feelings in the organization and the customers

7. Performance measurement: There is a strong relationship between the supplier, customer and organization. Supplier capabilities and customer relationships can be correlated with a firm performance. Performance is measured in different parameters such as costs, customer service, productivity and quality.

4.5. Research and Development

Research and development (R&D) personnel can play an integral part in strategy implementation. These individuals are generally charged with developing new products and improving old products in a way that will allow effective strategy implementation. R&D employees and managers perform tasks that include transferring complex technology, adjusting processes to local raw materials, adapting processes to local markets, and altering products to particular tastes and specifications. Strategies such as product development, market penetration, and concentric diversification require that new products be successfully developed and that old products be significantly improved. But the level of management support for R&D is often constrained by resource availability.

Technological improvements that affect consumer and industrial products and services shorten product life cycles. Companies in virtually every industry are relying on the development of new products and services to fuel profitability and growth. Surveys suggest that the most successful organizations use an R&D strategy that ties external opportunities to internal strengths and is linked with objectives. Well formulated R&D policies match market opportunities with internal capabilities. R&D policies can enhance strategy implementation efforts to:

- Emphasize product or process improvements.
- Stress basic or applied research.
- Be leaders or followers in R&D.
- Develop robotics or manual-type processes.
- Spend a high, average, or low amount of money on R&D.
- Perform R&D within the firm or to contract R&D to outside firms.
- Use university researchers or private sector researchers.

There must be effective interactions between R&D departments and other functional departments in implementing different types of generic business strategies. Conflicts between marketing, finance/accounting, R&D, and information systems departments can be minimized with clear policies and objectives.

Many firms wrestle with the decision to acquire R&D expertise from external firms and develop R&D expertise internally. The following guidelines can be used to help make this decision:

If the rate of technical progress *is* slow, the rate of market growth *is* moderate, and there are significant barriers to possible new entrants, then in-house R&D is the preferred solution. The reason *is* that R&D, if successful, will result in a temporary product or process monopoly that the company can exploit.

If technology is changing rapidly and the market is growing slowly, then a major effort in R&D may be very risky, because it may lead to the development of an ultimately obsolete technology or one for which there is no market.

If technology is changing slowly but the market is growing quickly, there generally is not enough time for in-house development. The prescribed approach is to obtain R&D expertise on an exclusive or nonexclusive basis from an outside firm.

If both technical progress and market growth are fast, R&D expertise should be obtained through acquisition of a well-established firm in the industry?

There are at least three major R&D approaches for implementing strategies. The first strategy is to be the first firm to market new technological products. This is a glamorous and exciting strategy but also a dangerous one.

A second R&D approach is to be an innovative imitator of successful products, thus minimizing the risks and costs of startup. This approach entails allowing a pioneer firm to develop the first version of the new product and to demonstrate that a market exists. Then, laggard firms develop a similar product. This strategy requires excellent R&D personnel and an excellent marketing department. A third R&D strategy is to be a low-cost producer by mass-producing products similar to but less expensive than products recently introduced. As a new product accepted by customers, price becomes increasingly important in the buying decision. Also, mass marketing replaces personal selling as the dominant selling strategy. This R&D strategy requires substantial investment in plant and equipment, but fewer expenditures in R&D than the two approaches described earlier.

4.6 The human Resources strategy

The job of human resource manager is changing rapidly as there companies that downsize and reorganize. Strategic responsibilities of the human resource manager include assessing the staffing needs and costs for alternative strategies proposed during

Strategy formulation and developing a staffing plan for effectively implementing strategies. This plan must consider how best to manage spiralling healthcare insurance costs. Employers' health coverage expenses consume an average 26 percent of firms' net profits, even though most companies now require employees to pay part of their health insurance premiums. The plan must also include how to motivate employees and managers. The human resource department must develop performance incentives that clearly link performance and pay to strategies. The process of empowering managers and employees through their involvement in strategic management activities yields the greatest benefits when all organizational members understand clearly how they will benefit personally if the firm does well. Linking company and personal benefits is a major new strategic responsibility of human resource managers. Other new responsibilities for human resource managers may include establishing and administering an employee stock ownership plan (ESOP), instituting an effective childcare policy, and providing leadership for managers and employees in a way that allows them to balance work and family.

A well-designed strategic-management system can fail if insufficient attention is given to the human resource dimension. Human resource problems that arise when business implement strategies can usually be traced to one of three causes: (1) disruption of Social and political structures, (2) failure to match individuals' aptitudes with implementation tasks, and (3) inadequate top management support for implementation activities. Strategy implementation poses a threat to many managers and employees in an organization.

New power and status relationships are anticipated and realized. New formal and informal groups' values, beliefs, and priorities may be largely unknown. Managers and employees may become engaged in resistance behavior as their roles, prerogatives, and power in the firm change. Disruption of social and political structures that accompany strategy execution must be anticipated and considered during strategy formulation and managed during strategy implementation. A concern in matching managers with strategy is that jobs have specific and relatively static responsibilities, although people are dynamic in their personal development. Commonly used methods that match

managers with strategies to be implemented include transferring managers, developing leadership workshops, offering career development activities, promotions, job enlargement, and job enrichment. A number of other guidelines can help ensure that human relationships facilitate rather than disrupt strategy-implementation efforts. Specifically, managers should do a form of chatting and informal questioning to stay abreast of how things are progressing and to know when to intervene. Managers can build support for strategy-implementation efforts by giving few orders, announcing few decisions, depending heavily on informal questioning, and seeking to probe and clarify until a consensus emerges. Key thrusts that needed should be rewarded generously and visibly. It is surprising that so often during strategy formulation, individual values, skills, and abilities needed for successful strategy implementation are not considered. It is rare that a firm selecting new strategies or significantly altering existing strategies possesses the right line and staff personnel in the tight positions for successful strategy implementation. The need to match individual aptitudes with strategy-implementation tasks should be considered in strategy choice. Inadequate support from strategists for implementation activities often undermines organizational success. Chief executive officers, small business owners, and government agency heads must be personally committed to strategy implementation and express this commitment in highly visible ways. Strategists' formal statements about the Importance of strategic management must be consistent with actual support and rewards given for activities completed and objectives reached. Otherwise, stress created by inconsistency can cause uncertainty among managers and employees at all levels. Perhaps the best method for preventing and overcoming human resource problems in strategic management is to actively involved many managers and employees' as possible in the process. Although time-consuming, this approach builds understanding, trust, commitment and ownership and reduces resentment and hostility. The true potential of strategy formulation and implementation presides in people.

The firm's external opportunities and threats on the one hand and its internal strengths and weaknesses on the other. In Human Resource Strategic management, the strategist tries to achieve a competitive advantage for his organization. The competitive advantage may be in the form of low cost relationship in the industry or being unique in

the industry along dimensions that are widely valued by the customers in particular and the society at large. And so that they can obtain a competitive edge by becoming a low-cost leader or a differentiator puts a heavy premium on having a highly competent and committed team for human resources. To quote Charles Greer,

In a growing number of organizations, human resources are now viewed as a source of competitive advantage. There is greater recognition that distinctive competencies are obtained through highly developed employee skills, distinctive organizational cultures, management processes and systems.

The role of human resources in enabling the organization to effectively deal with the external environmental challenges, the human resource management function has been accepted as a strategic partner in the formulation of organization's strategies and in the implementation of such strategies through human resource planning, employment, training, appraisal and rewarding of personnel. An organization's recruitment, selection, training, performance appraisal, and compensation practices can have a strong influence on employee competence is very important. The following points should be kept in mind :

1. Recruitment and selection: The workforce will be more competent if a firm can successfully identify, attracts, and select the most competent applicants.

2. Training: The workforce will be more competent if employees are well trained to perform their jobs property.

3. Appraisal of Performance: The performance appraisal is to identify any performance deficiencies experienced by employees due to lack of competence. Such deficiencies, once identified, can often be solved through counselling, coaching or training.

4. Compensation: A firm can usually increase the competency of its workforce by offering pay and benefit packages that are more attractive than those of there competitors. This practice enables organizations to attract and retain the most capable people.

PART 2
The South African wine industry

Chapter 5

Methodology

This chapter provides the research information by explaining the methodology employed in the course of investigation and the sampling criteria adopted. It also illustrates the validity and the limitations of the investigation, before results are showed in the next chapter.

Sampling and Research Data

Exploratory data was initially collected over a period of 6 months in 2011-2012. This involved 12 interviews with wineries operating in different regions throughout South Africa. The scope of the investigation was set to concentrate on firm's initial as well as continuing business practices oriented to the winery growth. With the hope of thoroughly exploring the validity of the derived propositions, it was planned for the focal investigation to adopt a sampling strategy which could facilitate this study's adoption of comparative analysis across wineries having different characteristics. As such, five factors had been adopted in composing the sampling strategy:

1. Winery's size
2. Export shares
3. Range of business
4. Year of operations
5. Major market

General information of the sampled wineries is illustrated in Table. The process of recruiting the 12 firms for conducting the focal study involved further sources of information than just the selection criteria listed above. It included the South Africa Association database and information drawn from the respective company websites. For conducting the focal investigation, candidates were contacted by sending email invitation and then with a frontal interview where was possible, for 3 of this 12, the interview was conducted by Skype or telephone. Figure 1 below shows the location of the candidates throughout South Africa.

Throughout sampling difficulties were faced by the researchers. For instance, lack of interests from some wineries conducted such no answering e-mail or the presence of gatekeepers in some cases, characterized the recruiting process. Furthermore, budget limitations, time and distance constrains made it difficult for the research team to interview winery owners nationwide.

	Winery's size	Export Shares	Range of business	Years of Operation	Major Markets
<i>First Winery</i>	Medium	96%	Winemaking	30	South Africa, US, UK,
<i>Second Winery</i>	Small	5%	Winemaking, Cellar door	6	South Africa
<i>Third Winery</i>	Small	50%	Winemaking, Cellar door	30	South Africa, Lesoto, Namibia
<i>Fourth Winery</i>	Small	32%	Winemaking, Wine Club	10	South Africa, Namibia
<i>Fifth Winery</i>	Small	Not Available	Winemaking, Wine Tourism	8	South Africa, Mozambico, Lesoto
<i>Sixth Winery</i>	Small	Not Available	Winemaking, Wine Tourism	26	South Africa, UK
<i>Seventh Winery</i>	Large	90%	Winemaking, Cellar door	9	South Africa, UK, Netherland, North Europe
<i>Eighth Winery</i>	Medium	84%	Winemaking, Cellar Door, Wine Tourism	22	South Africa, China
<i>Ninth Winery</i>	Large	75%	Winemaking, Cellar Door, Wine Tourism	48	South Africa, Japan, China, Honk Kong
<i>Tenth Winery</i>	Large	80%	Winemaking, Wine Tourism	20	South Africa, Europe
<i>Eleventh Winery</i>	Medium	30%	Winemaking, Wine Tourism	22	South Africa, US, UK, Australia
<i>Twelfth Winery</i>	Small	Not Available	Winemaking, Cellar door	Not Available	South Africa, Lesoto, Namibia

Figure 11: General information of the sampled firms

Data collection

The general process of data collection was performed via conducting in-depth interviews as it had a better alignment with the research objectives of the focal investigation. To cope with the unreliability of the human memory, where possible, these interviews were taped and other notes and transcripts made of these interviews and other meetings which occurred. However, 7 candidates preferred to have a conversation without being recorded, due to the strategic relevance of the information treated. The unstructured interviews meant that interviewees had full liberty to discuss opinion on particular issues. This was made possible through asking open-ended questions, which meant that respondents were free to answer according to their own preferences. Predominantly questions were based upon matters such as reasons which led establishing the winery, major barriers faced when entering the market(s), practices employed to understand the market(s), and support required to achieve business goals.

Due to the exploratory nature of this research, the desired outputs of this investigation are therefore novel knowledge regarding the patterns which influence the winery's growth, which can be far more effectively generated by using qualitative methods of investigations (Eisenhardt, 1989; Yin, 1989; Crouch and McKenzie, 2006). As a result, this study decided to choose the method of interviewing for information collecting as it is superior for gathering "authentic insights into people's experiences" (Silverman, 1993, p. 91), "whether or not these have been impacted by the enquirer" (Merton, Fiske & Kendall 1956, p. 12). In line with that, Appendix A provides a synthesis of the case selection method drawn from the process of building theory from a case study research presented by Eisenhardt (1989). Moreover, application of qualitative data has been acknowledged as reliable and valid method when building theory from case study evidence. Examples of qualitative case study research include Burgelman's (1983) management of new ventures, Sutton and Callahan's (1987) exploring causes of bankruptcy in Silicon Valley, and more recently Thomas (2003) highlights the adequacy of inductive approach for qualitative data analyses. Furthermore, it is recommended that an interview is a better method of obtaining quality data efficiently (Marshall & Rossman, 1995).

Validity and Reliability

To maximize the content validity and reliability of the research, a strategy of triangulation was used throughout for data testing which involved checking different information source through additional written data and websites. For instance, the validity in this research has guaranteed by adopting the interpretation suggested by Denscombe (2007, p. 297) where the concept is defined as “the extent to which qualitative research data... ..are accurate and precise”. Furthermore, the focal study has followed firstly the work of Shah and Corley (2006) and offered a detailed explanation about the sampling strategy, the research methods for reliability purpose. Therefore, accuracy has been ensured by following the principles of Carter and Little (2007), where research reliability is interpreted as repeatability, this thesis has illustrated Table 6 and Figure 10 to present the features and geographical positions of the candidates within the sample. It enables the future replication of the investigation. Moreover, by guaranteeing the validity of the investigation, this study has again reinforced its reliability, “since there can be no validity without reliability, a demonstration of the former [validity] is sufficient to establish the latter [reliability]” (Lincoln and Guba, 1985, p.316).

Limitations

Despite empirical evidence is at the base of this research, the exploratory nature of this investigation leads also to some weakness. For instance the objective impossibility to generalize the results obtained due to the restricted dimension of the sample collected. Furthermore, issues related to the ethical behavior of the respondents such as honesty, truthfulness in providing data might interfere with the investigation objectives (Marshall & Rossman, 1995), as well as misinterpretation or distortion in reporting the data (Cavana, Delahaye & Sekeran, 2000). Despite this risk has been minimized by following precise procedure (as showed in the prior paragraph), the transcript of the interviews could not be sent to the original candidates for removing

potential errors due to the time constrains. Furthermore, this focal study is deficient in its sampling processes. In fact, because of both money constrains and remoteness of some wineries, the research team based in Cape Town was impeded to interview candidates from Gauteng (the up of South Africa).

The last chapter showed the methodology undertaken to interview the candidates in this research. Information about the sample and description about the process adopted for collecting data were provided. Nevertheless, this chapter shows the results obtained after conducting 12 interviews with owners of South African wineries. As discussed in previous Chapter, appreciation of South African rand along with the contextual increase of the export of bulk wine, have heavily impacted the industry affecting the wineries' business performance. The previous chapter begins by comparing issues encountered in the course of the literature review to the findings from the interviews. Subsequently this information was used to explore how winery owners' background influences the decision making process and business model employed. To respect the relevance of the data collected, privacy has been guaranteed by treating information and presenting result on an anonymous basis.

The last paragraphs showed the methodology undertaken to interview the candidates in this research. Information about the sample and description about the process adopted for collecting data were provided. Nevertheless, this chapter shows the result obtain after conducting 12 interviews with owners of South Africa Wineries.

Chapter 6

The strategic management process in the wine industry

6.1 The South Africa environment

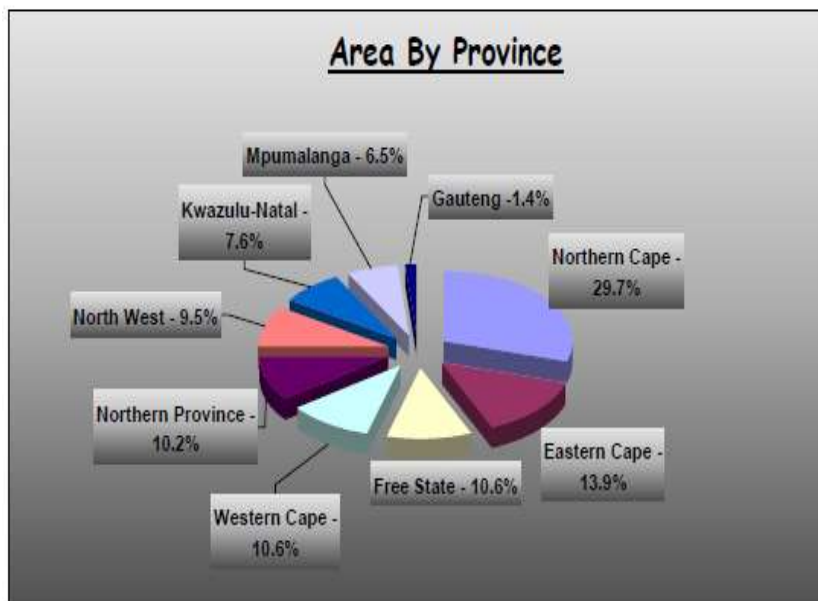
Geography

South Africa is situated at the southern tip of Africa. South Africa shares borders with Namibia, Botswana, Mozambique, Zambia, Swaziland and Lesotho. The Limpopo river forms the northern border between South Africa and Zimbabwe. Its surface area is 1219090 km. South Africa has a coastline of 3000 km, which means that the country boasts a number of splendid beaches.

South Africa has nine provinces; the Eastern Cape, Free State, Gauteng, Kwazulu-Natal, Mpumalanga, Northern Cape, Northern Province, North West and the Western Cape. The Northern Cape is the largest province and constitutes 29.7% of South Africa's surface area. Gauteng is the smallest province and only makes up 1,4% .of the surface area of South Africa.

South Africa has a warm, temperate climate, although the climate varies from region to region. The Western Cape for example has a Mediterranean climate, Kwazulu-Natal a sub-tropical climate, Gauteng has a more temperate climate whereas arid, semi-desert climatic features prevail in the Karoo. South Africa enjoys summer rainfall and has an average rainfall of 464mm. The Western Cape has the highest rainfall in winter, with an average winter rainfall of 82mm.

South Africa has a huge variety of fauna and flora, some nine hundred species of birds and an equally rich marine life. South Africa is also famous for its wildlife and has nineteen National Parks. The largest of these, the Kruger National Park is the size of New England.



History

The African continent is known as the birthplace of human life and Southern Africa has been home to humans for more than 100 000 years. South Africa has a very

rich history, one that is like in many other countries, dominated by a struggle between various groups of people for land and the natural resources of the country. A number of historical events have all played a role in shaping South Africa's political history and its unique social and cultural life. These are amongst other things the advent of colonialism and the settlement of Europeans in South Africa, the mineral revolution and the Anglo-Boer war. South Africa was originally inhabited by the Khoekhoe and San people who lead a nomadic lifestyle based on hunting and gathering. They were later joined by the Bantu-speaking people who arrived in the region from further up in Africa. These two groups however settled in different parts of South Africa. The Khoekhoe and San people settled in the western desert and south-west regions whereas the Bantu-speaking people settled in the coastal and eastern regions. This arrangement however was soon to be disrupted by the arrival of the first colonial settlers in the Cape.

South Africa was a regular stop for European sea-farers en route to India. In 1652, the Dutch established the Dutch East India Company in Cape Town and were thus the first Europeans to settle in South Africa. The colonial authorities provided them with farms which they used to grow wheat and grapes for wine production. Their need for labour to work these farms, soon saw the introduction of the slave trade in South Africa where slaves were imported from East-Africa, Madagascar and the East Indies. However these farmers did not settle in the Cape, but moved further up into South Africa. Their journeys eventually brought them into contact with the Bantu-speaking people which resulted in conflict and warfare over land. In 1795, the British occupied the Cape as a strategic base and in 1820, the first British settlers arrived in South Africa. At the same time, the original settlers, the Dutch or the trekboere as they came to be known, extended their settlement beyond the Cape and eventually occupied what came to be called the Transvaal and the Orange Free-State in which they applied the principles of racially exclusive citizenship. So, the trekboere came to dominate the Transvaal and the Orange Free-State while the British took over the Cape and later Natal. The discovery of diamonds on the Vaal River and later gold on the Witwatersrand in the Transvaal, or the mineral revolution, however soon brought these groups into an intense battle for dominance over the South African territory and also altered the existence of African people. The mineral revolution brought about a demand

for cheap labour to work on the diamond and gold mines. Africans were soon forced off the land that they still occupied through means such as taxation and pass laws as well as forceful dispossession of land, and were forced to go and work on the mines.

The battle between the trekboere and the British for dominance over the mineral resources soon culminated in the Anglo-Boer war which lasted for three years, between 1899-1902. Africans were also drawn into the war and many supported the British who promised to improve their situation should they win the war. The British eventually did win the war, but soon forgot the promises made to the Africans. Instead, the period following the war saw a tighter alliance between the Boers and the British in order to drive the interests of the white minority. This culminated in the unification of the four colonies, the Transvaal, Orange Free-State, Natal and the Cape into the Union of South Africa on the 31 May 1910. This gave birth to the policy of Segregation under which the right to citizenship of South Africa was reserved for whites only. However, all this happened within the context of resistance from black people who forced their way into the cities and towns from which they were excluded. This resistance gave birth to the formation of the African National Congress in 1912. The government's response to this resistance was to strengthen segregationist policies which resulted in the passing of the 1913 Land Act. This act established separate homelands/Bantustans for Africans and reserved 13% of South Africa's land for Africans and the rest for the white minority. Other laws such as the Job Colour Bar reserved skilled work for whites only and the Pass Laws ensured that Africans could gain access to South Africa in order to provide their labour, but prevented them from settling permanently in "white" South Africa. All these laws were designed to exclude blacks from South Africa and prevent them from enjoying the resources and wealth of South Africa while building unity between Afrikaners and the British.. However, this unity was very superficial and divisions persisted. Afrikaner nationalism grew after 1910 and this in many ways facilitated the formation of the National Party in 1914. The National Party appealed to the interests of the Afrikaners who were left impoverished by the Anglo-Boer War. In 1948, the National Party won the general election. Under the National Party, segregation was further entrenched and extended and gave birth to the even more oppressive system of Apartheid. The Apartheid system in many ways was to designed to advance the interests

of the white minority and specifically those of poor Afrikaners. The state played an active role in improving the economic condition of Afrikaners. Apartheid saw the introduction of a number of discriminatory laws such as the Population Registration Act which divided the South African population into different racial categories, the Group Areas Act which reserved certain residential areas for specific racial groups and saw the forced removal of millions of black people from so-called white areas and the Immorality Act which made marriage between blacks and whites unlawful.

All this happened within the context of massive resistance which saw different groups like the Indian Congress, the African National Congress and the Coloured People's Congress forming an alliance to combat the oppressive Apartheid system. This was met by even more repression by the state which resulted in tragedies such as the Sharpeville Massacre in 1961 in which 69 people were killed during a march against the pass laws. The state launched a serious attack on the leaders of the liberation movement and in 1963 during the Rivonia trial 30 of them, including Nelson Mandela, Walter Sisulu, Ahmed Kathrada and Govern Mbeki were sentenced to life imprisonment on Robben Island. This caused a temporary slow-down in the political resistance. However in the 1970's there was a resurgence in resistance following the birth of the Black Consciousness Movement under Steve Biko. This culminated in the Soweto uprisings of 1976, which saw thousands of young people protesting against the government's plan to change their language of instruction to Afrikaans. This climate of resistance intensified and persisted through the eighties and early nineties with the establishment of the United Democratic Front which eventually gave birth to the Mass Democratic Movement. This movement constituted a number of civic organizations, political organizations, workers and trade unions which were united in the struggle against Apartheid. This resistance combined with pressure from the international community in the form of economic and other sanctions, eventually forced the National Party government to sit down and negotiate with the leaders of the democratic movement. After a very long negotiation process which threatened to break down on more than one occasion, South Africa had its first democratic elections in April 1994. The African National Congress became the majority party and won 62% of the votes.



South Africa's post-apartheid growth can be separated into three phases. The **first phase** took place during the end of apartheid when the impact of the sanctions and the instability resulting from the end of apartheid led to a decrease in GDP in 1992 and

anemic growth in 1993. The **second phase** took place between 1994 and 2000, when Mandela became president and adopted a strategy of economic liberalization. Government reduced tariffs from 27.5% in 1990 to 7% in 1997, relaxed foreign exchange controls, and reduced government spending as a percent of GDP from 20.2% in 1992 to 18.3% in 1995 (Werker, 2007). Aside from a slight decrease in GDP in 1998 resulting from the Asian Financial crisis, the economy demonstrated strong and steady growth. The **third phase** started in 2000 when the Central Bank began targeting an inflation rate between 3% and 6%. This policy brought down inflation from 9.2% in 2002 to 4.5% between 2004 and 2006 (EIU, 2009) and South Africa experienced growth, exceeding 6% each year between 2004 and 2007. Admittedly much of that growth is attributable to the increase in global commodity prices.

In 2006, President Mbeki launched the Accelerated and Shared Growth Initiative for South Africa (AsgiSA) with the objective of reducing “unemployment and poverty, while increasing the country's gross domestic product growth rate to a sustainable level of 6% by 2010, through marshalling government and private resources to ‘eliminating’ constraints.” The identified constraints were: the overvaluation and volatility of South Africa's currency, an inadequate national infrastructure, a shortage of skilled labor, barriers to entry, limits to competition and limited new investment opportunities, a cumbersome regulatory environment and deficiencies in state organization, capacity and leadership (AllAfrica.com, 2009). Many of these constraints are in-line with those identified by a team of researchers from Harvard’s Center for International Development.

AsgiSA enabled the government to allocate \$87 billion to improve infrastructure (AllAfrica.com, 2009), which has proven to be astute given the global economic downturn since the funds also serve as a fiscal stimulus. Less progress has been made on initiatives outside of infrastructure, such as increasing participation in the formal economy.

People and Culture

South Africa has a population of 40.58 million. The female population is slightly bigger (52%) than the male population (48%). Kwazulu-Natal has the largest population (8.4 million), followed by Gauteng (7.3 million). The Northern Cape has the smallest population, with 840 321 people residing in this province.

Until 1991, under the Population Registration Act, the South African population was divided into four main categories, Africans, Whites, Coloureds and Asians. Africans make up 76.7% of the South African population, whites 10.9%, Coloureds 8.9% and Indians 2.6%

The urban population is slightly bigger than the non-urban population, with 53.7% of the South African population being urbanised. The Eastern Cape, Kwazulu-Natal, Mpumalanga, Northern Province and North-West are the provinces with a bigger non-urban than urban population.

South Africa has an average population density. Population density is a measure of how close people live together. South Africa has a population density of 34 people per square kilometer. Compared to countries like Singapore, where the population density is 5283 people per square kilometer, this is not high.

The South African population is relatively young, with 54% of the population under the age of 25 and less than 10% of the population 60 years and older. The population growth rate of the country has been decreasing for the past three decades, from 2.8% in the 1970's and 80's to 2.1% in 1999. The HIV/AIDS pandemic poses an even greater threat to the growth of the population and it is reported that most of the adult deaths in South Africa today, is linked to HIV/AIDS. This could seriously reduce the size of the South African workforce.

South Africa is a multi-cultural society. Although the laws that divided people into formal racial categories have been abolished, informal categorization still persist as many people continue to define themselves and others in terms of these categories

The African population is made up of different ethnic groups, for example the Nguni people who constitute 2/3 of the population, the Sotho-Tswana people, the

Tsonga and the Venda. The other groups that make up the “rainbow nation” as South Africa is often referred to, are white people who are mainly descendants of the Dutch, French, English and German settlers, colored people who are a mixture of the descendants of the early settlers and the indigenous people, Indian people who are the descendants of the Indians who were brought from India to work on the sugar plantations in South Africa as well as a big immigrant population from the rest of Africa, Europe and Asia

This diversity is captured in all other aspects of South African cultural life, in a huge variety of homegrown musical forms, such as choral music, township jazz and blues, kwela music and kwaito as well as an equally wide range of dance forms.

The country’s rich natural life and history were formally recognized when three sites in South Africa were declared World Heritage Sites. These are the Sterkfontein caves, Robben Island and the St. Lucia Lake.

Cultural villages such as the Basotho cultural village, the Makhosini cultural village and the Lesedi cultural village provide tourists as well as locals with an opportunity to learn more about different cultures in South Africa. South African arts and crafts are world-renowned and are exported all over the world. The arts and craft industry provides employment to close to one million people in South Africa.

South Africa has eleven official languages, with the majority of the population speaking isiZulu and isiXhosa. Eighty percent of the population is Christian. Other major religions are Hinduism, Islam and Judaism.

Economy

South Africa is a middle-income, developing country. South Africa forms the hub of economic activity on the African continent –it occupies only 4% of Africa’s landmass, yet it produces 40% of Africa’s output.

South Africa has good infrastructure with well-developed electricity, water and transport networks. South Africa generates more than ½ of Africa’s electricity and has more than 40% of telephone lines in Africa.

The South African currency is the Rand. The value of the rand has decreased by more than 40% against the dollar over the last few years due to the falling gold price as well as developments locally and in the region that have cast a negative light over South Africa. South Africa's stock exchange, the Johannesburg Stock Exchange (JSE) is one of the largest stock exchanges in the world.

Economic growth as measured by the gross domestic product (GDP) has fluctuated over the last few years. Growth in gross domestic product increased substantially in 1996, followed by a dramatic decrease in 1997 and an even further decline in 1998. Annual growth rates picked up somewhat in 1999 and 2000, however these are still well below the 6% growth target as set out in South Africa's macro-economic policy, the Growth, Employment and Redistribution (GEAR) policy.

The structure of the South Africa Economy

The South African economy is made up of three major groups of sectors; the *primary sector* which includes agriculture, forestry, mining and oil exploration, the *secondary sector* which includes manufacturing, electricity, gas, water and construction and the *tertiary sector* which includes services for example retail trade. The biggest sector is Manufacturing which contributes 20% to the South African GDP, followed by Finance, Real Estate and Business (18%), General Government Service (15%), Wholesale, Retail, Hotels and Restaurants (14%), Transport and Communication (11%), Mining and Quarrying (6%), Agriculture, Forestry and Fishery (5%), Electricity (4%), Construction (3%), Other producers (3%) and Other services (3%).

The last few years have seen some major changes in the structure of the South Africa Economy. The primary sector, traditionally formed the basis of the South African economy, with mining and agriculture being the major contributors to the South African GDP. However since the mid – nineties, the primary and secondary sectors have declined dramatically, accompanied by a rapid increase in the tertiary sector.

Recent economic growth

South Africa is the largest economy in Africa with total GDP at \$280 billion in 2007, well ahead of oil-rich Nigeria at \$166 billion (Economist, 2009). It is the 2nd wealthiest country in Africa, behind Botswana, with a per capita income of \$10,400, and is much wealthier than its neighbors. The average Sub-Saharan African (SSA) country has a per capita income of \$2,800, roughly one-quarter that of South Africa's (EIU, 2009). When compared to BRIC countries, South Africa has roughly the same GDP per capita as Brazil (\$10,300), but is poorer than Russia (\$15,900) and richer than India (\$2,900) and China (\$6,100) (EIU, 2009).

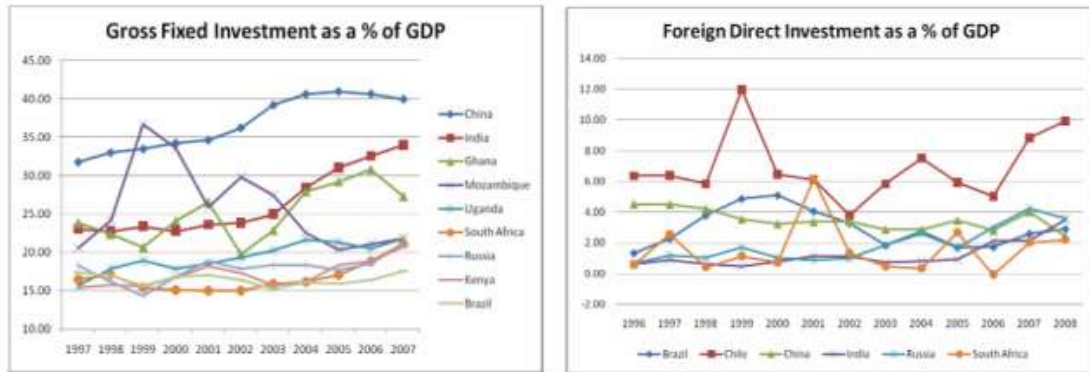
South Africa grew at about the same rate as its neighbors in SSA between 2001 and 2008. It demonstrated solid and consistent growth, averaging 4.1% per year versus 4.8% and 2.1% for SSA and OECD countries, respectively. South Africa has also improved its export performance, increasing its share of world exports from 0.38% in 2000 to 0.50% in 2007 (EIU, 2009).

South Africa's performance, however, appears less robust when compared to that of BRIC countries. Aside from Brazil, which grew slower than South Africa at 3.6% between 2001 and 2008, China, India and Russia all grew faster at 10.2%, 7.5% and 6.5% respectively (EIU, 2009).

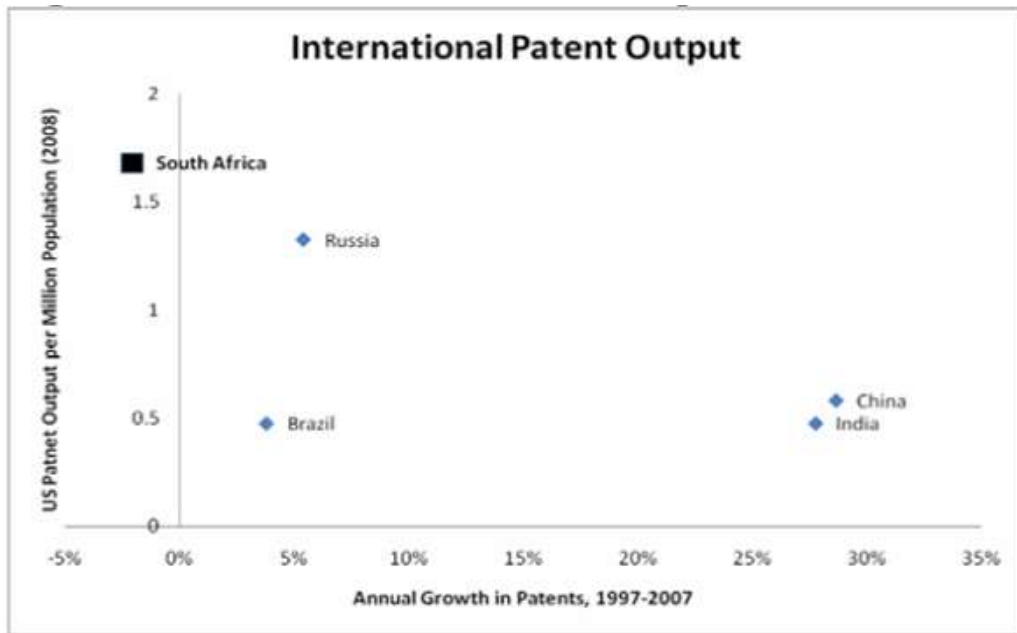
Challenges facing South Africa's economy

While South Africa's economy has been performing well, there are indicators that point to weaknesses in the structure of the economy. Inbound foreign direct investment (FDI) as a percentage of GDP is lower than all BRIC countries with inbound FDI hitting zero percent in 2006 (EIU, 2009). South Africa's Gross Fixed Investment as a % of GDP suggests an opportunity to increase domestic investment, although it has been ramping up in recent years. The recent increase may be driven by infrastructure investments related to AsgiSA. Compared against BRIC countries, South Africa's investment rate is lower than China or India, in the same range as Russia and slightly higher than Brazil. Higher domestic investment could provide additional employment

for a country with chronic underemployment, high unemployment and low labor force participation (Hausmann, 2008).



In addition to the lack of foreign and domestic investment, South Africa's patent output is decreasing. While South Africa's patent output per million people is higher than those of all BRIC countries, it is the only country with a negative patent output CAGR.



6.2 History of South Africa wine industry

As a wine producer, South Africa is considered to be part of the New World, along with the Americas, Australia, and New Zealand. But it has a long history with wine grapes, and its soils are among Earth's oldest. It is fitting that the best of its wines display the ripe fruit character that we typically enjoy from the New World, framed by minerality and earthiness often reminiscent of Old World European wines.

Early History

Portuguese explorer Bartolomeu Dias discovered a sea route to India in 1487. He was the first European to arrive on what Portugal's king named the Cape of Good Hope. The first European settlers did not appear until 1652, when Jan van Riebeeck was sent by the Dutch East India Company to set up a way station on the trade route between Europe and Southeast Asia. Along with other garden staples, grapevines were planted. The first ones did not survive, but vines planted in 1656, believed to have been cuttings from France, Germany, and Spain, produced the first Cape wine, from the 1659 harvest.

Simon van der Stel, the Cape's first governor, arrived in 1679 with expansion plans and the ambition to make good wine. To the east and inland of Cape Town he established the town of Stellenbosch ("van der Stel's bush), now a center for viticulture studies and home to many of the Cape's best known and highly regarded wine producers. In 1685 Van der Stel received a large land grant and founded the Constantia wine estate near the original settlement, with the planting of 100,000 vines, and oak trees to protect them from the gale-force southeasterly winds. By 1692 the wines were noted for their high quality. Many varieties were planted, some with names no longer in use, leaving their identities unknown, but several types of Muscat were grown and both red and white dessert wines were made from them. The red was to become celebrated throughout Europe.

At this time, many French Huguenots had fled to Holland to escape religious persecution. In 1688, about 180 of them were sent to populate and farm the new

outpost, most of them settling in what became known as the Franschhoek (French Corner) Valley, and giving French names to their farms. It is said that van der Stel asked the Dutch East India Company to give passage to those who had experience with grapevines. Today, Franschhoek is a food and wine hot spot, with many top restaurants.

By 1699, the Constantia wines had been exported to Europe and quickly gained a good reputation.

When van der Stel died in 1712, the Constantia estate was divided by three and the vineyards fell into neglect. Hendrik Cloete purchased the portion known as Groot Constantia in 1778, replanted the vineyards, and by 1792 had built a homestead and cellar which are now historical monuments exemplifying the Cape Dutch architecture of the time. The Cloete family held the estate for five generations. In the early 1800s, it achieved a level of worldwide acclaim previously accorded only to the great wine properties of Europe. The legendary sweet red Constantia wine appeared in literature, opera, and the courts of European royalty. Napoleon called for it in exile, and lore has it that he drank it on his deathbed.

Meanwhile, by the end of the 1700s, Dutch power had waned. The British occupied the Cape in 1795 and gained control of it by 1805. In 1815 it officially became a British colony, coincident with the fall of Napoleon and the beginning of over a century of world domination by what became the British Empire. During the Napoleonic Wars from 1803 through 1815, Great Britain no longer had access to French wine and encouraged wine production in its new possession. South African wine accounted for 10% of British wine consumption by 1822, and enjoyed preferential import tariffs from 1825 until 1860. From the late 1700s to the mid 1800s, South African wine basked in its heyday.

19th Century

Because South African wine was now significantly cheaper for the British, the South African wine industry took advantage of the opportunity to make and export low quality wine, eroding its reputation with the exception of Constantia. The difficult 1825

vintage began a slow decline in the fortunes of South African wine. The downturn accelerated in 1859, when the vineyards suffered from powdery mildew so severe that production was reduced by over 90%. Britain's tax protection ended in 1860, erasing the price advantage over wines brought in from France and elsewhere in Europe. The Groot Constantia wines won medals worldwide, but Jacob Cloete went bankrupt and the estate was purchased by the government in 1885. The phylloxera louse struck the Cape during this period, and though there is debate as to whether it was first noted in 1866 or 1886, it necessitated vast replanting of the vineyards. In haste to rebuild the industry, high-yielding, lesser-quality varieties were grafted to pest resistant American rootstock. The Anglo-Boer war at the turn of the century then cut off export trade, and the country was awash in an excess of wine.

20th Century

The Co-Operative Winegrowers' Association (Ko-operatiewe Wijnbouwers Vereniging van Zuid-Afrika or KWV) was founded as a company in 1918, becoming a co-op in 1924. It was established to address the surplus problem, ostensibly to assist growers by guaranteeing purchase and pricing for their fruit, much of which was used for distillation. In time, it became a government sponsored regulator of the entire wine industry, setting production quotas and limits, mandating where grapes could be grown, and controlling importation and propagation of vine cuttings. Ultimately, it supported high-yield bulk production and did little to encourage the pursuit of higher quality.

In 1925, Viticulturist A.I.Perold crossed Pinot Noir with Cinsaut, a southern French red grape variety sometimes called Hermitage in South Africa. The result, named Pinotage, is South Africa's own vinifera grape. The first bottling did not appear until 1961. With no European benchmark, and no particular success with either of the parent varieties, quality was wildly inconsistent. Some truly awful wine, much of which was exported, convinced many people to avoid Pinotage. Now, with lower yields, better site selection, and healthy vines, there are more good examples.

The Nederburg wine farm in Paarl was purchased in 1937 by Johann Graue, who began a history of innovative winemaking and viticultural practices. The winery was highly acclaimed and in 1975 held the first Nederburg auction, devised as a means of distributing the winery's reserve production. Held annually ever since, the auction showcases many of the Cape's fine and rare wines.

1959 saw the introduction of Lieberstein, a semi-sweet Chenin Blanc blend which became the world's best selling wine brand in the mid-sixties. In the mid-1970s, South Africa began its entry into the modern wine industry. The Wine of Origin system of regional definitions was introduced in 1973.

The Plant Improvement Scheme was started in 1976 by the KWV, evolving away from that organization to become the Vine Improvement Programme. Now overseen by the government Ministry of Agriculture's Wine and Spirit Board, it encompasses clonal selection, rootstock improvement, and the matching of these to appropriate terroir. In the early 80s, Chardonnay and Sauvignon Blanc vines were imported.

The Cape Wine Academy was founded in 1979, to promote awareness and appreciation of South African wine. Currently, it offers courses and tastings to the public, and training and certification for professionals.

The Cape Winemakers' Guild was formed in 1984, to advance vineyard and cellar techniques. Membership, by invitation only, must be maintained by consistently making wine that meets the self-imposed standards of the group.

Unfortunately, progress and modernization were impeded by apartheid, the draconian racial separation policy instituted in 1948 by the Afrikaner-directed National Party when it won control of the government. This regime attracted United Nations condemnation in 1962, followed by trade sanctions and an arms embargo, and kept the country isolated from the international community. While the rest of the world scorned South Africa and its wine, lack of exposure left it unprepared to enter the market upon the advent of democracy. Not having access to wines, knowledge, or plant material from

elsewhere had narrowed perspective and slowed development. There was a lot of catching up to do.

The political changes, when they arrived, proceeded very quickly. Nelson Mandela was released in 1990 from 27 years of imprisonment. An interim constitution was drafted by 1993, and sanctions were lifted. The 1994 election, in which the black majority at last had the right to vote, began South Africa's new identity as a democracy.

The role of the KWV as industry-wide regulator was dismantled, opening the door to fine winemaking. No longer restricted in the choice of where to grow, what to plant, and how much to produce, quality-minded vintners began exploring new growing areas and discovering how to make the most of existing ones. Many of the diseased vineyards were replanted with healthy vines and with careful consideration of which varieties were best suited to the site.

The KWV became a public company in 2003.

The old Constantia estate, over 6000 acres, is now broken up into Groot Constantia, Klein Constantia, Buitenverwachting, Steenberg Estate, and Constantia Uitsig. Klein Constantia began making Vin de Constance, a modern version of sweet Constantia, in 1986. Groot Constantia's Grand Constance was first released in 2003. Both are made from Muscat de Frontignan, believed to have been the primary grape of the original world-renowned wine.

21st Century

From 1996 to 2005, the number of wineries more than doubled. Most of the growth is in small, sitedriven properties. Though the majority of production is still by co-ops, it is no longer predominantly grapes for table use and wine for distillation. The percentage of grapes made into wine for consumption by the public rose from 30% in 1990 to 70% in 2003.

Winegrape vineyard planting and replanting is extensive. Virus-free rootstock now available is replacing unhealthy vines that have been torn out. Better and more varied clones, better matching of location to varietal, improved vineyard practices and

newly-explored planting areas are also advancing this renaissance. The percentage of red grapes to white increased from 29% to 44% from 1999 to 2009. Overall, as of 2009, more than half of all red grapevines are under 10 years old.

Wines of South Africa (WOSA), a non-profit, non-governmental organization, was established in 1999 to build the image and demand for South African wine. It represents all exporting producers, participates in international wine events, and promotes wine tourism to South Africa. It is funded by a per-liter levy on exported wine. Its Cape Wine exposition in Cape Town, first held in 2000, has brought buyers, importers, and journalists from around the world.

The wine industry is involved with many programs based on social and environmental responsibility. The government-instituted Black Economic Empowerment initiative was started in 1997 to address the unequal distribution of wealth and opportunity in South Africa. Ten years later, the South African Wine Council drafted a charter to outline goals and strategy for participation by wineries.

The Integrated Production of Wine program, established in 1998, consists of voluntary, self-regulated guidelines ensuring environmentally sustainable vineyard and cellar practices. Over 90% of exporting producers adhere to this system.

The Wine and Agricultural Industry Ethical Trade Association codifies employment practices. Begun in 2002 as a wine industry organization, it has expanded to the broader agricultural sector. 2004's Biodiversity in Wine Initiative has already resulted in a total of land under conservancy by winegrowers that is greater than the vineyard total. Land vegetation of the world is divided into six floral kingdoms, South Africa's Cape Floral Kingdom being the smallest, the most diverse, and the only one contained in one country. It is comprised of eight protected areas covering well over a million acres, and was declared by UNESCO in 2004 to be a World Heritage Site, of "outstanding universal significance to humanity." As it covers the Mediterranean climate regions of the country, much of it lies in winegrowing areas.

The Fair Trade movement, started in the 1940s, now works globally against poverty and exploitation. Involvement with wine is new, beginning in 2008 with Chile,

Argentina, and South Africa. Because of their legacy of apartheid, South Africa's Fair Trade guidelines are tied in with economic empowerment programs for previously disadvantaged workers.

As of 2010, an alliance between the Wine and Spirit Board, the Integrated Production of Wine program, the Biodiversity and Wine Initiative and Wines of South Africa has been created. Called Sustainable Wine South Africa, it will certify sustainable production of wine, and enable traceability to vineyards and their growing practices.

There is strong momentum in South Africa for fine wine. Many small producers are thoughtfully crafting wines from still-young vineyards on carefully chosen sites. They are re-educating themselves about how to get the best from older vineyards and warmer locations.

New growing areas are being established along the western and southern coastline, well beyond the central area that includes Stellenbosch, Franschhoek and Paarl. There are associations to advance and promote individual varieties including Pinotage, Chenin Blanc, Sauvignon Blanc and Shiraz. Italian, Spanish and Portuguese grapes are also being explored.

Rhone-style blends, red and white, are becoming popular, as are blends of classic Bordeaux varieties, Cabernet Sauvignon based for the reds, Sauvignon Blanc with Semillon for the whites. An emerging category based on Chenin Blanc combined with white Rhone varieties, Sauvignon Blanc or Chardonnay is creating some of the most exciting wines in the country.

South African wines offer a bridge between the all-too polarized styles familiar to wine drinkers today. These wines have improved exponentially since democracy was established in 1994. They have joined the modern international wine community, delivering high quality at reasonable prices, with true greatness just around the corner.

Of the 1089 million liters produced in 2008, 70.5% was used for wine production, 6.5% for the production of cognac style brandy, 7.5 % for grape concentrate

and grape juice production and the balance (15.5 %) was used for distilling (SAWIS, 2009).

According to the SAWIS commissioned macro-economic study of the wine industry on the Western Cape in 2003, the total turnover of the South African wine industry in 2003 amounted to R10.675,27 million. Of that amount R3.153,40 million was exported directly. An additional amount of R4.198.37 million was generated indirectly through wine tourism (Conningarth consultants, 2004).

At the time of the study, an attempt was made to estimate what the effect would be on the country's economy if the wine producing activities in the Western Cape would cease to exist — it was concluded in broad terms that local businesses would lose R7.0521,87 million for supplying raw material to this industry (Conningarth consultants, 2004).

The wine industry, including tourism, contributes R22.549 million to the annual GDP of the country. The wine industry has its roots in the Western Cape and it is estimated that 70% of the industry's activities have a direct impact on the Western Cape's economy (Conningarth consultants, 2004).

The wine industry supports employment opportunities for 256.908 people including tourism (Conningarth consultants, 2004). The Cape wine lands is said to draw 43% of all tourists to South Africa (Ewert, 2005).

Although up-to-date information regarding the financial contribution of the industry is not available, SAWIS statistics indicate that the industry has grown significantly in terms of production and in terms of exports. By implication it is accepted that the contribution to the annual GDP of the country, in terms of employment opportunities and in terms of tourism and other businesses has increased significantly too. A follow-up report has been commissioned and is expected to be made available to the industry in 2010.

Chapter 7

Corporate level strategy in the South African wine industry

The aim of the research was to find ways of enhancing and managing consolidation and branding in the South African wine industry. It sought to identify what needs to be in place to develop competitive South African premium brands. This dissertation is a presentation of the research results.

7.1 Overview of the global wine arena

In order to provide a snapshot of the global wine market, tables and graphs depicting the area under vine, wine production, wine consumption, wine exports and wine imports are provided.

The information underlying substantiating these graphs was derived from the South Africa Information Service Website (www.sawis.co.za) and is based on the universal provided by OIV (International Organization of Vine and Wine).

RANK	COUNTRY	HECTARES
1	Spain	1.082.000
2	France	825.000
3	Italy	798.000
4	Turkey	500.000
5	China	490.000
6	USA	398.000
7	Portugal	243.000
8	Argentina	228.000
9	Romania	205.000
10	Chile	200.000
11	Australia	170.000
12	Greece	115.000
13	Germany	102.000
14	South Africa	101.016
15	Bulgaria	79.000

For the second year, the development of the European Union vineyard has been affected by the implementation of new community regulations. From 2008/2009 until 2010/2011 inclusive, this common market structure allows wine producers to receive a

permanent uprooting subsidy, authorizing the uprooting of 175 000 hectares over 3 years.

Spain is still the main country affected, with an overall reduction in its vineyards of 31 000 hectares (2.8%). The Italian vineyard also suffered an overall reduction estimated to be 14 000 hectares including approximately 11 000 hectares that can be attributed to the EU premium. France, which before the implementation of the current community regulation, had started to reduce its vineyard using the premiums provided for in the previous community system, sees its vineyard reduced by a further 12 000 hectares.

The vineyard outside the EU seems relatively stable for the third consecutive year, except for Chilean vineyard continuing to grow at a steady pace. The Turkish and South African vineyards continue to decrease. Total area under vines in China is estimated at 490 000 hectares. The total worldwide area under vines amount to approximately 7.5 million hectares.



Figure World area under wine

7.1.1 South Africa vs Old world

Chardonnay and Cabernet Sauvignon are the leading wine grape varieties and represent 36.2% of the total area under vines South Africa’s area under wine grape vines amount to 101 016 hectares in 2010. The leading wine grape varieties, Chenin blanc and Carbernet Sauvignon, represent 30.5% of the total area under vine.

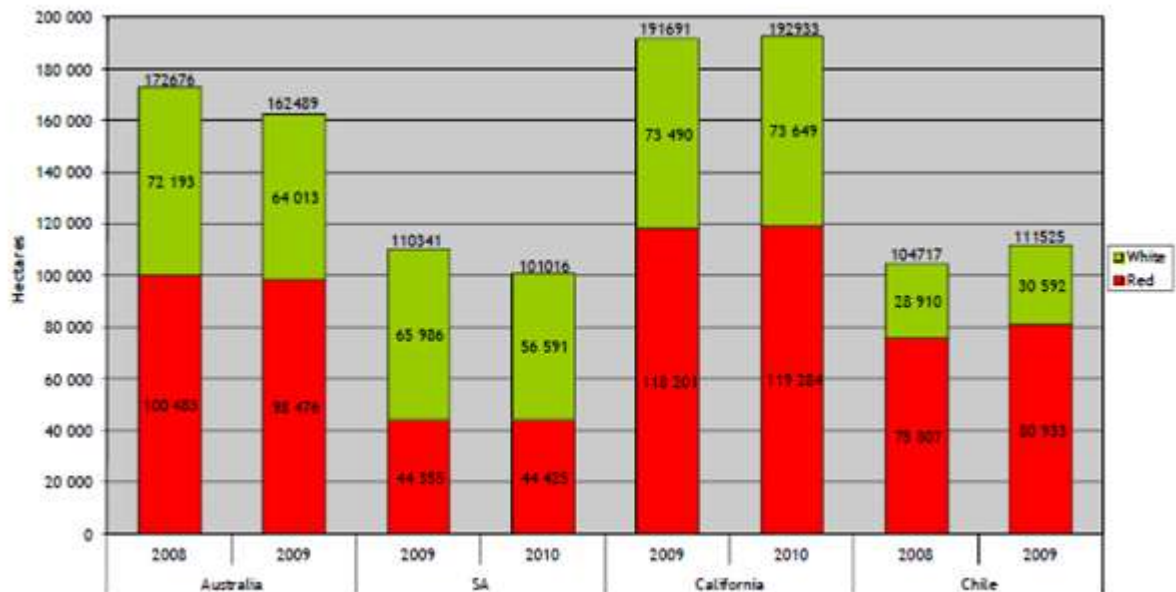


Figure Status of wine grape vines for selected new world countries⁵¹

⁵¹ SAWIS California Grape Acreage Report Catastro Viticola Nacional (2010 information not available) ABS Wine & Grape Industry 1329.0 (2010 information not available)

Production vs consumption

Italy is the world leader in terms of volume production,

TOP 15 COUNTRIES IN 2010 - WINE PRODUCTION (LITERS)		
RANK	COUNTRY	VOLUME
1	Italy	4.496.300
2	France	4.484.000
3	Spain	3.399.900
4	Usa	1.962.000
5	Argentina	1.625.000
6	Australia	1.124.000
7	South Africa	984.800
8	Chile	884.400
9	Germany	718.500
10	Portugal	676.000
11	Romania	495.700
12	Greece	310.000
13	Hungary	250.000
14	Brazil	245.400
15	New Zealand	190.000

Wine production in 2010 for both EU-15 and EU-27 member states is one of the lowest productions in the last 15 years. The 2010 wine production (15 290 million litres) did not even reach 2009 levels (16 289 million liters). Portugal and Bulgaria experienced a growth of 89.2 million liters and 2.9 million liters respectively. A significant decline in production occurred in Germany, Italy, Austria and Romania.

According to the findings of a VINEXPO study conducted by the International Wine & Spirit Record (IWSR), worldwide wine production grew by 1.78% to reach a

total of 2.828 billion 9-litre cases between 2003 and 2007. And it is estimated that production will continue to grow by 3.38% between 2008 and 2012 to reach 3.022 billion cases (Wine news, 2009). However, a FAS (Foreign Agricultural Service) report dated April 2009 negates these figures and indicates that world wine production is expected to continue trending downward to 250 million hectoliters, down about 5% in 2009 (Foreign Agricultural Service, 2009). EU production is expected to dip as a result of waning consumption and agricultural policy reform aimed at eliminating its oversupply and removing inefficient vineyards. Australian production is forecast down due to drought, low prices and high stock levels (Foreign Agricultural Service, 2009). Figures from the 'Market Insight Report' of January 2009 indicate that there has been a downward trend in world wine production following its peak in 2004. France and Italy are seen as the drivers of this downward trend. The graph below, based on the figures from this report, indicate that while there has been a decrease in the Old World, New World wine production has increased (Global wine supply monitor, 2009).

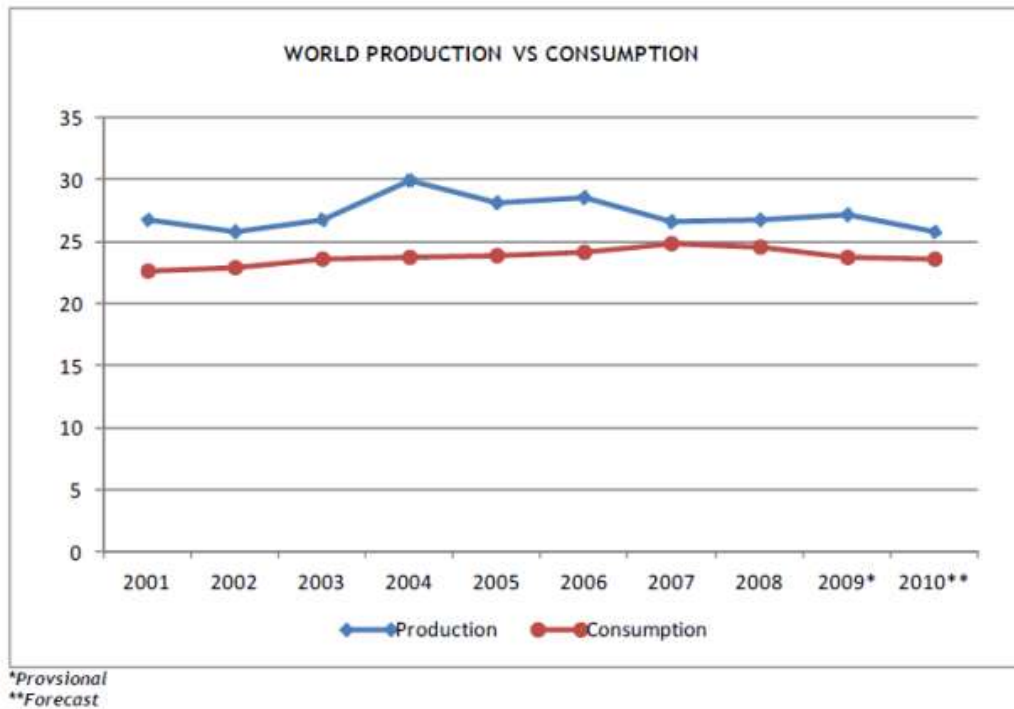
World wine consumption

During the 1980's there was a drop in world wine consumption. The 1990's was relatively unstable. 2001 saw the start of the increasing trend (SAWIS, 2009). Traditional wine producing areas have either seen stabilization or decrease in individual consumption. New producer countries continue to grow individual consumption. Countries which do not produce wine (or only marginally) continue to grow (SAWS, 2009).

RANK	COUNTRY	VOLUME
1	France	3.353.000
2	Italy	2.701.600
3	USA	2.511.000
4	Germany	1.984.800
5	Spain	1.368.600
6	China	1.350.000
7	UK	1.200.000
8	Argentina	1.097.200
9	Russia	1.050.000
10	Romania	580.000

According to the findings of a VINEXPO study conducted by the International Wine & Spirit Record (IWSR), the consumption growth rate will accelerate. In 2007, more than 3 1 billion bottles of wine were consumed around the world and the overall trend to 2012 indicates that consumption will increase by 6% over the 5-year period to reach a total of 2.816 billion cases (Winenews, 2009). This however is negated by a Datamonitor report, which indicates that wine consumption in 2008 reported a decrease of 2 million hectoliters versus 2007, mainly due to the continuous fail in the traditional European producing countries i.e. France, Italy, Spain and Germany. Consumption increases in the US, Australia and the Czech Republic have counterbalanced the overall effect. Consumption in South Africa, Chile and New Zealand has stabilized (Datamonitor, 2009). This is substantiated by a USDA report indicates that despite deteriorating global economic conditions, world demand for wine is likely to ease only marginally in 2009 as consumers shift to lower cost brands rather than significantly reducing their consumption (Foreign Agricultural Service, 2009).

The difference between production and consumption determines the level of oversupply. The graph below illustrates the gap that exists between production and consumption i.e. the extent of the oversupply.



Although the outlook is better than it was a few years ago, the worldwide wine industry is set to remain in a state of oversupply. More up to date figures indicate that as of 2008, worldwide per capita consumption has fallen for three consecutive years and is projected to fall even further. This is largely attributed to the mature wine markets in the European Union where lifestyle changes have been a major factor in the decline particularly in France and Italy, where wine has traditionally been consumed with meals (Wine Spectator, 2009).

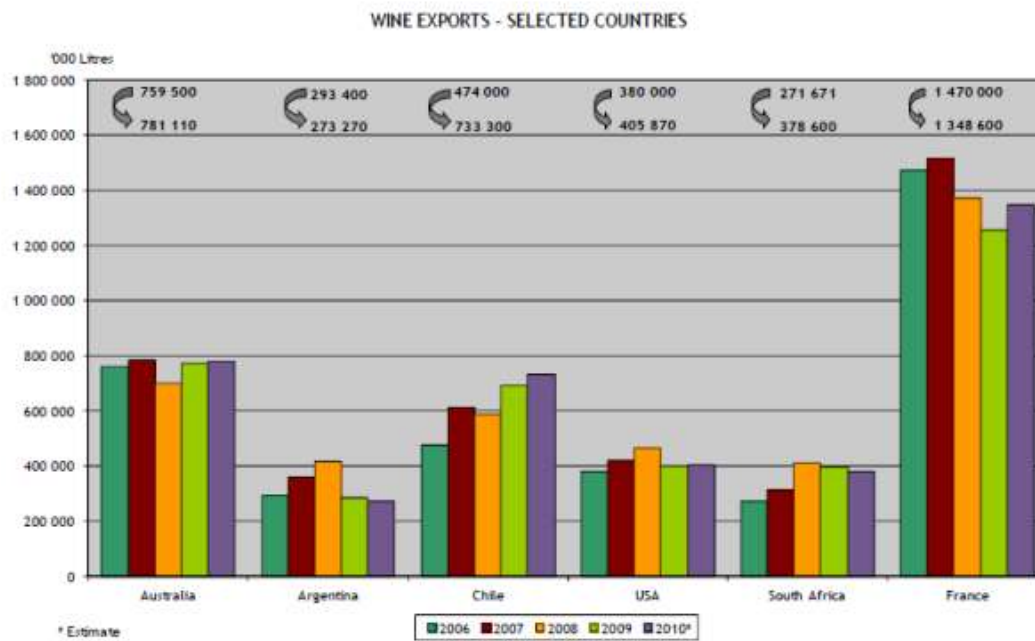
International wine trade: exports and imports

According to a Rabobank report published in 2007, world trade in wine had risen by more than 80% over the last twenty years to 78.7 million hl and a total value in excess of USD 20 billion. Exports then accounted for 28% of world production and 33% of world demand (Rabobank International, 2007).

EXPORTS

The Old World wine producers dominate world wine exports -with France, Italy and Spain particularly dominant. Spain has shown the most significant growth in exports, France has declined and Italy has grown again following a slump in 2003 (SAWIS, 2009). According to the USDA report, the EU accounts for about half of the world's wine trade (Foreign Agricultural Service, 2009).

The world market, considered as the sum of exports from all countries (monitored countries represent 94% of world exchanges) reached 9 210 million liters in 2010 (+6.7%/2009). The economic crisis has certainly contributed to the upward trend of an increasing amount of trade in bulk wines, already recorded the previous year. This also leads to trade which is increasingly complex, where the share taken by re-exports, particularly in trans-continental trade will grow. Companies from export countries very broadly adopt one of two attitudes, either focus on maintaining flows and the level of demand by lowering average prices for distributors or maintain these average prices and risk these distributors passing on the decline in demand. Countries such as Italy, Australia and Chile seem to have chosen the first option last year, while Spain and France tended to follow the second. Countries which if their export potential is taken into account, have best resisted the crisis in terms of volume are Chile (+40 million liters exported between 2009 and 2010), Italy (+140 million liters exported between 2009 and 2010), New Zealand (+30 million liters), Australia (+25 million liters) and Germany (+30 million liters). The countries that have almost completely recovered their losses in 2010 are Spain (-230 million liters then +230 million liters) and to the lesser extend France (-110 million liters then 90 million liters).



Exports from the New World wine producers are dominated by Australia. According to the USDA report, Australia is now the second largest exporter, making up 15% of the world's exports, despite only accounting for 5% of global production. However, exports are forecast to remain flat due to increased competition, lower demand and the strengthening Australian dollar (Foreign Agricultural Service, 2009).

South African wine export volumes have grown at a 19% CAGR from 1986 to 2006, driven by the end of apartheid, industry liberalization, active export promotion, and currency movements. Wine exports have also represented an increasing share of South Africa's total wine production, increasing from 14% in 1996 to 27% in 2006.

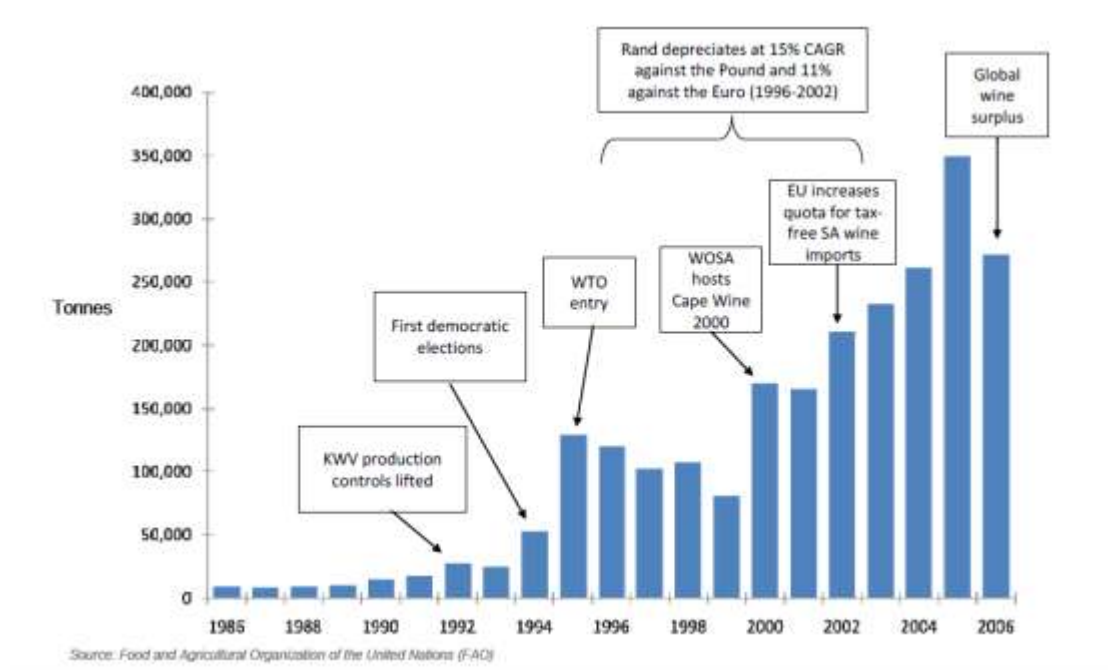


Figure South African wine export volumes⁵²

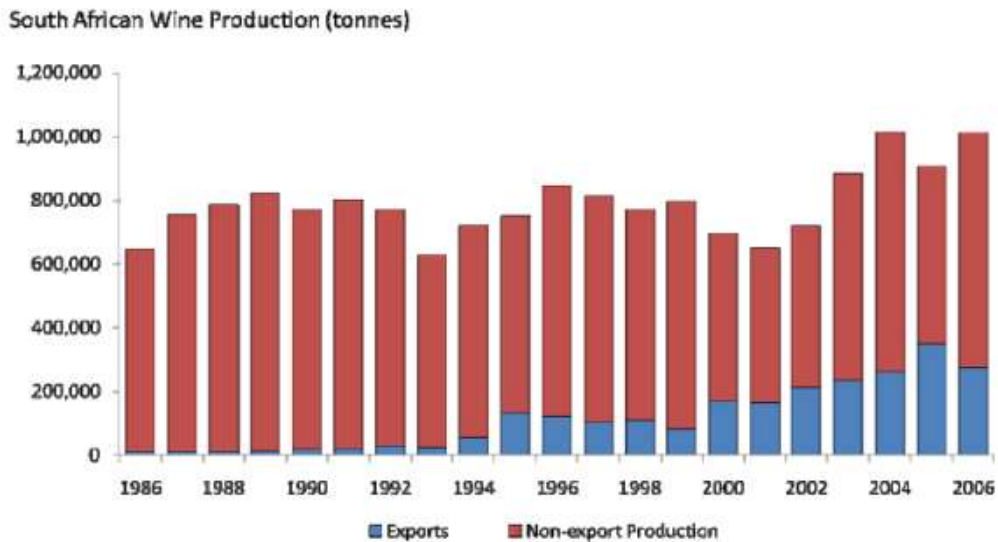


Figure South African wine Domestic Product and export volumes⁵³

⁵² Source FAO, 2009

⁵³ source FAO, 2009

These political reforms and trade policy measures led to a 114% and 146% increase in South African wine exports in 1994 and 1995 (FAO, 2009). South Africa's wine industry benefited from further reductions in trade barriers in 2002 with the 10 year EU-SA Wines & Spirits Agreement. This agreement increased the EU's quota for tax-free imports of South African wine by 30%, and allowed a 3% per year increase in the quota (Matthews, 2002). South African wine export volumes increased by 27% in 2002 (FAO, 2009). South African wine export growth over the past decade has also been driven by active and focused export promotion by various institutions for collaboration. Wines of South Africa (WOSA) has developed marketing strategies to increase international demand and hosted Cape Wine 2000, the first organized trade show of South African wines specifically targeted at international buyers and wine journalists. South African wine exports are vulnerable to global supply conditions and demand conditions in key export markets, particularly the UK, which remains South Africa's largest export market. According to Yvette van de Merwe, CEO of South African Wine Industry Information and Systems (SAWIS), the 2006 decline in export volumes was driven by lower demand from the UK and the Netherlands (WOSA, 2006). These were South Africa's biggest wine export markets, representing 44% and 14% of exports respectively as of 2005. South Africa is slowly diversifying to other export markets. Su Birch, WOSA CEO, views Sweden as a promising growth area (WOSA, 2006). Exports to Sweden have increased from 3% to 14% of total South African wine exports. There is also room for growth in the United States market, which currently only represents 5% of South African wine exports.

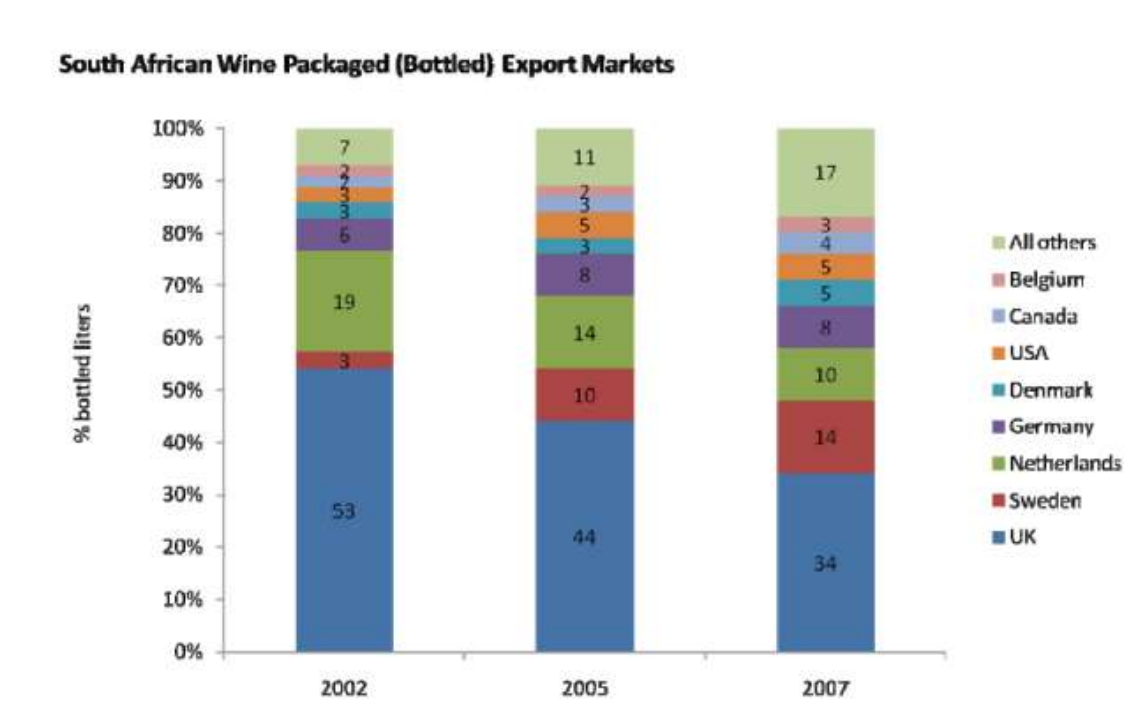


Figure South Africa wine export volumes⁵⁴

IMPORTS:

The situation until 2004 in terms of volume imports and value imports is reflected in the graphs that follow.

In terms of value, the UK has dominated since the second half of the 1990's, when it took over from Germany as the top value importer. The USA became increasingly important in the same period and has subsequently overtaken Germany too. A GAIN report of 2008 confirms the positioning of the UK as the biggest and the USA as the second largest importer of wine in the world (Office of Global Analysis, 2008).

⁵⁴ Source WOSA

7.2 The main structural characteristics of the sector

The wine sector can be classified as a fragmented industry, with more and more daring trends toward globalization. Porter (1980) defines a fragmented industry where many companies compete in which no holds a significant market share and thus can not substantially influence the results of the sector. These considerations are also confirmed by the specific characteristics of the wine sector:

- the presence of many small-and medium-sized;
- family-based enterprises;
- unlisted.

The main differential character of competition in a sector split is given by the absence of a market leader, with force needed to address events. This is what happens in the wine sector where the absence of one or more leading companies determines the inability of competitors to target events. The fragmented nature of the industry features, especially those countries with a strong tradition, for a variety of economic reasons that are complemented by historical ones. In particular, for this sector is possible to identify a series causes affecting fragmentation:

a. *Low economies of scale* and little relevance of the learning curves, equal to of other sectors fragmented, also the wine presents the low economies scale, rather than in the production process, in marketing, distribution and research. This sector is characterized by a high incidence factor.

b. *High transport costs*, which limit the size of efficient plants, the balance between transport costs and economies of scale determines the radius within which a production unit can operate economically (Porter, 1980).

c. *Different needs of the market*, based on different local or regional fractionate the needs of the market and affect, negatively, on the standardization of the product.

d. *High product differentiation*, based especially on the image, that limits the growth in size; the large size, in fact, is incompatible with the image of exclusivity.

e. *High exit barriers*, bringing marginal firms to remain in the sector, it happens that the stay in the field is also true of a sentimental reminder or cultural, bringing it to continue business with profit goals limited or not.

f. *Legislation*, which represents an element of fragmentation especially for the countries of the EU. Community regulations and national laws, forcing the enterprise to adapt to specific standards, determine one of the main sources fractionation.

The result of the fragmentation is to a marginal profitability; in this case, the strategic positioning is very important and strategic goal may be to accept the low concentration becoming a of the most successful businesses, although it controls a small proportion of market.

The main strategic alternatives, including those identified by the Porter global sectors are essentially three and have many points of contact among them:

1. Increase in value added, an effective strategy would be to focus on increasing the added value by offering additional services. These activities allow you to achieve greater differentiation and allow margins higher than those achievable with the traditional product. This choice was made by companies that have opened their cellars to wine tourists and tourists evolved, creating activities for the local knowledge of production and storage of products, through the organization of visits and cultural events related to the world of wine. The increase in value added can be achieved in some cases through actions of vertical integration.

2. Specialization by type of customer, it is what they are trying to accomplish those companies that are specializing in respect of customers who are less price sensitive offering them a product, or a better supply system, with high added value.

3. Vertical upstream integration, useful lowering costs and creating of barriers to competitors of which can not achieve this process.

The elements of fragmentation that still characterize the sector in Countries with a tradition of wine, are less relevant in other countries, manufacturers of C.D. New

World wines⁵⁵, leading to a different competitive environment and impacting significantly on the globalization of the industry. This trend towards globalization is reflected in some elements that characterize the global industry. Among the elements that push internationalization find:

- Economies of scale, technological advancements in logistics, distribution and, in particular, the research had a positive impact on the achievement significant economies of scale for large foreign producers, in particular the United States and Australia. Compete on a global scale has allowed to realize economies in logistics that also stem from the possibility of use of the systems specialized transport, the additional costs of an international logistics system implies, are killed by providing more national markets, thus creating cost advantages.
- The reduction of transaction costs, the advent of ICT has led to a reduction of logistics costs, transport, storage, representing a stimulus to the process of globalization.
- Relative uniformity in the economic and social conditions, the need for different variety of products, of different marketing activities, the problem of a distribution local, also stem from differences in the economic conditions of the distinct geographic markets. The trend towards greater homogeneity, under the economic and social, promotes competition is global.
- Redefinition of the product, which has led to a reduction of differentiation product between the different countries.

These elements are clear indicators of the excess, the initial of the fragmentation. The large Australian firms, California, South Africa and Chile, have been able to carry out a process of globalization of the intervening some of these elements. Their success was aided by the ability greater economies of scale, thanks to the exploitation of progress technology which has led to realize even

⁵⁵ With this sense refers to a number of countries (Argentina, Australia, Chile, New Zealand, South Africa, Uruguay, USA) which, while not having a centuries-old tradition of wine, a few decades have invested heavily in growing grapes get results flattering in terms of sales and recognition

concentration processes faces to increasing the average company size⁵⁶. Among the capabilities that must be recognized to foreign companies is also capacity that it has initiated a process of standardization of tastes through the affirmation of the "international style" that has encouraged the spread of a culture wine to new consumers⁵⁷. These wines found in the new world a collection of information quite simple, but complete and reassuring give reliable and allow easy recognition of a lovely wine and free from defects. The main strategic alternatives, including those identified by the Porter global sectors, are essentially two:

1. Global competition on an entire line of products in order to compete world, so companies compete on the entire line of products, making use of the advantages of global competition especially for lower prices.

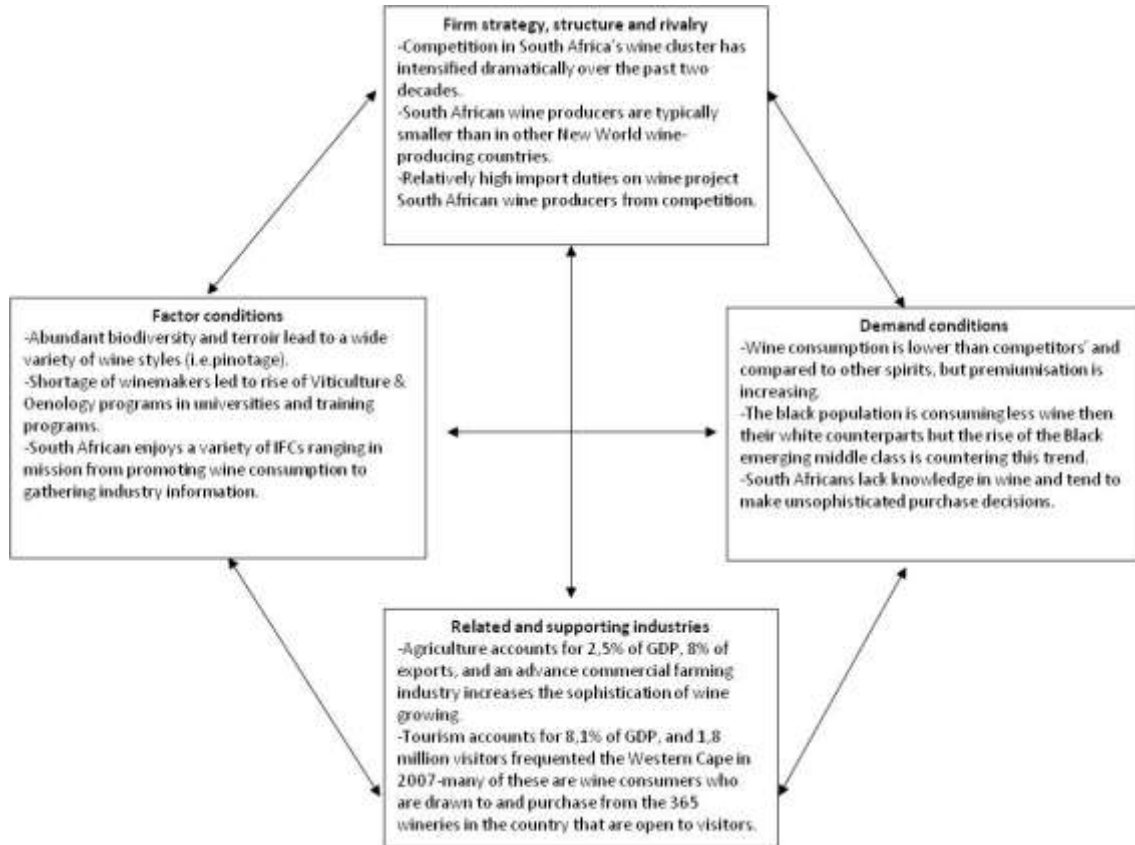
2. Global segmentation strategy, in order to compete on a particular segment of the industry in which the firm decides to compete globally.

These strategic choices are characterizing the behavior of firms the new world of higher dimensions which, taking advantage of the higher economies scale, try and fail to make a success of their management decisions, thus guaranteeing the achievement of a sustainable competitive advantage in an industry that is witnessing in recent times upheavals strategic epochal.

⁵⁶ The first two groups of companies, worldwide, Constellation Brands and the U.S. Foster's Group concluded in the period between 2004 and 2005 of the processes of external growth through the acquisition, respectively the sixth and the third global competitors. Following the acquisition of these two companies have exceeded three billion euro turnover, significantly outpacing other companies, in particular those of the old continent.

⁵⁷ New consumers are curious and not traditionalists, among them there is a strong component women and young people, with buying habits and tastes similar to those of new consumers in countries without a wine tradition. These consumers are characterized by being non-routine, transgressive compared to traditional consumption patterns, likely to give a high cultural content wine and food (Dickinson, 1997)

7.3 Cluster Diamond analysis



Factor Conditions

Location, Natural Resources and Endowments: South Africa's wine production is concentrated in the Western Cape, located at the confluence of the Indian and the Atlantic oceans. There are over 110,000 hectares of land under vine cultivation, with over 300 million vines of which 60% goes into wine production. Production is handled by 82 estates and 70 cooperative cellars (SouthAfrica.info, 2008 and Vinnovative Imports, 2005).

Terroir is defined as the complete set of local (natural and non-man controlled) conditions in which a particular wine or family of wines is produced, including soil-type, weather conditions, topography and wine-making savoir-faire (Wikitionary,

2009). South Africa enjoys fantastic *terroir* to grow high quality wine. The country is one of only three Mediterranean wine growing climates in the world.

Physical Infrastructure: South Africa's physical wine infrastructure seems to be a slight competitive disadvantage. The high and uncompetitive bottling costs of the industry are worrisome: Distell, South Africa's leading producer, estimates that bottling and packaging costs are approximately €1 per case cheaper in Europe than in South Africa (Fin24.com, 2006). Many importers are therefore importing bulk wine to be bottled in their home market. SAWIS reported that while bulk wine exports rose by 22.3% in 2005, packaged wine exports fell by 1.5% (Fin24.com, 2006). Considering that packaging costs make up around 50% of the total cost of producing a bottle of wine and that wine bottle costs make up half of packaging costs, this is very considerable (Fin24.com, 2006).

The higher bottling costs seem to be due to higher local glass, paper and printing costs due to smaller volumes and a lack of economies of scale. 75% of local packaging is handled by one player: Consol (Fin24.com, 2006). Industry consolidation and the lack of competitive pressures are putting upward pressure on the wine industry's cost structure.

Administrative Infrastructure: The administrative infrastructure is quite favorable. It is much easier to obtain a wine license than a liquor license in South Africa. South Africa's legislation allows supermarkets to sell wine, whereas they are not allowed to sell RTDs, beers and spirits (Euromonitor, 2009). Papsak wine (low-quality wine packaged in pouches), a legacy of the dop system (where workers are paid with low quality wine instead of money) (Kapila, 2009), is still prevalent in the country despite the fact that the Western Cape Liquor act outlawed this practice in 1961. A proposed legislation to ban papsak wine has been debated recently (Euromonitor 2008). Whereas such legislation would likely discourage the production of low-quality wine and promote that of high-quality wine, it would also distort the market.

Information Infrastructure: The South African wine cluster has over 15 wine associations and institutes for collaboration which are providing services such as marketing, export promotion and data gathering⁵⁸. However, it seems that many of these overlap in scope and mission.

Science and Technology: Despite some internal criticisms about the level of research in the wine industry, South Africa has a strong tradition of research. More recently, South Africa has established itself as one of the New World leaders in *terroir* research. For over 10 years, a multidisciplinary program has been carried out at the ARC Infruitec Nietvoorbij Institute of Viticulture and Oenology in Stellenbosch and the University of Stellenbosch (WOSA, 2009). This research has had a great impact on better matching between varieties and locations in the Cape winelands and on current viticultural practices that has unlocked the potential of new wine growing areas (WOSA, 2009).

Human Capital: The story of human capital in the wine cluster is mixed. On the one hand, due to South Africa's tradition in the wine industry, there are numerous Viticulture and Oenology programs in the country and scholarships are available in universities. However, these programs have not had very strong participation from the black South African population. This has led to a domestic shortage of sophisticated black winemakers.

Financial Capital: South Africa's wine industry enjoys good access to finance. Since 1997, Nedbank has established itself as the provider of specialized financial to the wine industry. Nedbank currently has a wine industry asset book exceeding a billion

⁵⁸ These associations include: Wines of South Africa (WOSA), South Africa Wine Industry & Systems (SAWIS), Agricultural Research Council (ARC), Biodiversity and Wine Initiative, Cape Winemakers' Guild, Chenin Blanc Association, Institute of Cape Wine Masters, Integrated Production of Wine scheme, Methode Cap Classique Producers' Association, Pinotage Association, South African Society for Enology and Viticulture, South African Wine Industry Council, South African Wine Industry Trust, Wine Industry Ethical Trade Association.

rand (Hill, 2004). Nedbank provides both direct (backing for farm purchases, specialized import service, debt finance, etc.) and indirect assistance (yearly donations to industry associations, etc.) (Hill, 2004). The Nedbank Cape Winemakers Guild Development Trust supports the education and social needs of farm workers and their families (WOSA, 2009).

Demand Condition

At R15 billion in 2008, the South African wine market was still lagging behind the larger categories of beer (R52 billion) and spirits (R29 billion). The wine sector experienced modest growth from 2003 to 2007, growing at a CAGR of 4,3% (Euromonitor, 2009).

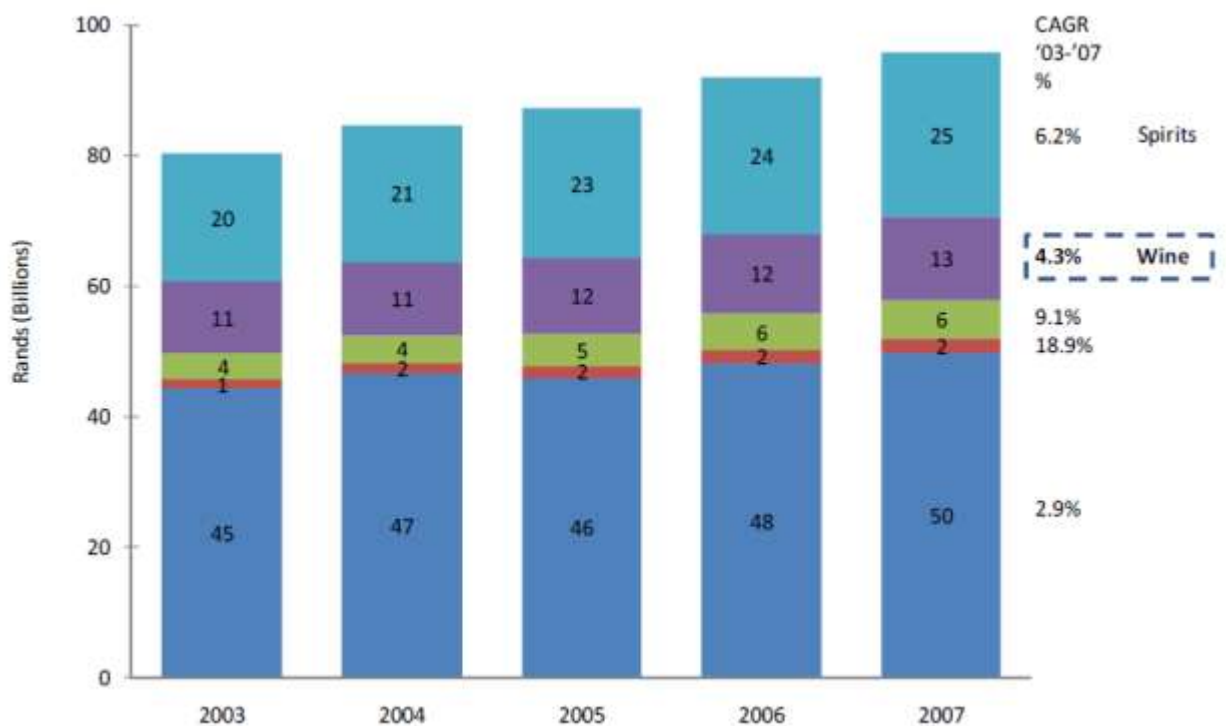


Figure South African Market for Alcoholic Beverages⁵⁹

⁵⁹ Source: Euromonitor 2009

South Africa’s wine consumption per capita (8.37 liters/ capita in 2005) is also lagging.

This can be explained by the fact that the black South African population still considers wine to be an inaccessible drink. 80% of the South African population is black and their “non-consumption” has therefore kept the aggregate national consumption low.

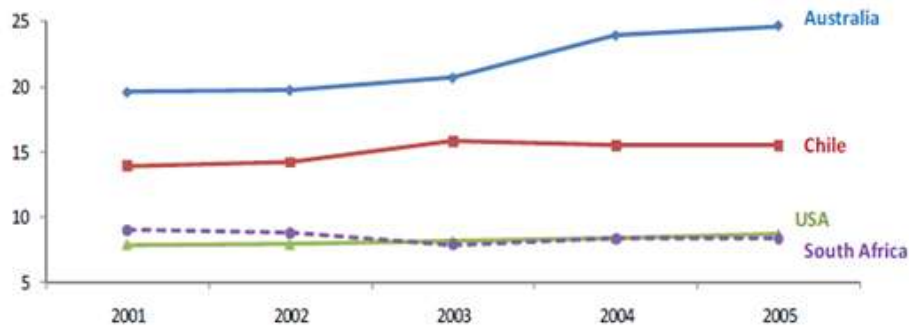


Figure Selected Countries’ annual Wine Consumption per Capita (liters)⁶⁰

Marilyn Cooper, managing director of the Cape Wine Academy and organizer of the Soweto Wine Festival, explains:

“Wine drinking is still seen as elitist and white among the black population who traditionally have drunk beer and brandy. A lot of them think, “That’s not for me, it’s for the whites””. (The independent, 2007).

Adding to the inaccessibility of wine for the Black population is the fact that their participation in the industry has remained limited. The South African Black Vintners Alliance estimates that as a result of apartheid, there are only 25 black winemakers in South Africa (The Independent, 2007). Despite the fact that the majority of wine South Africans consume is of low quality (in 2007, 82% of white wine consumed retailed for less than R25), premiumisation has been increasing in the wine

⁶⁰ Trade Data Analysis, Heritage Link Brands; Euromonitor, FAO

industry (Euromonitor, 2008). The share of white wine sold for more than R25 increased from 11% of total wine consumption to 18% in 2007 (The Independent, 2007). In 2007, wine sales continued to indicate a share shift from lowend to highend, as consumers sought out quality wine that reflect a higher social status (The Independent, 2007).

Context for Firm Strategy, Structure and Rivality

The KWV had a profound impact on rivalry in winemaking since 1918, as it was empowered by Parliament to set and enforce production quotas for all growers and to set minimum prices for grapes to eliminate “harmful” price competition. It was “a system which tended to handicap the private wine producer and favor the bulk grape grower.” (Robinson, 2006). This state of affairs persisted until the 1990s, when the KWV was relieved of its regulatory authority and converted into a private company. The effects on the industry were quickly felt. The number of grape farmers in South Africa fell 16% between 1991 and 2007, suggesting consolidation motivated by farmers seeking economies of scale; during that same period, the number of winemakers more than doubled, likely in response to increasing returns to quality that market de-regulation and the opening of export markets permitted⁶¹.

Today, the structure South African wine industry resembles those of New World producers like the United States and Australia in terms of producer concentration. South African wine producers are typically much larger than those in Europe, producing 1.75 million hectoliters on average versus 200,000 hectoliters in France, for example (Roberto, 2003). This allows South African winemakers to achieve economies of scale (albeit not to the extent of winemakers in the United States and Australia, where average production is even higher). Therefore, there are many fewer wine producers in South Africa: 68,500, versus 232,900 in France, for example (Roberto, 2003).

However, South African wine producers, who (as already noted) sell nearly 75% of their output on the domestic market, are protected from foreign competition.

⁶¹ http://www.sawis.co.za/info/download/book_2008_web.pdf

Historically, South Africa levied extremely high import duties on wine, sometimes as high as 160% (Ntege, 2001). Since 1996 these tariffs have been reduced to 25% for wine from non EU countries (a bilateral trade agreement with the European Union secured lower tariffs for European imports). Nevertheless, this tariff is still high compared to import duties on wine that other important wine producers impose. Chile, Australia, the United States, and the EU all impose tariffs of 6% or less on imported wine.

Related and Supporting Industries

The wine cluster is adjacent to two important South African industries, tourism and agriculture. South Africa is the 28th most visited country in the world, and experienced 5% annual growth in international arrivals 2002–2007. In 2007 tourism accounted for 8.1% of GDP, when South Africa received 9.1 million international arrivals; of these, 1.8 million visited the Western Cape, where they spent R18 billion (\$2.6 billion). The top three countries of origin for international visitors to the Western Cape are the United Kingdom, Germany, and the United States—all major wine consuming countries. The Cape winelands are less than an hour's drive outside of Cape Town, and there is an extensive tourist infrastructure of hotels and restaurants.

Indeed, 145 wine producers in South Africa have organized into “wine routes” catering to tourists, offering tastings and bottle sales.

Agriculture is another successful South African industry the strength of which supports the wine cluster. South Africa is a net food exporter and self-sufficient in most agricultural products. Agriculture accounts for 2.5% of GDP, 8% of exports, and 8% of employment. It boasts significant competitive advantages, including an advanced infrastructure relative to that of the rest of the continent, counter seasonality to Europe, plentiful availability of cheap labor, and free trade agreements with many important markets. Aside from grapes used for wine production, South Africa is among the top five exporters of table grapes globally. However, large scale commercial agriculture coexists with sub-scale subsistence agriculture, a legacy of apartheid. Under an

ambitious land reform plan, the government plans to redistribute 30% of white-owned commercial agricultural land to previously disadvantaged persons by 2014.

7.4 Cluster-level strategic issues

Factor condition issues

Shortage of black winemakers: With only 1.5% of winemakers, black winemakers are still too few to dispel the myths that wine is an “elitist and white” drink and to encourage greater consumption among the black population.

High and uncompetitive bottling cost: the disadvantage in bottling costs is leading to higher proportions of wine being exported in bulk and bottled overseas. This not only affects the capacity utilization and performance of the local bottling operations, but also seriously compromises the quality of South African wine available in international markets. Reports have indicated that when bulk wine is imported, it is sometimes mixed with other wines of lower quality (Fin24.com, 2006).

Low coordination among IFCs: The effectiveness of IFCs is not maximized since their mandates overlap. This results in wasted resources and sub-optimal industry support.

Demand Condition issues

Low and unsophisticated demand among black South Africans: Despite the growth of the South African Black middle class, the black population is still not consuming significant quantities of wine. Many Black South Africans still consume Papsak wine or sweet wine, depressing the quality of wine since producers have no incentives to improve quality to satisfy local demand.

Export Market Concentration: South African wines are concentrated in a few international markets; 71% of exports are concentrated in the Euro zone and in the UK, thus making exports vulnerable to appreciations of the rand against these currencies.

Firm Strategy, Structure and Rivalry Issues

High tariffs on imported wine: Even though they have considerably decreased over the past few years, South African tariffs on imported wine are still too high. This considerably reduces the supply of imported high quality wine in the country.

Brand Differentiation: South Africa competes against many countries in the competitive “table wine” segment and thus finds it difficult to differentiate itself from the competition.

Presence of capital controls: South Africa’s use of stringent capital controls limits FDI, which could lead to beneficial knowledge and skills transfer in the wine industry.

Related and Supported industry issues

Wine tourism not popular among local South Africans: most tourists who visit the Cape winelands are international. This lack of local tourists not only hinders south Africans’ education about wine, but also increases the likelihood that quality-conscious consumers will choose premium imported wines instead of premium South African wines.

Recommendations

Short term recommendation

- *Support local highway development* by using central government to facilitate development of local transportation infrastructure across the various provinces.
- *Reduce import tariffs* to force local companies to be internationally competitive and increase local buyer sophistication.

- *Maintain macroeconomic stability, loosen capital controls and further liberalize trade policies* to allow stability necessary for business growth despite current volatility in international markets.

Medium term recommendation

- *Improve inadequate education system and upgrade worker skills.* In particular vocational training and industry institutes should be further developed. At tertiary level, increase coordination of educational and research focus with industry needs.
- *Fix incentive problems created by Black Economic Empowerment policies* and focus on management training and social services that create long-term opportunities for the black population. This is an urgent, but politically sensitive priority which will take time to implement.
- *Address instability in electricity supply* by privatizing electricity provision and/or facilitating construction of new power generation facilities.
- *Tighten regulatory standards* to increase sophistication of domestic products.

Long-term recommendation

- *Toughen regulations on union activities* which maintain labor market rigidity. Create necessary goodwill to push this agenda through progress on black empowerment efforts.
- *Develop cluster development and collaboration strategy* for high potential cluster. Focus on policies which will help all clusters without choosing favorites. Also, diversify economy by supporting cluster development in service sectors.

Country level recommendations

Short-term recommendation

- Stellenbosch University and other universities could offer *scholarships to Black students for viticultural programs*. Nedbank's Trust could contribute to them.
- *WOSA should become the umbrella organization of all IFCs* to ensure that mandates and responsibilities are clearly defined and do not overlap.
- *WOSA should continue to support events such as the Soweto Wine Festival* (organized in predominantly black neighborhoods) that help educate the Black population about wine.
- *WOSA should develop a high-end premium sub-brand, distinguished by varietal or appellation*, to promote increasing winemaker sophistication. Pinotage would be an excellent option to develop this brand.
- *WOSA and the South African FIFA chapter should take advantage of the 2010 World Cup to publicize South African wine*. The premium sub-brand would be an ideal “sponsor” of the South African team that could be featured on marketing materials. This should allow WOSA to reach an audience of international tourists coming from a wide range of countries.

Medium-term recommendations

- Parliament should *further reduce tariffs on imported wine*. Whereas some could argue that this will have the impact of increasing imported wine consumption over domestic wine consumption, it will actually contribute to increasing the sophistication of South African consumers.
- Parliament should *reduce (and potentially eliminate) capital controls*. This will be beneficial for the wine industry. The feasibility of this measure might be compromised by the inflation targeting policy that the Central Bank is pursuing. Parliament should therefore coordinate with the Central Bank.

- *WOSA should encourage winemakers to focus on the U.S.* WOSA could facilitate this by organizing road shows in the U.S. and encouraging the participation of South African wine brands in America wine festivals and tastings.

Long-term actions

- *Western Cape Tourism Authorities should launch a TV branding campaign about wine tourism* to publicize it to the local population.
- *South Africa should also aim to penetrate the growing regional wine market.* South Africa should position itself as the premier African wine producer and aim to increase its shelf space in markets where the middle class is growing quickly (e.g. Angola). It is critical that high-quality wines are exported to these markets to create from start the perception that South Africa wine is high quality.

Chapter 8

Business level strategy in the South African wine industry

8.1 Drivers in the South Africa wine arena

282 million hectoliters of wine was produced in 2005, of which 28% was internationally traded (OIV, 2005). Three European countries (France, Germany, and Italy) are the largest producers, making 142 hectoliters combined. United States and Australia compose the second tier, with China, Argentina, and South Africa being the most important third tier producers. These eight countries account for 76% of global wine production. On the demand side, the United Kingdom and Germany are the largest importers of wine globally, together accounting for about one third of internationally traded wine. Spain, France, and to a lesser extent the United States are significant wine consumers but can rely on domestic production to supply a greater fraction of their demand. The wine trade has changed significantly over the last five years. Volume has been growing at an average of 3.9% per year, and in value terms the growth is an even more dramatic 25% per year (in non-inflation adjusted terms) (OIV, 2005). France's historically dominant position in exports has been eroding, its market share having fallen by 4%, with smaller gains in market share being realized by a number of countries, including New Zealand, Argentina, Germany, South Africa, and Chile. The average value of wine exported from France (\$5.35/liter FOB) is much higher than that from any other country, a lead which has widened over the last five years (FAO, 2009).

The world wine market is characterized by tradition and dynamic development. Key words for describing the global wine arena include globalization; increasing importance of brands; changes in demand behavior and market balance (Agri/evaluation, 2002). Rabobank International has developed the following model depicting the drivers of change in the global wine arena and their interrelationship with each other.

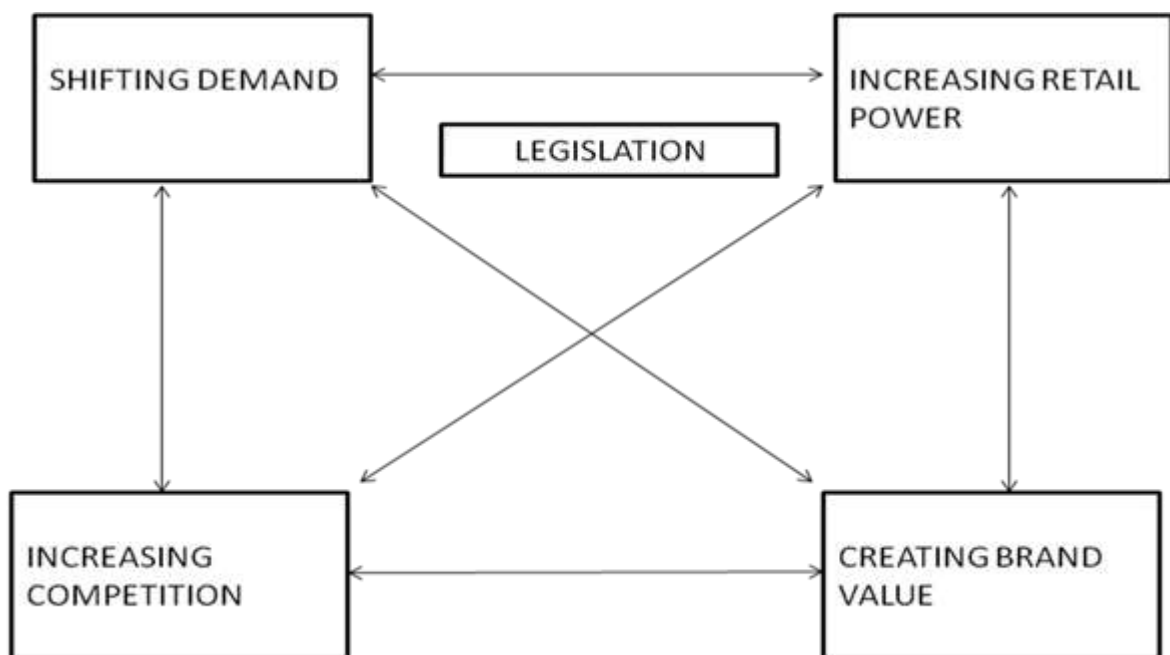


Figure Drivers of change in the global wine arena

Euromonitor’s description of the world wine market in 2009, confirms this depiction. The growth in consumer sophistication is resulting in a shift towards premium, high-quality wines. This is underpinned by increasing consumer knowledge about the products themselves, fuelled by the international media, wine clubs, samples and in store tastings. (Shifting demand) Off-trade and on-trade wine sales have both grown, but off-trade dominates as at-home consumption of competitively priced supermarket-bought New World wines has grown significantly. (Increasing retail power)The global wine market is characterized by greater consolidation as regional and national players position themselves as global wine producers and capitalize on growing

demand for wine in developed and developing markets. (Increasing competition) Brands appeal to consumers who are unfamiliar with wine products. Branding strategies are becoming increasingly influential. (Creating brand value) More effective attempts to combat drink-driving has resulted in an increase in at-home consumption (Legislation).

Since the consolidation of retailers has resulted in the consolidation of wine companies, Rabobank International has identified the increasing retail power as the strongest wine industry driver. However, it could be argued that the power ultimately lies with the consumer and that shifting demand is the strongest driver, especially in an industry characterized by oversupply.

Both the wine industry and the retail industry are dependent on the consumer for continued survival. Consumer loyalty is fickle - the inability to deliver and meet the shifting demands of the consumer will result in them going somewhere else to find what they want.

Strategies in the global wine arena

In an increasingly competitive global wine arena, the challenge is for wine businesses to develop strategies for success. Rabobank International has developed a model representing the elements of winning strategies in the wine industry.

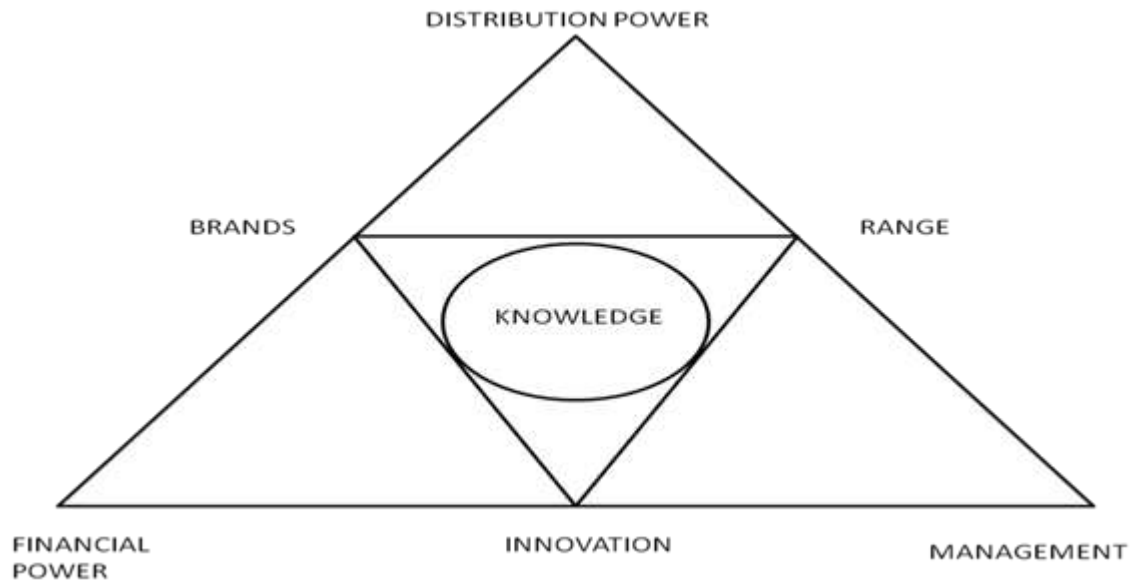


Figure Key success factors for the wine industry

Distribution power, at the top of the pyramid, refers to access to distribution channels. All wine companies need to strengthen access to the distribution channels. Wine companies build distribution power in different ways – through building a range of attractive brands; through innovations; through cost leadership. The greater the consumer interest and demand for the brand, the more inclined distribution channels will be to list the product.

The base of the pyramid concerns financial power and business management. The wine market is characterized by price and margin squeeze, making cost control and financial power increasingly important not only for survival in the down cycle, but also in terms of investing in innovations and making strategic acquisitions (Rabobank International, 2006).

The heart of the pyramid is knowledge. This is a culmination of an understanding of the quality segments of the industry, the drivers of the wine industry and the strategic positioning of the wine company, as illustrated in the following figure (Rabobank International, 2006).

Within this model, three components are represented namely that of market success, financial success and organizational success.

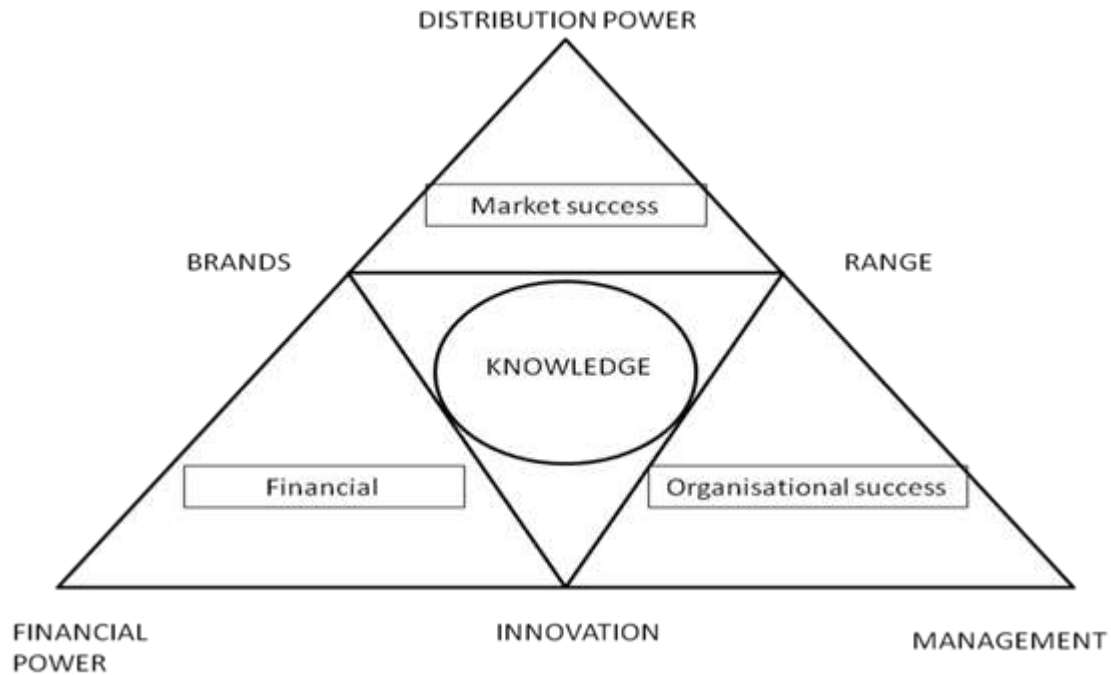
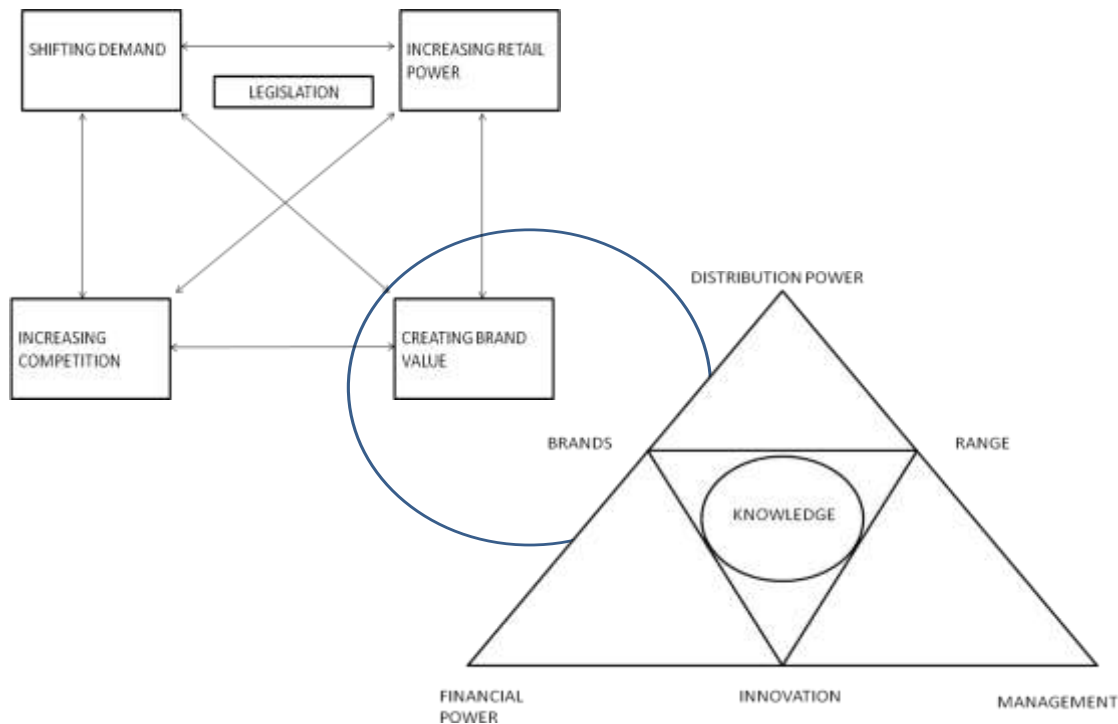


Figure Key success factors for the wine industry

The premise is that market success drives financial success and organizational success.

Role of branding

Importance of “branding is highlighted when one considers the two Rabobank models in conjunction with each other. The area of overlap is that of “creating brand value” and “brands”. This is significant, in an arena which appears beyond the control or influence of wine business.



'Branding' strategies — which wine businesses overtly manage — determine the industry driver of 'creating brand value'. It is the only industry driver that wine businesses can directly influence to effect change in the status quo of the global arena.

According to the model, an improvement in 'brand value' will lead to an improvement in the competitiveness of wine companies and wine countries involved; consumers will demand the brand and the position of the wine company in relation to that of the retailers will be improved.

For clarification, it should be noted that the concept of 'branding' is used to indicate the process of building a brand i.e. creating brand value. The two most important components of creating brand value are brand awareness and perceived quality (Wilcox, Laverie, Kolyesnikova, Duhan, & Dodd, 2008). Brand awareness is defined as the ability of the individual to recall a brand name in a product category. Perceived quality is defined as the consumer's perception of a brand's quality (Wilcox, Laverie, Kolyesnikova, Duhan, & Dodd, 2008).

It is widely recognized that brands can provide value and strength in the market well beyond that which is provided by the intrinsic characteristics of the products (Wilcox, Laverie, Kolyesnikova, Duhan, & Dodd, 2008).

Research indicates that while perceived quality is important, the main driver of brand value in the wine industry is brand awareness. “Without brand awareness there is no brand equity — awareness is a necessary condition for brand familiarity, brand preference, brand loyalty also for a trial of a wine or a visit to the winery” (Wilcox, Laverie, Kolyesnikova, Duhan, & Dodd, 2008). In a wine market with a brand mortality rate of over 50% in sixteen years, brand awareness has to form an integral part of the brand building process.

Brand awareness is the process of exposing the brand to potential consumers and can be achieved in various ways, ranging from advertising, third party media endorsements, sponsorships, direct communication etc. Linked to this, is the availability and accessibility of the product which has a volume implication.

Despite the increasing importance of brand awareness and brand value across the segments, brand loyalty across the segments in wine is not strong. In the large popular premium segment it seems easier to realize as most consumers in this segment lack any kind of wine knowledge and well-known brands give them some security. In the premium segment, consumers want choice, want to be surprised in a positive way and like to experiment (Rabobank international, 2003).

Wine brands need to be deliberately built to create consumer loyalty. In so doing they generate a price premium or at least a buying preference over wines without a clear brand (Rabobank International, 2003).

The segmentation of the wine industry means that a given brand is unlikely to achieve success in all segments, from basic to ultra premium, since each segment has specific and different requirements. A brand should target a specific market segment in which it can build recognition and increase market share. Brand ladders can be utilized at a later stage to encourage consumers to trade up within the existing brand (Rabobank International, 2003).

Strong brands lead to strong companies, consumer loyalty and to an overall strong industry (Vrontis & Papasolomou, 2007). By having a strong brand a company can enjoy cost effective marketing campaigns, greater trade leverage, higher margins, ease of extending lines, stand out of competition and defence against price competition (Vrontis & Papasolomou, 2007).

Rabobank identifies the main challenge for wine companies is achieving the critical mass needed to create significant brands, coupled with the limited budgets available for reaching the right consumers (Rabobank International, 2003).

In the next section, an overview of the South African wine industry is presented, together with an assessment of the competitiveness of this industry.

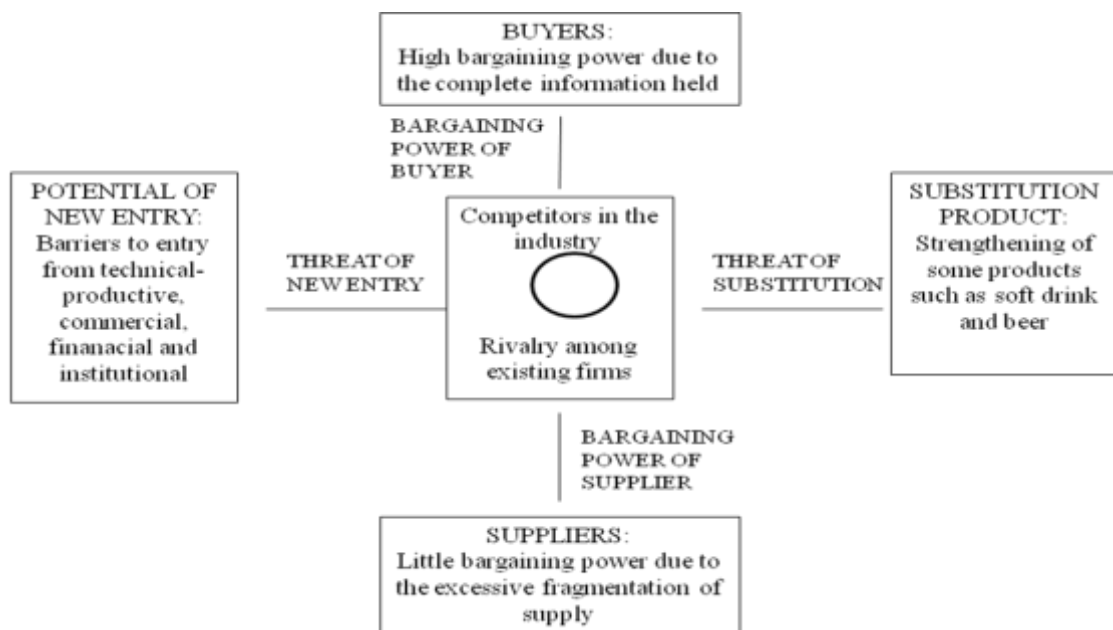
8.2 The managerial choices and strategic behavior of wineries

The basis of the strategy is the competition because without it the strategy would lose its meaning. Since the moves of a competitor induce reactions in the other competitors, you must take this into account before taking decisions.

Firm operating in a specific area, in fact, is in direct competition with a number of other companies and will, therefore, have to make strategic choices that depend on the sectors in which it operates, competitors it faces, its internal organization and the many other factors. Preliminary management must be able to analyze the various areas to which it belongs, especially in a perspective view, this will lead to define strategies, able to place it in a condition of dynamic equilibrium between its structure, the markets in which it operates and the environment. The basic premise of the analysis is that the sectorial level of industry profitability is not a historical accident or the result of specific influences entirely at the sectorial level, but is determined by the characteristics of the structure sector.

The theory that underlies the relationship between sectorial structure, behavior competitive sector profitability is given the approach Structure-Conduct-Performance, but closely connected with this is the model of the five competitive forces of Porter.

According to The American researcher the attractiveness of an industry is determined by the profitability that companies can achieve inside it. It is established, usually taking into account the return on investment (ROI)⁶². A sector, in fact, exerts a catalytic role against companies when there is the possibility of achieving an ROI greater than the cost of capital. The wine sector has a rate of return on invested capital (ROI) interesting (7.7% in 2005), but lower than the companies in the sector beverages. In 2005, the average ROI of the leading industrial was 10.6%. Below the average overall value are placed the firms in the drinks (with 9%).



From a 2007 survey on the wine sector is evident the regressive trend in the undertaking winery. The main profitability indicators for 2005 showed unsatisfactory results when compared with companies in the beverage industry.

Applying Porter's model to the wine sector should go to consider each of the five forces that influence the attractiveness: the entry of new competitors, the threat of substitute products, rivalry among competitors present, the bargaining power of

⁶² Grant R. (1994), *L'analisi strategica nella gestione aziendale*, il Mulino, p. 63

customers, bargaining power of suppliers. The first three are sources of competition "horizontal", the second two are sources of competition "vertical".

Competition from substitute products.

The potential for profitability at the industry level is determined by the maximum price that consumers are willing to pay. This in turn is dependent mainly on the existence of substitute products. Where there are few substitutes, consumers willing to pay a potentially high price are few. In other words, the demand is inelastic. If there are a lot of products next to the reference product then there is a limit to the price that consumers are willing to pay. In this case demand is price elastic. This second situation which approaches the situation of the wine sector. Replacement products are, in fact, a competitive strength of considerable importance. Even if for a part consumer (the most faithful), the wine is not a real alternative and may deny the transfer of market share from wine to alternative products. Of all the substitutes, mineral water is particularly important. The consumption of mineral water, positioned between the end of the development phase and the beginning of the maturity stage, is located around 110 liters per person per year. A water play for the absence of an upper limit to the physiological consumption, its ability to quench thirst, that they are indispensable to human life. Its neutral flavor also makes bottled water a product suitable for any age group. It also has a positive image in terms of digestive power, lightness, of dieting and content generally healthy. The competitive action against the wine is carried out, by mineral water, especially in correspondence for use functions and refreshing accompaniment to meals, with particular reference to working meals both domestic and non domestic. It should be kept in mind that in many cases water and wine coexist on the table of the consumer and this also has implications on competition that did not materialize in connection with any act of consumption.

The beer is placed in the maturity stage, with a per capita consumption of around 30 liters per year. Until a few years ago, the growth rate of this drink was accentuated because of the enlargement of consumption opportunities related to this product. Subsequently, there has been an adjustment of the rate of development and the creation

of a segment of loyal users. Compared to wine is an advantage by higher valence refreshing, symbolized by effervescence and freshness flavor. His image is more youthful and modern than that of wine. His weaknesses are identified in the less refined taste, in less elegance, personality and less pronounced in the more distant by tradition. Competitiveness against the wine is carried out both meals that as an accompaniment to meals, especially in the case of meals weekdays, tend to be fast and unstructured. Even in festive meals, however, the beer may appear on the tables of younger people, or when meals are consumed away from home as an accompaniment to certain foods (such as pizza).

Soft drinks are also in the maturity stage, they experience a consumption of about 50 liters per capita per year. Penalized by even a moderate seasonal consumption of these products can benefit from incisive marketing strategies and communication, based on placements carefully designed and targeted to specific functions and occasions. Competition in respect of wine realized mainly in the direction of certain types of wine products: sparkling wine that can be exposed more often to the alternative of choice with soft drinks. The competitiveness concerns with wine in most cases, young people or moments of consumption outside the main meals. The functions specific use are the satisfaction of thirst and / or hedonistic needs, emerges also a component of performance in correspondence of the occasion appetizer. Weaknesses are healthy and lived poorly genuine.

The spirits whose consumption while being about 4 liters per capita per year is being slow but steady decline is to be considered in competition with wine with respect to a wide range of functions for use and consumption opportunities. Used especially between meals or at most after a meal, the use functions fulfilled are oral gratification, gift and motivation compensatory. The most important concern, however, socialization and performance.

Fruit juices shows an increasing consumption, which stood about to 9 liters per capita per year. Strengths are authenticity and the health aspect, as well as the capacity and refreshing, for clear juices, the reduced sugar content. For all juices is important

nutritional intake, the possibility, therefore, functions to coat food themselves. In some cases replace the drinks for purposes refreshing.

USE FUNCTION	SUBSTITUTES PRODUCTS
Refreshing	Mineral water, Beer, Soft Drink
Socialization	Spirits, Soft drinks
Bracing	Coffee, The, Spirits
Feed	Soft Drink, Mineral water
Gift	Spirits

Table Principal substitutes product

There are other products, in addition to those so far analyzed, which come into competition with wine. It is in most cases a competition more indirect or otherwise limited from the standpoint of the quantity of wine involved. In the compensatory function, for example, the wine located alternatives in a range of sweet products. As part of the function food substitutes may be the milk and a wide variety of foods can be used as ingredients in the preparation of the dishes.

Threats of entry.

The attractiveness of the sector is also affected by possible new revenue. What discourages the entry of new competitors in the field are especially the C.D. sunk cost (hidden costs or underwater)⁶³. The possibility of entry in the wine field by new companies are significantly hampered by a number of barriers: institutional, technical and manufacturing, commercial, and financial. And 'in fact necessary to make investments in property, specifically adapted to the business sector, which are difficult

⁶³ With this expression we mean all those costs already incurred that can not be recovered

to recoverable output. The existence of economies of scale⁶⁴, legal barriers, possible retaliation by competitors, product differentiation and the capital requirements reduce the likelihood of new entrants. With regard to the wine sector despite the existence of sunk costs, the satisfactory profitability in recent years has not only led to the emergence of new international competitors (the so-called New World wines), but it has meant that also entrepreneurs from other industries have begun to invest in wine. In the wine sector with regard to the barriers to entry are considered characteristic⁶⁵ the following factors:

- • product technology: both fine wines for both common wines is an obstacle to low-level;
- • Process technology: the level of this barrier increases with the quality of the product; however, represents an obstacle relative to both the not excessive cost of financial investments, both for expertise in common field;
- • capital requirements: a barrier is only relevant in the case of productions particular object of aging or of productions such as sparkling with the classic method;
- • access to distribution: it could be a problem for the company that wanted to reach a larger size high quality / high price, as businesses of this type are rare, and the investment would be to be very expensive;
- • communication: the input in the field implies the choice, depending on the type of product that you want to achieve, the type of communication to be adopted with costs depending on the choice also very high.

Rivalry between established competitors. The main factor that determines the state overall competition and the level of overall profitability in most of the fields is given by the intensity of competition between firms within the sector. Among the most

⁶⁴ "The economies of scale, ie the phenomenon of lowering unit costs of production and sales to the achievement of certain volume of operations, are obtainable not only in the technical or processing of goods, but also in the supply of materials and services and marketing of the final products. "V. Sciarelli S. (1997), Economics and management, Cedam, page 44

⁶⁵ Spano F. M. (1997) L'economia delle imprese vitivinicole, Giuffr  Editore, Milano, p. 503-504

important factors that determine the nature and the intensity of competition between consolidated companies in a sector are: the degree of concentration, diversity of competitors, product differentiation, the existence of excess capacity, the exit barriers and the conditions of cost:

- the degree of concentration of the basic characteristics of the wine sector there is a very low concentration of supply, which happens to be one of the lowest observable in the food industry. The pulverization supply constitutes a structural condition which will tend to characterize the sector still long. This despite the crisis in demand favors the gradual withdrawal from the market firms "fringe" which not being able, for a dimensional constraint, implement policies to differentiation, end up being more exposed to competition based on price. The acquisition and merger, many in the last decade, substantial changes to the structure competitive. The element of fragmentation is the most important point of weakness sectoral, compared with a market condition that requires joint policy initiatives to limit the drop in consumption with policies revitalization and enhancement of the product. In fact, in the rare cases which, in specific segments, agreements and strategies are possible outcomes, the impact the market was significant;
- the least diversity of competitors and the lack of product differentiation, the wine sector has a large number of competitors and also characterized by the similarity of the firms in terms of objectives, strategies and costs, meaning that in the eyes of consumers many companies are homogeneous and with a very low differentiation of the products. The rediscovery of many vines did not lead to upheavals competitive, but simply influenced consumer choices more evolved yet today, however, fail to make big distinctions between the offers of different wineries. For consumers, the differences are even less developed minor because the production of the traditional countries were complemented by those of the countries new ones that have also led to a standardization of taste, with the emergence of an international taste;

- economies of scale, the ratio of fixed costs / variable costs and barriers output, the wine sector is characterized by high fixed costs that influence both the entry of competitors and competitive dynamics; economies of scale within the area should affect how incentives to expand sales, but the hyper competition, both globally and at the local level, has negative effects in terms of capacity utilization. Everything connected with the very high exit barriers, related to investments specific measures taken, make the sector attractive but highly risky. Considering the effect of entry and exit barriers can be determined the degree of competitive pressure within the wine sector. These barriers are different mechanisms which have, however, correlations; their joint presence gives rise to different combinations of risk / profitability. This sector presents a situation of barriers to entry low and high exit barriers, resulting in a low profitability and risky. The sector, in fact, has the low barriers to entry which, for the excessive fragmentation of supply, not to protect the firms in the sector by ensuring satisfactory profitability, but not high. These are complemented by high exit barriers that do not allow easy disposals, do not allow the elimination of marginal producers.

		Barriers to exit	
		low	high
Barriers to entry	low		low profitability and risk
	high		

Tabella: the degree of competitive pressure⁶⁶

⁶⁶ Processing to Porter data, 1980

Bargaining power of suppliers.

In the determination of what is the attraction a sector an important role is played by the bargaining power of suppliers. If the size of the suppliers of raw materials, semi-finished products and components are lower than those of their customers and if their products are relatively undifferentiated, their bargaining power tends to be weak. With regard to the wine sector providers grapes are numerous. In Italy there are 1.2 million farms with vines. The relationships with the farmers are usually stable and, in the case of production of fine wines and / or DOC, characterized in contact direct. Suppliers of bulk wine cellars are mainly social and cooperatives, which have acquired a leading role in the first transformation of wine. The type of grape and the use made of it, affects substantially the criteria according to which the processing companies choose suppliers. For the production of grapes for fine wine the processor considers it essential personal knowledge of their suppliers and the establishment of a relationship of cooperation and mutual understanding staff of its suppliers. For grapes destined for wine common, however, the main critical success factor is the cost of raw materials. Suppliers of grapes have in principle a great bargaining power. A structural overcapacity, offering fragmented and the trend for enterprises of wine to be integrated upstream are all that work against the purchase price of the raw material. the situation changes when the production level is low or when the trading refer to grapes to products of particular value.

In such cases the competition between processing works to the advantage of the farmer. Similarly the power of suppliers of bulk wine is reduced. Fragmentation of and large stocks of product does not leave room for negotiation. The many possibilities of interaction that exist between agricultural processing and within the industrial sector have led to a degree of vertical integration substantially high. For industrial groups the choice to produce the internally the raw material is mainly dictated by the requirements of control the quality of the product, wines of particular value or with strong connotations geographical require, in fact, of the raw material (with specific characteristics) not always available on the market.

The bargaining power of buyers.

The attractiveness of the sector, then, depends also the bargaining power in the market for output, namely the sale to customers. This is determined primarily by two factors: the sensitivity price of the buyers and the relative bargaining power. The more products are poorly differentiated more buyers are likely to replace the suppliers in based on price. The most relevant for determining the bargaining power of buyers are⁶⁷:

- • the extent of the volume of the transaction;
- • the structural abundance or shortage of supply of the product;
- • the degree of concentration of the tenderers.
- Based on these elements is different the level of bargaining power exercised intermediaries:
 - • wholesalers: enjoy a privileged position, in that they collect the product small bottlers or purchase the bulk of average wine producers and then proceed to bottling, and often they are to play a role key with the end-user market rather than producers;
 - • The wine: in the past resorted to this channel producers of fine wines, who wanted to support the high quality image of the product, the situation is changed in recent years and their bargaining power has gone to increase forming a channel chosen by more and more people;
 - • the large retail sector has a high bargaining power because it imposes large quantities with small margins, precision delivery, payment delayed, compliance with the standards;
 - • the retail trade: it has a reasonably easy to access, but significant costs due to the dispersion of the points of sale;
 - • Restaurants and bars: their bargaining power is high and requires an effort substantial commercial for the dispersion of customers;

⁶⁷ Ivi, p. 505.

- catering: sales volumes, the format needs, optimizing quality / price ratio, the logistical problems of supply made In the past this channel unattractive; few years many companies, however, they have started to become interested in opportunities that these intermediaries offer.

In the wine sector, the bargaining power of customers is very high and this is particularly due to two factors: the pulverization of the offer and the completeness of the information held in relation to the market. This latter feature arises from the fact that consumers have a comparison shopping and quality of the products which are offered to them.

8.3 The application of the Abell model to the wine sector

In any firm one must distinguish, on the one hand, the "strategic structure", in sense of different ASA or business, which can be segmented the firm itself; on the other hand, the "strategic architecture", as they are relevant distinctive competencies characterizing the firm, ie the set of skills and knowledge that it possesses at the level of excellence⁶⁸. The company is a collection of distinctive competencies business and at the same time, closely interconnected, whose integration comes the ability to compete for business. The "strategic framework" of the enterprise is embodied in the perimeter of the competitive territory, in the sense of clearly identifying the strategic framework reference. Since the late seventies, given the difficulty of putting into practice operating procedures applied so far in terms of product / market and sector, has established the concept of "business" or "Strategic Business Unit" (SBU) ". The strategic framework of undertaking depends, in essence, on the articulation of SBU, in which it can be segmented from the strategic point of view. The company may be engaged in a single competitive system of reference (SBU only) or have fields or different territories with different perspectives of reference and rules of the game (other than SBU). "The strategic architecture" of a company concerning its distinctive competencies in the sense of set of skills and knowledge which the firm has at of excellence are vital asset of a

⁶⁸ Ivi, p. 491-492.

company, in respect of which it must seek the concentration, understood as an action against their dispersal; accumulation, understood as the action of a logic of investment in long- period, and integration, understood as efforts to create a portfolio of complementary skills and synergies; conservation, understood as action against pollution or depletion of skills. Strategic alternatives to complement SBU through a process consisting of the following stages:

- definition of the SBU;
- choice of the type of competitive advantage;
- the strategic choice to pursue;
- arrangements for pursuing the chosen orientation.

Strategic analysis of an industry-dimensional model of Abell (1980) represents one of the patterns that allows to have an overall view and globally. The three-dimensional model of Abell has the undoubted advantage of establishing the company's business by referring not to a criterion based supply side, but to a criterion based on the application. Very often in the determination of strategies in general, and of those competitive in particular, reference is made to the concept of sector, or at a definition commodity for which you consider belonging to the same field competitive firms that produce similar goods produced with the same technology. Is more significant, sometimes, the search areas of competition it is not only important to understand which firms produce similar goods, but also provide insight into what products and services are perceived competition between them by consumers. The model of Abell aims to meet this need using multi-dimensional mixing criteria based supply- criteria based on the application. In this way, we have moved from the concept of industry to business area. In the definition of the business is necessary to take account of three dimensions: the group of customers who will be served, the functions in use (or needs of customers) that will be satisfied and the technology to be employed for this purpose. This analysis

model is used to define the SAB (Strategic Areas Business)⁶⁹ in which the company is operating. It exceeded, thus, the traditional definition of business sector to reach a definition of the business that, on the one hand, has a more restricted (only customer groups, functions of use and technologies affecting the company) and, on the other, has a connotation larger (as the three dimensions of interest can also refer to more than one product sector). This model applied to the wine sector is used to determine the business opportunities of any business and, later, to determine the competitive advantage.

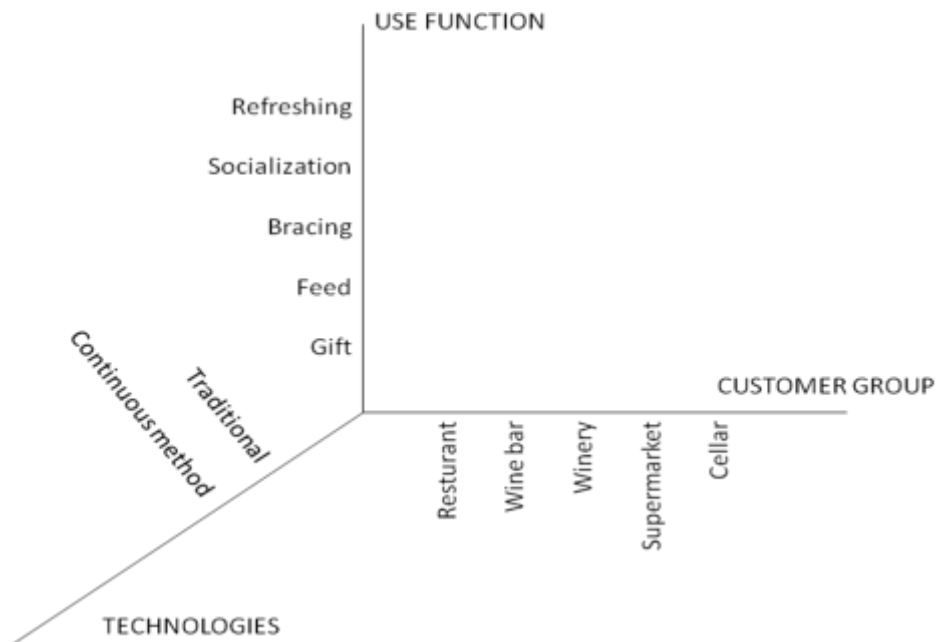


Figure Application of the three-dimension model at the wineries

Customer groups. When defining groups of customers to serve companies wineries are faced with multiple alternatives. The choice depends on many factors which can be summarized in the will of the positioning adopted by the company. In the past, attention was particularly directed to the high food and at wine bars, especially for

⁶⁹ "The concept of ASA is now being used in the literature and in business practice with two complementary meanings.'s First to define a distinctive environment / market enterprise. Depending on which unit or the activities of which serves a specific environment / market ... SBU is defined as strategically important subsystem which coincides with an area of specific market that becomes the mission of the products and services of the company. the extreme, the concept, the ASA is an activity that could be spun off from 'company and therefore able to survive on their own. "V. Valdani E., Strategic Marketing. Proactive enterprise to develop skills and driving market value, Etaslibri, p. 265.

labels that performed a positioning oriented high quality. Over time, as competition intensifies (the new competitors in the world), the spread of a new culture of wine, they taken to ensure that the wineries, although reluctance and misgivings, began to discern in modern distribution and a very profitable customer profitable. Finally, we must not forget the importance of direct sales to consumers end. Both the direct supply, as the mail-order (3%) mean that over a third of purchases is realized directly between producer and consumer without the intervention of intermediaries, or with the interposition only to the people of shipments.

Use functions. The purchase and consumption of wine are characterized by a multiplicity of functions and occasions of use, the analysis of which is essential for the understanding of the mechanisms of substitution with other products and for the study of factors under which takes place the choice of a specific wine, in different situations. Several decades ago, one of the main functions of use of wine was the food / energy. The wine could be considered as a source of energy for the work of muscle fatigue. It was, moreover, an element toning cheap. Today these two functions of use have greatly declined in importance, disappeared almost completely. This is due to two factors: on the one hand given the overabundance of the diet has generated a reduction in alcohol intake, on the other hand the working population and rural saw compress their consistency. Consequently, the consumption of wine growing segments of consumers are relegated only for holidays, when you can indulge in some more pleasure. The same function as accompaniment to a meal is resized: wine has been confined to a number of meals / year far more reduced than in the past This is justified by the passage of the role of wine as a food product of the occasion, as a result of a convergence of factors represented by the greater importance of meals outside the home as well as, more generally, the need to take fewer calories and eat more lightly. In such cases, however, this function in use is preempted by other moments of consumption, e.g. relating a symbolic roles (the wine for the toast or the bottle for guests), of oral gratification, socialization, performance. This has affected the total quantities of consumption and has instead favored the request of a higher quality wines and orientation towards more emotionally engaging. The wine thirst-quencher has lost over the decades, the original significance. For this function have been favored, by the consumer, the lighter wines

and sparkling wines. Another function of use is the compensatory technique: in this case, the consumer buy, but most of all wine consumed to compensate for problems in its structure psychological or temporary situations. Also important is the function gifts, which has historical roots and should cover a percentage of just under 10% of the market Wine. We can not forget, finally, the purchase of the wine collection, a function However, declining even to the gradual disappearance of the relevant background culture at large segments of the population. In recent years, we are witnessing a process of review that is affecting the wine in his kit as symbolic in its consumption patterns. The origin of the great cultural impetus discount wine is definitely a change in the relative consumption opportunities, methods of approach and an important operation rejuvenation practices carried on the supply side. These elements indicate a radical transformation that elevates the wine from the rank of commodity (and therefore undifferentiated) to specialty (a good stimulant with a high emotional investment and hedonistic). However, the structural data that serves as the backdrop for this historic transition is a decline in consumption, which proceeds without interruption since the early eighties and has accelerated in recent times. At the base of this phenomenon is the erosion of the segment high consumption, socio-culturally backward and linked to a pattern of drinking wine and divested routine. The rise of a more simplified structure of the meal, the need to contain daily calorie intake, the option for a more unstructured style food and increasingly divided rectory released meals, are among the reasons at the base of this progressive loosening of the traditional modes of consumption of wine. This physiological decline is, however, offset by an increase in consumer segments socio-culturally more advanced drinkers but sporadic carriers a new philosophy of drinking and in a sensitivity that does not reward more wine as necessary and customary product types but promotes brands and qualified. Looking at the main wine consumption occasions it can be observed as, compared to a decline of more habitual consumption with meals, is developing a trend - particularly marked among younger segments and modern - favoring the wine (and wine quality) at the same meals emotionally and gastronomically invested, which is exploited to the full call "Socializing" of wine. But more generally, are the opportunities to more informal and friendship to record growth more interesting. Used to denote a relationship with the product more and more

associated with moments of relaxation or leisure, faces a recovery conscious enjoyment of wine and where often the "good drinking" is at the center of an experience of more wide-ranging. Just in this sense to think of the proliferation of places of consumption unpublished and successful ("wine boutique", wine bar, wine bars and wineries revisited in key food and wine) where the drink is immersed in a scenario relation to the experience completely new wine in our country. This process demonstrates the radical change of a product is extraordinarily timely, that has been able to catch the big trends taking place in the food sensitivity. However, if it is true that wine now enjoys boundary conditions extremely conducive to the process of cultural rejuvenation, two remain still issues of concern from the consumer side: the price and the hyper offer. The marked price sensitivity of consumers today could be a disabling element to be reckoned among the factors of choice, especially if the purchase is made in the bottle shop - retail or large surface - And even more so if in the new consumers are increasingly remember young target (and therefore with a capacity of spending less). On the side of the set is again the large retailers have to deal with a consumer who often finds himself in the position of having to choose between alternatives in his eyes highly fungible with lengthy periods spent in front of the shelf, embarrassment and difficulty of choice. Obviously possible without a specialist who addresses the choice is therefore crucial than ever for manufacturers build brand highly distinctive to communicate the uniqueness of the product through the business cards coming directly into the hands of the consumer: bottle and label.

Technologies used. The manufacturing process for the production of red wine can be carried out according to four different methods: traditional, continuous, thermovinification, carbonic maceration. The first, traditional defined, is divided schematically in nine stages, above which is obtained by the product ready for consumption. They are: destemmed, alcoholic fermentation, racking, slow fermentation, racking in number of four and storage or aging. To these may be added to one-tenth, consisting of bottling. The continuous method differs from the traditional one for the power supply performed in a regular manner, but more or less accelerated, the must (or pressed) in batteries of fermenters communicating with each other, so as to obtain the extraction of marc macerated. And 'this technique using the businesses that rely on

differentiation strategy, because they are able to offer a wine with characteristics superior quality. They, therefore, pursue a method of machining to satisfy in an inimitable way a growing demand oriented to a product of high quality. With the thermovinification is achieved the separation of the marc continuous by heating at 50-75 ° of the must. This technique lends itself very good for the treatment of grapes moldy for a series of reasons of biochemica nature. These three processes are aimed at the production of red wine common. One occurs, however, the transformation carbonic maceration to obtain wines so-called "novel" that is, wines that can be put on the market within only a few days after harvest. As regards the transformation cycle of white grapes, it does not is distinguished in particular from the traditional one for the production of wine red, if not for the operation of defecation that must be carried out before that in must take start the alcoholic fermentation. As for red wines, even for the white ones are not made or grapes or cuts, in order to obtain wines with a strong personality and easily recognizable by consumers. It is no coincidence, in fact, that these techniques will come across in companies more sensitive to aspects quality of the wine. The different combinations allow to realize a parallelepiped that defines the area of strategic affairs. Defined the business, the company wine must determine, then, the competitive advantage that, on the basis of what is stated by Porter (1986), can be divided into three types:

- a) the cost advantage;
- b) the advantage of differentiation;
- c) the advantage of focusing on differentiation

The competitive advantage of cost

The wine firms are characterized by the presence of non-high economies of scale in the transformation phase, and for this reason the cost containment production must be achieved through other phases, such as the provision of raw material, the packaging and especially access to commercial channels (Spano, 1997). The bonds are strong in the sense that the bargaining power of buyers is strong, then you are in the presence of

profit margins and content must act on large volumes. Thus, it becomes difficult to produce fine wine because of the savings on the material and processing costs. Typical products covered by this strategy are those poorly characterized, such as common wines, new wines, wines with low alcohol content. The producers are those typical of bulk wine or semi-employed for cutting or the completion of the winemaking process. Those are the typical cooperatives in large volumes. The strategy is called "product-oriented". With regard to the critical success factors, there must be a perfect control of production costs, which leads to a pricing policy contained, through a knowledge of production processes high. In phase distribution should occur access to distribution channels is not too expensive.

The competitive advantage of differentiation

To achieve the goal of differentiation, it acts through image of communication through a "brand", to highlight a high quality / price ratio (Spano 1999).

The constraints are related to the high costs of promotion and support the brand, to make it recognizable to the final consumer, in addition to the need to make consistent also the intrinsic characteristics of the product, as regards the characteristics fundamental (taste, alcohol content, organoleptic).

The products are characterized by a high ratio price / high quality.

The producers, who work with this strategy, or those companies that have argued in the past at lower cost, a policy-based image on the brand and today can afford not to invest all due, enjoying an advantageous position, or companies belonging to international groups, exploit the synergies distribution of drinks not wine. These operators are "market oriented" with a brand policy designed to exploit the "Company brand" product diversification is both horizontal (range products) and vertical (quality wine).

The critical success factors consist of the quality assurance in the use of raw material and through the supply and through upstream integration, the recognition and trust of the brand, from research and development, the appropriate policy of price and access to the correct distribution channels.

The advantage of differentiation focused

As part of this strategy, operators are turning to a band restricted to consumer or to an extension of the limited market through one or more products, which are directed specifically to that area and / or the target market (Spano, 1997).

The constraints consist of strong disincentives to growth in size for not alter the flexibility and avoid investments that would not give adequate returns.

The operators are the typical small-size, operating on a limited extension of the market and with a limited range of products. Not These marginal firms, but companies at low cost but highly flexible, that make the conservation of the niche market strategy desired.

The critical success factors consist of cost control, politics for appropriate and by differences in the products offered sharply from competitors in that segment served.

8.4 SWOT Analysis

Since 2000, various reports have been written assessing the competitiveness of the South African wine industry. The most widely recognized are those by Rabobank International. Other reports include a USDA GATN report and a study commissioned by the now defunct South African Wine and Brandy Company. In the part that follows, a summary of these reports is offered.

The USDA GAIN report of 2002 focuses on statistical information such as area planted, percentage white vs. red grapes, total production, exports and imports (USDA Foreign Agricultural Service, 2002).

It indicates that the wine industry is becoming increasingly market-focused and producing wines that are acceptable to the world market at prices that are offering value. It reports on its international market share growth. It does not offer conclusions or opinions.

Of more value, is the SWOT analysis of the South African wine industry

<p>STRENGTHS</p> <p>Ideal climate, with many different regions.</p> <p>Overall good image.</p> <p>Different wine style; elements of Old and New World.</p> <p>Attractive varieties eg. Shiraz; Sauvignon Blanc.</p> <p>Strength in basic and popular premium segments and wines in super premium and ultra premium segments.</p> <p>Low costs producer, land and labor is inexpensive.</p> <p>Strong position in a few markets eg. UK, Netherlands.</p> <p>Flexibility.</p> <p>Less in need-to-sell situation than some other countries.</p>	<p>WEAKNESSES</p> <p>Highly fragmented industry structure.</p> <p>No strong companies or brands in the premium segment; in UK only 2,5% sold above GBP 5 per bottle.</p> <p>Only 2 brands with 1 million + cases, only in popular premium segment.</p> <p>Not enough red wine.</p> <p>Not consistent enough.</p> <p>Too many “me-too” brands.</p> <p>Hardly in USA.</p> <p>Capital scarce and expensive.</p> <p>Not involved in global consolidation process.</p>
<p>OPPORTUNITIES</p> <p>Internal consolidation; build strong companies.</p> <p>Develop strong premium brands as a trade up from existing popular premium brands.</p> <p>Increase market share in key markets.</p> <p>Access to USA and Canada.</p> <p>Develop on-trade distribution in expert markets.</p> <p>Get involved in global consolidation process.</p> <p>Wine tourism.</p>	<p>THREATS</p> <p>Fluctuations in the Rand effects cost of imported equipment and uncertain margins.</p> <p>Continued oversupply of world market, pressure on margins.</p> <p>Global consolidation.</p> <p>Risk of being trapped as value-for-money producer.</p> <p>Uncertainty for investors with respect to politics.</p>

Based on this analysis, I proposed the following strategic options:

- Internal improvements – investments of profits into optimizing branding strategy rather than paying out profits to members – especially in the case of co-operatives.

- Consolidate in South Africa – to develop a 2-3 million case brand in the premium segment.
- Seek an international partner – access to finance and international experience. Hopefully this will trigger further international investment.

“An inquiry into the competitiveness of the South African wine industry”, was commissioned by the Wine & Brandy Company (SAWB) and published in October 2005 (Esterhuizen & Van Rooyes, 2005). This report highlights the major “enhancements” and “constraints” of competitiveness of the wine industry in South Africa and concludes with four proposed strategies.

The five major enhancements include the intense competition in the local and international market: the availability of unskilled labor; the regular entry of new competitors into the market; the production of affordable high quality products; the production of environmental friendly products.

Other factors that are rated as positive are economies of scale; strategies by wine firms to utilize quality technology in the vineyards and cellars; the availability of competitive local suppliers of primary outputs; the high level of trust and ethics in the production process; continuous innovation, research and development; investment in human resources; scientific research and stringent regulatory standards in the industry.

Only three major constraints are listed: The strong Rand; the fluctuation in the exchange rate; and the low trust in political support to drive a second economic agenda. Other constraints include the difficulty of starting a new business in the industry, the competence of the bureaucracy in the public sector and the burdensome administrative regulations, crime factors and aspects of South Africa’s labor policy.

Uncertainty on matters related to South Africa’s Black Economy Empowerment and transformation policies and impact of the tax system were also noted as constraints. Together with cost of finance, the quality of skilled labor, the land issue and the size and growth of the local market.

Based on this study, the following strategies were proposed:

- The development of ‘Brand South Africa’ to portray the uniqueness of the country as a wine producing region.
- Introducing measures and approaches to combat the sectors reliance on a weak Rand value.
- The promotion of successful BEE activities.
- The establishment of a sound industry government partnership to stimulate growth, investment and development of the sector.

Linked to the report on the ‘Changing competitiveness in the wine industry: the rise and fall of wine countries’ (2007) Rabobank analyzed the competitiveness of South Africa again, this time comparing it to the competitiveness of other wine producing countries like Chile, Argentina, France, Italy etc.

In terms of production factors, strengths and weaknesses are listed as follow:

	STRENGTHS	WEAKNESSES
Geography	Same time zone as EU;	Long distance to markets;
Climate	Mild to warm, many microclimates;	Annual quality shifts; High disease pressure;
Land	Numerous terroirs; Limited space for development;	Increasingly expensive;
Raw Materials	All modern grape varieties; Pinotage unique;	Virus-infected vines; Too much white; Water availability; High cost of technology; Glass supplier monopoly;
Labor	Skilled management; Low, but increasing labor costs;	Farm labor unskilled; Vineyards not mechanized;
Capital		Expensive and scarce; Limited foreign investment;
Infrastructure	Good roads;	Capacity at ports limited in season;
Knowledge structure	System being built;	

In terms of the industry structure, it is noted that the fragmentation is high and the number of smaller wineries continues to grow. The top 10 wine companies account for 55% of the total exports. The level of consolidation is comparable to Chile and is low – making it difficult for foreign companies to invest in strong premium brands.

In terms of marketing, branding and style, the major weakness is the absence of strong (popular) premium brands. Despite the success of Kumala (2.4 million cases) and Kaapse Pracht (1 million cases) South Africa is perceived primarily as a supplier of

cheaper wines. As yet, no distinct South African wine style exists and to date, no “icon” wines have emerged.

In terms of the domestic demand, most of the domestic wine market is based in basic wine and does not stimulate and drive innovation. However, wine tourism is well developed.

The government is regarded as reluctant to provide structural support since its focus is on transformation, land ownership and black empowerment.

In terms of economic variable, the interaction between companies and the exchange of knowledge is recognized and said to be increasing. The high cost of capital appears to be hindering entrepreneurial activity in the industry, while the fluctuation of the rand remains a challenge.

In summary, the report indicates that South Africa is on the verge of a second repositioning — having moved into the market in the 90’s as a new world producer, it is now carving out its own position, However, without consolidation and the development of strong premium brands, it is feared that South Africa will continue to be regarded as a producer of ‘cheap’ wines (Rabobank International, 2007).

The most recent report addressing the areas that are challenging the competitiveness of the South Africa wine industry, was published by WOSA in January 200. Eight problems are were identified while researching ways of “Trading up South African wine in the European country”

- The structure of the wine industry is highly fragmented and comprised of many small producers – resulting in a weak structure.
- The domestic market is not strong and is declining resulting in a weak domestic profit pool and limited demand for innovation.
- Although some strides have been made in the popular premium segment, there is a lack of strong brands in the premium segment resulting in the lower cost image that prevails. SA brands seem to lack provenance; integrity

and authenticity, required in the premium segment. While the estates do well at this level, their volumes limit visibility.

- Lack of clear USP's for the country category. The lack of clarity reduces the impact of communications with consumers.
- Lack of clear USP's for the country category. The lack of clarity reduces the impact of communications whit consumers.
- Value of the rand is volatile and effects margins dramatically, especially on exports.
- Transformation of the industry in terms of land reform and black economic empowerment scorecards is not as straightforward as with other industries creating uncertainties.
- Cleaning up the vineyards to eradicate leaf roll virus and mistakes made in matching varieties to suitable terroir.

Incorporating these issues in an affinity diagram results in the emergence of three broad categories, namely that of fragmentation, branding and domestic issues.

FRAGMENTATION	BRANDING	DOMESTIC ISSUES
Structure of wine industry	Lack of strong premium brands	Weak domestic market
	Lack of icon brands	Volatility of ZAR
	Lack of clear country USP's	Complicated transformation
		Vineyard state

The conclusion drawn from the studies is that the South African Wine industry has the potential to improve its competitiveness through a strategy that combines consolidation and branding. The domestic issues involve long-term investment and government support to effect change. The fragmentation and branding issues can be addressed by industry immediately and by the industry participants themselves.

8.5 Value Chain

The value chain can help to identify the competitive strategy most suitable for the company (Porter, 1985). According to the researcher, in fact, the company despite being united must necessarily be divided into several parts in order to seize competitive advantage. This division is necessary because every part produces added value and this tool is used to understand which sector the company has an advantage sustainable competitive. Porter distinguishes in detail the activities of a company into two broad categories:

- primary activities, i.e. all the activities related to the physical implementation of good,
- support activities, i.e. all activities that support the core business activities.

An enterprise should assess its strengths and weaknesses in each activities and then compare their activities with those of competitors. The application of the value chain for wine companies can identify those functions, primary or stand that is, that contribute an important factor in determining competitive advantage. For the American scholar primary activities are inbound logistics, the operating activities, outbound logistics, marketing and sales and services, not all, however, assume the same importance within an enterprise wine. The specificity of the sector, in fact, leads to highlight a greater weight to some than others. The most important activities are certainly those related to the process technical production, marketing and sales. Although the organization and management of physical and information flows, both incoming and outgoing, contributes the creation of value, the specific management problems of the wine business lead to having to treat here of these activities as the main

functions of the value-added business. The activity of the wineries is characterized by the extreme importance of technical and production process in the strict sense. The technological processes are characterized by a large variety attributable to two factors: the first, with the different size of the company, the second reported the different varieties of wine, which can be obtained from grapes⁷⁰. Basically there are two types of wine:

1. the red winemaking;
2. the white winemaking.

These two procedures share many common characteristics, some operations carried out by winemakers in the early stages of their vinification are the same even if the intervention times are not constant, but changing from situation to situation, from wine to wine also depending on the quality of the grapes. For red winemaking the procedure involves first alcoholic fermentation followed by maceration of the marc and, finally, by malolactic fermentation.

The white vinification provides, instead, first the extraction of the must followed by the alcoholic fermentation and, finally, by the prevention of oxidation. The hard work of production processes leads us to consider the operational activities as one of the primary functions of a winery. This is so more so in the presence of companies that decide to pursue a competitive advantage based on differentiation or, more importantly, focused on differentiation. The increasing competition has led to increasing attention in respect of the production process especially for companies that have invested in the cultivation of vines that, natural features, require greater attention and the presence of qualified staff (agronomists and wine in the first place).

The activities related to marketing and sales are a function that, over time, is becoming more important. Actions marketing applied specifically for wine products can not be adapted to the production of wine in general, but must be specifically selected depending on whether the common wines or wines light. The importance of activities related to marketing and sales is also demonstrated the distribution choices that

⁷⁰ Spano F.M. (1997), *Opera citata*, p. 207.

companies have to face wine. the distribution in the sector is characterized by some important factors:

- the high fragmentation of the points of sale in the market;
- a common practice to direct supply from the manufacturer;
- the lack of leading brands due to the extreme pulverization the offer;
- used primarily for the consumption of wine in your region,
- the high incidence of transport costs.

For the peculiarities of the sector a significant presence at the national level is possible only to undertakings which pursue a strategy of diversification product, supported by investment in support communicational image such as to allow a high level of price positioning, covering the sustained distribution costs (Spano, 1997). The high costs that can be generated from activities related to the marketing and sales often lead companies, even larger ones, to resort to a sales force of external type, in particular, there is the type of sales through representatives non-employees. Support activities, in the scheme of Porter, are the infrastructure activities, the human resource management, technology development, supply.

Even for these, as already seen for the primary activities, it is necessary to carry out a distinction between the most relevant and less relevant for businesses wine. As part of the **infrastructure activities** take on a quite important **the financial assets** that have an impact on the management consistently of wine companies. Financial management is not uniqueness within the sector does not exist, In fact, a standard in the financial structure relatively to the investment of capital and funding sources. These differences have their origin in the different ability to set the business long the supply chain. It is not easy to deduce the reference values in the different categories of investment. The specificity of the sector leads to highlight a remarkable weight of tangible assets, which can exceed 50% of the total investments, a minimum weight of intangible and financial assets, even though the latter in some cases reach a percentage

of 15%, and a weight quite as important as the inventories of cash liabilities (trade receivables in particular). As for the uses, even for the sources is difficult to draw values of homogeneity relative. Social capital, in general, does not exceed 10%, even if the equity can arrive at percentage close to 50%. Considerable importance current liabilities that have turn out to be far superior to the liabilities consolidated because there is a common tendency to not borrow, trade and not in the long term. The choices of a financial nature are influenced by the characteristic length the financial cycle in this sector, which leads to penalize the profitability in the early stages of expansion of the production base. The 2007 survey of Rabobank showed an increase in capital expenditures, (228 million rand in 2005 compared to € 204 million rand in 2004), while working capital has increased only 2%. From the side of the shell, in the presence of a low cost of money (3.8%, 0.2 percentage points less than in 2004 and 1.8 percentage points less than in 2002) there has been a slight increase in volume of debt, and those are expensive increased slightly from 108.6% to 109.9% of the equity, however, confirming the usual balanced capital structure. The cash-flow always exceeds the investment spending. **The management of human resources** is one of the areas with the highest value added. Wine companies have similar problems to that of companies in other sectors. The figures type sought are those related to:

- personnel management function;
- administrative staff;
- personal cellar;
- staff employed in the vineyard.

The only figure that may be considered characteristic of the sector is that of the personal wine-type managerial and specialist staff. These, usually, companies operating in the employ of the head of the technical production, which, often, the same cultural background.

There are rare cases in which, especially in small companies, the figure is a wine consultant outside the company.

The process of technological innovation is the typical object function research and development. This innovation requires research, analysis, research project the company in meeting the future needs of the market in a process continuous change. When it comes to research and development (R & D) is necessary to make distinctions leading positions within these two categories. The research, which is the set of studies, analyzes, processes aimed at increasing resources of both scientific and technical knowledge in the possession of the can be basic or applied. Development understood as the testing of innovative ideas ongoing experimental verification and prototyping, can be distinguished in proper development or adaptation / improvement. In technological innovation we can identify different classes of innovations:

1. innovation of production processes,
2. product innovation,
3. combinations innovative processes and products.

In the wine sector observed changes both in respect of the products is in relation to production processes. The implementation of product innovations and process, as well as combinations thereof, depends largely on the strategies chosen by the company in relation to its markets and its size (Spano, 1997).

With regard to the first it is observed that in the wine sector recourse product innovation is relevant with the aim of diversifying the range of products offered. This is typical of large companies with broad national and international, which through diversification and differentiation, offer customers an additional element specifically designed for their needs, which have invested resources, thanks to the promotion of the brand and at high volume can return obtainable in liquid form, investment, in a limited period. This strategy is difficult to pursue by small producers could hardly bear the costs of launching the new product, and for the which inevitably returns on the investments made, could not be realized. In relation to the second type of innovation, in the wine sector not attends to the implementation of new processes, such as to change the way of producing wine. The processing steps are always the same, and even companies with R & D centers are not subject to the technological revolution, but more improvement, in

the sense of rationalization or of greater preservation of stability of the wine and the various steps against chemical deterioration.

The adaptive process improvement and is characterized by changes in manufacturing process, which do not generate any technological leap, but the advantages of another type, such as increased stability in the treatment of the product, the reduction in pollution by waste water, the lower consumption of productive resources⁷¹.

Supplies represent a fundamental role in the industry. Not all businesses have problems in the management of vineyards, as they can directly acquire the grapes or the bulk to make wine. The problem is most relevant for companies that aim to producing quality wines, which can not avoid making investments in force, even though these may not be sufficient for the entire production. The most common is the situation of production-buying grapes in pre-determined proportions business plans for the long term, with an incidence of own grapes which tends to decrease as the size of the economic entity (Spano, 1997).

The different combination production-purchase varies depending on the social form and competitive strategies pursued. Cooperative societies, in fact, not produce the grapes, but the gain as a capital contribution by the shareholders. The situation is different for businesses wine and wine. Companies wishing to implement a strategy-high price high-quality must acquire agricultural properties making processes of integration upstream of the supply chain. It's the typical strategy implemented by producers who are seeking to establish an image of high quality with a brand as a symbol of wine of the product. In other cases, firms rather than proceed with the purchase of vineyards, agree with the owners to send their wine technicians to keep track of the growth of the screws and the ripening of the grapes in order to obtain a raw material first quality certified. The procurement function has essentially two issues:

- a. the choice of suppliers;
- b. the degree of vertical integration to be taken.

⁷¹ Ivi, p.381

a. **The selection of suppliers** is an act that is gained by companies in different ways depending on whether they are:

- Suppliers of grapes destined to become fine wines.;
- Suppliers of grapes for wine consumption or common table.

In the first case, the firm tends to favor stability of the relations in as the quality of the wine depends on the quality of the grapes and the controls are more stringent and timely: the trust between producer and buyer is essential. In the case of grapes intended for wine other or to other uses, the ratio is less narrow because the interest of the manufacturer becomes to increase the yields per hectare, to sell, to the same bid price, a quantity greater than grapes.

b. **The degree of integration** can take on different meanings within the chain. In particular, the integration develops upstream of the supply chain between companies farms and firms, specifically for wines with a designation as to produce quality wines, in compliance with the specifications, the decision to integrate upstream is not only necessary, but it becomes obligatory. The situation is different in the case of common wines because the cost of the raw material, because of excess production, is less than the cost of production of the same.

Chapter 9

Functional level strategy in the South African wine history

Until now have been highlighted strategic marketing operations in the wine sector starting from the problems of the international globalization of markets, the decision to work abroad to the choice and establishment in the country chosen target. Of Consequently, the presentation of the main marketing strategies operating in the same sector is the subject of this chapter. The treatment does not ignore the original meaning of the Marketing Management, nor the indissoluble binomial wine - an area where typical and localism intersect in order to enhance, protect and enhance the wealth of a place.

It will be found as easily as it is natural that relationship that combines the product wine to its territory of origin and as, moreover, it represents a perfect means of communication of traditions, history and uniqueness of a place, where typical food and products they are the masters. It is wrong, therefore, that implementation of an operational plan for marketing to find its strength in the area of origin of the product that is the subject. The focus on main levers of the marketing mix ends the fifth chapter of reproducing, in parallel, the characteristics, organization and evolution of the wine industry. Shall be deemed effective the marketing policy that will ensure consistency between the use of these levers, the objective predetermined and rationality in the location of a resource, limited by definition, among the various elements the marketing mix.

9.1 Strategies and role of territorial marketing: Branding value

It has been long since debunked the myth that the territory traditionally represents the area geographic political boundaries and physical well-defined. The limits of traditional and modern cultural needs have helped to give a completely new. The territory becomes source of creativity, where the different expressions of time can take shape: the economy, technology, history, art, tradition, nature. Territorial marketing becomes element essential, focusing in identifying the set of values and vocations characterize an area that is so because, in addition to a morphological and natural, it is identification of a community over time has given a given area personalities, styles of life, culture and economic contributions that make a single territory. Territorial marketing is aimed at the promotion, both locally and internationally, production characteristics, the goods produced, the elements of value associated with a given area constitute an aggregation of services and business opportunities. The ultimate goal is to optimize physical resources, natural and productive to reach an interest of stakeholders involved, leading to economic growth tangible and structured. The strategic importance of initiatives refers to the comparison of an open area with other like him to check the level of results, and create excellence to develop and treat the core business. The concept father territorial marketing and its endless wealth consists in consolidating community as an expression of a territory, its derivation and symbiosis. The latter, in fact, is an important vehicle for the continuity of traditions and promotions initiatives related to the different types of marketing. Territory and communities generate brand, making it a key for their identification and recognition at each target target audience. The community, in particular, supports the brand with the way of life, the culinary traditions and in the people. It is clear then reason for which the local marketing is a growth possibilities available for each type of land, corresponding to the profiles and the objectives set, and for each company in it present.

9.2 From marketing to marketing mix in the wine company

"You can not learn to run without being able to walk." The reference to this ancient proverb is not random: in fact, even before analyzing the components of the marketing mix should be understand its true meaning. It is usual to define the marketing mistake as the set of techniques of selling a product. However, contrary to general opinion, it is the joint work of thought and action of the company, making the customer the hero of the its activities, enabling it to better sell its product, which is different from and sell it. Marketing is not, therefore, a commercial function, nor its articulation, the latter being reductive activity with respect to the potential of the principles of marketing. Nor is a way of gaining an end in itself, but rather a system to improve the relationship with the customer, a sign of a growing and lasting value for the whole company. The current introduction of the marketing function in almost all companies is due to two factors: the growth of competition between companies, aided by a geographical extension of the market and its deregulation, and the increasing the bargaining power of consumers, today more than ever, they can choose among different products that meet the same needs and benefit from many more tools to inform and guide their choices. All these factors have prompted companies to develop a specific function to manage the relationship with the market: the marketing, precisely. Two of its objectives: providing interaction between the consumer and the product, through careful selection of the market to reach, to structure the offer in relation to the preferences of consumers. Also, if the marketing we expect the best results, its action will not have a beginning and an end programmed as is the case for any other operation commercials; will to contrary, a constant element in the organization. Among the many definitions and correct that experts offer in the way, the more complete it would seem that describes marketing as the complex of activities which originates from the study of the customer / consumer, and more generally of the demand and competition, aimed at the achievement of the Company's medium-to long- term through the satisfaction and loyalty of the consumer.

Translating what was said in the wine world⁷², it is imperative to make a clarification: the marketing of a single sector does not exist, just as there is room for marketing that involves only large industries, all also applies to small craft that make good products such as wine. Furthermore, the expression "wine marketing" does not mean anything unless the appropriate case reference for the actor: the wineries, distributors, consortia of companies, and so on. Each of them has its own authenticity, its own market and different marketing needs. One wonders, at this point, which are the phases of programming for a successful marketing strategy. The first factor to consider is definitely the expertise in marketing, then the knowledge of the market and then the definition of the offer, bearing in mind their distinctive properties, then the sale of the product. By itself any product, even the best, do not sell yourself. It is necessary, first of all, a study of the application (needs, purchasing behavior, satisfaction), competition (behavior of other similar companies) and the competitive general (investigation of activities of similar sales in other territories and markets potential), to be considered a leading company.

In the wine sector companies are oriented to the market and the consumer, replacing the old entrepreneurial intuition, based mainly on the sale of the product material, with a selection of the best opportunities on the production-oriented markets. These are the essential elements to make the marketing strategy tool with which to win the war, and not reduce it to a simple tactic, which would only win a battle.

The real strategy is, therefore, one that considers all decisions⁷³ that allow the company to grow from a current state to a future, hopefully better. The marketing strategy sets out the objectives, identify your target market and the marketing mix formula, namely the characterization of the offer to reach that target and that goal. These are the pillars that properly combined, they are able to hold a real marketing strategy. As for the objectives, we must recognize their heterogeneity and variability (sales quantity, value, abundance of customers, market share, contribution margins, customer satisfaction and customer loyalty, return on investment) and then associate to

⁷² Cfr. Hausmann C. Marketing e strade del vino. In viaggio tra saperi e sapori (2005) p. 59 e ss.

⁷³ Cfr. Tesio L., Decidere. Piccola enciclopedia del comportamento organizzativo (2004), p. 3 ess.

each a corresponding strategy. For example, if a wine producer had as its objective to increase sales, not This necessarily means increasing the number of customers, you can simply boost the per capita consumption of existing customers. However, if the manufacturer decides to put the customer at the heart of its strategy, because he knows he can do cross-selling, then you must focus on the number and try to increase it. The fact that the objectives are varied means greater difficulty in achieving them all at once. In this sense, it is important size the achievement of the objectives in terms of time (short, medium, long) and space (Local, national, international), perhaps placing them along a hierarchy of priorities. Particular the subsequent selection of the target market, so that the goal is achievable default and the dosage of the levers of the marketing mix. In this regard, it is assumed the case of a distributor of Italian wine. He once made the objectives, must choose which segment address (wine bars, restaurants, department stores), assessing whether it pays to serve all target or focus on some of them, and this depends on the objectives and affect the characteristics of the offer. In the case in which decides to concentrate on wine bars, will need a wide range of brands and types of wine of medium to high quality, will reduce payment times because the frequency of purchase will not be very high. If, instead, was interested in the GDO, the quality will be low to medium, the time of payment hardly negotiable, but the frequency will undoubtedly be greater. Substantially, compared to the target, can be alternating between three types of strategy:

- Undifferentiated: in the presence of coincidence-target total demand.
- Separation: market segmentation has detected more target goals. Note that, to the growth target to follow, the greater the costs to follow in the future.
- Niche: there is only one target, usually small enough to hit.

Now, in accordance with the objectives and the selected target, it will combine all of those factors, suitably regulated, distinguish and differentiate their offerings from competitors. This refers, generally, to those contained in the acronym of the Anglo-Saxon "4 Ps", that is:

- Mix of products and services (product)

- Mix of prices (price)
- Mix of the factors of distribution (placement)
- Mix of the factors of communication (promotion)

Each is, in itself, an element "strategic" because it requires careful planning, but also "Tactical", because with respect to variations in environmental conditions is compensated by replacing in the components of supply. Suppose, for example, a wine that has defined its strategy with objectives, targets and marketing mix. At a certain point, due to work in progress that hamper access, at certain times of the day the place is half empty, because the work discourage the customer to come.

You can avoid this problem by designing a happy hour, sacrificing prices temporarily but without that the customer should not go, or worse, to move from competitors. So we understand the strong dependence of the strategic choices to marketing analysis.

9.2.1 "P" - product

The product is the first of the four elements that characterize the "Marketing Mix", a term referring commonly use in integrated form of the famous "4 P" of marketing: product, price, placement, promotion, which together make up the company's offer, defining the presentation and subsequent sale on the market. The strategic combination of these variables allows in fact, to sell the product at a given price at point of sale carefully selected. The communication, for his part, creates awareness offer. Each of them presents the peculiarity that differentiates them from other, depending on the field of reference market, geographic scope of the target, the objectives set in the strategy and other factors. There is talk of a use in an integrated form of these marketing tools, both for identify the dosage that the composition, and to ensure that each of them is used consistent with each other and with the strategy, in the first place. This could be translated as a culinary metaphor: if the elements of the marketing mix were the ingredients available in the kitchen, they must be assayed

compounds and to obtain a good recipe (i.e. a good product). Some will be used and others not (composition), and also those used will not be measured for prominent or in contrast with others (dosage).

In the world of wine, in particular, the choice of production⁷⁴ much influence on global characterization of the offer. In fact, in the case of a generic winery, many are the elements to consider in this regard: first, the selection of varieties, native (those cultivated and distributed in the same historic area of origin) and the "international" because transplanted from other areas of origin.

The question arises: where to draw the composition of a product in terms of wine? Simply by two factors: the first of a technical nature, which prefers wines that score the yield best in terms of quality to be obtained, the other of a managerial nature, highlighting the wines required by current and potential market. In addition to these, numerous other factors affecting the product, by elements softer but essential for the consumer (the color and perfume) to technical elements (Use of organic practices), packaging or aesthetics of the product (the shape, the color of the bottle), cap (classic cork, plastic or glass, rising by modern technology) and the label (information and back doors). It is common to think that the product of a winery both the wine. In reality, the wine is not the only component of the product, but there are others from consider. The wine, in short, has many facets, it is spoken in relation to the characteristics intrinsic distinction between pure wine or assembly, aged or ready to drink filtered or not, and if it is discussed in connection with the secondary characteristics and ancillary, such as the bottle, label, company visits and so on. Elements that grip the consumer final evaluates them together, before we get to the final choice of purchase. In addition, the wine to be produced must be assessed in terms of the type (white, rose, red), in terms of grapes used and winemaking techniques. Each of these elements depends in addition to the requests for market, the capabilities of those who make the wine and especially the properties of the territory in which the wine is an expression. Nothing is taken for granted in the wine world, because everything needed to reach the final quality and economic returns. Next remember that the product has a strong significance in

⁷⁴ Cfr. Rouzet E. Seguin G., *Il marketing del vino, Il mercato, le strategie commerciali, la distribuzione* (2003), pp. 33 e ss.

communicational perspective, think of the good fortune to have a great wine. Also on the label is expressed in a few words, the label and the label against both enjoy great prestige both reported for the normative content (quality label, the presence of sulfites, etc.) and in terms of Attraction for the consumer, sparking at most the imagination of the manufacturer. Label chart, the company name, brand or better (and if it becomes) the brand. Finally the services, often overlooked by those who think that wine sells itself. Their importance is twofold: on the one hand form the basis for customer loyalty, on the other hand increase the potential of the product wine. Recalling that a loyal customer is worth much more than a merely satisfied, we will say that those elements will make a difference! Especially true when it comes to wine. Examples are, all after sales services and visits, related to the opportunity to taste and buy.

9.2.2 “P” - Placement

In response to the demands of consumers who are increasingly prepared and the proven success of the wine, sales strategies⁷⁵ leave room for creativity, changing the whole landscape of the distribution of quality wine. The way to sell and buy wine in our country continues to change at the speed of light, in order to adapt quickly to the demands of a consumer audience that is becoming wider and prepared. Until a few years ago, followed traditional patterns and sales strategies were poorly differentiated, as opposed to today. Most of the wine reaches the consumer marketed through retail sales channels, but we can not forget the tip which in recent years has produced the on-trade channel, applying a different mark up in restaurants, bars and other exercises on trade. Globally, there has long been a growth in consumption outside the home of wine; demonstration of the change in consumption habits in traditional markets. From the side of the producers, the choice of the distribution channel depends on the customers and the positioning chosen. Direct selling is preferred for the sale of bulk wine for their own consumption, ensuring a turnover not negligible. Make use of means enjoying a good

⁷⁵ Cfr. Largo consume. Pianeta distribuzione: rapport annuale sul grande dettaglio internazionale. Supplemento al num. 7/8, 2008, pp. 5-18

product presentation and the security of a direct relationship with the consumer. Essential requirement for success is, among other things, the allocation of a place dedicated to the sale, reception, presentation of products, the tasting. Some companies specialize in the single task of tasting-sales, other operations in different tasting-sale, visit the company, accommodation and catering. The latter formula the world's most popular wine, ensuring an exclusive contact between producers and customers in the company. The wine merchants, independent or franchised, are a good percentage of distribution in Italy, and organized to ensure a traditional sale of their products. Initially favored an activity that combined the sale of wine in bulk to private and sales in bottles, wine bars have opened today to a full range of wines and spirits as well. Their activity is therefore more dynamic than in the past, always looking for products and selective acquisitions in order to meet a loyal clientele or in customer loyalty. Irreplaceable in the supply of wine products: large-scale distribution, characterized by chains grouped under several brands, becoming the main place of purchase for consumers. The current market environment has contributed to the development of new methods of marketing and selling products, forcing a greater professionalisation of the main brands to ensure the success of sales to customers who are increasingly demanding, through the balance in Sets, for the presentation of products on the shelf, attractive promotional campaigns and awareness-raising activities of the customers. The mass distribution develops more and more own brands and for some specific signs, thus completing this strategic asset. The circuit is certainly more dynamic Horeca (hotel, restaurant, café), embodying an outlet is not negligible in the sector and this is an important means of communication for the market. The restaurant chains represent a market with attractive prospects especially for individual producers because it promotes penetration useful to local or regional level.

Positioning sensory wine: quality management

There is, in fact, an international wine tasting? There are, in other words, characters common to taste wines leader in major international markets? The answer is yes, in the sense that within the segment prices or color can be compatible tastes, but that does not mean that their products are "international". Speaking of taste, quality or market means first consider the consumer, so the elements they wanted in a product.

Among the most important: the health and safety with respect to the use (for example, not to injure yourself when you open a bottle), and the satisfaction of hedonistic expectations (from the product itself and the image it conveyed), the right quality / price, ancillary services (information technology). Quality for consumers is this.

A weak company, even if just one of these aspects is countered fierce competition able to respond quickly to these needs, in order to deprive it of the market shares initially held. The immediate response to the expectations of all consumers defines the quality of the product International⁷⁶. A wine with an international flavor at the same time is what ensures the protection of health, safety use, satisfaction during eating and other services. Belong to this category: white and red wines, processed with a single grape variety wines and cutting, fresh wines made in regions with a viticulture which allows full maturity and those produced in hot, dry regions; European wines, from the cultivation of the earth and ancient wines from other countries viticulture pretty young. What I have just described is a proof, rather than the existence of an international flavor, with a plurality of wines, arising out of human diversity, geographical and cultural producers. Diversity are essential to consolidate the image of wine and make it special among the food quality and taste.

Quality: a word often abused, most often misused; thought to wrap a bit of everything '. Together with innovation and differentiation, it is a viable solution for business success in the conquest of the domestic and international markets. The attractiveness stems from its ability to parameters of different nature, some of which are detectable label and the sale, other less obvious and more subjective, I would call "hedonic variables." Among these detect the taste, the color, the ability to be in the market to stand out from the competition and be talked about.

Legally, the quality of a good or service is defined as the ability of a product or service to meet the needs of both explicit and implicit user. The generality of this definition, let us imagine how the quality is a multi purpose term. Just think of the vast

⁷⁶ The concept of "universal product" is not unique. In some cases refers to the presence of standardized physical attributes, including the packaging and the brand, in every country and for every product, in other means of image and positioning, everywhere perceived as homogeneous and, in other cases, is a product manufactured and assembled in many countries of the world

variety of requirements in the field of food: nutritional and hygienic quality, service quality and availability. However, when viewed individually, these prerequisites are not sufficient to explain the concept of quality. Symbols, signs, myths and fantasies are together essential in the system of choice of the modern consumer. All taken together, they play a fundamental role in the purchase of the product and they not only affect the success often. At the beginning of treatment it has been said that selling a wine is a way to make itself heard, tell others who we are, where we come from, sell the difference. In times like these, the diversity from other manufacturers is the result impressiveness of those intangible elements that make up the quality. Today, the value of quality has grown steadily, becoming the only characteristic that can not be reproduced and imitated a product. Quality, therefore, is the real asset to the company. The side of the producer, then, the focus is how to produce more and more connected to where produce. It goes without saying that respect for the production environment, the origin of the product, the preservation of the landscape and its modeling in the area are perceived by the consumer, such as value signals that determine different effects as the final price of the product. It must be recalled that, in addition to play the lead role in competitive environment, the modern consumer on the role of a real explorer is able to grasp all the nuances, contradictions, the sense of the impalpable behind any marks or labels. So, the real difficulty for the manufacturer is no longer limited to the manufacturing quality, but to know how to manage over time. Nothing must escape, then, the control of quality management.

In addition to the above, is of great importance in quality assurance. The term "certification" is derived from the Latin *Certum facere*, which means "to make certain, obvious." The certification is, therefore, the statement made by an appropriate body (not linked to the supplier or purchaser) that the product and the quality provided by the company comply with a certain standard. The operation consists of a certificate by which the body gives the company the right to use its brand. Setting activities according to the criteria indicated in the reference standards, companies assure customers that their products or services below a certain level of quality and, above all, to be able to keep in time with a constant commitment to improvement, according to the their needs. All

aspects up to now form part of the Quality System⁷⁷, which is a set of resources, behaviors and documents that testify to the company's activities and how to keep them under control.

9.2.3 “P” – Price

When the wind blows from the crisis, the temptation to dip into the lists becomes stronger and stronger, as the greater the tendency of consumers to prefer choices to save rather than those of consumption. Talking about wine today, especially in our country, does not leave much room for the determination of a perfectly profitable price of its quality.

Undisputed element of the marketing mix, the price⁷⁸ assumes the role of scapegoat for a long series of negative elements in the wine sector, intimidating scenario future of a sector that until a few years ago has experienced its greatest euphoria. The price is considered the most famous and notorious element supply company from which, mistakenly, is made to depend largely on the preferences of the consumer. "Mistakenly" because not everyone knows that the price as a marketing tool, it is intended to affect the relationship between companies and consumers, which is why any strategic decision in this regard should be undertaken with knowledge of the facts and taking into account the effects that may have. It is not always true, then, that the decision to purchase a product is formed in relation to the price, but rather the expectations of use of a product or service, and then the price. If not, we all want only low cost products. But I do not think this will happen, especially for us young people are increasingly being drawn to capture the quid more than a commodity has over another, which leads us to buy it at any cost. It seems to me that the wine product perfectly reflects what was said. The latter, in fact, incorporates a lot of things: a brand, an experience, a territory, a memory, and much more. In this sense, the first thing to ask

⁷⁷ Cfr. Housamann C. ; Marketing e strade del vino. In viaggio tra saperi e sapori, pp. 91-106 e 173-190.

⁷⁸ Cfr. Bertoli G., “la politica dei prezzi: gli aspetti gestionali”, in E. Valdani, C. Guerrini, G. Bertoli, Marketing Globale (2000).

Vedasi anche Busacca B., Ancarani F., Prezzo e valore per il cliente. Tecniche di misurazione e applicazioni manageriali. (2004).

yourself is "how to fix the price"? The literature lists many criteria, from the simplest, which is called the "method of 3C" to the more complex, defined in relation to the objective wine (How I produce? With that style?) And the market (What channel can I contact? regard to cost my wine?). In the latter case, to define a price, it is best to start by setting a margin profitable business activity and, in cascade, arrive at the price of the bottle (top-down approach). Or, conversely, to be estimated production costs, as sales and marketing, taxes, depreciation, applies its own mark-up to arrive at a price defined (bottom-up).

The pricing and the "method of the 3 C"

1. The first "C" to consider is the cost: the minimum value below which we can not go down in price determination, not to lose value. There are special conditions: for example in the case in which a product is to maturity. Think of the white wine ready to drink: If you do not want to be thrown into the sink or used for salad dressing (and in both cases the user will not be happy) we have to think about how to get rid of it quickly. A sale below cost may be a good method. As long as the problem does not become structural, in which case we must also think the assumption that the product is not suitable for the market.

2. The second "C" is that of the client: the price that he is willing to pay, is the speed at which a producer can aspire to. Exceeding the upper limit, there will be no safe purchase because the price he requested goes beyond the purchasing power of the consumer. This "C" unlike the other is not easy to find, because while the costs are known, the tendency of the client to pay or not a certain amount will be deducted from his behavior. In this sense, it is perhaps easier for a company already in existence that has been able to verify the initial results of its offer. The other, however, you must give to do with the analysis of demand.

3. The third and final "C" is the competition: set the maximum price (customer) and the lowest (cost), consider the prices of the competition is essential to get an idea of how the other bidders are oriented within the price range. In particular, it is important to

understand who the market leader and at what price to offer their product; doing obviously attention in what is a leader. There will be a price leader (or cost), one of quality, one of communication etc. At this point urgently needed a couple of clarifications. Primarily on cost: not everyone will count in the calculation of the cost of production refers to the first "C", but only the costs directly related to that product. So if you produce 5 different types of wine, the costs to be considered for one of those wines are those directly attributable (eg, barrels, cap, bottles, labels) and part of the general (administration, wine, etc..). The risk of overestimating what it would otherwise cost. The second point concerns the third "C": once the leader or leaders of the market, it is said that the producer must necessarily arise at a price below them. Everything depends on the strategy and, in particular, the objective that is to be achieved and the target chosen: for the same product (although in the world of wine is quite questionable thing) you might choose a low price to penetrate the market (penetration strategy) or a high to position myself differently in the mind of the consumer.

One last thing. We know that the wine product is subject to two variables in particular: the climatic season and made wine. These two parameters influence and place vary considerably from one year to the product. At this point it would be a good rule wisely preferred by some, do not go out with leading products, adjust the price vintage, or encourage the consumer. Just the thought of lowering the price is a lousy way to hide a bad year, because today's consumers are more informed than you think!

Price Strategy in the South Africa wine arena

The environmental, in which wine business operate, is the global wine arena. This environmental is increasingly complex, competitive and fraught with challenges (Rabobank International, 2003).

The dynamics of the global wine industry are better understood with knowledge of the history of wine and the multidimensional nature of wine product itself.

Wine has been part of Western history since the Neolithic Period (8500-4000 BC) (Orth, Lockshin, & d'Hauteville, 2007). Roman Imperialism helped to spread the production of wine across most of the countries in the Empire, which included most of

North Africa and Southern Europe. The use of wine as part of Christian religious practices aided the spread of wine production and wine consumption across Europe after the collapse of the Roman Empire, eventually spreading throughout the world with the European Imperialism of the 15th -19th centuries (Silverman, Castaldi, Baack, & Sorlien, 2000).

Wine business has been dominated through most of the 20th century by Western Europe. “Old World” countries such as France, Spain, Italy, Portugal and Germany accounted for the majority of grapes and wines produced. Most of the consumption was also concentrated in these markets since wine was considered part of the traditional way of life. In the last decade, rising “New World” wine countries such as Australia, USA, Chile, Argentina, South Africa and New Zealand, have been challenging the stronghold of the traditional producers (Orth, Lockshin, & d’Hauteville, 2007). Originally rooted in production agriculture, the wine business has become more commercial and global in the last decades.

However, wine is still a product defined by its place of production. Information on the origin of the grapes generates inferences about its quality and style. On one end of the spectrum are single-vineyard designations, on the other end, international wine brands which originate in a specific country (Orth, Lockshin, & d’Hauteville, 2007).

Greek and Roman records, referring to vintage dates and specific vineyards as superior to others, are seen as the beginnings of the wine quality system linked to the concept of “terroir” i.e. climate, soil, aspect of a vineyard site. This system developed further in the middle ages and became entrenched in the 19th century (Orth, Lockshin, & d’Hauteville, 2007).

After appellation (the area in which the wine is produced), the distinguishing wine factor is varietal. ‘Varietal’ refers to the type of grape used to make the wine - each with unique flavours, and each exhibiting unique flavours when grown in a different place (Silverman, Castaldi, Baack, & Sorlien, 2000). As a product category, wine is probably one of the most complicated to manage.

The core product can be red, white or blush, sparkling or still, with different levels of residual sugar, tannins, acid or other ingredients of interest. Add packages in various sizes and shapes (e.g. bottle, barrel, can, box) a brand name, sub-brand name, price, grape variety or blend, a vintage year, a country, region or other place of origin and a winemaker (Orth, Lockshin, & d’Hauteville, 2007).

Then there is the price segmentation. Wine prices vary significantly, both within individual countries and in international markets, based primarily on appellation and grape varietal differences, the perceived quality associated with those varieties and appellations, and marketing factors such as brand name (Schnepf, 2003). The segments with higher prices are very fragmented and show considerable product differentiation. The lowest price segments, with the lowest quality, are more homogenous - related to demand for human consumption as well as for industrial uses (Agri/evaluation, 2002). This price/quality segmentation has lead to the development of recognized price/quality categories depicted in the illustration below.

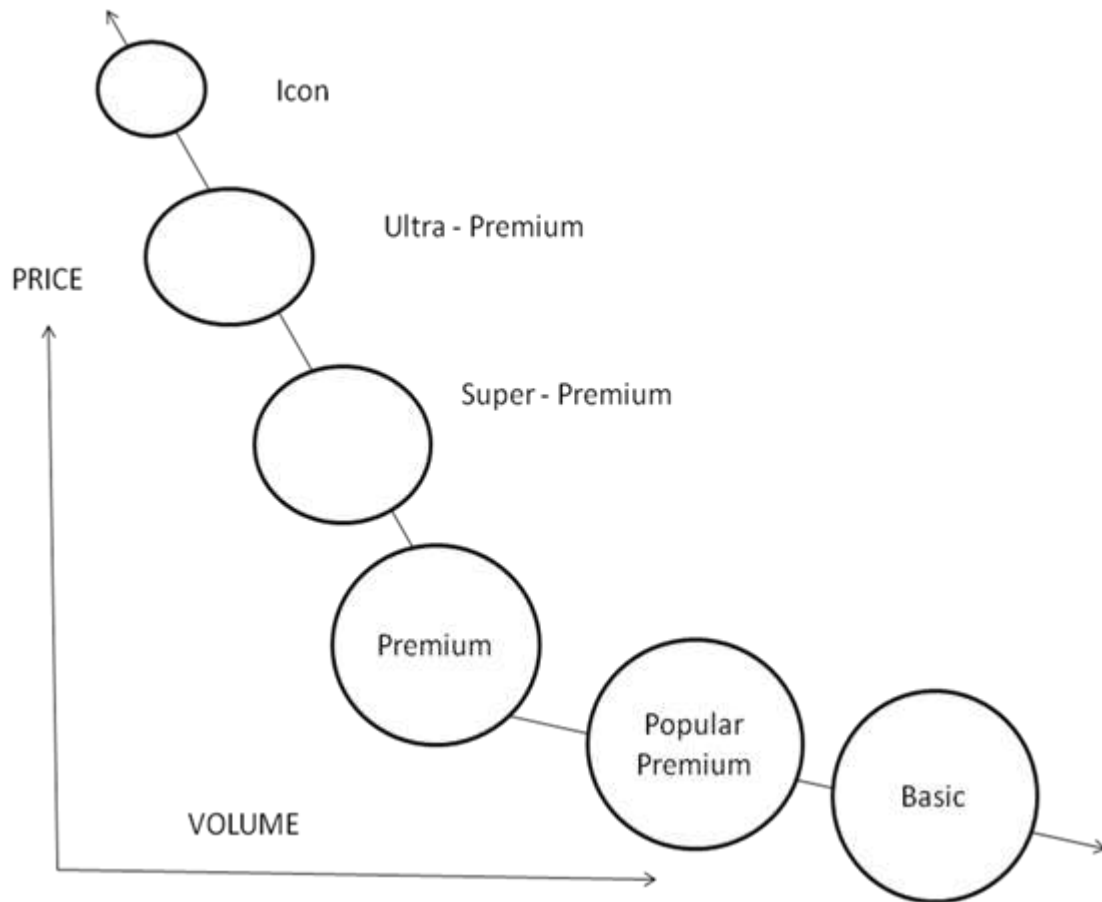


Figure Price-Quality Segment

Each segment represent a price category that exists across the market. Linked to this, is the expectation that consumers in this category demand from wine at that price. In the table that follows, the expectations and requirements of each segment and the corresponding price point of each category is offered.

CATEGORY	EXPECTATION/REQUIREMENT	RETAIL PRICE: Euro
BASE	Low price, sweet.	< 3.50 €
POPULAR PREMIUM	Varietal, fruit driven, accessible, clear branding.	€ 3.50 – 5.50
PREMIUM	Character, accessible, recognizable variety and origin characteristics, clear branding.	5.50 – 10.00
SUPER PREMIUM	Brand name, brand awareness, authenticity of origin, full bodied, more character, richness, typical of variety.	10 - 15
ULTRA PREMIUM	Typical, varietal or good blend, more complexity, origin, image, quality brand, cellar potential, critical acclaim.	15 - 150
ICON	Long-term image, complexity, cellaring potential, high scores.	≥ 150

Along with the complexity in wine as a product category, comes the complexity in production and marketing. Wine can be made in many different ways in many different styles. Gravity flow vs. using pumps, fermentation in stainless steel tanks vs. oak barrels, malo-lactic fermentation or not, machine harvesting vs. picking by hand, different trellis systems vs. bush vines, irrigation vs. non-irrigated vines (Orth, Lockshin, & d’Hauteville, 2007).

The wine sector includes a large variance in company types ranging from large global corporations to small family-owned and operated firms. Wine is being sold directly from wineries as part of a tourism experience, to local shops and restaurants, to agents or distributors who take the product to market, or using Internet (Orth, Lockshin, & d’Hauteville, 2007).

9.2.4 "P" - Promotion.

In the world of wine⁷⁹ communication is an essential component of the marketing mix because it allows the company to better directed to selected customers.

As reported by the media is a typical product of our "Mediterranean", such as wine, given the evolution of the tools and methods of communication that bind the manufacturer in the his choices? To groped for an answer you should know all the changes in the way and then show it or tell what weight today has its presence. The phenomena of competition, the different forms of distribution and the variety of products on the market, led the operators to build trade routes and promotions (price discounts, refunds, gadgets tribute) intended to send a number of messages to customers and influence their choices. One is found that is not the same thing as telling and communicating wine on television or through the radio microphones; changing expectations differ emotions perceived since the one or the other lends itself to different styles of information and communication approaches. In the specific case of the wine industry, I relies mainly on direct contact (where information and communication passes from one consumer to another through events, tastings, festivals, wine tasting), so that the consumer can relate to the product through the five senses, and where the use of the two affects the final outcome of communication and, upstream, the strategy. An effective communication strategy to ensure awareness of wine regardless of the medium used. How? By answering the following questions:

- What can I say?
- Who?
- With what objectives?
- What are the techniques?

On the wine market, the purpose of the communication is mainly to acquire a reputation "product" and "brand" in reinforcing the image, to inform about new products, to convince, to recall the existence of a product, to introduce its own brand.

⁷⁹ Cfr. Piccioli F., La comunicazione nel food and beverage. Farsi riconoscere con i piccoli budget (2005), pp. 31-73 e 75-112.

To be effective, it must attract the consumer's attention in order to arouse his interest and involve until time of purchase. Question, therefore, to define a real plan communication that meets the objectives of the company and the industry. We consider, first, the communication within the company, including the people who work there, as part of the image building and essential part of the management. This is followed by a communication outside, which emphasizes the environment surrounding the company, characterized by its points reception, tasting locations, but also the name of the estate, the specific brand, business cards, brochures that highlight the logo are an integral part. A product of excellent quality, offered at a reasonable price, distributed in a manner accessible to consumers will be favored if accompanied by all the necessary information to meet the needs the customer. What, then, are the best suitable means to pass a message to the customer, as it draws its attention and which tool can seduce him, given the overview of the opportunities that being proposed? The means which allow an individual to recognize a product, identify and distinguish it from others on the point of sale, stimulating an act of purchase, immediate or delayed, should be combined with each other to ensure the success of commercialization. There are, in this regard, two communication techniques important: that media and without the media. The first is based on the use of tools such as printing, television, radio, and the other is based on the use of complementary techniques such as marketing direct, sales promotion and sponsorship. In a nutshell, it is possible to identify two different communication patterns, each corresponding to the following purposes:

- Transfer of knowledge (informal look / cognitive);
- Communicate passions and feelings (aspect passionate / hedonistic)

Regarding the first point, what matters is the depth of information, but in the world wine, emerge superficiality and incompleteness in the messages sent, usually at knowledge component. Currently, operators have backed a new tool communication, the Internet, to make known them their products. Most skeptics believe a unrealistic target given that a bottle of wine to be touched, tasted uncorked and to know it duty and certainly not enough of a screen pixel sostituir this type of sensory experience. The fact is that many wineries produce their own web site, as an additional communication tool

and waiting can turn into sales channels working. Probably Internet is offering to the world of wine the opportunity to start to use synthetic sentences and understandable, able not only to inform but also to excite. A beautiful challenge hiding, no doubt, a transformation of the principles that have guided so far the whole system of wine communication, Internet, in fact, is expanding dramatically the number of potential readers / consumers of wine news, which so far had been confined to the circle of super fans and allowing companies to do what had never been able to do: get in all the houses, to address all segments of consumers, at any time of the day or night. The network, compared to television, radio and newspapers, offers another major advantage: in many cases is also 58th consulted during office hours so that, check the news, you go hunting their hobbies and interests personal, including the wine. To conclude this section, it would be best to analyze the case of a sole proprietor and see possible actions which would constitute an effective communication campaign. In the first place, it carry out an analysis of the customers of the vineyard, choosing your market (number of customers, their profile, the retention rate); analyze the previous communication actions made on that market (sales, loyal customers, increase of awareness); choose a new strategic goal for the campaign (increase in direct and indirect sales, development notoriety through products or brands, reinforcing the brand image of the company); define the actions to achieve the objectives set (events, trade fairs, mailings), and finally define the support needed to implement the strategy.

Chapter 10

Finding

It was noticeable from the investigation, how the previous issues highlighted in the literature review were still concerning the candidates. In fact, matters such as the strength of national currency, excise on alcohol and complexity in getting financial support were the major hurdles to clear. Surprisingly bulk wine was not selected as alternative to the exports, mainly due to the stock of wine that in average was inferior to the rest of the industry, and also due to particular strategies related to positioning the product at certain level on the market. Furthermore, all candidates agreed on how a major government support in terms of subsidies to enhance the export activities, was crucial for the sustainability of the wine sector in South Africa. In particular three of them accentuated how the government's funds were largely destined to different industries just reserving a back seat to South Africa wine; in this respect an owner claimed for more consideration as the industry itself is a rural based industry which most of the time tends be in the lower population area having a significant impact in term of employment, due to the conspicuous amount of labour jobs which generates. However, regardless of the general problems shared by the whole industry, another key component was identified as crucial to further understand the patterns standing behind the process which leads to the profitability. According to the data collected, the entrepreneur's background was decisive in characterizing business model and growth inspiration. Yet, such element was a key point which defined marketing strategies, export performance and diversification into wine tourism, risk exposure and ultimately the concept of co-creating industry value by exploiting the investments from off-shore multinational companies. Such factor represented a new component to consider when

exploring the profit dynamics within the South African wine industry. Figure 2 proposes a model which simplifies the key issues (themes) that arose from the interviews.

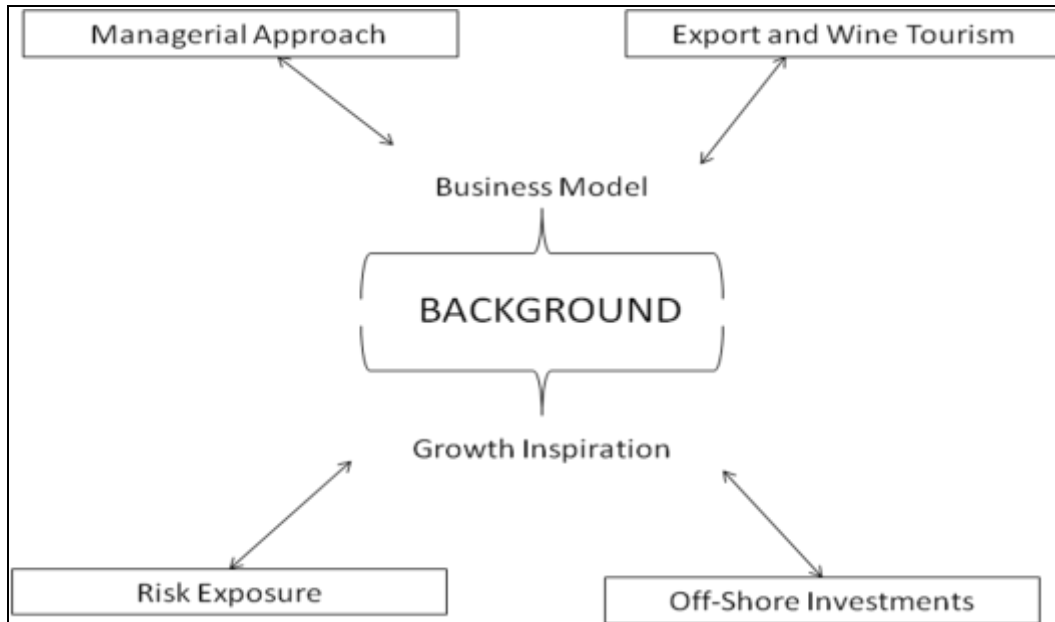


Figura Representation about the interaction between the background and the parameters taken into account

Background

Among the wineries interviewed, six of them were run by owners coming from different professional background, who had been operating within the industry for about 10 years. Having previously spent a large part of their life employed in different fields such as academic world, public health or accounting sector, those wineries started the activity thanks to a conspicuous financial availability which was earned and transferred from the prior occupation. Mainly pushed by the dream of having a vineyard and by the contextual way of life that such activity could guarantee, they exploited the boom that occurred within South African wine industry in the last decade. To better address the analysis applied in the following paragraphs, these wineries are conventionally renamed *first category*. That said the other part of the sample was composed by owners/managers who had remarkable experience maturated in over 25 years working at both national and international level. Having a deep understanding of all practices needed into the world-

wide wine industry, they belonged to a generation of entrepreneurs who founded their own business when the South African wine industry was still far from being internationally acclaimed - as illustrated in the course of the literature review. These wineries are renamed *second category*. Certainly the know-how acquired with the experience was a significant factor within the two macro-categories, however, understanding how decisions across the parameters showed in Figure were made, is crucial for the purpose of this study.

Managerial approach

Certainly the previous background conditioned the preliminary planning and level at which market research was done. In fact, before starting their business, owners within the first category did not gather information about the state of the market and about the effective presence of opportunities in it - only some exceptions came from one of them who advanced the first steps into the wine industry by figuring out whether or not to viability for his firm could be guaranteed. Rather different was the initial phase for the wineries within the second category, whose owners made a decision on that stage coherently to a broader business vision. It was true for both varieties selected as a principal supply, and for the geographical position where wineries were established. For instance, one of them planted his vineyard in a particular area, as the combination of weather patterns along with suitable soils characteristics, could guarantee a premium quality Pinot Noir. He admitted that such intuition came from his previous experience working in North South Africa, where he was used to deal with very dry place and rain shadow, being accordingly ideal climate conditions for such variety:

“I was brought up in the North of the Country so I was used to wine being grown in a very dry place in the rain shadow as it were. This part of the world, the eastern side of the country’s in the rain shadow to the Westerlies. And this just looked like a far more intelligent place to grow grapes to me”.

At the time he made this decision Pinot Noir was fairly unknown in South Africa, while today is the first red wine in terms of consumption.

Another owner decided to start his firm in a specific area for both reasons illustrated above and also due to the proximity to one of the biggest ports in the country, showing clearly his intention of exporting even before planting the first vine:

“It was here that we started and I guess up till now it’s followed for commercial reasons. We’re close to all export, we’re much closer to the port, it’s much cheaper to send wine, to actually transport grapes down to Pretoria from here and send them out by container through Johannesburg”.

Moving on, a consistent discrepancy had noticed in matter of understanding/monitoring the demand and those practices required in this process. According to the data collected, respondents within the first category did not provide a clear sight of the methodology adopted to identify new trends or potential customer needs. Most of the time the system utilized was a general opinion from some retailers, or distributors in case the business size was bigger. Contrarily, the other candidates showed a remarkable understanding about the complexity of this procedure and, by creating a qualified feed-back model, an efficient time-management could be pursued. In fact, regardless of a constant information flow across all actors involved in the supply chain, a real marketing research was outsourced, allowing the relative findings to be straight away implemented in order to satisfy market requests. Accordingly, such an approach enabled these wineries to tailor their products to the different segments, i.e. by making sweeter wine for USA or by treating UK as very sophisticated market.

In this respect, even the conception of packaging was differently taken into account. Very significant is the point of view from some wineries within the first category which saw such activity marginally related to the success of the wine. Being the core business encompassed within the concept of quality, one of them – in order to emphasize the family owned angle- decided to do not differentiate his supply and send the same message to the every market, despite no particular initiatives to meet the demand were taken. Another owner pointed out how quality as such was the real discriminant which could realistically differentiate the product, because the numerous labels which composed the wine supply in the recent years made label itself unable to sell the wine:

“Yeah at the end of the day we actually got the point where we didn’t think, the label doesn’t sell wine. There’s just so many labels out there now it’s more about the relationship you build up with the distributors who know the wine stores, the wine stores who they know the people that work there and they’re able to convey that story through to their, because there’s so many brands out there you know, as long as we thought it looks smart and it looks good on a restaurant table more so than trying to stand out on a supermarket shelf by putting fluorescent yellow on it or something”.

Another owner just distinguished his wines by using labels home-reproduced and subsequently undergoing them to a panel of judges mainly composed by friends or relatives. Diametrically opposed was the degree of importance reserved to this practice by the respondents within second category. Particularly, one of them to better brand his wines and further transmit all emotional values related to that, hired marketing agencies in the UK and USA, as being the latter the major exporting markets for his company:

“All of that, plus we’ve actually linked that to go to design agencies in that particular country because if we’re going to sell a brand in America we will be American design agency to do research on it because they know that market better than somebody here. In the UK we use design agencies for their market too that are based there”.

On the same line another owner took very seriously the branding activity, and according to him it has been the decisive factor which enabled his firm to find importers or distributors overseas: the look, the brand both in terms of graphic and name adopted, and the choice of the price in accordance to the position he meant to operate at, are just some practices that have been explicitly listed.

Nevertheless, it would be fair to state that, despite the remarkable differences just highlighted, all candidates share the same orientation in terms of corkage employed for bottling the wines. Screw cap definitely dominated the form of closure utilized. Broadly perceived as a better option to ensure the high hygiene standards required and as better solution to preserve the wine, according to the candidates, the domestic market was rather reluctant from adopting cork mainly due to those practical benefits that could be guaranteed by sealing the wine with screw cap. Surprisingly, no particular issues

were faced by the interviewees in the overseas markets, and at the time data had been collected, even the Asian market was welcoming screw cap. An owner stated:

“We’ve never had any issues in Asia about wanting to have a cork in it. China the same they’re more than happy to have a screw cap, in fact you’re the first to mention it probably for China. It’s never even been an issue here, just screw caps”.

The previous point was largely in contrast to existing literature, since it has been highlighted how Asian markets – due to the dominion of French wines and the usage of cork – definitely preferred this typology of closure as the ceremony of uncorking a bottle of wine made the perception of the product itself sensibly higher. Just a few exceptions had seen a candidate using cork for a small segment of end-consumers, even within South Africa, however it represented decisively a minority since nowadays over 93 per cent of domestic market is characterized by screw cap. Nevertheless, at the time data have been collected, the linkage between screw cap and the consideration of cheap wine was still taking place in the Chinese market. In response of that, the South Africa Winegrowers Association conducted a proper market analyses on how better position South Africa wine brand in China, as underlined by the Global Marketing Director:

“So therefore you’re starting to, so then the Chinese premium wine consumer’s coming at it from a different space and also the market is still developing very quickly particularly and screw cap, all they’ve seen is screw cap is cheaper wine. So there’s been some push back on that. I’m flying up to China next week and we’re doing some research about that in terms of how we best position the South Africa wine brand in China”.

When the interview took place, the research was still ongoing. The continuous appreciation of cork in the Chinese market had confirmed certain aspects encountered in the review of the framing literature.

Export and wine tourism

Certainly the background was a determinant point which had contributed to establish the path towards the external trade, as the owners’ track record was another

characteristic which affected the export performance in this survey. Not only the percentages, but also the typologies of barriers faced were different, likely due to the dissimilar stage of maturity of their export markets. In fact, despite a different ratio of products shipped overseas, wineries within the first category were still at the stage of conquering distributor/importer's loyalty, and developing a solid network trade was still an important result to accomplish. For instance one of them expressed his disappointment about his distributor in UK, arguing on how such a lack of consideration was actually shaping the commercial partnership between them:

“But so we've just got, had a new distributor in a company who's got London, Manchester and Liverpool but their owner's just pretty terrible to work with. He never replies to emails and all that sort of thing and he's got guys working for him who are really good”.

Still at the beginning level of the his entrepreneurial learning curve, his winery was characterized by medium small size, being the latest according to him a direct problem related to the export's outcome. Specifically this owner reported how the Chinese giant distributors were pretty intimidating for his business as the pressure they could charge in terms of quantity and price could not be sustained by his relatively modest volume:

“The one main one take China for example, would be they're keen as but they want it for half price. So you'll go through a lot of work you know establishing relationship they love the wine and might send some over but when it comes down to it they might be ready to put a big order in but they'll say we want to buy it, your whole production or whatever but we want it at a price that doesn't really come close to covering our costs sort of thing. So yeah I guess being a small producer that's a barrier for us. We can't produce it as cheaply as the big guys. Not even entertain the idea of being able to compete on price there really”.

Yet another interviewee after two years exporting was still struggling with the distribution model adopted, pointing out how the amount of actors involved in this

process eroded too much producer's profit. Alternative channels such as door to door distribution could not be undertaken due to the dimension of its supply and to gain momentum his winery needed the presence of a middle man:

“It's often a matter of scale I think. You either need to be really small or reasonably large. In the middle it's difficult. So small means you can concentrate on your retail sales a lot and also supply directly to the restaurants without using distribution because you haven't got a lot of product to move. So it's not difficult. That's not an option for us. We produce too many cases of wine to do that. So we need to use a middle man and that's difficult. I also think the distribution model will change because of that. I think it won't be too many years before there's a difference in the way the model goes it's not just really sustainable the way it is. It's just too hard on the producer”.

Furthermore, he stated how difficult it was involving third parties in creating brand value, as many overseas importers were dropping prices to offset the weight of GST, but without reducing their margin. Instead, the candidates within the second category were already familiar with these sorts of obstacles and in response to that some of them tailored accurate strategies, while others were on the way to adopt a new supply chain model. An interviewee, given the remarkable experience within the wine industry, knew how distributors operate when asking for a particular price and in this regard he highlighted how the role played by the media was crucial. The latest mainly represented by magazines, writers and other forms of insiders, were a competitive advantage for producers to be exploited when bargaining with third party, as according to him international fame was the best deterrent to the price sensitivity:

“When we started exporting the first thing they really look at is the wines or your reputation for the quality of the wines you've made, then they look at the business. They look at it a little more closely if they've never heard of your or your brand they will, well these days I guess the first thing you do is Google it but it was way before then. But they go to the magazines or the writers, the opinion formers find out what's been written about us in the past. The first thing they'll do is go to our website and work back, take their margins off our retail price and then ask us for a price. So it's a

way of them checking that we're selling to them at the right price that is as soon as we display a price we're locked into that worldwide because if they're importing then they'll say we're prepared to pay so much, we've got to put our margin on".

In 2010 his long view paid off when in one issue of *Decanter* – the world's best wine magazine – his Pinot Noir was awarded with the cover page. However, another producer was fully committed to change the process of distributing his wines by establishing, in his markets of reference, overseas import subsidiaries. Despite at the time data had been collected work was still in progress, his idea was very clear and aimed at skipping some legal and bureaucracy steps which were compulsory in some markets where he was exporting to. Along with one branch already open in Australia, he planned within 5 years to enlarge his overseas network in the UK and USA and projects were ongoing. Nevertheless, the latter was explicitly due to overcome the three tiered system which forces overseas wine to be sold in series through an importer, distributor and eventually retailer having a massive impact on the final price and disadvantaging them when competing to the local producers. Obviously investments of such significance were completely justified by the nature of his business model, since 96 per cent of his turnover was made up by off-shore markets, therefore priority and great deal of commitment was reserved to the external trade (i.e. he also employed a consultant to constantly monitor the currency exchange rate, the biggest trouble for somebody who exports almost entirely what produces).

Regarding the wine tourism, it has been noticed that regardless the different degree of development in terms of infrastructures and facility provided, the wineries within the second category had higher propensity to see wine tourism as new form of activity to be incorporated in their business model. Most of the time this decision was due to overcome the low degree of export and those difficulties which are implicitly present when it talks about external trade. However, caution should be taken into account in asserting decoupling between the two activities as more specific research should be done in this respect. Nonetheless, very significant is the example reported from an owner who was rather gratified about his decision of staying exclusively on the domestic market and use wine tourism as main gate to gather new customers. At the

time the interview took place, his estate could accommodate across eight or ten guests and new insights about finer hospitality services were thought to be executed. Making his visitors his first consumers was according to him a stable way to ensure his business from all scepticisms about finding the right distributors, and from those hitches in matter of trade barriers. However, his ambition of capturing new overseas market shares was not abounded at all, rather he stated how more regularity in the export orders could be the best tool to fix the notorious problem of distribution:

“If we look for export orders we don't want just a few cases. We want somebody who will take 200 cases every year at the same time. Now once you've got the regular account behind you, once you've got also the publicity I think around that regular account then people will I believe the problem of distribution will solve itself especially for a small vineyard where you will have people coming to us to ask for our wine”.

Apart from this example, other producers achieved a modest level of facilities which most of the time did not go beyond the cellar door or sometime a wine club. Despite valid traces of real wine tourism business were not found, these producers expressed their positivity about the idea as such, but at the same time they pointed out how the objective remoteness in which their vineyards are located, could be a barrier very high to surmount. Diversely the respondents within the first category saw this activity very far from being part of the business model, mainly due to the scale of the export shares which made them sometimes almost unknown in the domestic market. No particular insights were , even though one of them acknowledged that wine tourism could be an opportunity to be exploited in the long term. Although deeper studies should be purposely done in order to prove negative correlation between export and wine tourism, the global Marketing Director of South Africa Winegrowers, pointed out how those two elements could strategically be connected. He reported that some wineries – mainly small players – were using wine tourism and the facilities provided with that, to sell their wines through newsletters and e-mail and sending them to both national and international visitors. In some cases, he reported how this channel made up the major source of sales for those wineries. However, he stated how the presence of fixed such as staff, place and manning in general, could ultimately affect the return, and

underlined how differentiation was the cardinal point to bear in mind when including this activity within the business model:

“There may be ten wineries down the road here as well, so you have to have a point of difference as well”.

Furthermore, the exchange rate was seen as another potential drawback which might affect the wine tourism, remarking how this problem can have double effect on the industry.

Risk exposure

This section illustrates how different entrepreneurial approach was undertaken in assessing the concept of risk. The general orientation within the first category was distinguished by a remarkable risk aversion manifested under the form of staff employment and openness towards joint venture. More specifically, most of the time the manning was exclusively represented by owner’s family members with just some exceptions for some winemaking consultant, and retaining 100 per cent of the operational control was decidedly a priority. Again, achieving a determinate level of profit by which a certain lifestyle could be assured, was seen as primary objective to pursue, therefore very cautious initiatives only were undertaken from these respondents in this regard. Nevertheless, two of them admitted their concern about the sustainability of the business model in relation with the recent issues faced by the industry, leading them to review more critically the concept of future growth. Regardless of the prior attributes in which disparity between first and second category was also due to operational size, the main discrepancy identified throughout the research was a matter of risk differentiation, leaving room for allusion about the relevance of a proper background when running a business. In this regard very significant is the example reported from a candidate within the first category whose on trade business was 40 per cent domestically dependent from one city, Christchurch. After the tragedy of the earthquake occurred in February 2011, he had seen almost half of his turnover disappearing and at the time the interview took place, the winery was still recovering

from such unexpected event. Despite an objective impossibility to foresee such a catastrophe where obviously the human edge prevails over all business dynamics, when it talks purely in terms of risk mitigation it would be fair to say that an appropriate subdivision of market shares should be accurately planned. Diametrically opposed was the experience faced by an interviewee within the second category, where action persuaded inertia. He explicitly stated that the decision of redistributing some export shares in favor of others within the domestic market, took origin when the remarkable issue of the strength of the national currency was still more a precaution rather than the prime hitch for external trading:

“Roughly off the top of my head most of ours is export. So it’s about 95 or 96% now, it used to be 99%. But we are slowly addressing that. The main reason for that is the exchange really, just the return we’re getting on the export market particularly where our biggest markets are, the UK and the US”.

At the time data had been collected, this process was still ongoing and many efforts were being made in order to penetrate the domestic market, as strategies were more focused at international level rather than domestically. Another owner combined each market share in such a way as to further spread wine pricing and shield his winery from leak of demand. In this complementary method each market was independent and demand could be met at certain level of price that could guarantee viability and risks covering.

Conclusion

Review of the focal study

The overall objective of this study was to explore the practices within the wine industry in South Africa which have led this business towards a remarkable success nationally, but especially internationally, due to the extraordinary performance in terms of exports. Starting from the origin in the mid-1800s, this study sought to explain key reasons which had allowed the birth of this industry in a part of the world which was considered at that time fairly unusual for this kind of crop. Many cardinal events occurred ever since, and in the course of this study they have been recollected by following a chronological approach in order to understand what caused the boom of the industry and what key factors interfered throughout this long journey. Surely the fickle behavior of the government, originally concerned about alcoholism and then fully committed in avoiding industry cartel, forced wineries to capture new market shares, making exporting a crucial activity to pursue in to maintain viability of their business model. Since its birth the wine industry has always alternated period of prominent growth followed by period of crisis and it was only in the last decade in which the situation had become pretty stable. Although optimism and satisfaction have overwhelmed the industry in the last decade, it has been highlighted by the number of new wineries established which increased by 75 per cent in ten years (South Africa Winegrowers, 2012b), something is still unbalanced. The continuous export growth unfortunately do not coincide with the same increase of the profit. With the opportune limitations, this study sought to explore the paradoxical dynamic which made the industry growing in terms of sales, but decreasing in terms of revenues. The findings of this study have suggested that one part of the industry is represented by new wineries

and new owners which joined the industry for life-style reason. Being previously employed in different professional sector, once gained a considerable wealth, they decided to invest in the wine industry in South Africa. Again with the opportune limitations, this study suggests that this part of the industry has accumulate a remarkable delay in terms of understanding the practices needed in the wine industry, as the novel entrepreneurs are still at the initial phase of the learning curve.

The extension of the framing literature with the empirical findings is discussed in the next paragraph.

Literature review and empirical research findings

Regardless the emotional reasons and the sex appeal which attracted many people in establishing their own winery, when it talks about growth and viability, it should be opportune to consider also some motives which are based upon logic. Undoubtedly passion is a key factor for having success, however a series of components and elements should be carefully analyzed when planning a new business. The explosion of the wine industry in South Africa which occurred in the last decade is likely one of the best example of how the dream of owning a winery darkened the profit from being a priority. In fact, even though a very tough international competition and all threats related to that, the mushrooming of new actors within this sector, made almost 700 South Africa wineries producing as much wine as does one Australian on South Africa. Perhaps the industry should meditate about this point as competition is a concept which is intrinsically compromised. As highlighted in the course of this study, the new political and macro-economic scenario which came into force in the early 1990s, set the scene for the boom of the exports, making South Africa exclusively dependent from external trade. Since today 70 per cent of wine produced is shipped overseas and in about 300,000 tones of fruit grown a year, just 50 are requested domestically, new markets accessibility is a difficult challenge to face. For sure market penetration is something which might be more feasible by joining forces instead of continuing with a micro-capillarization within the industry. In this respect, mergering activities among existing players and welcoming offshore capitals, may be decisional tools to apply in

order to overcome this issue. Clayton and Stevens (2007) have already highlighted how co-operative and innovative mindset might build the bases for a solid and viable business model. In line with that, the financial support which might be provided by multinational spirits companies is vital to capture new markets shares. Despite this study suggests that some operators within the industry do not want overseas companies ruling the wine industry, it would be fair to state that this is one of the best practices that the South Africa wine industry might exploit to “open the door” of overseas markets. The new knowledge created after undertaking 12 interviews suggests that the wine industry in South Africa is principally composed by two different categories of managers and it is precisely in one of them in which the main issues are concentrated. Wineries born in the attempt of ensuring a particular life-style to their owners are the weak part of the industry, where production costs are too high and reasonable level of profit is far from being a reality. This study has provided an identikit of these firms and underlined how this performance was an imminent consequences caused by a lacking management experience of their owners. Contrarily, another part of the industry is literally driving the wine sector in South Africa and fully committed in pursuing viability through the implementation of sustainable business models. Undoubtedly the long experience acquired in many years of work in the wine industry is a competitive advantage which is still paying off, as highlighted in the course of this study. Overall this study supports the existing literature. Particularly, it has been confirmed that building a solid relationship with suppliers/distributors is hard and it is determinant for the company’s life. In fact, small and medium wineries faced these typologies of issues, underlining a sort of impossibility to change their supply-chain model. It has also confirmed another aspect highlighted in the existing literature that is the inertial or adaptive behavior of the SME’s with their suppliers/distributors, due to the limited resources. Therefore, finding a right distributor is crucial for the firm’s success. Branding has been identified as an important activity. Being perfectly in line to what that the previous literature stated, the smallest wineries believe that quality is the real factor which can convince a consumer to buy the wine. By contrary, biggest wineries highlighted the importance of the label, shape and packaging to attract wine purchasers and consequentially building long terms relationship, as highlighted in the course of the

literature review. Furthermore, winning prize and award is very significant in this industry and is a strategic element which attracts consumers and allows the wine companies to be able to increase the price of wine.

Wine tourism is surely an important activity which might increase the perception of value of the brand, however the same issues highlighted in the course of the literature review have been supported by this study. Remoteness of the wineries is a real issue and the lack of suitable infrastructures kept away many wine companies from this activity, as they were too afraid to invest in wine tourism. Other concern regards the negative interaction between wine tourism and the facilities provided at the winery (restaurant, vineyards tour, cellar door) with the objective perception of the wine, which led some wine companies to avoid this activity. However, it has been noticed that the propensity to invest in wine tourism was also dependent to the degree of development of the export market of the winery (the more export shares were big, the less the interest was to invest in wine tourism). This point extends the existing literature about this subject. That said, this study has supported the literature regarding the South Africa wine industry, but at the same time, it has created new knowledge about this research area. Despite the young age, the industry has already developed a strong identity and personality which are fundamental when competing at international level. In this respect, this thesis suggests that the South Africa wine industry should compete by placing more emphasis on branding and marketing strategies. Consequentially, differentiating the products in all of their aspects is advised: screw caps instead of corks, innovative packaging and newest materials are just some examples which might enable this process. Since the wine industry is in general subdivided into two parts, *Old World Wines* and *New World Wines*, and South Africa belongs to the latter, energies and resources should be invested to achieve leading position within the second macro category. Due to the crucial diversities in terms of heritage/tradition, quantity/price of wine produced and profile of customers, an hypothetical competition with countries such as France, Italy and Spain might not be sustainable. Despite an excellent white, red and sparkling wines, this thesis suggests that the industry should aim on Sauvignon Blanc as a benchmark product, to give continuity to the great marketing work which has been done in promoting this variety, since today it is synonym of South Africa all over the world.

Recommendations for novice managers

The first recommendation for novice managers regards the enhancement of market and business research. Undoubtedly researching is important activity in any business and allows firms to stay competitive in the market, to understand the latest market trend and consequentially to exploit opportunities. This is true at any stage of a company life including the initial phase. This is the main weakness which has been found within this category and it is the main cause which triggered a series of problems that had negatively affected operational result since the first steps were moved into the wine market. Having a clear sight about the environment where the firms (wineries) operate in, is surely a crucial advantage which enables owners/managers to punctually make strategic decision and to mitigate the risk of failure. Secondarily gathering information of the market is a necessary practice to better understand the demand. Therefore, more investments in marketing activities and should be opportunely considered, because once a company knows the traits of its demand, tailoring products and satisfying customers is decidedly easier. Despite in the course of the investigation some candidates underlined that the quality of the wine was sufficient to guarantee sales, this concept should be carefully reinterpreted due to the high quality of South African wine. Differentiating the product in terms of brand, packaging and in terms of transmitting emotional values covers a pivotal role in a industry characterized by a homogenous level of products (just some exceptions arise from the highest segments). Furthermore, the concept of business vision should be fully integrated in the business plan: What do we do? For whom do we do it? How do we excel? (Scott Armstrong, 1986), are questions to answer to define strategies or directions and making decisions in order to allocate resources to pursue goals and objectives initially set. In this respect, initial planning should embrace a long term growth approach and set the activities in such a way to achieve viability and sustainability for the business. Hiring talented personnel can surely enable this result, even though this procedure should be accomplished regardless of the degree of kinship. Therefore, it requires to go beyond the emotional reasons which have seen (in the course of this study) the winery's owners most of the time giving the priority to the family members, without making sure about the presence of right skills and right knowledge of their employees-relatives.

Recommendations for expert managers

In the course of this study this part of the industry has showed to have a deep understanding of what should be done in order to maintain competitiveness and ensure viability. In order to further consolidate this position, the level of market research should be kept high and innovation should be noted down in their agenda. Monitoring what the competitor does and enhancing the original idea in order to exploit further opportunities which arises from the advantage of being “the first”, is likely the smartest way to operate. Wine in South Africa is a new and dynamic industry which, thanks to the leading wineries, has already achieved a remarkable degree of innovation; it witnesses the high degree of creativity and the convinced propensity to differentiate the products. Meeting the latest and exigent customer’s requests by lightening the alcohol content or revolutionising the packaging by adopting plastic bottles in order to decrease the cost of transport and consequentially reduce the price of the wine, are just some significant examples of bright ideas which have taken place in the South African wine industry. Furthermore, due to their scale this wineries should constantly monitor the emerging wine markets and the extraordinary opportunities that they offer, and then take action. The framing literature has already highlighted the prominence of being the first to penetrate the market. In this regard should be kept in mind that South Africa belongs to the *New World Wine* and it incorporates a series of differences with the *Old World Wine* i.e. varieties, packaging, cork versus screw cap which contribute to a different perception of the same class of product. Beal and Rod (2010), highlighted the issues faced by the South Africa wine in the Japanese and Singaporean market due to the typology of bottle closure employed. In fact, the authors highlighted how the South Africa wine was perceived as cheap wine, just because it was bottled by using screw cap instead of cork, regardless of the real quality of the wine. As the corked French wine was the first to be exported in those countries, it subsequently influenced all wine market preferences, creating many obstacles for those wines coming from different countries which employed screw cap instead of cork. This example is very significant and underlines the importance of being the first to penetrate a new market and how such position can facilitate the companies (wineries) in retaining the leadership.

Directions for future researches

There are two directions towards which future researchers of the South Africa wine industry are suggested to conduct their investigation. Firstly, for researchers that share the common interest as the focal study, the suggestion is to re-examine the affiliated investigation for detecting flaws and room for improvement. By doing so, their studies can overcome the weaknesses which have been faced in the development of this study. A good starting point would be enlarging the sample size, therefore more wineries should be included in the course of the investigation in order to reinforce the reliability of the findings obtained. Furthermore, interviews could be undertaken throughout the Central Otago region in order to comprise wineries specialised in the production of red wine, as this area is well known as the capital of the Pinot Noir in South Africa. The future findings related to this segment of the industry might reinforce and extend the validity of this research and create new knowledge about the wine industry in South Africa.

Secondarily, quantitative research might be applied to explore the wine tourism and the degree of involvement of the wineries in this activity. In fact, in the course of the investigation came out that wine tourism was an activity rather preferred by the small wineries with a modest export shares. Being South Africa the principal market, these wineries were positively oriented to exploit the opportunities which could be offer by the wine tourism. By contrary, the bigger wineries had just a marginal consideration of this

activity (likely due to the high degree of concentration in the overseas markets). Obviously this perception follows the limitations which have been highlighted in the Chapter 3, that is the reason why further research should be purposely done. Understanding whether the size affects the propensity to the wine tourism is surely a remarkable contribution to a subject which is still considered pretty new in South Africa. This also could be interesting in order to understand how strategies are implemented and resources are allocated. Furthermore, having a scientific certainty might stimulate small wineries (the majority in this industry) to enter in this business and learn from previous cases of success. Therefore, diversifying the pure winemaking

activity by introducing the wine tourism within the business model might help to diversify the risk, matter which is still delicate for the small wineries within the South African wine industry.

Appendix A

WOSA is the national organisation for South Africa's grape and wine sector. Today the organisation has approximately 1000 grower members and 700 winery members. Established in March 2002 as a joint initiative of the South Africa Grape Growers Council, it represents the interests of South Africa's independent grape growers, while the Wine Institute of South Africa, represents South Africa wineries. South Africa Winegrowers is governed by a Board of Directors of 12, comprising 7 representatives from the Wine Institute and 5 representatives from the Grape Growers Council. The parent bodies continue to operate as separate voting colleges and funders of South Africa Winegrowers, although operational activities are conducted on a combined basis through the united organisation (South Africa Winegrowers, 2012a).

Established in 1975 by and for South Africa winemakers, the Wine Institute is an incorporated society funded to promote, develop, research and serve the general advancement of South Africa grape wine producers. The Institute is governed by a Board of Directors. The current composition of the board is as follows (Mc Gregor, Gregan, & van der Zijpp, 2007):

- Category I winemakers - two voting directors elected by members with annual grape wine sales of not more than 200,000 litres each;
- Category II winemakers - two voting directors elected by members with annual grape wine sales of not less than 200,000 litres and not more than 2,000,000 litres each;
- Category III winemakers - three voting directors elected by members elected by wineries with annual grape wine sales of more than 2,000,000 litres.

Established in 1968, by and for South Africa Grape Growers, the Council represents all contract grape growers. The Council undertakes research and disseminates information to its

members and is also an advocate for grape growers on national issues relevant to the industry. The Council's activities are directed by a board of 10, elected by and from regional grower associations (Mc Gregor, Gregan, & van der Zijpp, 2007).

South Africa Winegrowers is funded through: a levy on the sale of grapes collected by the Grape Growers Council under the Commodity Levies Act 1991; a levy on the sale of wine collected by the Wine Institute under the Wine Act 2003; as well as user pays activities and sponsorships. Winemakers and grape growers are automatically entitled to membership of South Africa Winegrowers through payment of the grape or wine levies. Associate members are also accepted, although such members do not enjoy voting rights (South Africa Winegrowers, 2012a). Under the Commodity Levies Act, organisations wishing to impose a compulsory levy on a commodity must first obtain a specific mandate from potential levy payers through a referendum. Both organisations hold referendum support for their respective commodity levies. The commodity levy on grape wine is imposed by the Wine Institute in accordance with the Commodity Levies Act, but under the provisions of the Wine Act, support for the commodity at a referendum must meet 60%. The commodity levy over winegrapes, imposed by the Grape Growers Council, is governed solely by the Commodity Levies Act. The referendum threshold remains at 50%. The current levy on winegrapes is instituted under the Commodities Levies (Winegrapes) Order 2004 (Mc Gregor, Gregan, & van der Zijpp, 2007, p.6). Table A-2 shows how the levy is applied to the grape growers, while Table A-3 shows the procedure implemented for the wineries and instituted by the Wine (Grape Wine Levy) Order 2005.

Table A-2. Levy on the winegrapes⁸⁰

<ul style="list-style-type: none"> • A levy is imposed on winegrapes grown in South Africa for sale.
<ul style="list-style-type: none"> • The levy is to be calculated on the basis of the value of winegrapes produced for sale.
<ul style="list-style-type: none"> • Growers are primarily responsible for the payment of the levy
<ul style="list-style-type: none"> • The levy is calculated on the basis of the value of winegrapes produced for sale. The value is either the farm-gate price (for grapes sold in South Africa), the FOB value (for grapes exported from South Africa) or the notional value (for grapes processed into grape juice or grape juice concentrate).
<ul style="list-style-type: none"> • The maximum levy rate is 1.5% of the farm-gate price, notional price or FOB value.
<ul style="list-style-type: none"> • The levy rate is set annually by the Grape Growers Council. The current levy rate has been set at 0.75% of the farm-gate price, notional price or FOB value.
<ul style="list-style-type: none"> • The order sets the time frame within which payment must to be made to the Council.
<ul style="list-style-type: none"> • The levy is spent on activities closely related to the interests of wine grape growers.

⁸⁰ Source: Winegrowers legal guide, September 2007

Table A-3. Levy on the grape wine⁸¹

<ul style="list-style-type: none">• The commodity levied is grape wine and the grape wine component of grape wine products.
<ul style="list-style-type: none">• Wineries are primarily responsible for the payment of the levy.
<ul style="list-style-type: none">• The levy is calculated on the basis of the volume, in litres, of grape wine sold in a levy year.
<ul style="list-style-type: none">• The maximum levy rate is 3.5 cents (plus GST) per litre of grape wine sold in New Zealand and overseas in a levy year.
<ul style="list-style-type: none">• Levy payments are due quarterly, with the exception of wineries making the minimum levy payment of \$400 per year.
<ul style="list-style-type: none">• The levy rate is set annually by the Board of the Wine Institute. The current levy rate is set at 2.5 cents (plus GST) per litre of grape wine sold in New Zealand and overseas in a levy year.
<ul style="list-style-type: none">• The levy is spent on activities closely related to the interests of wineries.

⁸¹ Source: Winegrowers legal guide, September 2007

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