On completion of this chapter, you will be able to:

1. Understand the importance of strategic management to a small business.
2. Explain why and how a small business must create a competitive advantage in the market.
3. Develop a strategic plan for a business using the nine steps in the strategic planning process.
4. Discuss the characteristics of three basic strategies—low cost, differentiation, and focus—and know when and how to employ them.
5. Understand the importance of controls such as the balanced scorecard in the planning process.
Few activities in the life of a business are as vital—or as overlooked—as that of developing a strategy for success. Too often, entrepreneurs brimming with optimism and enthusiasm launch businesses destined for failure because their founders never stop to define a workable strategy that sets them apart from their competition. Because they tend to be people of action, entrepreneurs often find the process of developing a strategy dull and unnecessary. Their tendency is to start a business, try several approaches, and see what works. Without a cohesive plan of action, however, these entrepreneurs have as much chance of building a successful business as a defense contractor attempting to build a jet fighter without blueprints. Companies lacking clear strategies may achieve some success in the short run, but as soon as competitive conditions stiffen or an unanticipated threat arises, they usually “hit the wall” and fold. Without a basis for differentiating itself from a pack of similar competitors, the best a company can hope for is mediocrity in the marketplace.

In today’s global competitive environment, any business, large or small, that is not thinking and acting strategically is extremely vulnerable. Every business is exposed to the forces of a rapidly changing competitive environment, and in the future small business executives can expect even greater change and uncertainty. From sweeping political changes around the planet and rapid technological advances to more intense competition and newly emerging global markets, the business environment has become more turbulent and challenging to business owners. Although this market turbulence creates many challenges for small businesses, it also creates opportunities for those companies that have in place strategies to capitalize on them. Historically important, entrepreneurs’ willingness to adapt, to create change, to experiment with new business models, and to break traditional rules has become more important than ever. “It’s not the strongest or the most intelligent [companies that] survive,” says American Express CEO Ken Chenault, “but those most adaptive to change.”

Perhaps the biggest change business owners face is unfolding now: the shift in the world’s economy from a base of financial to intellectual capital. “Knowledge is no longer just a factor of production,” says futurist Alvin Toffler. “It is the critical factor of production.” Today, a company’s intellectual capital is likely to be the source of its competitive advantage in the marketplace. Intellectual capital comprises three components:

1. **Human capital**, the talents, creativity, skills, and abilities of a company’s workforce, shows up in the innovative strategies, plans, and processes that the people in an organization develop and then passionately pursue.
2. **Structural capital**, the accumulated knowledge and experience that a company possesses, can take many forms including processes, software, patents, copyrights, and, perhaps most important, the knowledge and experience of the people in a company.
3. **Customer capital** is the established customer base, positive reputation, ongoing relationships, and goodwill that a company builds up over time with its customers.

Increasingly, entrepreneurs are recognizing that the capital stored in these three areas forms the foundation of their ability to compete effectively and that they must manage this intangible capital base carefully. Every business uses all three components in its strategy, but the emphasis they place on each one varies.

**Whole Foods**, a highly successful retailer of natural and organic foods with 172 stores in North America and the United, relies heavily on human capital as the basis for its competitive advantage in the marketplace. The company subjects all job applicants to a thorough screening process, carefully selecting only those who demonstrate a passion for what lies at the heart of its competitive edge: a love of food and dedication to customer service. Unlike most of its competitors in the supermarket industry, Whole Foods invests heavily in training its workers (called Team Members inside the company) so that they can demonstrate and explain to customers the features and the benefits of the company’s natural foods. In addition, managers recognize that food preferences vary from one region of a nation to another, and they give Team Members at the local level a great deal of autonomy in the selection of foods they stock. Because of its recognition of the role Team
This knowledge shift will create as much change in the world’s business systems as the Industrial Revolution did in the agriculture-based economies of the 1800s. The Knowledge Revolution will spell disaster for those companies who are not prepared for it, but it will spawn tremendous opportunities for those entrepreneurs equipped with the strategies to exploit these opportunities. Management legend Jack Welch, who masterfully guided General Electric for many years, says, “Intellectual capital is what it’s all about. Releasing the ideas of people is what we’ve got to do if we are going to win.”

However, in practice, releasing people’s ideas is much more difficult than it appears. The key is to encourage employees to generate a large volume of ideas, recognizing that only a few (the best) will survive. According to Gary Hamel, author of Inside the Revolution, “If you want to find a few ideas with the power to enthrall customers, foil competitors, and thrill investors, you must first generate hundreds and potentially thousands of unconventional strategic ideas. Put simply, you have to crush a lot of rock to find a diamond.” In other words, small companies must use the creative techniques discussed in Chapter 2 as one source of competitive advantage over their rivals.

The rules of the competitive game of business are constantly changing. To be successful, entrepreneurs can no longer do things in the way they’ve always done them. Fortunately, successful entrepreneurs have at their disposal a powerful weapon to cope with a hostile, ever-changing environment: the process of strategic management. Strategic management involves developing a game plan to guide a company as it strives to accomplish its vision, mission, goals, and objectives and to keep it from straying off its desired course. The idea is to give an entrepreneur a blueprint for matching the company’s strengths and weaknesses to the opportunities and threats in the environment.

Building a Competitive Advantage

The goal of developing a strategic plan is to create for the small company a competitive advantage—the aggregation of factors that sets a small business apart from its competitors and gives it a unique position in the market that is superior to its competitor. From a strategic perspective, the key to business success is to develop a unique competitive advantage, one that creates value for customers and is difficult for competitors to duplicate. A company that gains a competitive advantage becomes a leader in its market and can achieve above-average profits.

Early in its existence, the Blockbuster Video chain gained a significant advantage over rival video rental stores when it negotiated a deal with the major movie studios to purchase videos for just $6 each, plus a revenue sharing agreement of 40 percent of the rental fees. The agreement meant that Blockbuster could lower the cost of its inventory to less than one-tenth of that of its competitors, who were still paying an average of $65 per video! Blockbuster’s significantly lower costs meant that it could stock thousands more video titles than any of its rivals, enabling the company to offer customers a tangible benefit (greater selection and in-stock guarantees) while creating a sizeable competitive advantage in the market.

Building a competitive advantage alone is not enough; the key to success over time is building a sustainable competitive advantage. In the long run, a company gains a sustainable competitive advantage through its ability to develop a set of core competencies that enable it to serve its selected target customers better than its rivals. Core competencies are a unique set of capabilities that a company develops in key operational areas that allow it to vault past competitors.
customer service, innovation, team-building, flexibility, responsiveness, and others, that allow it to vault past competitors. As the phrase suggests, they are central to a company’s ability to compete successfully and are usually the result of important skills and lessons a business has learned over time. Two of the Disney Company’s core competencies are animation and the ability to create magical experiences for guests at its theme parks through superior customer service. After company founder Walt Disney died, however, the company lost its focus, moved away from these core competencies, and struggled as its competitive edge in animated films slipped away to smaller competitors such as Pixar.

Typically, a company develops core competencies in no more than five or six (often fewer) areas. These core competencies become the nucleus of a company’s competitive advantage and are usually quite enduring over time. Markets, customers, and competitors may change, but a company’s core competencies are more durable, forming the building blocks for everything a company does. To be effective strategically, these competencies should be difficult for competitors to duplicate, and they must provide customers with an important perceived benefit. Small companies’ core competencies often have to do with the advantages of their size—such as agility, speed, closeness to their customers, superior service, or the ability to innovate. In short, their small size is an advantage, allowing them to do things that their larger rivals cannot. The key to success is building the company’s strategy on these core competences and concentrating them on providing superior service and value for its target customers (see Figure 3.1).

![Company Profile: Netflix](image)

Netflix

Reed Hastings, founder of Netflix, transformed the video rental industry when he created a Web-based model that allows customers to make their video selections online and to avoid having to pay late fees. Hastings’ next innovation is to deliver movies over the Internet without having to ship DVDs through its distribution centers.

Blockbuster Video’s early market dominance in the video rental business did not go unchallenged, and its competitive advantage proved to be unsustainable over time. The most serious challenge comes from Netflix, a small company that has created a unique online DVD rental service. Software entrepreneur Reed Hastings saw the Web as a way to revolutionize the delivery of videos to consumers and launched the company in 1997 by investing his own money and raising $120 million in equity capital. For a monthly subscription fee, customers log onto the Netflix Web site and pick the movies they want to rent and the order in which they want to receive them. The order goes to one of the 35 Netflix regional distribution centers that is closest to the customer, where employees fill the order. Customers can keep a DVD as long as they want without incurring any late fees, and shipping (both ways) is free. When a customer returns a DVD, a computer scans it, looks up the next video on the customer’s order, and sends it out. About 90 percent of DVDs come in and go out on the same day. Netflix is building its competitive advantage on several core competencies. Hastings created the business system that drives Netflix using his extensive knowledge of computer software. One venture capitalist says Netflix’s “film recommendation software, its merchandising, and the inventory control systems are so sophisticated. It isn’t that they couldn’t be replicated, but they’re hard to do, and it’ll take a lot of money, time, and commitment to get it right as Netflix has.” CineMatch, the company’s proprietary film suggestion software (29,000 lines of code), uses customers’ ratings from past films they
No business can be everything to everyone. In fact, one of the biggest pitfalls many entrepreneurs stumble into is failing to differentiate their companies from the crowd of competitors. Entrepreneurs often face the challenge of setting their companies apart from their larger, more powerful competitors (who can easily outspend them) by using their creativity and the special abilities their businesses offer customers. Developing core competencies does not necessarily require a company to spend a great deal of money. It does, however, require an entrepreneur to use creativity, imagination, and vision to identify those things that it does best and that are most important to its target customers. Businesses have a huge number of ways to create a competitive edge, but building strategy around a company’s core competencies allows it to gain a sustainable competitive edge based on what it does best.

Tom's of Maine has built its reputation over the last 35 years as a back-to-nature company that sells a line of more than 90 all-natural personal care products with environmentally friendly packaging and donates 10 percent of its pre-tax profits to charity. Founder Tom Chappell's company competes in the same industry as giants such as Unilever, Colgate-Palmolive, and Procter & Gamble by focusing on its base of environmentally conscious customers and by promoting itself as a company “working with nature to make a difference.” Gearing up for growth, Tom's of Maine has introduced a line of herbal remedy products as well as a line of toothpastes for adults and children. Like all of its other products, the new toothpastes contain no artificial flavors, dyes, sweeteners, or preservatives, nor are they tested on animals. Tom’s of Maine is the only company to have a complete line of all-natural fluoride toothpastes that are approved by the American Dental Association. The toothpastes and all of the company’s product extensions are based on its core competency of developing and manufacturing all-natural, environmentally friendly products that meet the highest standards of quality and safety, something that enables Tom’s products to sell at a premium. Another core competency is the company’s stellar reputation among a loyal customer base as a business with a deep sense of ethics and environmental and social responsibility. (Chappell is the only CEO to have earned a master's degree at the Harvard Divinity School.) Explaining the company's enduring success, Gwynne Rogers of the Natural Marketing Institute says, “Lots of companies foster sustainable business practices, but they don’t make them relevant to consumers. Tom’s has positioned its mission right at the point of sale.”

When it comes to developing a strategy for establishing a competitive advantage, small companies such as Tom’s of Maine have a variety of natural advantages over their larger competitors. Small businesses often have narrower product lines, more clearly defined customer bases, a special connection with their customers, and specific geographic market areas. Entrepreneurs usually are in close contact with their markets, giving them valuable knowledge on how to best serve their customers’ needs and wants. Because of the simplicity of their organization structures, small business owners are in touch with
employees daily, often working side by side with them, allowing them to communicate strategic moves first-hand. Consequently, small businesses find that strategic management comes more naturally to them than to larger companies with their layers of bureaucracy and far-flung operations.

Strategic management can increase a small company’s effectiveness, but entrepreneurs first must have a process designed to meet their needs and their business’s special characteristics. It is a mistake to attempt to apply a big business’s strategic development techniques to a small business because a small business is not merely “a little big business.” Because of their size and their particular characteristics—small resource base, flexible managerial style, informal organizational structure, and adaptability to change—small businesses need a different approach to the strategic management process. The strategic management procedure for a small business should include the following features:

- Use a relatively short planning horizon—two years or less for most small companies.
- Be informal and not overly structured; a shirtsleeve approach is ideal.
- Encourage the participation of employees and outside parties to improve the reliability and creativity of the resulting plan.
- Do not begin with setting objectives because extensive objective setting early on may interfere with the creative process of strategic management.
- Maintain flexibility; competitive conditions change too rapidly for any plan to be considered permanent.
- Focus on strategic thinking, not just planning, by linking long-range goals to day-to-day operations.
- Let planning be an ongoing process because businesses and the competitive environment in which they operate constantly change.

Who Says Shopping for Groceries Can’t Be Fun?

In an industry famous for razor-thin profit margins, high levels of employee turnover, and intense competition usually based on price, Wegmans, a family-owned chain of 67 supermarkets in New York, New Jersey, Pennsylvania, and Virginia, is quite unique. It has to be. Traditional grocers are under attack on many fronts. Mass merchandisers such as Wal-Mart with its superstore concept are taking customers, sales, and market share from traditional grocers. Mass merchandisers’ now control one-third of the grocery market, and experts predict that their market share will continue to rise, hitting about 40 percent in 2008. Customers say they are bored with the shopping experience at most traditional grocers. One recent study reports that 84 percent of shoppers say that traditional grocery stores are all alike. Over the past several years, several chains have struggled to survive, and some have declared bankruptcy or were bought out by competitors.

How does this relatively small chain of grocery stores founded in 1930 by brothers John and Walter Wegman manage not only to survive, but also to claim a spot near the top of the industry? Although the answer to that question involves as many components as the number of brands on the cereal aisle in one of the Wegmans stores, much of the credit goes to the company’s clever retail strategy and the way it treats employees. That strategy took root early in the company’s existence when its founding brothers built a 300-seat café in their first store in Rochester, New York, a concept that was unheard of in 1930. When Robert Wegman, son of one of the founders, took over the company in 1950, he instituted a host of employee-friendly benefits such as profit-sharing and full medical coverage long before benefits of this type were popular. When asked why he made such a bold move, Robert, now chairman of the company, says simply, “I was no different from them.”
Wegmans’ annual salaries for full-time workers and hourly wages for part-time workers are among the highest in the industry. Not only do the higher wages discourage labor unions from setting up shop, but they also keep the employee turnover rate—and the resulting costs of constantly having to hire and train new workers—well below the industry average. Wegmans’ generous pay scale and its consistent listing as one of the 100 best companies to work for also attracts quality workers. In fact, the sous chef at its Pittsford, New York, store previously worked at the French Laundry, the famous Napa Valley restaurant that is consistently voted as the best in the United States.

In addition to excellent pay, Wegmans also offers college scholarships for both its full- and part-time employees. Over the last two decades, the company has awarded more than $54 million in scholarships to some 17,500 workers. Wegmans also sends many of its employees to locations around the world to learn about or to locate new and unique sources of foods—from wine and cheese to mushrooms and sushi. After all, reasons Robert’s son, Danny, who now manages Wegmans, what good is it to offer 500 varieties of cheese if employees can’t explain to customers the best way to serve them, which types of crackers to serve them on, and which wines go best with them?

Although Wegmans approach to managing people pushes its labor cost to 15 to 17 percent of sales (compared with 12 percent of sales for the average supermarket), its annual turnover rate for full-time employees is just 6 percent, less than one-third the industry average of 19 percent. More than 20 percent of Wegmans’ employees have 10 years or more of service, and this shows up in the wealth of knowledge about the company’s products that they enthusiastically share with customers. “It’s our [employees’] knowledge that can help the customer,” says Danny. “So the first pump we have to prime is our own people.”

Almost everyone Wegmans hires has a keen interest in food, but the real acid test for new hires is a passion for taking care of customers. Indeed, Wegman’s focus on customer service is another component of its strategy for success. Every employee in the store has the power to do whatever it takes to keep customers happy without having to involve a manager higher up the chain of command. One worker even cooked a customer’s Thanksgiving turkey for her in the store when the bird proved to be too big to fit in her oven. Why does Wegmans go to such lengths for its customers? Because it pays big dividends! The Wegmans know that satisfied customers keep coming back and that they spend more when they do. However, Wegmans’ wants to do more than satisfy customers; the goal is to build an emotional connection with them. One Gallup survey finds that shoppers who were emotionally connected to a supermarket spent 46 percent more than shoppers who were satisfied but lacked an emotional bond with the store.

Wegmans’ retail strategy involves offering customers superior service and the convenience of one-stop shopping. Each store—the new ones are 130,000 square feet, three times the size of the typical supermarket—provides shoppers with a huge selection of top-quality products ranging from national brands such as Cocoa Puffs to upscale organic produce, all displayed with the flair and style of an upscale retail boutique. Each store also boasts a bookstore, child play centers, a dry cleaner, a photo processing lab, a video rental center, a wine shop, a pharmacy, a florist, international newspapers, and an $850 espresso maker. “Going there is not just shopping,” says one industry consultant. “It’s an event.” The result is that Wegmans’ sales per square foot of store space is 50 percent higher than the industry average of $9.29.

The Wegman family intentionally follows a methodical growth strategy, opening only two new stores a year. To make sure each new store is a success, the company puts some of the best and brightest workers from its existing stores to work in its new ones. After earning an undergraduate degree in mechanical engineering and an MBA, Heather Pawlowski decided to enter Wegmans management training program, in which she learned all of the aspects of store operations first-hand. When asked about the company’s consistent track record of success, Pawlowski, now one of the company’s vice presidents, says, “We’re taking customers to a place they have not been before.”

1. Explain the core competencies that Wegmans has built. What is the source of its core competencies?
2. Identify Wegmans’ strengths, weaknesses, opportunities, and threats. (You may want to use the Web or your library to read more about this interesting company.)
3. How has Wegmans’ strategy created a competitive edge for the company in its markets? How does the company sustain its competitive edge? What suggestions can you offer for ensuring that Wegmans maintains its competitive edge?

The Strategic Management Process

Strategic management is a continuous process that consists of nine steps:

**Step 1** Develop a clear vision and translate it into a meaningful mission statement.
**Step 2** Assess the company’s strengths and weaknesses.
**Step 3** Scan the environment for significant opportunities and threats facing the business.
**Step 4** Identify the key factors for success in the business.
**Step 5** Analyze the competition.
**Step 6** Create company goals and objectives.
**Step 7** Formulate strategic options and select the appropriate strategies.
**Step 8** Translate strategic plans into action plans.
**Step 9** Establish accurate controls.

**Step 1. Develop a Clear Vision and Translate It into a Meaningful Mission Statement**

**Vision** Throughout history, the greatest political and business leaders have been visionaries. Whether the vision is as grand as Martin Luther King Jr.’s “I have a dream” speech or as simple as Ray Kroc’s devotion to quality, service, cleanliness, and value at McDonald’s, the purpose is the same: to focus everyone’s attention on the same target and to inspire them to reach it. The vision is future-oriented and touches everyone associated with the company—employees, investors, lenders, customers, and the community. It is an expression of what an entrepreneur stands for and believes in. Highly successful entrepreneurs are able to communicate their vision and their enthusiasm about that vision to those around them.

A vision is the result of an entrepreneur’s dream of something that does not exist yet and the ability to paint a compelling picture of that dream for everyone to see. It answers the question “Where are we going?” A clearly defined vision helps a company in three ways:

1. **Vision provides direction.** Entrepreneurs who spell out the vision for their company focus everyone’s attention on the future and determine the path the business will take to get there.
2. **Vision determines decisions.** The vision influences the decisions, no matter how big or how small, that owners, managers, and employees make every day in a business. This influence can be positive or negative, depending on how well defined the vision is.
3. **Vision motivates people.** A clear vision excites and ignites people to action. People want to work for a company that sets its sights high.

Vision is based on an entrepreneur’s values. Explaining how an entrepreneur’s values are the nucleus around which a company grows, author and consultant Ken Blanchard says, “Winning companies first emphasize values—the beliefs that you, as the business owner, have about your employees, customers, quality, ethics, integrity, social responsibility, growth, stability, innovation, and flexibility. Managing by values—not by profits—is a powerful process.” Successful entrepreneurs build their businesses around a set of three to six core values, which might range from respect for the individual and innovation to creating satisfied customers and making the world a better place.

In 1957, 18 years after they had launched the company bearing their names, Bill Hewlett and Dave Packard were pleased with their company’s rapid growth but were concerned that the business might lose its “small company atmosphere.” The cofounders took 20 of their best employees to an upscale resort in California’s wine country (on one of the first recorded corporate retreats) to define the type of culture Hewlett Packard would foster. By the end of the retreat, the team had drafted a set of values that ultimately became the basis of “the HP Way,” the highly admired culture the company retained long after the death of its founders.
Indeed, truly visionary entrepreneurs see their companies’ primary purpose as more than just “making money.” One writer explains, “Almost all workers are making decisions, not just filling out weekly sales reports or tightening screws. They will do what they think best. If you want them to do as the company thinks best too, then you must [see to it that] that have an inner gyroscope aligned with the corporate compass.” That gyroscope’s alignment depends on the entrepreneur’s values and how well he or she transmits them throughout the company.

The best way to put values into action is to create a written mission statement that communicates those values to everyone the company touches.

**Mission Statement**  The mission statement addresses another basic question of any business venture: “What business are we in?” Establishing the purpose of the business in writing must come first in order to give the company a sense of direction. “If you don’t reduce [your company’s purpose] to paper, it just doesn’t stick,” says the owner of an architecture firm. “Reducing it to paper really forces you to think about what you are doing.” As an enduring declaration of a company’s purpose, a mission statement is the mechanism for making it clear to everyone the company touches “why we are here” and “where we are going.”

Truett Cathy, founder of the highly successful restaurant chain Chick-fil-A, recalls a time when his business was struggling because of intensifying competition from big hamburger chains. The company, with 200 outlets at the time, was struggling to keep operating costs under control as inflation threatened to push them ever higher. Cathy scheduled an executive retreat at a lake outside of Atlanta, where managers could relax and talk about their concerns and ideas for the company. His oldest son, Dan, director of operations, asked, “Why are we in business? Why are we here?” Cathy was about to tell his son that this retreat was no time to dwell on philosophical issues because there were bigger problems to solve. “Then,” recalls Cathy, “I realized he was serious. His question both challenged and inspired us.” In the ensuing brainstorming session, the group defined values that became Chick-fil-A’s mission statement: “To glorify God by being faithful stewards of all that is entrusted to us. To have a positive influence on all who come in contact with Chick-fil-A.” With their purpose clearly defined, the management team went on to lead the company in a growth spurt in which sales climbed 30 percent a year. Today, the company has more than 1,000 restaurants across the country (none of which are open on Sundays).

Without a concise, meaningful mission statement, a small business risks wandering aimlessly in the marketplace, with no idea of where to go or how to get there. The mission statement sets the tone for the entire company and focuses its attention on the right direction.

**Elements of a Mission Statement**  A sound mission statement need not be lengthy to be effective. Three key issues entrepreneurs and their employees should address as they develop a mission statement for their businesses include the following:

- **The purpose** of the company: What are we in business to accomplish?
- **The business** we are in: How are we going to accomplish that purpose?
- **The values** of the company: What principles and beliefs form the foundation of the way we do business?

A company’s mission statement may be the most essential and basic communications that it puts forward. If the people on the plant, shop, retail, or warehouse floor don’t know what a company’s mission is, then, for all practical purposes, it does not have one! The mission statement expresses a company’s character, identity, and scope of operations, but writing it is only half the battle, at best. The most difficult part is living that mission every day. That’s how employees decide what really matters. To be effective, a mission statement must become a natural part of the organization, embodied in the minds, habits, attitudes, and decisions of everyone in the company every day. According to the Workplace 2000
Employee Insight Survey, 89 percent of employees say their companies have mission statements. Unfortunately, only 23 percent of workers believe their company’s mission statement has become a way of doing business!15 One business writer claims, “If what you say about your firm’s values and mission isn’t true, you’re in worse trouble than if you’d never articulated it in the first place.”16 Five years after founding Field Trip Factory Inc., a business that organizes life skill educational field trips for students, Susan Singer saw the need to update the company’s mission statement. At a company retreat, she and her employees decided that their existing mission statement no longer reflected what the company actually stood for and did. A brainstorming session yielded a new mission statement that Singer says is helping her company improve its bottom line. “It became so clear what we do vs. what we want to be,” she says.17

A well-used mission statement serves as a strategic compass for a small company. In its mission statement, Starbucks commits not only to building a successful coffee business, but also to strengthening the communities in which the company operates and to protecting the environment. Consider the message that Starbucks’ two-part mission statement sends to company stakeholders:

Starbucks Mission: Establish Starbucks as the premier purveyor of the finest coffee in the world while maintaining our uncompromising principles while we grow. The following six guiding principles will help us measure the appropriateness of our decisions:

- Provide a great work environment and treat each other with respect and dignity.
- Embrace diversity as an essential component of the way we do business.
- Apply the highest standards of excellence to the purchasing, roasting, and fresh delivery of our coffee.
- Develop enthusiastically satisfied customers all of the time.
- Contribute positively to our communities and our environment.
- Recognize that profitability is essential to our future success.

Environmental Mission Statement: Starbucks is committed to a role of environmental leadership in all facets of our business.
A company may have a powerful competitive advantage, but it is wasted unless (1) the owner communicates that advantage to workers, who, in turn, work hard to communicate it to customers and potential customers and (2) customers recommend the company to their friends because they understand the benefits they are getting from it that they cannot get elsewhere. That’s the real power of a mission statement. Table 3.1 offers some useful tips on writing a mission statement.

Step 2. Assess the Company’s Strengths and Weaknesses

Having defined the vision that he or she has for the company and translated that vision into a meaningful mission statement, an entrepreneur can turn his or her attention to assessing company strengths and weaknesses. Building a successful competitive strategy requires a business to magnify its strengths and overcome or compensate for its weaknesses. **Strengths** are positive internal factors that a company can draw on to accomplish its mission, goals, and objectives. They might include special skills or knowledge, a positive public image, an experienced sales force, an established base of loyal customers, and many other factors. **Weaknesses** are negative internal factors that inhibit a company’s ability to accomplish its mission, goals, and objectives. A lack of capital, a shortage of skilled workers, the inability to master technology, and an inferior location are examples of weaknesses.

Identifying strengths and weaknesses helps owners to understand their businesses as they exist (or, for start-ups, will exist). An organization’s strengths should originate in the core competencies that are essential to gaining an edge in each of the market segments in which the firm competes. The key to building a successful strategy is using the company’s underlying strengths as its foundation and matching those strengths against competitors’ weaknesses.

One effective technique for taking this strategic inventory is to prepare a balance sheet of the company’s strengths and weaknesses (see Table 3.2). The positive side should reflect important skills, knowledge, or resources that contribute to the firm’s success. The negative side should record honestly any limitations that detract from the company’s ability to compete. This balance sheet should analyze all key performance areas of the business—human resources, finance, production, marketing, product development, organization, and others. This analysis should give owners a more realistic perspective of their businesses, pointing out foundations on which they can build future strengths and obstacles that they must remove for the business to progress. This exercise can help entrepreneurs move from their current position to future actions.

Step 3. Scan the Environment for Significant Opportunities and Threats Facing the Business

**Opportunities** Once entrepreneurs have taken an internal inventory of company strengths and weaknesses, they must turn to the external environment to identify any opportunities and threats that might have a significant impact on the business. **Opportunities** are positive external options that a firm can exploit to accomplish its mission, goals, and objectives. The number of potential opportunities is limitless, so entrepreneurs need to analyze only those factors that are most significant to the business.
### TABLE 3.1 Tips for Writing a Powerful Mission Statement

A mission statement is a useful tool for getting everyone fired up and heading in the same direction, but writing one is not as easy as it may first appear. Here are some tips for writing a powerful mission statement:

- **Keep it short.** The best mission statements are just a few sentences long. If they are short, people will tend to remember them better.

- **Keep it simple.** Avoid using fancy jargon just to impress outsiders such as customers or suppliers. The first and most important use of a mission statement is inside a company.

- **Take a broad view, but not too broad.** If it is too specific, a mission statement can limit a company's potential. Similarly, a mission statement is too broad if it applies to any company in the industry. When asked what business his company was in, Rob Carter, a top manager at FedEx, did not mention shipping packages quickly; instead, his response was, “We’re in the business of engineering time.”

- **Get everyone involved.** If the boss writes the company mission statement, who is going to criticize it? Although the entrepreneur has to be the driving force behind the mission statement, everyone in the company needs the opportunity to have a voice in creating it. Expect to write several drafts before you arrive at a finished product.

- **Keep it current.** Mission statements can get stale over time. As business and competitive conditions change, so should your mission statement. Make a habit of evaluating your mission periodically so that it stays fresh.

- **Make sure that your mission statement reflects the values and beliefs you hold dear.** They are the foundation on which your company is built.

- **Make sure your mission includes values that are worthy of your employees’ best efforts.** One entrepreneur says that a mission statement should “send a message to employees, suppliers, and customers as to what the purpose of the company is aside from just making profits.”

- **Make sure your statement reflects a concern for the future.** Business owners can get so focused on the present that they forget about the future. A mission statement should be the first link to the company’s future.

- **Keep the tone of the statement positive and upbeat.** No one wants to work for a business with a pessimistic outlook of the world.

- **Consider using your mission statement to lay an ethical foundation for your company.** This is the ideal time to let employees know what you company stands for—and what it won’t stand for.

- **Look at other companies’ mission statements to generate ideas for your own.** Two books, *Say It and Live It: The 50 Corporate Mission Statements That Hit the Mark*, by Patricia Jones and Larry Kahnener (New York: Currency/Doubleday, 1995), and *Mission Statements: A Guide to the Corporate and Nonprofit Sectors*, by John W. Graham and Wendy C. Havlick (New York: Garland, 1994), are useful resources.

- **Make sure that your mission statement is appropriate for your company’s culture.** Although you should look at other companies’ missions, do not make the mistake of trying to copy them. Your company’s mission is unique to you and your company.

- **Use it.** Don’t go to all of the trouble of writing a mission statement just to let it collect dust. Post it on bulletin boards, print it on buttons and business cards, stuff it into employees’ pay envelopes. Talk about your mission often, and use it to develop your company’s strategic plan. That’s what it’s for!


(possibly two or three at most). The key is to focus on the most promising opportunities that fit most closely with the company’s strengths and core competencies.

When identifying opportunities, an entrepreneur must pay close attention to new potential markets. Are competitors overlooking a niche in the market? Is there a better way to reach customers? Can we develop new products that offer customers better value? What opportunities are trends in the industry creating?
TABLE 3.2 Identifying Company Strengths and Weaknesses

<table>
<thead>
<tr>
<th>Strengths (Positive Internal Factors)</th>
<th>Weaknesses (Negative Internal Factors)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Aviation Partners</td>
<td></td>
</tr>
</tbody>
</table>

Rising fuel prices have created problems for many businesses, but few have felt the impact as directly as those in the airline industry. Yet rising energy prices have produced a significant opportunity for Aviation Partners, a small company founded by a group of retired aeronautic engineers. Noting that birds’ wings turn up at the tips to provide more lift and less drag (hence requiring birds to use less energy), the founders of Aviation Partners developed “winglets,” small fins attached to the ends of wings that extend upward, for use on commercial jets. Tests indicated that jets using the winglets were far more fuel-efficient than those without them. In the late 1990s, however, the small company found it difficult to market the winglets because jet fuel prices were just 50 cents a gallon. As jet fuel prices climbed significantly over the next several years, Aviation Partners, now partnering with Boeing Company, found airlines much more interested in their product. Although the cost to install the winglets can run as high as $700,000 per plane, the savings in fuel costs add up to the millions over the life of a jet. Aviation Partners is capitalizing on this opportunity and counts among its customers virtually every airline in operation today.¹⁹

As Aviation Partners’ experience illustrates, opportunities arise as a result of factors that are beyond entrepreneurs’ control. Constantly scanning for those opportunities that best match their companies’ strengths and core competencies and then pouncing on them ahead of competitors is the key to success.

When demand for the composite materials manufactured by Steve Warshaw’s company M Cubed declined as the semiconductor market slumped, he began searching for opportunities to apply the company’s expertise in other industries. As the United States stepped up its efforts in the war of terrorism, Warshaw spotted an opportunity to produce the ceramic plates used in bulletproof vests. Although the finished product was quite different from semiconductors, M Cubed found it quite easy to adapt its techniques and technology to produce strong yet lightweight panels capable of stopping even armor-piercing bullets. Shifting to this new market has accelerated M Cube’s sales, and Warshaw sees tremendous potential for future growth as both law enforcement and military officials increase their purchases of bulletproof vests.²⁰

**Threats** Negative external forces that inhibit a company’s ability to achieve its mission, goals, and objectives are referred to as threats. Threats to the business can take a variety of forms, such as competitors entering the local market, a government mandate regulating a business activity, an economic recession, rising interest rates, technological advances making a company’s product obsolete, and many others. For instance, video on demand and digital downloading pose a serious threat to both retailers of DVDs and to companies that rent them from storefronts (Blockbuster) or online (Netflix).

Many small retailers face a threat from “big box” retailers such as Wal-Mart, Home Depot, Circuit City, and others offering lower prices because of their high-volume purchasing power, huge advertising budgets, and mega-stores that attract customers for miles around.
Kenneth Stone, a professor at Iowa State University and a leading researcher on Wal-Mart’s impact on small companies, says that after Wal-Mart entered Iowa in 1983, 23 percent of drugstores and 45 percent of hardware stores disappeared.²¹ However, small businesses with the proper strategies in place do not have to fold in the face of intense competition.

After Wal-Mart, Home Depot, Tractor Supply Company, and Lowe’s opened next to their second-generation small hardware store in Greenville, South Carolina, Terry and Debbie Dobson changed their competitive strategy and refocused their business, Dobson’s Gifts and General Hardware, more on gifts and less on the standard hardware items their larger rivals sold. The Dobsons now rely on a focus strategy that emphasizes unique gifts and home décor items with a distinctively local flavor and specialty hardware items such as loose nuts and bolts, pocket knives, and Radio Flyer wagons that their big box competitors overlook. The Dobsons continue to set their business apart by offering a high level of personal service, including knowledgeable, long-time employees and a home delivery service that customers love. “I’m within a rock’s throw of my two major competitors,” says Terry, “and actually we’re glad they’re here now. They bring in traffic, and we draw off that traffic.”²²

Although they cannot control the threats themselves, entrepreneurs such as the Dobsons must prepare a plan for shielding their businesses from these threats.

Figure 3.2 illustrates that opportunities and threats are products of the interactions of forces, trends, and events outside the direct control of the business. These external forces have direct impact on the behavior of the markets in which the business operates, the behavior of competitors, and the behavior of customers. Table 3.3 provides a form that allows business owners to take a strategic inventory of the opportunities and threats facing their companies.

The interactions of strengths and weaknesses and opportunities and threats can be the most revealing aspects of using a SWOT analysis as part of a strategic plan. This analysis also requires entrepreneurs to take an objective look at their businesses and the environment in which they operate as they address many issues fundamental to their companies’ success in the future.

<table>
<thead>
<tr>
<th>TABLE 3.3 Identifying Opportunities and Threats</th>
</tr>
</thead>
<tbody>
<tr>
<td>Opportunities</td>
</tr>
<tr>
<td>(Positive External Factors)</td>
</tr>
</tbody>
</table>

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²¹

²²
Before music downloading became so popular, music lovers often bought a single CD for just one song. Given the attitude, “Who wants to pay nearly $20 for one song?” it is little wonder that customers embraced “free” music download services such as Napster (the original), KaZaA, and Grokster. Still, those downloading music without paying for it had to feel a twinge of guilt about the ethics of their actions. Then there were all of those lawsuits that the Recording Industry Association of America (RIAA) was filing against heavy downloaders, many of them college students. Who wants to be sued for downloading music, especially when damages can range from $750 to $150,000 per copyright violation? Representing the five major music companies, the RIAA filed 261 lawsuits against individuals it claimed had illegally used file-sharing software to distribute vast numbers of copyrighted songs. The suits claim that illegal file sharing is responsible for falling sales of recorded music and for robbing artists of their royalties. In addition, modern technology makes it quite easy for computer users to “rip and burn” tracks from CDs to create their own favorites or to store on their MP3 players. Indeed, shipments of recorded music have fallen 26 percent since 1999, and sales of blank CDs now exceed those of prerecorded CDs. “Our industry is being ravaged by piracy,” says a top executive at one music company.

To combat declining sales, the recording industry is attempting to create new business models that incorporate the legitimate sale of recorded music online. All of the major music companies are cooperating with Apple Computer Inc.’s industry-leading iTunes Music Store, which allows users to download songs legally for just 99 cents each. (Music companies receive roughly 65 cents for every downloaded song.) Users can listen to a 30-second preview of any song and, if they like it, can purchase a high-quality legal download with just one mouse-click. There is no subscription fee, and the iTunes library contains more than 1.5 million songs from the major music companies and more than 1,000 independent record companies as well as 10,000 audiobooks. Shoppers can browse titles by artist, song title, or genre. Because of the many benefits it offers, industry analysts predict that by 2010, digitally downloaded music will comprise between one-fourth to one-third of the recording industry's sales. “It pained us to see the music companies and the technology companies threatening to take each other to court,” says Apple founder Steve Jobs. “We thought that rather than sit around and throw stones, we’d actually do something about this.”

Throughout its history, the music industry has benefited from introducing new musical formats, from 78 rpm singles to the 33 rpm vinyl LP album to the eight-track tape to the Compact Disc. The transformation to digitally downloaded music, however, may be the most significant change of all. Not only would it be more convenient for customers, but the switch also would cut costs for all of the music companies by virtually eliminating manufacturing and distribution costs.

Music artists themselves see downloading as a double-edged sword. One survey reports that only three percent of music artists say that the Internet has hurt their ability to protect their creative work. Forty-seven percent agreed that peer-to-peer networks prevented them from earning royalties from their songs, but 43 percent said that those same networks helped artists promote and distribute their material. Two-thirds of the survey’s respondents said that file-sharing posed little threat to them.

It’s ironic that the music industry is struggling in an era when people are listening to music more than ever before. They simply aren’t paying for the privilege of listening the way they used to. Downloading, file sharing, and ripping and burning also pose a serious threat to music retailers, most of which are stuck selling music in a format (CDs) customers seem to dislike. Many music retail chains have either filed for Chapter 11 bankruptcy protection (Wherehouse and Tower Records) or have simply closed (National Record Mart).

Entrepreneur Bob French thinks he may have discovered one way to preserve retail music outlets with his
Mix and Burn machine, a device that allows users to scroll through a database of songs, listen to the ones they choose, create a personal playlist, and then burn the songs to a CD. French’s company, Mix and Burn, currently provides a library of 320,000 songs but offers additions weekly. French has established relationships with all five of the major music companies but has had difficulty signing independent record labels onto the company’s service. “We really focused on getting those major labels done to make this a viable business,” explains French. “Next year at this time, there will be more content from independent producers.”

Jack Dennis, owner of the Earshot Music store in downtown Greenville, South Carolina, was one of the early adopters of the Mix and Burn technology. Still a traditional music store, Earshot has transformed itself with the addition of 12 Mix and Burn stations grouped together in an area of the store called “The Blender” that in just a short time has become one of the most popular spots in the store. There customers can download five songs for $9.99 and 99 cents for each subsequent song. “We wanted to be able to offer digital technology in a retail environment,” says Dennis. You buy songs just like you would off the Internet, except you are here at our store.”

1. One analyst says, “Many music listeners have shown little regard for the idea that downloading a song from a file-sharing service such as KaZaA is tantamount to shoplifting from Tower Records.” Comment.
2. What strategic recommendations can you make to the music industry concerning the future of digital downloading?
3. What strategic recommendations can you make to music retailers concerning the future of digital downloading?


Step 4. Identify the Key Factors for Success in the Business

Key Success Factors Every business is characterized by controllable variables that determine the relative success of market participants. Identifying and manipulating these variables is how a small business gains a competitive advantage. By focusing efforts to maximize their companies’ performance on these key success factors, entrepreneurs can achieve dramatic market advantages over their competitors. Companies that understand these key success factors tend to be leaders of the pack, whereas those that fail to recognize them become also-rans.

Key success factors (KSFs) come in a variety of different patterns depending on the industry. Simply stated, they are the factors that determine a company’s ability to compete successfully in an industry. Every company in an industry must understand the key success factors driving the industry; otherwise, they are likely to become industry “also-rans” like the horses trailing the pack in the Kentucky Derby. Many of these sources of competitive advantages are based on cost factors such as manufacturing cost per unit, distribution cost per unit, or development cost per unit. Some are less tangible and less obvious but are just as important, such as superior product quality, solid relationships with dependable suppliers, superior customer service, a highly trained and knowledgeable sales force, prime store locations, readily available customer credit, and many others. For example, one restaurant owner identified the following key success factors:

- Tight cost control (labor costs, 15 to 18 percent of sales and food costs, 35 to 40 percent of sales)
- Trained, dependable, honest in-store managers
- Close monitoring of waste
- Careful site selection (the right location)
Identifying Key Success Factors

<table>
<thead>
<tr>
<th>Key Success Factor</th>
<th>How Your Company Rates</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Low 1 2 3 4 5 6 7 8 9 10 High</td>
</tr>
<tr>
<td>2</td>
<td>Low 1 2 3 4 5 6 7 8 9 10 High</td>
</tr>
<tr>
<td>3</td>
<td>Low 1 2 3 4 5 6 7 8 9 10 High</td>
</tr>
<tr>
<td>4</td>
<td>Low 1 2 3 4 5 6 7 8 9 10 High</td>
</tr>
<tr>
<td>5</td>
<td>Low 1 2 3 4 5 6 7 8 9 10 High</td>
</tr>
</tbody>
</table>

Conclusions:

List the specific skills, characteristics, and core competencies that your business must possess if it is to be successful in its market segment.

- High food quality
- Consistency
- Cleanliness
- Friendly and attentive service from a well-trained wait staff

These controllable variables determine the ability of any restaurant in his market segment to compete. Restaurants lacking these KSFs are not likely to survive, but those that build their strategies with these factors in mind will prosper. However, before entrepreneurs can build a strategy around the industry’s KSFs, they must identify them. Table 3.4 presents a form to help owners identify the most important success factors in the industry and their implications for their companies.

Identifying the KSFs in an industry allows entrepreneurs to determine where they should focus their companies’ resources strategically. It is unlikely that a company, even a large one, can excel on every KSF it identifies. Therefore, as they begin to develop their strategies, most entrepreneurs focus on surpassing their rivals on one or two KSFs to build a sustainable competitive edge. As a result, KSFs become the cornerstones of a company’s strategy.

John H. Daniel Company, a custom tailor of high-end men’s suits in Knoxville, Tennessee, understands that attracting and retaining skilled master tailors is crucial to its success. The company, founded in 1928, produces 75,000 to 80,000 made-to-measure suits a year that retail at prices ranging from $800 to $3,000, and sells them under a variety of labels. Unfortunately, the number of master tailors in the United States is negligible, and the family-owned business dedicates a significant portion of its budget to searching them out in foreign countries such as Turkey, Italy, and Vietnam. Owners Richard and Benton Bryant send scouts on recruiting trips to these countries and then pay to relocate the master tailors they hire along with their families to Tennessee. The company provides low-interest loans to help families get settled, and a company attorney handles all of the paperwork necessary to get visas for the tailors and their families.

Step 5. Analyze the Competition

Ask most small business owners to identify the greatest challenge their companies face and the most common response is competition. One study of small business owners by the National Federation of Independent Businesses (NFIB) reports that small business owners believe they operate in a highly competitive environment and that the level of competition is increasing. The World Wide Web and e-commerce have increased the ferocity and the scope of the competition entrepreneurs face as well and have forced
many business owners to reshape completely the ways in which they do business. Figure 3.3 shows the competitive strategies that small business owners rely on most heavily to compete with their rivals.

Neil Van Uum, owner of Joseph-Beth Booksellers, a small chain of six bookstores, faces intense competition from larger, more powerful rivals in an industry that has seen thousands of small booksellers close within the last decade. Yet, Joseph-Beth Booksellers manages not only to survive, but also to thrive in an industry where giants such as Barnes and Noble and Borders Books saturate local markets with retail outlets and Amazon blankets the market from its perch high atop the online food chain. “Either you have to be very niche-oriented, or you need a physical presence that says you’re significant,” says Michael Powell, owner of Powell’s Books, a legendary 70,000-square-foot bookstore in downtown Portland, Oregon. Like Powell, Van Uum has chosen to create a significant physical presence. His stores average 30,000 square feet, about 5,000 square feet larger than a typical Barnes and Noble store. Like most successful independent bookstores, Joseph-Beth emphasizes superior customer service, sponsors unique, in-store events (wine tastings, book signings, appearances by the Berenstain Bears for kids), and specializes in books that reflect local tastes. For instance, the Lexington, Kentucky, store located in the Mall at Lexington Green stocks more than 1,000 books by local authors, something national chain stores don’t do. Going one better than Barnes and Noble’s coffee bar and pastry shop, each Joseph-Beth store contains a full-service restaurant, each offering entrees inspired by cookbooks the company sells. Every store also includes a stationery department, a board game section, and a “health and well-being section” selling lotions, soaps, scented candles, and quilted tote bags. A store décor that includes cherry bookcases, comfortable couches, and fireplaces encourages shoppers to linger, and, of course, buy more. Dan Burstin, author of the popular Secrets of the Code, recently appeared in two Joseph-Beth stores to discuss his work. “What they’ve done,” he says, “is turn these stores into cultural centers.”

Keeping tabs on rivals’ movements through competitive intelligence programs is a vital strategic activity. “Business is like any battlefield. If you want to win the war, you have to know who you’re up against,” says one small business consultant. Unfortunately, most businesses are not very good at competitive intelligence; 97 percent of U.S. businesses...
do not systematically track the progress of their key competitors. The primary goals of a competitive intelligence program include the following:

- Avoiding surprises from existing competitors’ new strategies and tactics.
- Identifying potential new competitors.
- Improving reaction time to competitors’ actions.
- Anticipating rivals’ next strategic moves.

**Competitor Analysis** Sizing up the competition gives a business owner a more realistic view of the market and his or her company’s position in it. Yet not every competitor warrants the same level of attention in the strategic plan. Direct competitors offer the same products and services, and customers often compare prices, features, and deals from these competitors as they shop. Significant competitors offer some of the same products and services. Although their product or service lines may be somewhat different, there is competition with them in several key areas. Indirect competitors offer the same or similar products or services only in a small number of areas, but their target customers seldom overlap yours. Entrepreneurs should monitor closely the actions of their direct competitors, maintain a solid grasp of where their significant competitors are heading, and spend only minimal resources tracking their indirect competitors.

A competitive intelligence exercise enables entrepreneurs to update their knowledge of competitors by answering the following questions:

- Who are your primary competitors? Where are they located? (The Yellow Pages is a great place to start.)
- What distinctive competencies have they developed?
- How do their cost structures compare to yours? Their financial resources?
- How do they market their products and services?
- What do customers say about them? How do customers describe their products or services; their way of doing business; the additional services they might supply?
- What are their key strategies?
- What are their strengths? How can your company surpass them?
- What are their major weaknesses? How can your company capitalize on them?
- Are new competitors entering the business?

According to the Society of Competitive Intelligence, 95 percent of the competitive intelligence information is available from public sources that anyone can access—if they know how. Gathering information on competitors does not require entrepreneurs to engage in activities that are unethical, illegal, or unsavory (such as dumpster diving). One expert says that competitive intelligence (CI) involves “taking information from the public domain, adding it to what you know about your company and your industry, and looking for patterns.” Entrepreneurs using the following low-cost competitive intelligence methods can collect a great deal of information about their rivals:

- Read industry trade publications for announcements and news stories about competitors.
- Ask questions of customers and suppliers on what they hear competitors may be doing. In many cases, this information is easy to gather because some people love to gossip.
- Regularly debrief employees, especially sales representatives and purchasing agents. Experts estimate that 70 to 90 percent of the competitive information a company needs already resides with employees who collect it in their routine dealings with suppliers, customers, and other industry contacts.
- Attend trade shows and collect competitors’ sales literature.
- Watch for employment ads and job postings from competitors; knowing what types of workers they are hiring can tell you a great deal about their future plans.
- Conduct patent searches (see Chapter 2) for patents that competitors have filed. This gives important clues about new products they are developing.
- Environmental Protection Agency reports can provide important information about the factories of manufacturing companies, including the amounts and the kinds of
emissions released. A private group, Environmental Protection, also reports emissions for specific plants.31

- Learn about the kinds and amounts of equipment and raw materials competitors are importing by studying the *Journal of Commerce* Port Import Export Reporting Service (PIERS) database. These clues can alert an entrepreneur to new products a competitor is about to launch.
- If appropriate, buy competitors’ products and assess their quality and features. Benchmark their products against yours. The owner of a mail-order gourmet brownie business periodically places orders from her primary rivals and compares their packaging, pricing, service, and quality to her own.32
- Obtain credit reports on each of your major competitors to evaluate their financial condition. For as little as $122, Dun & Bradstreet and other research firms provide detailed credit reports of competitors that can be helpful in a strategic analysis.
- Publicly held companies must file periodic reports with the Securities and Exchange Commission (SEC), including quarterly 10-Q and annual 10-K reports. Information on publicly held companies is available at the Securities and Exchange Commission Web site (http://www.sec.gov).
- Investigate Uniform Commercial Code reports. Banks file these with the state whenever they make loans to businesses. These reports often include the amount of the loan and what it is for.
- Check out the resources of your local library, including articles, computerized databases, and online searches. Press releases, which often announce important company news, can be an important source of competitive intelligence. Many companies supply press releases through the PR Newswire. For local competitors, review back issues of the area newspaper for articles on and advertisements by competitors.
- Use the vast resources of the World Wide Web to learn more about your competitors. Visit their Web sites periodically to see what news is contained there. The Web enables small companies to uncover valuable competitive information at little or no cost. (Refer to our Web site at http://www.prenhall.com/scarborough for an extensive listing of more than 1,200 useful small business Web sites.)
- Visit competing businesses periodically to observe their operations. Tom Stemberg, CEO of Staples, a chain of office supply superstores, says, “I’ve never visited a store where I didn’t learn something.”33

Entrepreneurs can use the results of their competitive intelligence efforts to construct a competitive profile matrix for its most important competitors. A **competitive profile matrix** allows owners to evaluate their firms against the major competitor using the key success factors for that market segment. The first step is to list the key success factors identified in Step 4 of the strategic planning process (refer to Table 3.4) and to attach weights to them reflecting their relative importance. (For simplicity, the weights in this matrix sum add up to 1.00.) In this example, notice that product quality is weighted twice as heavily (twice as important) as is price competitiveness.

The next step is to identify the company’s major competitors and to rate each one (and your company) on each of the key success factors:

<table>
<thead>
<tr>
<th>If factor is a:</th>
<th>Rating is:</th>
</tr>
</thead>
<tbody>
<tr>
<td>Major weakness</td>
<td>1</td>
</tr>
<tr>
<td>Minor weakness</td>
<td>2</td>
</tr>
<tr>
<td>Minor strength</td>
<td>3</td>
</tr>
<tr>
<td>Major strength</td>
<td>4</td>
</tr>
</tbody>
</table>

Once the rating is completed, the owner simply multiplies the weight by the rating for each factor to get a weighted score, and then adds up each competitor’s weighted scores to get a total weighted score. Table 3.5 shows a sample competitive profile matrix for a small company. The results should show which company is strongest, which is weakest, and
TABLE 3.5 Sample Competitive Profile Matrix

<table>
<thead>
<tr>
<th>Key Success Factor (from Step 4)</th>
<th>My Company Weighted Score</th>
<th>Competitor 1 Weighted Score</th>
<th>Competitor 2 Weighted Score</th>
</tr>
</thead>
<tbody>
<tr>
<td>Quality</td>
<td>0.25 4 1.00</td>
<td>2 0.50 2</td>
<td>0.50</td>
</tr>
<tr>
<td>Customer Retention</td>
<td>0.20 3 0.60</td>
<td>2 0.40 3</td>
<td>0.60</td>
</tr>
<tr>
<td>Location</td>
<td>0.16 4 0.60</td>
<td>3 0.45 4</td>
<td>0.60</td>
</tr>
<tr>
<td>Perception of Value</td>
<td>0.20 4 0.80</td>
<td>2 0.40 3</td>
<td>0.60</td>
</tr>
<tr>
<td>Cost Control</td>
<td>0.20 3 0.60</td>
<td>1 0.20 4</td>
<td>0.80</td>
</tr>
<tr>
<td>Total</td>
<td>100% 3.60</td>
<td>1.95 3.10</td>
<td></td>
</tr>
</tbody>
</table>

which of the key success factors each one is best and worst at meeting. By carefully studying and interpreting the results, an entrepreneur can begin to envision the ideal strategy for building a competitive edge in her or his market segment.

Knowledge Management

Unfortunately, many small companies fail to gather competitive intelligence because their owners mistakenly assume that it is too costly or simply unnecessary. In reality, the cost of collecting information about competitors and the competitive environment typically is minimal, but it does require discipline. Thanks in large part to the Internet, “all companies, large and small, have virtually the same access to information,” says competitive intelligence consultant Leonard Fuld.34 Identifying and organizing the information a company possesses and then getting it efficiently to those who need it when they need it is the real challenge. In an age in which knowledge is the primary source of a company’s competitive edge, the key is learning how to manage the knowledge and information a company accumulates. A study by software firm Business Objects found that 90 percent of managers admit they make most of their decisions using instinct because they lack the right information when they need it!35

Knowledge management is the practice of gathering, organizing, and disseminating the collective wisdom and experience of a company’s employees for the purpose of strengthening its competitive position. “Knowledge management allows you to determine the explicit knowledge that is somewhere in your organization and that you can leverage rather than having to reinvent the wheel,” says Dorothy Leonard-Barton, author of Wellsprings of Knowledge.36 Unfortunately, a study by Accenture reports that nearly half of businesses have no formal process for capturing workers’ knowledge so that it can be passed on to others.37 As growing numbers of baby boomers retire and take their accumulated knowledge with them, these companies face the threat of a serious “brain drain” that could hurt their ability to compete. Business owners who do practice knowledge management realize that knowledge is power and that managing it can produce huge benefits. Because of their size and simplicity, small businesses have an advantage over large companies when it comes to managing employees’ collective knowledge.

The first step in creating a knowledge management program is to take an inventory of the special knowledge a company possesses that gives it a competitive advantage. This involves assessing the knowledge bank that employees at all levels of the organization have compiled over time. The second step is to organize the essential knowledge and disseminate it throughout the company to those who need it. High-tech solutions such as e-mail, computerized databases, document sharing, and special knowledge management software that allows many different employees to work on a project simultaneously are important tools, but low-tech methods such as whiteboards, Post-it notes, and face-to-face meetings can be just as effective in small companies. “To understand and respond to the kaleidoscopic patterns of new opportunities and potential dangers to its mission, an organization must mobilize the distributed intelligence of its members and listen to the collective knowledge of the whole,” says one expert.38
As eBay, provider of the popular online marketplace, expanded its operations globally, managers began to assemble the collective knowledge from employees about what works—and what doesn’t—and make it available to everyone in the company. The resulting playbooks—one for every function within the company, from product management to Web development—give managers and employees in every country how-to manuals for establishing the eBay model and expanding their divisions. They teach managers how to create the ideal conditions for electronic trading on eBay to flourish in a particular country. For instance, Gregory Boutte, country manager for France, learned from an eBay playbook that it doesn’t make sense to spend money on television ads until the number of customers using the site reaches a critical mass. As new ideas arise throughout the company, managers make a concerted effort to capture them and incorporate them into each playbook.

Kevin Plank may not have been a star when he played college football at the University of Maryland, but he has become an entrepreneurial superstar because the success of Under Armour, the company he founded during his senior year in college. As a special teams captain, Plank grew weary of wearing a heavy, sweat-soaked cotton T-shirt under his football pads. He began to research the properties of various fabrics, and he produced sample shirts made with a polyester blend base layer that fit as snugly as Spiderman’s suit and were extremely lightweight, durable, and capable of wicking away perspiration so that they stayed dry. He tested early prototypes himself, and, at first, his teammates laughed at him because the fabric resembled lingerie. Before long, however, those teammates were asking for shirts of their own!

After graduating, Plank received a trademark for the name Under Armour and launched a business from the basement of his grandmother’s townhouse in Washington, D.C., which served as the company’s first office, warehouse, distribution center—and bedroom. He started the company with $20,000 of his own money and $40,000 in credit card debt he ran up on five cards before landing a $250,000 loan guaranteed by the U.S. Small Business Administration. Plank used a network of contacts he had developed during his years of playing football to get Under Armour shirts into the hands of top college and professional football players such as Eddie George and Frank Wychek.

Sales for Plank’s company started slowly, but he managed to land accounts with the football teams at the University of Arizona and Georgia Institute of Technology. Under Armour’s first big break came in 1999, when its shirts appeared in the film Any Given Sunday. Before the film aired, Plank took out a $25,000 ad in ESPN magazine, counting on the movie to attract attention for the small company’s products. It worked. Today, thousands of athletes in a variety of sports wear Under Armour clothing, generating more than $200 million in annual sales for the company. Under Armour has since developed distinct product lines for six different sports under every playing condition and every season. Athletes from little league to the pros are dedicated to their Under Armour clothing. Although Plank’s company pays a few star athletes to wear Under Armour; most of its endorsements are unofficial. Yet the company gets tremendous amounts of publicity when Barry Bonds, Roger Clemens, Allen Iverson, LaVar Arrington, and other pros display Under Armour garments on national television.

The market for performance apparel, which Plank created almost single-handedly, is the fastest-growing segment of the athletic equipment market. Under Armour has extended its product line to include sports bras, batting gloves, loose-fitting shirts, sweat suits, boxers, and many others—for a total of 300 products. Succeeding against the odds, Plank’s bold entrepreneurial moves, aggressive advertising and public relations campaign, and superior product quality have enabled Under Armour to capture about 75 percent of the market for compression performance apparel, far surpassing the “big three” industry giants, Nike, Reebok, and Adidas. Although Under Armour may have caught the
industry giants napping, they have awakened and are fighting back. All three companies have introduced products similar to Under Armour and are promoting them aggressively. “We’re not taking this lying down,” declares Ken Barker, director of apparel at Adidas America. “It’s a war.” Nike, whose Nike Pro brand is second to Under Armour, launched an ad campaign aimed squarely at Under Armour. Its “For Warriors” campaign was one of the largest in the history of the company, whose $13 billion in annual sales dwarfs Under Armour’s annual revenues.

Small companies such as Under Armour that surprise the established players in a market with an innovative approach soon find themselves facing what some experts call the “disruptor’s dilemma.” Although Under Armour took the lead when it jolted the industry with its innovative new products, Plank’s small company has become the hunted in a high-stakes game of cat and mouse. The dilemma Plank’s company faces is, “What do we do next?” With competition intensifying, Under Armour cannot bask in the glow of its past successes. “Most people are saying [that] we’re going to trip up at some point—it’s just a matter of when,” says Plank. “Our job is to prove them wrong.”

One of Under Armour’s most recent moves was to aim its products at women, which also poses a challenge. Most of the company’s early ads (which proved to be hugely successful) were testosterone-laden spots featuring his former teammate Eric Ogbogu from the National Football League with the tag line “Protect this house,” a reference to sports teams winning on their home fields. The challenge the company faces is appealing to women without alienating its core customer base, which consists primarily of young male athletes. Ads featuring soccer star Heather Mitts wearing Under Armour garments made for women are designed to introduce the brand to women athletes, to many of whom the brand is new. Under Armour also has received exposure in some 50 movies, including the hit Million Dollar Baby, and on a dozen TV shows, including The Apprentice. After the ads and television and movie placements, Under Armour has seen sales to women climb from 13 percent of revenue to 19 percent.

Plank knows that his company is in a battle and that his competitors are much bigger and stronger. Yet he remains confident that his company’s future is bright because he has been both a fierce competitor and an entrepreneur since he was a child. Ignored as a scholarship player in college, Plank made the team as a walk-on and then went on to become a starter and a team captain thanks to his persistence and dogged determination. Once, when he was assigned to block his friend, 6-foot, 4-inch, 269-pound Eric Ogbogu, the much smaller Planck undertook the task with such enthusiasm that Ogbogu ended up on the his back with a mild concussion. Can he do the same to Nike, Reebok, and Adidas?

1. What strategic challenges does the “disruptor’s dilemma” pose for Under Armour?
2. What strategic recommendations can you make for Under Armour as the competition in the performance apparel heats up?
3. Work with a group of your classmates to develop a list of lessons you can learn from Kevin Plank and Under Armour about how small companies can compete successfully with much larger firms that have more resources.


Step 6. Create Company Goals and Objectives

Before entrepreneurs can build a comprehensive set of strategies, they must first establish business goals and objectives, which give them targets to aim for and provide a basis for evaluating their companies’ performance. Without them, it is impossible to know where a business is going or how well it is performing. The following conversation between Alice and the Cheshire Cat, taken from Lewis Carroll’s Alice in Wonderland, illustrates the importance of creating meaningful goals and objectives as part of the strategic management process:40

“Would you tell me please, which way I ought to go from here?” asked Alice.

“That depends a good deal on where you want to get to,” said the Cat.

“I don’t much care where . . . ,” said Alice.

“Then it doesn’t matter which way you go,” said the Cat.
A small business that “doesn’t much care where” it wants to go (i.e., one that has no goals and objectives) will find that “it really doesn’t matter which way” it chooses to go (i.e., its strategy is irrelevant).

Goals  Business goals are the broad, long-range attributes that a business seeks to accomplish; they tend to be general and sometimes even abstract. Goals are not intended to be specific enough for a manager to act on, but simply state the general level of accomplishment sought. Do you want to boost your market share? Does your cash balance need strengthening? Would you like to enter a new market or increase sales in a current one? Do you want to develop new products or services? Researchers Jim Collins and Jerry Porras studied a large group of businesses and determined that one of the factors that set apart successful companies from unsuccessful ones was the formulation of very ambitious, clear, and inspiring long-term goals. Collins and Porras call them BHAGs (“Big Hairy Audacious Goals,” pronounced “bee-hags”) and say that their main benefit is to inspire and focus a company on important actions that are consistent with its overall mission.

Addressing these broad issues will help you focus on the next phase—developing specific, realistic objectives.

Objectives  Business objectives are more specific targets of performance. Common objectives concern profitability, productivity, growth, efficiency, markets, financial resources, physical facilities, organizational structure, employee welfare, and social responsibility. Because some of these objectives might conflict with one another, it is important to establish priorities. Which objectives are most important? Which are least important? Arranging objectives in a hierarchy according to their priority can help an entrepreneur resolve conflicts when they arise. Well-written objectives have the following characteristics:

They are specific. Objectives should be quantifiable and precise. For example, “to achieve a healthy growth in sales” is not a meaningful objective; however, “to increase retail sales by 12 percent and wholesale sales by 10 percent in the next fiscal year” is precise and spells out exactly what management wants to accomplish.

They are measurable. Managers should be able to plot the organization’s progress toward its objectives; this requires a well-defined reference point from which to start and a scale for measuring progress.

They are assignable. Unless an entrepreneur assigns responsibility for an objective to an individual, it is unlikely that the company will ever achieve it. Creating objectives without giving someone responsibility for accomplishing it is futile.

They are realistic, yet challenging. Objectives must be within the reach of the organization or motivation will disappear. In any case, managerial expectations must remain high. In other words, the more challenging an objective is (within realistic limits), the higher the performance will be. Set objectives that will challenge your business and its employees.

They are timely. Objectives must specify not only what is to be accomplished, but also when it is to be accomplished. A time frame for achievement is important.

They are written down. This writing process does not have to be complex; in fact, the manager should make the number of objectives relatively small, from 5 to 15.

LEARNING OBJECTIVES
4. Discuss the three basic strategies—low cost, differentiation, and focus—and know when and how to employ them.

The strategic planning process works best when managers and employees are actively involved in setting goals and objectives together. Developing a plan is top management’s responsibility, but executing it falls to managers and employees; therefore, encouraging them to participate broadens the plan’s perspective and increases the motivation to make the plan work. In addition, managers and employees know a great deal about the organization and usually are willing to share their knowledge.

Step 7. Formulate Strategic Options and Select the Appropriate Strategies

By this point in the strategic management process, entrepreneurs should have a clear picture of what their businesses do best and what their competitive advantages are. They also
should understand their firms’ weaknesses and limitations as well as those of its competitors. The next step is to evaluate strategic options and then prepare a game plan designed to achieve the stated mission, goals, and objectives.

**Strategy** A strategy is a road map of the actions an entrepreneur draws up to achieve a company’s mission, goals, and objectives. In other words, the mission, goals, and objectives spell out the ends, and the strategy defines the means for reaching them. A strategy is the master plan that covers all of the major parts of the organization and ties them together into a unified whole. The plan must be action oriented; it should breathe life into the entire planning process. An entrepreneur must build a sound strategy based on the preceding steps that uses the company’s core competencies and strengths as the springboard to success. Joseph Picken and Gregory Dess, authors of *Mission Critical: The 7 Strategic Traps that Derail Even the Smartest Companies*, write, “A flawed strategy—no matter how brilliant the leadership, no matter how effective the implementation—is doomed to fail. A sound strategy, implemented without error, wins every time.”

An avid bicyclist, Grant Petersen, quit his job at the bicycle division of Japanese conglomerate Bridgestone in 1994 to start his own specialty bicycle manufacturing business, Rivendell Bicycle Works. In an industry dominated by giant companies, Petersen and his eight workers, including his bookkeeper wife, succeed by implementing a well-planned niche strategy, selling “retro-bikes” that are made of old-fashioned steel rather than the latest carbon fiber composites and use manual derailleurs rather than modern sophisticated electronic gear shifters. “Our whole business is based on selling things that are unpopular,” says Petersen. Rivendell sells just 600 bicycles a year, but they are all hand-built with exquisite attention to detail and sell for $1,700 to $4,000. To promote his business, Petersen sells subscriptions to a quarterly publication called the *Rivendell Reader* for $20 a year ($200 for 99 years) in which bicycle enthusiasts can read articles covering everything from “Bicycling 101” to “Comparing Centerpulls and Cantilevers.” Of course, a catalog featuring the company’s products accompanies every issue of the reader. Petersen says that the 6,200 subscribers purchase an average of $260 of merchandise through the catalog each year. Demand for Rivendell bicycles is so strong that customers wanting to purchase one of the high-end custom models are on a waiting list of 18 months. To fuel the company’s growth, Petersen has introduced two new lower-priced models and has expanded his base of dealers. Moderate growth is fine with Petersen, but he still wants his company to remain small. He seems to enjoy the fact that he makes the beeswax lubricant for bolt threads in his kitchen and sells it in Dixie cups.

A successful strategy is comprehensive and well integrated, focusing on establishing the key success factors that the manager identified in Step 4. For instance, if maximum shelf space is a key success factor for a small manufacturer’s product, the strategy must identify techniques for gaining more in-store shelf space (e.g., offering higher margins to distributors and brokers than competitors do, assisting retailers with in-store displays, or redesigning a wider, more attractive package).

**Three Strategic Options** Obviously, the number of strategies from which the small business owner can choose is enormous. When all the glitter is stripped away, however, three basic strategies remain. In his classic book *Competitive Strategy*, Michael Porter defines these strategies: (1) cost leadership, (2) differentiation, and (3) focus (see Figure 3.4).

**COST LEADERSHIP** A company pursuing a cost leadership strategy strives to be the lowest-cost producer relative to its competitors in the industry. Low-cost leaders have a competitive advantage in reaching buyers whose primary purchase criterion is price, and they have the power to set the industry’s price floor. This strategy works well when buyers are sensitive to price changes, when competing firms sell the same commodity products and compete on the basis of price, and when companies can benefit from economies of scale.
scale. Not only is a low-cost leader in the best position to defend itself in a price war, but it also can use its power to attack competitors with the lowest price in the industry.

There are many ways to build a low-cost strategy, but the most successful cost leaders know where they have cost advantages over their competitors, and they use these as the foundation for their strategies. They also are committed to squeezing unnecessary costs out of their operations.

Because its workforce is not unionized, JetBlue Airlines has a significant advantage over its rivals in labor costs, and it has more flexibility in job assignments for its cross-trained workers. Pilots even pitch in to help flight attendants clean cabins, which keeps flight turnaround times short. Reservation-takers work from their homes, creating significant cost savings for themselves and for the company. Because the company offers stock options to its workers, employees often are willing to work for lower salaries. The result is that JetBlue’s labor cost is just 25 percent of revenues compared to 33 to 44 percent of revenues for its competitors, and the company uses this to deploy its fleet of planes more efficiently and more profitably than its competition. JetBlue also flies just two types of planes—Airbus A320s and Embraer 190s—to keep maintenance and training costs low. Every JetBlue seat is upholstered in leather, a luxury that costs $15,000 more per plane but sends an important signal to passengers. In addition, the leather surfaces are easier to maintain and last much longer, lowering JetBlue’s costs. The net effect of this cost-leadership strategy is that JetBlue’s operating cost is the lowest in the industry—just six cents per seat-mile compared with eight to twelve cents per seat-mile for older, “legacy” carriers.

JetBlue and other low-cost carriers use their lower cost structures to put pressure on legacy carriers (many of which have declared bankruptcy), who find it increasingly difficult to raise fares in markets where they compete directly. “The low-cost airlines are now dictating pricing in our business,” says a top manager at one legacy airline. “Every time the [legacy airlines] match the fares of the discounters, they lose money.”

Of course, there are dangers in following a cost leadership strategy. Sometimes, a company focuses exclusively on lower manufacturing costs, without considering the impact of purchasing, distribution, or overhead costs. Another danger is incorrectly identifying the company’s true cost drivers. Although their approach to managing is characterized by frugality, companies that understand cost leadership are willing to invest in those activities that drive costs out of doing business, whether it is technology, preventive maintenance, or some other factor. Finally, a firm may pursue a low-cost leadership strategy so zealously that in its drive to push costs downward, it eliminates product or service features that customers consider to be essential.

Under the right conditions, a cost leadership strategy executed properly can be an incredibly powerful strategic weapon. Small discount retailers that live in the shadows of Wal-Mart and thrive even when the economy slows succeed by relentlessly pursuing low-cost strategies. Small chains such as Fred’s, Dollar General, Family Dollar, and 99 Cents Only cater to low- and middle-income customers who live in inner cities or rural areas. They offer inexpensive products such as food, health and beauty products, cleaning supplies, clothing, and seasonal merchandise, and many of the items they stock are closeout buys (purchases made as low as 10 cents on the dollar) on brand name merchandise. These companies also strive to keep their overhead costs as low as possible. For instance, 99 Cents
Only, whose name describes its merchandising strategy, is housed in a no-frills warehouse in an older section of City of Commerce, California. The success of these stores proves that companies pursuing a cost leadership strategy must emphasize cost containment in every decision, from where to locate the company headquarters to which items to stock.

**DIFFERENTIATION** A company following a differentiation strategy seeks to build customer loyalty by positioning its goods or services in a unique or different fashion. That, in turn, enables the business to command a higher price for its products or services than competitors. There are many ways to create a differentiation strategy, but the key is to be special at something that is important to the customer. In other words, a business strives to be better than its competitors at something customers value.

Urban Outfitters, a 75-store chain selling clothing for young people, has achieved success by implementing a contrarian strategy to distinguish itself from the cookie-cutter stores on which many of its national retail competitors rely. “Shopping here should be like a treasure hunt,” says the company’s general merchandising manager. Indeed, the company engages customers’ sense of adventure by displaying one-of-a-kind vintage garments next to new fashions and unique, funky home décor items such as beaded curtains and cocktail shakers. Founder Richard Hayne encourages customers to return to Urban Outfitters outlets by stocking small batches of new merchandise and employing a visual arts staff to redesign its stores every two weeks. “Rather than relying on identical stores,” says one industry analyst, “Urban creates an experience that’s intellectually stimulating.” Customers seem to enjoy the “organized clutter” layout because they shop for an average of 45 minutes per visit, twice as long as shoppers spend in a typical clothing store. In another clever move, every Urban Outfitters store places Xboxes and vintage video games in the men’s section to keep bored boyfriends from pressuring female shoppers into leaving! To ensure that it sells the latest fashions, the company sends teams of buyers and designers on globe-hopping trips, where they look for design inspirations. The teams have come back with ideas for tunics from Stockholm and art deco jewelry from a Prague art museum. Urban Outfitters’ differentiation strategy works well; its stores generate $596 in annual sales per square foot of space, 80 percent higher than its competitors.

If a small company can improve a product’s (or service’s) performance, reduce the customer’s cost and risk of purchasing it, or provide intangible benefits that customers value (such as status, prestige, a sense of safety, among others), it has the potential to be a successful differentiator. Companies that execute a differentiation strategy successfully can charge premium prices for their products and services, increase their market share, and reap the benefits of customer loyalty and retention. To be successful, a business must make its product or service truly different, at least in the eyes of its customers.

Entrepreneur Yngve Bergqvist has no trouble setting his hotel in Jukkasjärvi, Sweden, apart from others. Located 125 miles above the Arctic Circle, the aptly named Ice Hotel offers travelers a unique experience. Everything in the hotel—walls, beds, night tables, chairs, cinema, bars—is made from 30,000 tons of snow and 10,000 tons of crystal clear ice harvested from the Torne River! Each of the 60 rooms is unique, designed by a different artist from around the world. Guests sleep in insulated sleeping bags on ice beds covered with thin mattresses and plenty of reindeer blankets. Because temperatures inside the hotel typically hover at 5 degrees below zero (centigrade), guests cannot take their luggage to their ice rooms; it will freeze! Amenities include an ice bar, an ice chapel, an ice cinema, and an ice art exhibition. The Ice Hotel is the ultimate example of a differentiation strategy.
Although few businesses are innately as unique as the Ice Hotel, the goal for a company pursuing a differentiation strategy is to create that kind of uniqueness in the minds of its customers. The key to a successful differentiation strategy is to build it on a core competency, something a small company is uniquely good at doing in comparison to its competitors. Common bases for differentiation include superior customer service, special product features, complete product lines, instantaneous parts availability, absolute product reliability, supreme product quality, and extensive product knowledge.

To be successful, a differentiation strategy must create the perception of value in the customer’s eyes. No customer will purchase a good or service that fails to produce its perceived value, no matter how real that value may be. One business consultant advises, “Make sure you tell your customers and prospects what it is about your business that makes you different. Make sure that difference is on the form of a true benefit to the customer.”

Other small companies that are deploying a differentiation strategy successfully include the following:

- **Woodentoys-and-more.com** is an online store that sells upscale children’s toys. Shoshana Bailey started the company when she had difficulty finding creative, educational toys for her grandchildren at mass merchandisers such as Wal-Mart and Toys-R-Us. Some of her company’s best-selling items include a $147 hand-made wooden train set and a $420 cherry wood rocking horse made by a Tennessee craftsman. “Mass-market retailers can’t stock all of these unique toys,” explains one industry analyst. “Their job is to stock the most in-demand toys.”

- **Prairestone Pharmacy** is using technology to offer fast service and individual attention to customers getting drug prescriptions filled. At locations inside Lund Food Holdings, a chain of upscale supermarkets in the Minneapolis-St. Paul area, Prairiestone stores drugs in a high-tech vertical container that saves space, dispenses the most often prescribed drugs automatically, and allows pharmacists to have more face-to-face time with customers. A system of bar-code scanners verifies the accuracy of every order and protects customers from medication errors. Prairiestone also was the first pharmacy in the nation to offer automated multidose packaging for customers taking multiple medications. A specialized machine organizes the various drugs and then packages them in a sealed sleeve marked with the time of day the patient should take the medication. Not only does the technology provide cost savings for Prairiestone, but it also speeds up transaction times, enhances safety for customers, and gives pharmacists more time to spend working with customers rather than counting pills manually.

Small companies encounter risks when pursuing a differentiation strategy. One danger is trying to differentiate a product or service on the basis of something that does not boost its performance or lower its cost to customers. Another pitfall is trying to differentiate on the basis of something that customers do not see as important. Business owners also must consider how long they can sustain a product’s or service’s differentiation; changing customer tastes make the basis for differentiation temporary at best. Imitations and “knock-offs” from competitors also pose a threat to a successful differentiation strategy. For instance, entrepreneurs in Finland have built an ice hotel to compete with the original ice hotel in Sweden. Designers of high-priced original clothing see much cheaper knock-off products on the market shortly after their designs hit the market. Another pitfall is overdifferentiating and charging so much that the company prices its products out of the market. The final risk is focusing only on the physical
FOCUS  A focus strategy recognizes that not all markets are homogeneous. In fact, in any given market, there are many different customer segments, each having different needs, wants, and characteristics. The principal idea of this strategy is to select one or more market segments, identify customers’ special needs, wants, and interests, and approach them with a good or service designed to excel in meeting these needs, wants, and interests. Focus strategies build on differences among market segments. For instance, most markets contain a population of customers who are willing and able to pay for premium goods and services, giving small companies the opportunity to follow a focus strategy aimed at the premium segment of the market.

A successful focus strategy depends on a small company’s ability to identify the changing needs of its targeted customer group and to develop the skills required to serve them. That means an entrepreneur and everyone in the organization must have a clear understanding of how to add value to the product or service for the customer. How does the product or service meet the customer’s needs at each stage—from raw material to final sale?

Rather than attempting to serve the total market, the focusing firm specializes in serving a specific target segment or niche. A focus strategy is ideally suited to many small businesses, which often lack the resources to reach the overall market. Their goal is to serve their narrow target markets more effectively and efficiently than do competitors that pound away at the broad market. Common bases for building a focus strategy include zeroing in on a small geographic area, targeting a group of customers with similar needs or interests (e.g., left-handed people), specializing in a specific product or service (e.g., Batteries Plus, a store that sells and services every kind of battery imaginable), or selling specialized knowledge (e.g., restoring valuable works of art).

After researching the $6.2 billion-a-year breakfast cereal industry, David Roth and Rick Bacher decided to start a restaurant dedicated to the popular breakfast food. (One of the factors that prompted Roth, a former marketing consultant, to come up with the idea was a meeting with an executive who kept a stash of Cocoa Puffs hidden in his briefcase.) Initially targeting college students (“They basically live on cereal,” jokes Roth), the two friends launched Cereality in the Arizona State University food court in 2003. The pilot store was so successful that Roth and Bacher have opened stores in Philadelphia and Chicago and are planning to set up Cereality outlets in hospitals, airports, train stations, office buildings, and other college campuses. For about $4, customers can fill up their Cereality Chinensis-food-like bucket with two scoops of any of the more than 30 brands of cereal on the menu (from Fruit Loops to Corn Chex), add one of more than 40 toppings, ranging from bananas or dried cherries to chocolate malt balls, and top it off with milk (several varieties here as well). “Cerealologists” dressed in pajama tops also sell cereal bars, Cereality Bites™ snack mixes and “Slurrealities®” (smoothies made with cereal) that account for one-third of a Cereality outlet’s sales. “The idea is to become the Starbucks of cereal,” says Roth.52

The most successful focusers build a competitive edge by concentrating on specific market niches and serving them better than any other competitor can. Essentially, this strategy depends on creating value for the customer either by being the lowest-cost producer or by differentiating the product or service in a unique fashion, but doing it in a narrow target segment. To be worth targeting, a niche must be large enough to be profitable, reasonably reachable through advertising media, and capable of sustaining a business over time (i.e.,...
not a passing fad). Consider the following examples of companies that operate quite successfully in small, yet profitable, niches:

- The Flutter Fetti Fun Factory specializes in making—and dropping—confetti. The small company has dropped its patented product, Flutter Fetti (“The only party confetti that Flutters, Flies, and Floats™”), at a variety of high-profile events, including the Republican and Democratic national conventions, the Olympics, Mardi Gras, presidential inaugural balls, the Macy’s Thanksgiving Day Parade, and music concerts by Shania Twain, Britney Spears, and Paul McCartney.53

- After his father, Joe, moved into his new Beverly Hills, California, home, Jeff Smith, a wine connoisseur, organized Joe’s 5,000-bottle wine collection. When a family friend saw the result, he offered the younger Smith $500 to organize his wine cellar. “That’s when the light bulb went off,” says Smith, who then started his company, Carte du Vin, from a spare bedroom in his Hollywood Hills, California, home. A customized software package categorizes his clients’ wine collections by type, vintage, critics’ ratings, peak drinking date, and price. The database that he uses contains information on more than 10,000 wines, but Smith and his two part-time employees are constantly updating and expanding it. Once he organizes a client’s wine cellar, Smith provides a leather-bound printout and a password-protected Web site customers can access anytime. Smith also performs monthly wine cellar maintenance for many of his clients after initially organizing their collections.54

Although it can be a highly profitable strategy, pursuing a focus strategy is not without risks. Companies sometimes must struggle to capture a large enough share of a small market to be profitable. If a small company is successful in a niche, there is also the danger of larger competitors entering the market and eroding it. Entrepreneurs following this strategy often face a constant struggle to keep costs down; the small volume of business that some niches support pushes production costs upward, making a company vulnerable to lower-cost competitors as their prices spiral higher. Sometimes a company with a successful niche strategy gets distracted by its success and tries to branch out into other areas. As it drifts farther away from its core strategy, it loses its competitive edge and runs the risk of confusing or alienating its customers. Muddying its image with customers puts a company in danger of losing its identity.

**Strategy in Action** The strategies a small business pursues depend on its competitive advantages in the market segments in which it competes. In some cases, the business will implement multiple strategies across several segments. When a business has a well-defined strategic advantage, it may pursue highly aggressive growth strategies in an attempt to increase its market share. This is especially true when a business achieves a “first-mover” advantage in a market with little direct competition. By being the first in the market, it establishes name recognition and a loyal customer base. Starbucks Coffee continues to reap the benefits of being the first company to establish a chain of upscale retail coffee houses in major markets after Howard Shultz traveled to Milan, Italy, and noticed the tremendous popularity of espresso bars. A year later, in 1984, Schultz launched his coffee bar concept as a test in Seattle, Washington. Today, the chain has nearly 6,000 locations around the globe! Aggressive strategies sometimes can backfire if larger competitors decide to fight back. In many cases, the old adage of being the “big frog in a small pond” allows a small business to earn a handsome profit in a market niche without attracting the attention of larger competitors.

Small companies must develop strategies that exploit all of the competitive advantages of their size by:

- Responding quickly to customers’ needs.
- Remaining flexible and willing to change.
- Constantly searching for new, emerging market segments.
- Building and defending market niches.
- Erecting “switching costs,” the costs a customer incurs by switching to a competitor’s product or service, through personal service and loyalty.
- Remaining entrepreneurial and willing to take risks and act with lightning speed.
- Constantly innovating.
Beat Big-Box Competitors

It’s the news that sends shivers down the spines of small business owners everywhere: Wal-Mart (or any other “big-box” retailer) is coming to town. “How can my small business compete against the largest company in the world?” they wonder. “Can my business survive?”

Although no business owner welcomes a threat of this magnitude from a giant competitor with greater buying power, more name recognition, and a reputation for driving small companies out of business, it is no reason to fold up the tent and go home. Smart entrepreneurs know that, by formulating and executing the proper strategy, they not only can survive in the face of big box competitors, but they also can thrive in their presence.

Rule 1. Don’t play their game. A fundamental concept in strategy is to avoid matching your company’s weaknesses against a competitor’s strengths. For instance, because Wal-Mart buys in such huge volume from its supplier, it can extract the lowest prices from them. Small companies purchasing from those same suppliers cannot; therefore, it makes little sense for small companies to try to compete with Wal-Mart and other giant retailers on the basis of price. Unless your small company has another, more significant cost advantage, competing on the basis of price is a recipe for disaster.

Rule 2. Hit ‘em where they ain’t. Jeff Brotman, founder of Costco, a discount warehouse that goes up against Wal-Mart’s Sam’s Club discount warehouses, has been competing in competition with the industry giant for two decades. “When [Wal-Mart] comes to town,” he says, “it usually means death and destruction.” By pursuing a niche, however, Costco has managed to grow despite Wal-Mart’s power. Even though Costco has 218 fewer locations than Sam’s Club, Costco manages to generate more sales and higher profits than its rival. Brotman’s strategy is to target small business owners with more upscale products than Sam’s Club typically offers. When he first launched the company, Brotman’s research showed that small business owners were among the wealthiest people in a typical community, but, because of their business experience, they were always looking for a good bargain. “They want high-end merchandise that reflects their status, but they’d prefer it cheap,” he says. That’s just what Costco delivers. A Costco store carries only half as many items as a Sam’s Club outlet, but the selection is quite different and is designed to appeal to upscale shoppers—Godiva chocolates, Coach handbags, Waterford crystal, Dom Perignon champagne, J. A. Henckels International cutlery, and others. Like Wal-Mart, Costco has developed a highly effective supply chain system to keep stores stocked with the best-selling items. “This business is a game of inches,” says Brotman, “so we’ll get a little better every year.”

Rule 3. Hire the best . . . and train them. Costco pays its workers at rates well above the industry average, which keeps turnover rates low (in fact, the lowest in the industry) and productivity high, giving it another edge over Wal-Mart. Small companies cannot always afford to pay the highest wages in an area; however, because their companies are small, entrepreneurs have the opportunity to create a work environment in which employees can thrive. For instance, one small company attracts and retains quality workers by allowing them to use flexible work schedules that make it easier for them to manage their busy lives. The owner also invests heavily in training workers so that they can move up the organization—and the pay scale—faster. The training pays off, however, in the form of greater productivity, lower turnover, increased customer satisfaction, and higher sales per employee. Paying attention to seemingly small details such as more communication, frequent recognition for jobs well done, less bureaucracy, and flexible benefits enables small companies to build a loyal, motivated workforce that can outperform those at larger companies.

Rule 4. Bring back what the big boys have eliminated. Many companies in the supermarket industry have taken a beating as discount mass retailers have expanded their superstore concepts into more markets across the United States. Yet, many small supermarket chains have thrived by taking a completely different strategic approach, building small stores that allow shoppers to make
Step 8. Translate Strategic Plans into Action Plans

No strategic plan is complete until it is put into action; planning a company’s strategy and implementing it go hand in hand. Entrepreneurs must convert strategic plans into operating plans that guide their companies on a daily basis and become a visible, active part of the business. No small business can benefit from a strategic plan sitting on a shelf collecting dust. Unfortunately, failure to implement a strategy effectively is a common problem. In a recent survey conducted by Marakon Associates and the Economist Intelligence Unit, senior executives reported that their companies had achieved only 63 percent of the results expected in their strategic plans. The lesson is that even sound strategies, unless properly implemented, will fail.

**Implementing the Strategy** Implementing a strategy successfully requires both a process that fits a company’s culture and the right people committed to making that process...
work. Getting the right people in place starts with the selection process but includes every other aspect of the human resources function, from job design and training to motivational methods and compensation. To make their strategic plans workable, entrepreneurs should divide them into projects, carefully defining each one by the following:

- **Purpose.** What is the project designed to accomplish?
- **Scope.** Which areas of the company will be involved in the project?
- **Contribution.** How does the project relate to other projects and to the overall strategic plan?
- **Resource requirements.** What human and financial resources are needed to complete the project successfully?
- **Timing.** Which schedules and deadlines will ensure project completion?

Once entrepreneurs assign priorities to projects, they can begin to implement the strategic plan. Involving employees and delegating adequate authority to them is essential because these projects affect them most directly. If an organization’s people have been involved in the strategic management process to this point, they will have a better grasp of the steps they must take to achieve the organization’s goals as well as their own professional goals. Early involvement of the work force in the strategic management process is a luxury that larger businesses cannot achieve. Commitment to reaching the company’s objectives is a powerful force, but involvement is a prerequisite for achieving total employee commitment. The greater the level of involvement of those who will implement a company’s strategy (often those at the lower levels of an organization) in the process of creating the strategy (often the realm of those at the top of an organization), the more likely it is that the strategy will be successful. Without a team of committed, dedicated employees, a company’s strategy, no matter how precisely planned, usually fails.

### Step 9. Establish Accurate Controls

So far, the planning process has created company objectives and has developed a strategy for reaching them, but rarely, if ever, will the company’s actual performance match stated objectives. Entrepreneurs quickly realize the need to control actual results that deviate from plans.

**Controlling the Strategy** Planning without control has little operational value; therefore, a sound planning program requires a practical control process. The plans created in the strategic planning process become the standards against which actual performance is measured. It is important for everyone in the organization to understand—and to be involved in—the planning and controlling process.

Controlling plans and projects and keeping them on schedule means that an entrepreneur must identify and track key performance indicators. The source of these indicators is the operating data from the company’s normal business activity; they are the guideposts for detecting deviations from established standards. Financial, production, sales, inventory, quality, customer service and satisfaction, and other operating records are primary sources of data managers can use to control activities. For example, on a customer service project, performance indicators might include the number of customer complaints, the number of orders returned, the percentage of on-time shipments, and a measure of order accuracy.

The most commonly used indicators of a company’s performance are financial measures; however, judging a company’s performance solely on the basis of financial measures can lead to strategic myopia. To judge the effectiveness of their strategies, many companies are developing a **balanced scorecard**, a set of multidimensional measurements that are unique to a company and that incorporate both financial and operational measures to give managers a quick yet comprehensive picture of the company’s overall performance. One writer says that a balanced scorecard is a sophisticated business model that helps a company understand what’s really driving its success. It acts a bit like the control panel on a spaceship—the business equivalent of a flight speedometer, odometer, and temperature gauge all rolled into
It keeps track of many things, including financial progress and softer measurements—everything from customer satisfaction to return on investment—that need to be managed to reach the final destination: profitable growth.66

Rather than sticking solely to the traditional financial measures of a company’s performance, the balanced scorecard gives managers a comprehensive view from both a financial and an operational perspective. The premise behind such a scorecard is that relying on any single measure of company performance is dangerous. Just as a pilot in command of a jet cannot fly safely by focusing on a single instrument, an entrepreneur cannot manage a company by concentrating on a single measurement. The complexity of managing a business demands that an entrepreneur be able to see performance measures in several areas simultaneously. “Knowing whether an enterprise is viable or not doesn’t mean looking at just the bottom line,” says one manager.57 Scoreboards that combine relevant results from all aspects of the operation allow everyone in the organization to see how their job performance connects to a company’s mission, goals, and objectives.

When creating a balanced scorecard for a company, an entrepreneur should establish goals for each critical indicator of company performance and then create meaningful measures for each one.

Court Coursey, founder of Certifiedmail.com, a company that delivers certified mail electronically, has developed a scorecard that encompasses measures on everything from financial performance to employee satisfaction. Every quarter, Coursey presents Certifiedmail.com’s one-page scorecard to his 10 employees for review. “It’s a good way to get a grasp on the company and how it’s performing,” he says. The scorecard gives Coursey important feedback that allows him to adjust his management style and the company’s direction when necessary. The scorecard already has improved Certifiedmail.com’s performance. One of Coursey’s top priorities is cost control, and the scorecard recently pointed out a wasteful practice that he halted. The scorecard “showed me a way to save money,” he says. “And it was something I may not have seen without this feedback.”

Ideally, a balanced scorecard looks at a business from four important perspectives (see Figure 3.5):

- **Customer Perspective: How do customers see us?** Customers judge companies by at least four standards: time (how long it takes the company to deliver a good or service), quality (how well a company’s product or service performs in terms of reliability, durability, and accuracy), performance (the extent to which a good or service performs as expected), and service (how well a company meets or exceeds customers’ expectations of value). Because customer-related goals are external, managers must translate them into measures of what the company must do to meet customers’ expectations.

- **Internal Business Perspective: At what must we excel?** The internal factors on which managers should focus are those that have the greatest impact on customer satisfaction and retention and on company effectiveness and efficiency. Developing goals and measures for factors such as quality, cycle time, productivity, costs, and others that employees directly influence is essential.

- **Innovation and Learning Perspective: Can we continue to improve and create value?** This view of a company recognizes that the targets required for success are never static; they are constantly changing. If a company wants to continue its pattern of success, it cannot stand still; it must continuously improve. A company’s ability to innovate, learn, and improve determines its future. These goals and measures emphasize the importance of continuous improvement in customer satisfaction and internal business operations.

- **Financial Perspective: How do we look to shareholders?** The most traditional performance measures, financial standards tell how much the company’s overall strategy and its execution are contributing to its bottom line. These measures focus on such
Financial Perspective

How do we look to shareholders?

Measures
Goals

Innovation and Learning Perspective

Can we continue to improve and create value?

Measures
Goals

Customer Perspective

How do customers see us?

Measures
Goals

Internal Business Perspective

What must we excel at?

Measures
Goals

FIGURE 3.5
The Balanced Scorecard
Links Performance
Measures

factors as profitability, growth, and shareholder value. On balanced scorecards, companies often break their financial goals into three categories: survival, success, and growth.

Although the balanced scorecard is a vital tool that helps managers keep their companies on track, it is also an important tool for changing behavior in an organization and for keeping everyone focused on what really matters. Used properly, balanced scorecards allow managers to see how actions in each of the four dimensions of performance influence actions in the others. As competitive conditions and results change, managers can use the balanced scorecard to make corrections in plans, policies, strategies, and objectives to get performance back on track. A practical control system is also economical to operate. Most small businesses have no need for a sophisticated, expensive control system. The system should be so practical that it becomes a natural part of the management process.

Conclusion

The strategic planning process does not end with the nine steps outlined here; it is an ongoing procedure that entrepreneurs must repeat. With each round, managers and employees gain experience, and the steps become easier. The planning process outlined here is designed to be as simple as possible. No small business should be burdened with an elaborate, detailed formal planning process that it cannot easily use. Such processes require excessive amounts of time to operate, and they generate a sea of paperwork. Entrepreneurs need neither.

What does this strategic planning process lead to? It teaches business owners a degree of discipline that is important to business survival. It helps them to learn about their businesses, their core competencies, their competitors, and, most important, their customers. Although strategic planning cannot guarantee success, it does dramatically increase a small company’s chances of survival in a hostile business environment.
**Chapter Summary by Learning Objectives**

1. **Understand the importance of strategic management to a small business.**
   Small companies that lack clear strategies may achieve some success in the short run, but as soon as competitive conditions stiffen or an unanticipated threat arises, they usually “hit the wall” and fold. Without a basis for differentiating itself from a pack of similar competitors, the best a company can hope for is mediocrity in the marketplace. In today’s intensely competitive global environment, entrepreneurs who are not thinking and acting strategically are putting their businesses at risk. Strategic management is the mechanism for operating successfully in a chaotic competitive environment.

2. **Explain why and how a small business must create a competitive advantage in the market.**
   The goal of developing a strategic plan is to create for the small company a competitive advantage—the aggregation of factors that sets the small business apart from its competitors and gives it a unique position in the market. Every small firm must establish a plan for creating a unique image in the minds of its potential customers. A company builds a competitive edge on its core competencies, which are a unique set of capabilities that a company develops in key operational areas, such as quality, service, innovation, team building, flexibility, responsiveness, and others, that allow it to vault past competitors. They are what the company does best and are the focal point of the strategy. This step must identify target market segments and determine how to position the firm in those markets. Entrepreneurs must identify some way to differentiate their companies from competitors.

3. **Develop a strategic plan for a business using the nine steps in the strategic planning process.**
   Small businesses need a strategic planning process designed to suit their particular needs. It should be relatively short, be informal and not structured, encourage the participation of employees, and not begin with extensive objective setting. Linking the purposeful action of strategic planning to an entrepreneur’s ideas can produce results that shape the future.

   **Step 1** Develop a clear vision and translate it into a meaningful mission statement. Highly successful entrepreneurs are able to communicate their vision to those around them. The firm’s mission statement answers the first question of any venture: What business am I in? The mission statement sets the tone for the entire company.

   **Step 2** Assess the company’s strengths and weaknesses. Strengths are positive internal factors; weaknesses are negative internal factors.

   **Step 3** Scan the environment for significant opportunities and threats facing the business. Opportunities are positive external options; threats are negative external forces.

   **Step 4** Identify the key factors for success in the business. In every business, key factors that determine the success of the firms in it, and so they must be an integral part of a company’s strategy. Key success factors are relationships between a controllable variable and a critical factor influencing the firm’s ability to compete in the market.

   **Step 5** Analyze the competition. Business owners should know their competitors’ business almost as well as they know their own business. A competitive profile matrix is a helpful tool for analyzing competitors’ strengths and weaknesses.

   **Step 6** Create company goals and objectives. Goals are the broad, long-range attributes that the firm seeks to accomplish. Objectives are quantifiable and more precise; they should be specific, measurable, assignable, realistic, timely, and written down. The process works best when managers and employees are actively involved.

   **Step 7** Formulate strategic options and select the appropriate strategies. A strategy is the game plan the firm plans to use to achieve its objectives and mission. It must center on establishing for the firm the key success factors identified earlier.

   **Step 8** Translate strategic plans into action plans. No strategic plan is complete until the owner puts it into action.

   **Step 9** Establish accurate controls. Actual performance rarely, if ever, matches plans exactly. Operating data from the business assembled into a comprehensive scorecard serve as an important guidepost for determining how effective a company’s strategy is. This information is especially helpful when plotting future strategies.

The strategic planning process does not end with these nine steps; rather, it is an ongoing process that an entrepreneur will repeat.

4. **Discuss the characteristics of three basic strategies—low cost, differentiation, and focus—and know when and how to employ them.**
   Three basic strategic options are cost leadership, differentiation, and focus. A company pursuing a cost leadership strategy strives to be the lowest-cost producer relative to its competitors in the industry. A company following a differentiation strategy seeks to build customer loyalty by positioning its goods or services in a unique or different fashion. In other words, the firm strives to be better than its competitors at something that customers value. A focus strategy recognizes that not all markets are homogeneous. The principal idea of this strategy is to select one or more segments, identify customers’ special needs, wants, and interests, and approach...
them with a good or service designed to excel in meeting these needs, wants, and interests. Focus strategies build on differences among market segments.

5. Understand the importance of controls such as the balanced scorecard in the planning process.
   Just as a pilot in command of a jet cannot fly safely by focusing on a single instrument, an entrepreneur cannot manage a company by concentrating on a single measurement. The balanced scorecard is a set of measurements unique to a company that includes both financial and a balanced scorecard of financial and operational measures gives managers a quick yet comprehensive picture of the company's total performance.

Discussion Questions

1. Why is strategic planning important to a small company?
2. What is a competitive advantage? Why is it important for a small business to establish one?
3. What are the steps in the strategic management process?
4. “Our customers don’t just like our ice cream,” write Ben Cohen and Jerry Greenfield, co-founders of Ben and Jerry’s Homemade Inc. “They like what our company stands for. They like how doing business with us makes them feel.” What do they mean?
5. What are strengths, weaknesses, opportunities, and threats? Give an example of each.
6. Explain the characteristics of effective objectives. Why is setting objectives important?
7. What are business strategies?
8. Describe the three basic strategies available to small companies. Under what conditions is each most successful?
9. “It’s better to be a company with a great strategy in a crummy business than to be a company with a crummy strategy in a great business,” says one business expert. Do you agree? Explain.
10. Explain how a company can gain a competitive advantage using each of the three strategies described in this chapter: cost leadership, differentiation, and focus. Give an example of a company that is using each strategy.
11. How is the controlling process related to the planning process?
12. What is a balanced scorecard? What value does it offer entrepreneurs who are evaluating the success of their current strategies?

Business Plan Pro

We are now going to think about your business from a strategic perspective. This will involve first describing your business objectives, drafting your mission statement, identifying “keys to success,” conducting a SWOT analysis, and making initial comments about your strategy and your competitive advantage.

Business Plan Exercises

On the Web
Visit http://www.prenhall.com/scarborough and click on the Business Plan Resources tab. Scroll down and find the information with the heading Standard Industry Classification Codes. Step through the process to find the Standard Industry Classification code associated with your industry. Then, review the information associated with the Competitor Analysis section. This information may provide insight into learning more about your industry competitors on a global, national, or even on a local basis.

In the Software
Open your business plan in Business Plan Pro. You are now going to add text to the strategic areas mentioned in this chapter. Don’t worry about perfecting this information. You will want to capture your thoughts and ideas so you can come back to these topics, add detail, and make certain the sections are congruent with your entire plan. Before we do that, let’s look at some examples of each of these sections in one or more of the sample plans that you had selected earlier.

Sample Plans

Review the following sections, as they appear, of one or more of the sample plans that you identified earlier:

- Mission Statement
- Objectives
- SWOT Analysis
- Keys to Success
- Competition, Buying Patterns, and Main Competitors
- Value Proposition
- Competitive Edge
- Strategy and Implementation Summary

Note the information captured in these sections of the plans. Some areas may be quite elaborate, whereas others might be brief and contain only bullet points. As you look
Building Your Business Plan

Here are some tips you may want to consider as you tackle each of these sections:

**Mission statement.** Use your mission statement to establish your fundamental goals for the quality of your business offering. The mission statement represents the opportunity to answer the questions “What business are you in?” and “Why does your business exist?” This may include the value you offer and the role customers, employees and owners play in providing and benefiting from that value. A good mission statement can be a critical element in defining your business and communicating this definition to key stakeholders including investors, partners, employees, and customers.

**Objectives.** Objectives should be specific goals that are quantifiable and measurable. Setting measurable objectives will enable you to track your progress and measure your results.

**SWOT analysis.** What are the internal strengths and weaknesses of your business? As you look outside the organization, what are the external opportunities and threats? List these and then assess what this tells you about your business. How can you leverage your strengths to take advantage of the opportunities ahead? How can you further develop or minimize the areas of weaknesses?

**Keys to success.** Virtually every business has critical aspects that make the difference between success and failure. These may be brief bullet point comments that capture key elements that will make a difference in accomplishing your stated objectives and realizing your mission.

**Competition, buying patterns, and main competitors.** Discuss your ideal position in the market. Think about specific kinds of features and benefits your business offers and how that is unique compared to what is available to your market today. Why do people buy your services instead of other services your competitor offer? Discuss your primary competitor’s strengths and weaknesses. Consider their service offering, pricing, reputation, management, financial position, brand awareness, business development, technology, and any other factors that may be important. What market segments do they occupy? What strategy to they appear to pursue? How much of a competitive threat do the present?

**Value proposition.** A value proposition is a clear and concise statement that describes the tangible value-based result a customer receives from using your product or service. The more specific and meaningful this statement is from a customer’s perspective, the better. Once you have your value proposition, look at your organization—and your business plan—in terms of how well you communicate the service proposition and fulfill your promise to your customers or clients.

**Your competitive edge.** A competitive edge may build on your value proposition and seeks to capture the unique value—in whatever terms the customer defines that value—that your business offers. Your competitive edge may be through your product, customer service, method of distribution, pricing, or promotional methods. It describes how your business is uniquely different from all others in a way that is sustainable over time.

**Strategy and implementation.** This is a section that you will build on and, for now, make comments that capture your plans for the business. This describes the game plan and provides focus to realize your venture’s objectives and mission. Based on your initial strategic analysis, which of the three business strategies—low cost, differentiation, or focus—will you use to give your company a competitive advantage? How will this strategy capitalize on your company’s strengths and appeal to your customer’s need? You will later build on this information as you formulate action plans to bring this strategic plan to life.

Capture your ideas in each of these sections and continually ask yourself about the relevance of this information. If it does not add value to your business plan, there is no need to include this information.

### Beyond the Classroom . . .

1. Contact the owner of a small business that competes directly with an industry giant (such as Home Depot, Wal-Mart, Barnes & Noble, or others). What does the owner see as his or her competitive advantage? How does the business communicate this advantage to its customers? What competitive strategy is the owner using? How successful is it? What changes would you suggest the owner make?

2. In his book *The HP Way*, Dave Packard, co-founder of Hewlett Packard, describes the seven commitments of the HP Way:
   - Profit—the ultimate source of corporate strength.
   - Customers—constant improvement in the value of the products and services the company offers them.
CHAPTER 3 • DESIGNING A COMPETITIVE BUSINESS MODEL AND BUILDING A SOLID STRATEGIC PLAN

Field of interest—seeking new opportunities but limiting them to complementary products and services based on company core competences.

Growth—a measure of strength and a requirement for survival.

Employees—provide opportunities for advancement, share in their success, and offer job security based on performance.

Organization—foster individual motivation, initiative, and creativity by giving employees the freedom to work toward established goals and objectives.

Citizenship—contribute in a positive way toward the community and society at large.

In what ways do these values help HP to define its vision? Its competitive edge? How important is it for entrepreneurs to define a system of values to guide their companies?

3. Contact a local entrepreneur and help him or her devise a balanced scorecard for his or her company. What goals did you and the owner establish in each of the four perspectives? What measures did you use to judge progress toward those goals?

4. Use the strategic tools provided in this chapter to help a local small business owner discover his or her firm’s strengths, weaknesses, opportunities, and threats; identify the relevant key success factors; and analyze its competitors. Help the owner devise a strategy for success for his or her business.

5. Choose an entrepreneur in your community and interview him or her. Does the company have a strategic plan? A mission statement? Why or why not? What does the owner consider the company’s strengths and weaknesses to be? What opportunities and threats does the owner perceive? What image is the owner trying to create for the business? Has the effort been successful? (Do you agree?) Which of the generic competitive strategies is the company following? Who are the company’s primary competitors? How does the owner rate his or her chances for success in the future (use a low [1] to high [10] scale). When you have completed the interview, use the evaluation questionnaire (1 = low to 10 = high) to rate the company’s strategic orientation. Compare your evaluation with other classmates. What, if any, generalizations can you draw from the interview?