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## **Cost Leadership Strategy for Competitive Advantage**

### **Introduction**

Business has entered a new era of hyper-competition in which competition is violent and intense. In order to sustain competitive advantage, business firms must continually reconfigure internal resources and capabilities to assume corporate responsibility for adapting turbulent environment. Therefore, dynamic capabilities are raised and defined as a firm's strategy to constantly integrate, reconfigure, renew, and recreate internal and external resources in response to dynamic and rapidly shifting market environments in order to attain and sustain competitive advantage.

Dynamic capabilities can explain how business firms create, define, discover, and exploit entrepreneurial opportunities in complex and volatile external environments in search for a strategic matching of resources and market needs.

### **Cost Leadership Strategy and Sustainable Competitive Advantage**

Cost Leadership is a strategy used by businesses to create a low cost of

operation within their niche with the primary objective of gaining advantage over competitors; this is achieved by reducing operating costs below that of others in the same industry. Sustainable Competitive Advantage on the other hand is a long-term process that allows a business to remain ahead of its competitors. Unlike short-term advantages, such as being the first to market a new type of product, a sustainable competitive advantage may be built into the fabric of a business, and will help maintain its dominance over years and even decades. The development of such an advantage often takes dedicated effort, the ability to consistently innovate, and even some luck.

According to Porter (1998), when a firm sustains profits that exceed the average for its industry, the firm is said to possess a competitive advantage over its rivals. The goal of much of business strategy is to achieve a sustainable competitive advantage, which can be achieved through cost advantage. Cost leadership strategy is usually developed around organization-wide efficiency. Therefore, for firms implementing the cost leadership strategy to maintain a strong competitive position and sustain their profit margin for a considerable period of time; they have to place a premium on efficiency of operations in all functional areas (Porter,1998).

## **Benefits**

Firms that implement a cost leadership strategy are able to secure relatively large market share by being the lowest cost producers and service

providers in their industry or market. Thus, firms implementing the cost leadership strategy can obtain above-normal profits because of their ability to lower prices to match or even below those of competitors and still earn profits. By pursuing low costs, companies not only operate efficiently, but also become an effective price leader, undermining competitors' growth in the industry through its success at price war and undercutting the profitability of competitors.

By innovating best-practice organizational processes, with careful monitoring on purchasing expenditures, application of computer and communications technology in a cost-effective way, trimming of overhead cost, and efficient operations, a firm can achieve the cost reduction. Sometimes, cost reduction can also be achieved by outsourcing manufacturing and services when outsider providers offer lower-cost alternatives. With the same quality level but lower cost, the low-cost firm could be able to undermine the price of competing firms. The reason for applying the strategy on cost leadership is to obtain the advantage by reducing economic costs relative its competitors. This strategy highlights efficiency by producing qualified and standardized products or services. At the same time, with economies of scale and experience curve, the firm strives to gain sustainable competitive advantage among its competitors.

### **Ways to Cost Leadership**

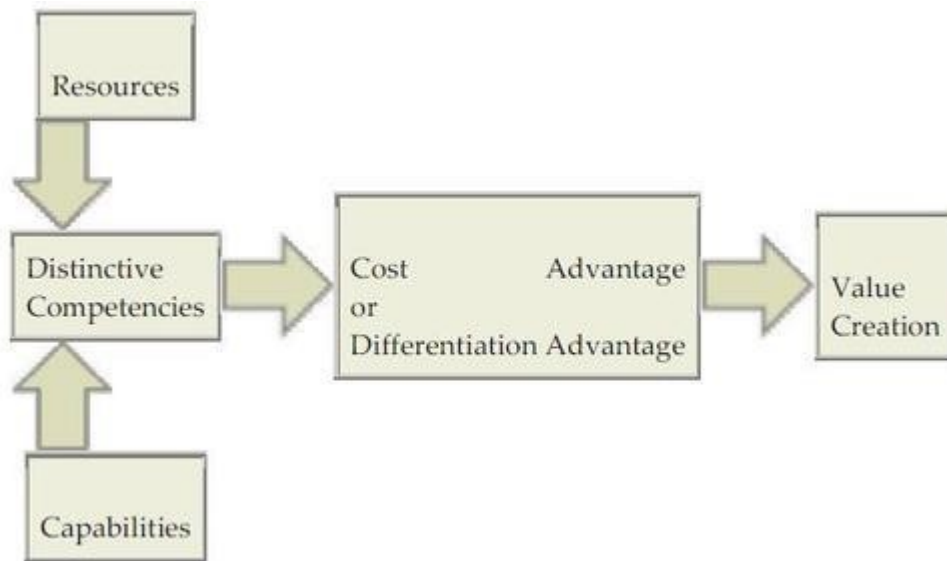
Basically, the firm has two major ways to maintain this cost advantage either by controlling the cost drivers, which cover proportion of total cost; or

by reconfiguring the value chain, in other words, with the adoption of different and more efficient ways to manufacture, promote, distribute and design the product.

A firm may produce a relative low profit margin by adopting the strategy of cost leadership. However, cost leadership strategy helps firms to produce the standard, high-volume product or service at the most competitive price to customers. Emphasizing on a cost leadership strategy is largely to create higher financial performance for firms competing in emerging economies with comparatively lower income levels, where firms can gain a relative advantage because of their lower costs in labor resource and manufacturing. Furthermore, from the customers' point of view, the strategy of cost-leadership is the most attractive in emerging economies, offering the product or service to people with low level of disposable income. If a firm can achieve and sustain overall cost leadership, then it will be an above-average performer in its industry, provided it can command prices at or near the industry average. At equivalent or lower prices than its rivals, a cost leader's low-cost position translates into higher returns.

A sustainable competitive advantage comes into being through the dynamic interplay between a firm and its external environment. Thus, sustainability can be best achieved through the use of more than one dominant strategy, because competitors may not use the same options as the incumbent organization. In the field of **'whole competitive advantage concept'**, Michael

Porter's view that such strategies can be classified into generic categories namely, **cost leadership, differentiation, focus or a combination of these** has been the most influential organizational strategies. According to Porter these generic strategies if used efficiently are capable of attaining above average industry results among the competitors.



**Figure: A model of competitive advantage**

### **Challenges of cost leadership strategy implementation**

The major challenge with cost leadership strategy is the ability of competitors to produce at a lower cost. The success of competitors in realizing this would put the cost leader at par with the competitors rendering strategy unsustainable. The ability of competitors to imitate a firm's production process and product also renders the strategy unsustainable. This strategy therefore places high demands for

organizations to invest in new technology and modern equipment in order to sustain the strategy. Another great risk of this strategy is too much focus on reduction of costs, which may lead to overlooking the changes in customer needs.

Other challenges that may hamper a firm's ability to grow new offers include financial requirements, technological advancements, regulatory issues imposed by the government. Moreover, the climatic and ecological concerns brought about by unseen weather conditions may also influence firms whose products are seasonal in nature. Social factors concerning values and attitudes of people, customers and employees can equally affect the strategy. Changes in technology also affect operations and products and can offer opportunities as well as threats..

To mitigate the above challenges, firms that pursue a similar range of competitive strategies can form a strategic group in response to particular industry conditions facing them. They may have the same selling price and quality reaches, covering the same geographical areas, having comparable product line and emphasizing on the same types of distribution channels.

## **Strategy Implementation**

A strategy implementation is made possible by people. Therefore, it is important to select a strong management team with the right personal chemistry and mix of skills as the first implementation step. A capable team is one of the cornerstones of the Organization-building task. Strategy

implementation must, therefore, determine the kind of core management team they need to execute the strategy and to find the right people to fill each slot. People's intellect, creativity, skills, experience and commitment are necessary towards effective implementation. However selecting able people for key positions remains a challenge to many organizations.