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Revisiting Porter

Chris Grannell examines the strategy of Michael Porter, highlighting common mistakes made by marketers.

Twenty years ago, Michael Porter published his first paper in the *Harvard Business Review*. Since then, his very name has become a tool – although not always a terribly strategic one. Managers speak of 'doing a Porter' (even when they don't know which model they are talking about). Workshop participants gather, trembling, around Porter-themed diagrams. Consultants bash each other around with various Porter-inspired 'forces', and marketers have become terribly excited about 'differentiating to avoid low prices'. Oh dear.

Porter is one of the most widely-cited human beings in the history of commerce. The past 20 years have probably seen more than 20 years worth of trees sacrificed to printing discussion on his work. And deservedly so. His five forces, value chain, generic strategies, activity systems and other ideas are all insightful and incredibly useful tools.

Unfortunately, one of Porter's most popular models – that of the generic strategies – is commonly misunderstood. Particularly by marketers. So here I'll aim to sort out the misunderstanding. The model is commonly represented in the popular four-box framework. (see figure 1.)

In summary, the model tells us that a company can be low cost or differentiated; and that there are broad and focused versions of each approach. We'll worry about the focused

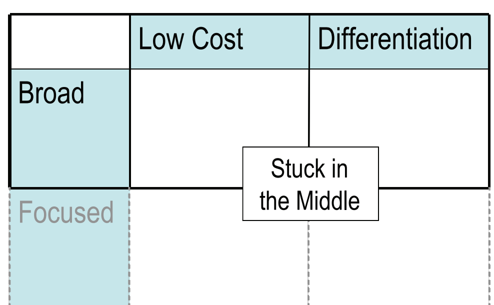


FIGURE 1

options later. I want to start with the concepts of low cost and differentiation, since they are the scene of the marketer's confusion. As concepts, they seem simple. Deceptively simple.

The marketer's mistake typically involves one or more misconceptions. All are wrong.

- misconception one: 'differentiation' means 'being different'
- misconception two: 'low cost' means 'low price' or 'charge less', and
- misconception three: the options are mutually exclusive – in other words, we do one or the other, but not both.

The first and second problems are caused by terminology, and the best way to avoid them is to remember that Porter himself is an economist, not a marketer. He clearly knows a lot about marketing, but he is, first and foremost, an economist. This is important because economists use terminology in subtly different ways to the rest of us. Take the word 'differentiation'. In marketing circles, this term refers to any way in which a product is unique. Under this definition, Tiger Airways is just as differentiated from the average airline as Aston Martin is from the average car. Not so for economists.

Economists use 'differentiation' to refer only to cases where customers can be persuaded to pay more money. We are talking here of benefits (tangible or intangible) for which punters will hand over more cash.

The term 'cost leadership' is deliberate. It does not mean 'price leadership'. It refers to costs for the company making the product. (Strictly speaking, these costs include costs for suppliers – both real and in terms of opportunities they lose by servicing you.) So a cost leadership or low cost position is one where a company has lower costs than its competitors.

It is worth thinking about this for a moment. As marketers, we are inclined to forget about anything 'back of house'. Even if this includes 95 percent of what the company is doing. But company costs – particularly if they are low ones – should be on the marketer's radar. If costs are low, this means you could drop your prices. But you don't have to. You could spend more on building the brand, or give the CEO a bonus. On the other hand, do low costs mean that the ability to innovate and respond to customers' needs has been curtailed? Are you using low costs to buy market share with low prices? Perhaps customers don't really like your product at all. If any of these scenarios hold true, you may be looking at a false economy. Consider getting your résumé prepared, quickly.

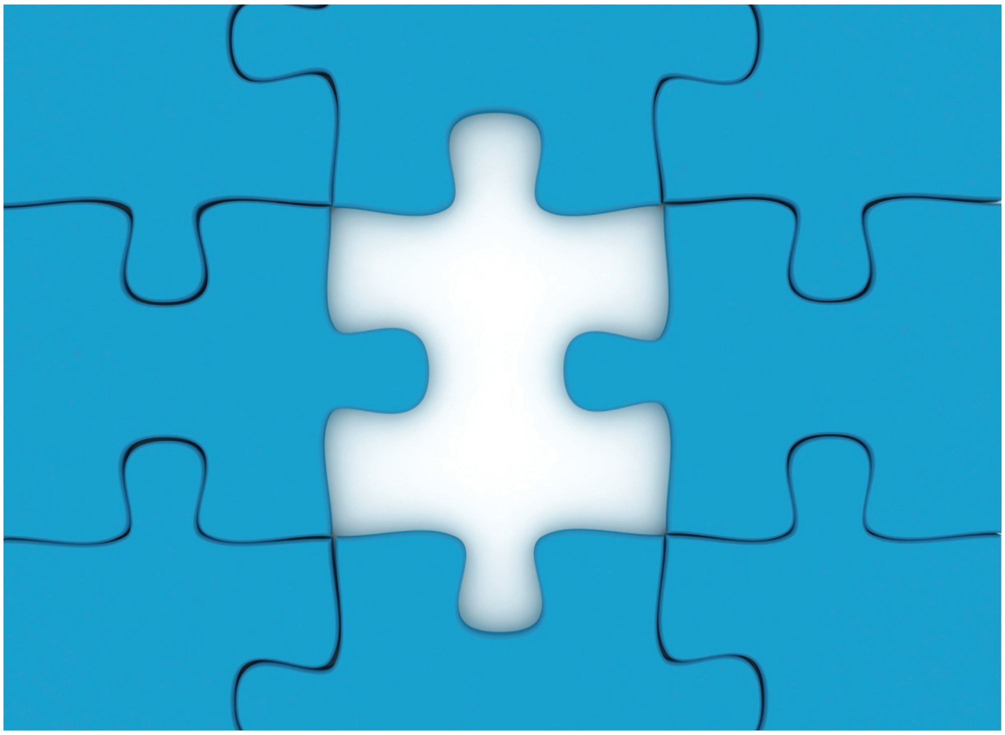
Moving on to those alluring 'focused' boxes at the bottom of our chart. If uniqueness is anywhere in the model, it probably sits here. In Porter's terminology, focused is the opposite of being mass. A marketer's segmentation/targeting/positioning approach corresponds roughly to some kind of focused strategy. In the case of a focused business, its differentiation or cost leadership has been tailored toward the needs of a particular target audience or sector of the market.

So, the four-box model starts to make a bit more sense. But with its seductive 'stuck in the middle' idea (stuck, literally, in the middle), it seems to suggest an either/or is at play. It seems to be saying woe betide anyone who isn't firmly in one camp or the other. To some extent, this is true. It is unlikely that a company can gain its competitive advantage equally from being (1) a cost leader and (2) from having customers who are willing to pay more for its products. But this dual approach isn't impossible. More importantly, many companies can have elements of both strategies at play, even if they lead with one or the other.

Franchises, for instance, frequently play in both areas. Often the biggest contribution to their competitive advantage comes from their cost leadership. Scale, aggregated buying, training and knowledge dissemination all reduce the costs faced by your local Subway. But customers – at the aggregate level – are willing to pay slightly more for a Subway than for many lesser-known brands. Something similar occurs with Jim's ever-extending mowing/dog washing/aerials businesses. (Subject to some limitations with image stretch and contamination, one imagines Jim will keep applying this logic. Jim's Colonic Irrigation, anyone?)

Firms that really are, unfortunately, 'stuck in the middle' are those that are in the centre of the diagram by mistake. Typically they really don't know where they are or where they should be. Avoid them like the plague. (See figure 2.)

Why is understanding Porter's generic strategies important? Failure to understand the model can lead marketers to make mistakes. It can also create a false sense of security. To assume you are safe because your products are selling at high prices is foolish. There are many reasons for high prices, and they may have little to do with customers' willingness to pay more.



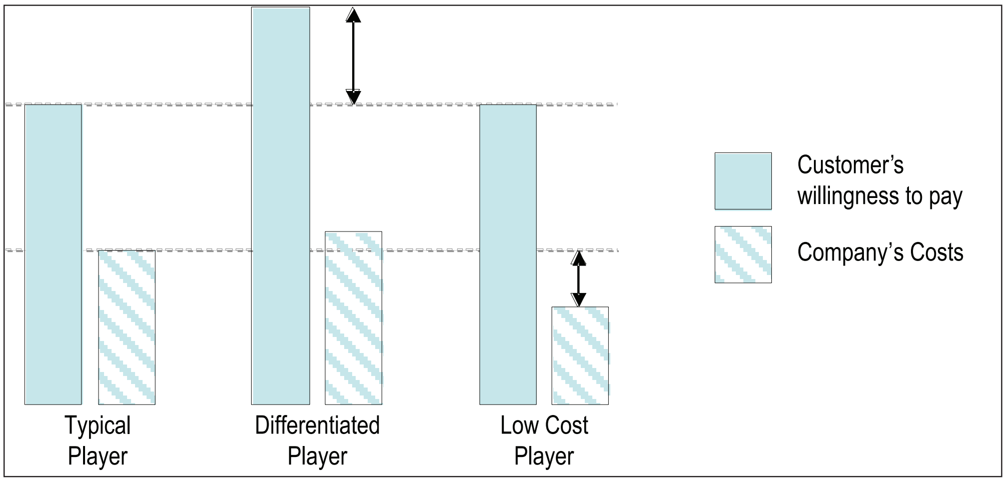


FIGURE 2

Similarly, anyone who sleeps comfortably just because their costs are low may be seriously mistaken.

Most importantly of all, differentiation and low costs are not opposites. There are examples of firms that play – to varying extents – both games. As well as sandwich shops, dog washing and burger bars, there are companies like Lexus. The ever-more-popular car company utilises the buying power and efficiencies of its parent Toyota Group to keep costs down, while doing everything it can to raise the amount that customers are prepared to pay for its products. Ever wondered how a small Japanese luxury car company could afford all that advertising and sponsorship?

Of course, many marketers believe that differentiation (I've switched back to the marketing lexicon, what an economist would call 'uniqueness') is a generic strategy and low prices are another. And to a large extent this is true. The received wisdom holds that a BMW carries a high price because it is a reasonably distinct product; a Hyundai is one cheap car among a number of others.

As a general rule of thumb, there is an implied trade-off at play between cheap and high quality. But the logic is oversimplistic and as such will only get us so far. Failure to appreciate the subtler issues beneath the surface could lead to a rather nasty surprise. **M**