Stockholm School of Economics
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Cost Leadership & Differentiation -

An investigation of the fundamental trade-off between Porter's cost leadership and differentiation strategies

Abstract

This thesis examines the fundamental trade-off between low cost and differentiation strategy at a business strategy level. In 1980 Porter introduced a model of generic strategies that has influenced much of the current thinking in strategy formulation. Although Porter did not coin the terms, he was the first to discuss the importance of choosing and focusing on one of the three alternatives: 1.Cost leadership, 2.Differentiation, and 3.Focus. Any attempt to combine or reconcile strategies would result in firms becoming "stuck in the middle", a poor strategic choice due to the existence of an inevitable trade-off. The dearth of recent research on the topic suggests that the initial debate has faded since the beginning of the 1990s, even though some discussions still take place in strategy textbooks and occasionally in the business press. IKEA, McDonalds, Southwest Airlines and Wal-Mart are examples of companies that are pointed out as having successfully reconciled both strategies. In order to investigate the question of an inevitable trade-off in general and the current state of art of the research topic in particular, a thorough literature review has been conducted. It is accompanied by a cross-check examination of contemporary practitioners' position in the matter, that is, whether current practitioners principally believe that strategies are mutually exclusive, or, reconcilable. Even though the lack of a concise definition of the concept "mixed strategy" or "combination strategy" (or "combined strategy") greatly hinders research on the topic, both theory and practice support the existence of a trade-off.

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1. Introduction

Cost leadership and differentiation strategies are popular research topics within the field of strategy and have been widely discussed, in particular since Michael Porter presented his model of generic strategies in 1980. Some rearchers, in fact, refer to this model as being among the most significant contributions to the strategic management literature. Whether cost leadership and differentiation strategies are mutually exclusive is a far less discussed issue however, as evidenced by the relatively scarce literature on the topic. During the end of the 1980s and the beginning of the 1990s there was a debate going on regarding the existence of a trade-off but it seem to have faded with the introduction of Japanese cost control methods, i.e. Total quality management (TQM) and Just in time (JIT). Grant (2005) argues: "Common to the success of Japanese companies in consumer goods industries such as cars, motorcycles, consumer electronics, and musical instruments has been the ability to reconcile low cost with high quality and technological progressiveness. The total quality managements methods that they adopted exploded the myth that there is a trade-off between high quality and low cost."[1] Thus while adherents of Porter's theory argue that cost leadership and differentiation strategies are irreconcilable, opponents advocate that a trade-off does not necessarily need to be, and refer to companies i.e. IKEA, Southwest Airlines, Toyota, IBM, Caterpillar, Wal-Mart and McDonald's as examples of firms that have successfully reconciled both strategies and thus enjoy "dual competitive advantages".

1.1. Why is this topic of interest?

Considering the impact of Porter's theories, in particular on managers, it is of interest to make a critical examination. Traditionally the belief that low cost and differentiation are mutually exclusive has been strongly embraced by practitioners. As some researchers start to question the *inevitable* trade-off, augmented attention and renewed debate on the topic is necessary. If the

[1] Grant (2005), p 244

traditionally accepted notion of an *inevitable* trade-off is inconsistent with the current state of affaires of the fundamental trade-off between low cost and differentiation in practice, and a mixed approach combining both strategies reveals to be successfully applicable on firms in general, perhaps managers need to rethink their strategic choices. Quoting Hill (1988): "By popularising the idea that differentiation and low costs are normally incompatible, Porter's work may have served to misdirect both managers and researchers."[2]

1.2. Purpose

The purpose of this thesis is to map the existing research on the fundamental trade-off between overall cost leadership and differentiation strategies by mean of a thorough literature review. In addition, practical conceptions and applications of the (in)compatibility of strategies (practice) will be examined as a complement to the literature base (theory) in order to shed some light on the relationship between theory and practice. Findings are intended to produce new insights on generic strategies and in particular on the (in)compatibility of cost leadership and differentiation strategies. Given that the author has identified no similar, previously conducted study, the paper may contribute to the research field by narrowing the knowledge gap that is reflected in the dearth of literature on the topic.

1.3. Delimitations

To begin, the thesis does not set out to present an analysis and critical examination of all research individually. This task has been conducted as pre-work but is insufficient to fulfil the purpose of a literature review.[3] Instead, the objective is to provide an analytical and critically evaluative stance to the existing literature on the topic in general, in order to establish the current state of art of the research field.

[2] Hill (1988), p 402
[3] See Hart (2001) for

What's more, it is necessary to distinguish between different strategy levels. Within the scope of this paper, the essentially broad concept of strategy is limited to business-level strategy; hereafter simply referred to as strategy. Although this limitation is determined by the purpose, it is repeated here for the reader to keep in mind.

At last, Porter's model of generic strategies per definition assumes that cost leadership, differentiation (and focus) strategies are valid independently of any particular industry or environment. Even so, thus had the author been aware of any discussion suggesting cost leadership and differentiation strategies are incompatible in some industries while reconcilable in others, it would have been excluded from this paper nevertheless. The last delimitation is mentioned as a precaution, in case such a discussion exists which the author is unaware of.

1.4. Disposition

In the next section, methodology and research quality are discussed, followed by a brief background of the topic and a theoretical framework in section 3. Section 4 is dedicated to a thorough literature review on the fundamental trade-off between overall cost leadership and differentiation strategies. It includes a table summarising the identified relevant literature. The literature review is accompanied by a "cross-check" examination of the state of art of the topic in practice, presented in section 5. Findings of the literature review (theory) and practical cross-check examination (practice) are discussed in section 6 and, ultimately, section 7 concludes.

2. Methodology

Because research findings and quality may vary depending on the adopted methodology, it is crucial to make an appropriate choice of method in order to obtain a valid research "solution.[4] The following section describes the selected methodology and motivates why it is considered appropriate to fulfil the purpose of this thesis.

2.1. Research design

The main objective of this thesis is to identify the current state of the art of the fundamental trade-off between cost leadership and differentiation in theory. Theoretical findings will be complemented by a few practical observations of the fundamental trade-off among practitioners.

In order to fulfil the stated purpose, the author has chosen to conduct a literature review. The reason is that the only way to identify the current state of the art of the topic in theory is by reviewing the existing theory, which is contained in the literature. Reviewing only parts of the literature may lead to an incomplete or erroneous picture of the current state of the art of the topic, and therefore the purpose requires all relevant literature to be reviewed. With this in mind, a literature review comes forth as a rather foreseeable and even inevitable method. Indeed, when research on a topic is at an early stage and knowledge is still relatively scarce, or the problem is still badly understood, *exploratory* methods, such as a literature review, are typically appropriate to conduct research.[5]

Next decision concerns the choice of data collection method. There are two alternatives: *quantitative* or *qualitative* data collection. A quantitative approach rests on facts and reasons. The objective is typically to explain and/or identify causal relationships and therefore

[4] Ejvegård (1996), 73
[5] Sekaran, (2000), p 123

requirements on objectivity of results and quantification of concepts and data are high. A qualitative method, on the other hand, aims at uncovering and understanding phenomenon about which little is known.[6]

Contrary to the research method decision, where the choice was rather evident, the choice of data collection method is more complicated. Both approaches could serve to collect the necessary data nevertheless a qualitative approach was adopted. The reason is that a qualitative method provides a more complete image of the state of the art of the topic, as it may offer a deeper insight into the trade-off issue. By disclosing the underlying arguments, the examples, and evidence presented by both schools of thought, the literature review reflects the up to date existing debate. This in turn allows the reader to gain a far better understanding and deeper insight into the topic. In addition it allows the reader to analyse and question the arguments that have been put forth. The disadvantage of a qualitative method, as opposed to a quantitative method, is that it does not provide a quantifiable answer as to which school of thought dominates. For example, the study could have identified the number of advocates in respective school of thought, to count the number of articles or quotes for and against an inevitable trade-off. Clearly, it may have revealed which school of though dominates in theory. Considering that there is relatively little knowledge on the topic, the author has preferred to choose a quantitative method, to expand the knowledge base in general and the understanding of the trade-off debate in particular.

2.2. Data

The literature review, which makes out the main contribution of this thesis, aims at mapping the existing literature base in order to frame the problem and determine the current state of art of the research question topic. By reflecting the debate, the topic is placed in a historical context, which may also reveal potential familiarity with state-of-the-art developments.[7]

[6] Ghauri & Grønhaug (2005), 109-110
[7] Hart (2001), p 27

Naturally, *secondary* data consisting of different types of literature has been collected for the literature review, in particular strategy textbooks, journals, reviews, and online sources. The most frequently used databases are ABI Inform Global, Business Source Premier, Google Scholar and Jstor The Scholarly Journal Archive. Three factors determined the use of these three databases. First, access is provided by the Stockholm School of Economics' library (SSE Library). Second, they were recommended by Peter Gavelin, Senior Librarian at the (SSE Library) after consultation and with consideration to the topic. And third, early in the research process these four databases came forth as the ones that most often resulted in a successful search for literature on the topic. In effect, one of the methods used to collect data consisted in searching by selected words or group of words, e.g. *Porter*, *generic strategies*, *overall cost leadership/low cost strategy and differentiation strategies*, *cost leadership and/or differentiation*, *low cost or differentiation* or *low cost and differentiatio*n, etc. Once some relevant literature had been identified by this mean, a great share of the data was collected by systematically searching through references in these texts, particularly the list of sources and references. Another method consisted in searching for and reading standard strategy textbooks, e.g. Porter (1980, 1985, 1988), Grant (2005), Barney (2002), Barney & Hesterley (2006), Ghemawat (1999), and Saloner, Shepard, & Podolny (2001). Most of the textbooks were recommended by Patrick Regnér, Advisor of this thesis and Associate Professor at the Stockholm School of Economics' institute of International Business- Department of Marketing and Strategy.

The greatest advantage of secondary data is that it is relatively easy and inexpensive to access and the verification process is relatively quick and simple. The inconvenience, in particular in the case of literature reviews, is that underlying concepts and definitions, measurement variables and units might differ and this in turn may have a negatively effect on validity of comparisons.

The literature that has been judged related and relevant by the author is classified according to two schools of thought, assuming different perspectives on generic strategies. On the one hand, Porter's school argues that cost leadership and differentiation strategies are mutually exclusive and therefore cannot be reconciled without a trade-off, and on the other hand, the opposing school of though, which argues that a trade-off does not necessarily need to be. The classification has been made according to the arguments and/or empirical observations presented in the collected literature.

The cross-check that precedes the literature review, and serves as a complement to the theoretical findings, will be based on *primary* data. As expressed by Ghauri & Grønhaug (2005): "We can hardly learn about opinions and behaviour without asking questions directly to the people involved".[8] The main advantage of *primary* data is the improved fit generated between necessary and collected data. However, such an improvement usually comes at the cost of increased collection difficulty. Research quality also becomes dependent on the availability and willingness of respondents.[9]

Four respondents will be interviewed using predetermined questions but allowing respondents to freely answer them in their own words. This type of interview is called *semi-structured* and allows a more clear and accurate picture of respondents' position to be obtained (compared to *structured interviews* where respondents' are limited to a number of proposed answers and a certain vocabulary). The participants have been selected as a *non-probability*, *convenience* sample, since it limits efforts in terms of time and resources. Such a sample could score relatively low on validity, nevertheless, it has been chosen because it is easy to draw and may still be relatively useful for gaining insights into a topic, in particular in the case of qualitative research.[10]

2.3. Research quality

The objective of research is to establish truthful and accurate findings, yet, the results of any study can only be as good as its measures and therefore it is important to evaluate the *goodness of measures*.[11] Particular attention should be paid to *validity* and *reliability*. These two factors ensure the scientific value of the research by asserting that findings are useful and appropriate. It

[8] Ghauri & Grønhaug (2005), p 103
[9] Ghauri & Grønhaug (2005), p 102-105
[10] Ghauri & Grønhaug (2005), p 146
[11] Sekaran (2000), p 209

can be mentioned that validity presumes reliability but the contrary does not necessarily hold true.[12]

Evaluating research quality of the literature review

Validity determines how truthful findings are, in other words, how well findings reflect reality. Three types of validity are distinguished: *construct validity, internal validity* and *external validity.* Considering that internal validity refers to the extent to which the research permits to conclude that a causal relationship exists between two (or more) variables, it is not of concern in this paper. The other elements of research quality shall be evaluated subsequently.

Construct validity refers to the extent to which an operalization measures the concept, which it purports to measure. It is a particularly important element of research quality because it is a condition for meaningful and interpretable findings; without construct validity there can be neither internal nor external validity.[13] When knowledge of a topic is limited, the prime requirement to ensure validity is to gain a good understanding of the issue. By providing a careful presentation of the relevant concepts and theories, section 3 aims at enhancing the understanding of the topic so that there is a good match between what the study set out to measure and what it actually measured. The lack of a clear and generally accepted definition of trade-off is most likely the main hinder in ensuring good construct validity. In fact, there may be discrepancies between the concept *trade-off* as defined in this paper and as defined by other researchers, which may have a negative effect on construct validity. Unless the definitions are identical, the examined concept will differ from the one that the paper initially sets out to study. Note that this requires that *cost leadership* and *differentiation* are identical across all research. In order to enhance validity, these three concepts are presented prior to the literature review. The author has also attempted to gain as much knowledge as possible during the pro-work and to use it at best when judging whether concepts correspond. Because the author's knowledge on the topic remains limited and due to the fact that there are systematically discrepancies between concepts, construct validity is considered to be only moderate.

[12] Ghauri & Grønhaug (2005), p. 80-89, Ejvegård (1996), 67-72
[13] Ghauri & Grønhaug (2005), p. 80-89, Sekaran (2000) p151-152

External validity refers to the transferability or generalizability of findings beyond the study, in other words, whether findings hold true also in and across actual settings and time. External validity is complex to evaluate when it comes to a literature review. Clearly, the study aims at examining the current state of the art of the topic and therefore findings are generalizable to the whole topic. On the other hand, the literature review is conducted at a certain point in time. Future research may produce findings that affect the external validity of the literature review negatively.

Reliability determines the stability of findings, that is, whether identical results are produced upon repeating measurements. In conducting the literature review, an attempt has been made to exhaustively identify the existing literature base. As presented in the methodology section, various data sources have been uses as well as various search methods. The search for literature has been thorough. In particular, upon identifying relevant literature, sources and references have been systematically scrutinized. In addition, a large number of search-words have been used and an effort has been maid to keep a list of search-words. Failure to identify some relevant literature or using each search-words in all data sources may have affected reliability negatively, nonetheless, it is considered to be relatively good. In order to enhance reliability further, a reference list is available at the end of the paper.

Evaluating research quality of the cross-check study

To a large extent, the validity of the cross-check study relates back to the literature review. The profound pre-study and background reading that makes out the literature review aspires to increase validity, nonetheless, a danger of subjective judgement in collecting data remains and reduces reliability. The questionnaire is developed based on the knowledge on the topic that has been acquired from the literature review. Moreover, efforts will be made to conduct the interviews in the same manner. The interview questionnaire is available in the appendix and aims at enhancing reliability. Due to the low number of interviewees, validity remains particularly questionable.

3. Theoretical Framework

Prior to the literature review, it is necessary to place the literature and provide a contextual introduction to the elements that will be studied.[14] The following section sets out to give a brief background to the topic by introducing the underlying concepts on the one hand and to present the theoretical framework that is the basis of the study on the other hand.

3.1. What is strategy?

Strategy is first and foremost a broad and complex concept. In an attempt to provide a definition, Porter (1996) states: "Strategy is the creation of a unique and valuable position, involving a different set of activities."[15] The essence of strategic positioning is to choose activities that yield superior profitability because they are different from rivals' and thus create a *sustainable competitive advantage*. Note that a competitive advantage is not necessarily enduring, which is why strategy must be distinguished from *operational effectiveness* (OE). Both elements can generate competitive advantage, which improves performance, but OE is relatively easy to imitate and, consequently, the competitive advantage risks eroding. In fact, Saloner, Shepard & Podolny (2001) mean that the major threat to the sustainability of a competitive advantage is that rivals can diagnose and duplicate or make obsolete the competitive advantage.[16]

3.2. The concept of "Strategic groups"

Traditional academic research made a number of contributions to the business-strategy field, starting in the1970s, and followed up by a large numbers contribution by pragmatics in the late

[14] Hart (2001), p 173
[15] Porter (1996), p 68
[16] Saloner, Shepard & Podolny (2001), p 65

1970s and the 1980s.[17] Before the development of concepts for competitive positioning, researchers considered that "two identical strategic settings never occur". This means that the research field of business business-level strategy was complicated to study.[18]

In the view of that, the introduction of the term "strategic groups", first coined by Hunt (1972) was a great step towards facilitating research. By assigning businesses that employ similar strategies (or "positioning") to a strategic group, the vast array of combinations is reduced. In other words, by identifying businesses with distinct, consistent, and recurring patterns of strategic behaviour, researchers can limit their studies to observing a number of different combinations, equal to the number of identified existing strategic groups, instead of the number of existing firms.

Strategy types have been identified in a number of several industries, e.g. Galbraith & Schendel (1983) in consumer products and industrial products, Hatten et al (1978) in brewing, Newman (1978) in chemical process, Fiegenbaum & Thomas (1990) in U.S. insurance industry). However, Miles & Snow's (1978) and Porter's (1980) *generic* strategic typology classification schemes have come forth as the most popular and widely used. Their appeal springs from the fact that *generic* strategies, by definition, are not limited to any particular industry or context. In particular Porter's (1980) model of generic strategies has outperformed all other contributions in terms of the impact on business-strategy formulation.

3.3. Porter

Porter is considered by many as the most influential strategist in the field of business-strategy. Eng (1994) for example estimates that "the arguments underlying the generic strategies advocated in Porter's, *Competitive Strategy* (1980) have influenced much of the current thinking in strategy formulation."[19] In effect, Porter's model has been widely tested (e.g. Hambrick, 1983;

[17] Ghemawat (1999), p 52. According to Ghemawat (1999), consultants in particular played a leading role among pragmatics, especially in the development of techniques for cost analysis.
[18] Hambrick & Lei (1985), p 764
[19] Eng (1994), p 43

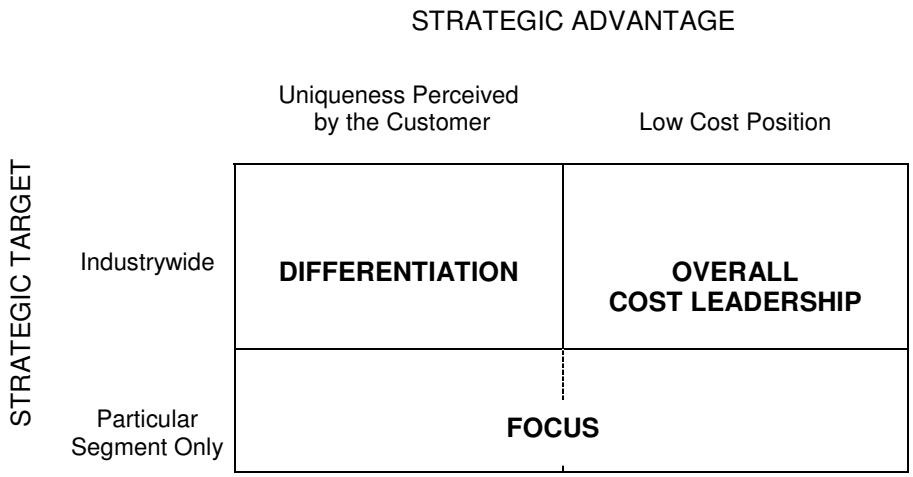
Dess & Davis, 1984; Akan et al, 2006; Reitsperger et al, 1993; Calingo, 1989) but despite criticism and efforts to modify, expand or combine the strategy typology with others' (i.e. Miles & Snow's (1987) typology), the original model has remained the most commented, analysed and tested contribution. It is has been praised for being easy to understand, appropriately broad without being vague, and building upon previous findings. The model shall be presented more thoroughly next.

Porter's (1980) model

Porter's (1980) model of generic strategies addresses practitioners with an analytical technique for gaining understanding of industries and competitors. By "practitioners" Porter implies "managers seeking to improve the performance of their businesses, advisors to managers, teachers of management, security and analysts or other observers trying to understand and forecast business success or failure, or government officials seeking to understand competition in order to formulate public policy."[20] The reason why strategic planning is a primary concern to business managers in particular but also other practitioners is that it may lead to significant benefits for a firm. In effect, an explicit process of strategy formulation can determine a firm's long-run competitive strength and generate a persistently higher rate of profit than its rivals by creating a sustainable competitive advantage. However, in order to compete successfully in the long-run a firm must first choose an appropriate positioning. Porter proposes three different approaches to gaining or strengthening competitive advantages (competitive strategies) proposed: 1.Overall cost leadership, 2.Differentiation, and 3.Focus. (Figure 1)

[20] Porter (1980), Introduction, p xxiii

Figure 1. Porter's typology of generic strategies[21]



All three strategies have the potential to result in above-average profits; however, all three strategies may not be equally suitable for a firm. The reason is that the three strategies differ on a number of dimensions and pose different requirements, for example in terms of resources, skills, organizational arrangements, control procedures, incentive systems and management style. Profitability may vary depending on the wellness of fit between the firm and the selected strategy, which make the decision of which strategy to adopt key to the benefits of strategic planning and requires that the choice be well founded. The challenge lies in selecting the strategy that best suits the firm's strengths and resources and is least replicable by competitors and this in turn necessitates knowledge about the firm, its business environment and competitors. With an explicit technique for analysing industry structure and competition, practitioner may gain better understanding and knowledge of both elements. Porter's (1980) model facilitates the decision-making process and improves the probability for a firm that chooses an appropriate strategy.

Overall cost leadership strategy

Low cost relative to competitors is the theme running through the entire *overall cost leadership* strategy and the objective is clearly overall industry cost leadership. Attaining cost leadership typically requires aggressive construction of efficient scale facilities and vigorous pursuit of cost

[21] Porter (1980), p 39

reductions through experience, tight cost and overhead control, avoidance of marginal customer accounts, and cost minimization in areas like R&D, service, sales force, advertising, etc. When attempting to achieve an overall cost leadership position, low cost relative to competitors is the theme running through the entire strategy.

To understand how overall cost leadership strategy may generate superior profitability, it is necessary to identify the *benefits of a low-cost position*. As suggested by Porter "[a low-cost position] gives a firm a defense against rivalry from competitors, because its lower costs mean that it can still earn returns after its competitors have competed away their profits through rivalry. A low-cost position defends the firm against powerful buyers because buyers can exert power only to drive down prices to the level of the next most efficient competitor. Low cost provides a defense against powerful suppliers by providing more flexibility to cope with input cost increases. The factors that lead to a low-cost position usually also provide substantial entry barriers in terms of scale economies or cost advantages. Finally, a low-cost position usually places the firm in a favourable position vis-à-vis substitutes relative to its competitors in the industry."[22] Because scale economies and cost advantages tend to defend a firm against powerful buyers and suppliers and provide substantial entry barriers, achieving a low overall cost position often requires a high relative market share. In other words, cost advantages can create value for a firm by reducing the five threats of entry, rivalry, substitutes, suppliers and buyers.

More specifically, Barney & Hesterley (2006) mean that there are six main cost advantages, or, *sources of cost advantages* for firms that successfully adopt cost leadership: 1.Size differences and economies of scale, 2.Size differences and diseconomies of scale, 3.Experience differences and learning-curve economies, 4.Differential low-cost access to productive inputs, 5.Technological advantages independent of scale, and 6. Policy choices.[23] Further, the authors explain that the ability of a valuable cost leadership strategy to create a *sustainable competitive advantage* is conditional upon the strategy being rare and costly to imitate. The above-mentioned sources of cost advantage are classified into two categories according to likelihood of rarity. Leaving-curve economies of scale (especially in emerging businesses), differential low-cost access to productive inputs and technological software are generally considered "likely-to-be-

[22] Porter (1988), p 35-36
[23] Barney & Hesterley (2006), p 117

rare sources of cost advantage", while economies of scale (except when efficient plant size approximately equals total industry demand), diseconomies of scale, technological hardware (unless a firm has proprietary hardware development skills) and policy choices are generally considered "less-likely-to-be-rare sources of cost advantage". Similarly, the sources of cost advantage are more or less replicable. Creating a sustainable competitive advantage also require that competitors cannot easily imitate the strategy. Sources of cost advantages that tend to be difficult thus costly to duplicate include: differential access to cost productive inputs and technology software. Learning economies and technological hardware may be costly to duplicate if they are proprietary.[24]

Organising to implement a cost leadership strategy requires particular consideration to the organizational structure, management controls, compensation policies, and implementing cost leadership strategies. The organizational arrangements and implementation tools should not only fit but reinforce the strategy. Porter (1980) has divided requirements of overall cost leadership strategy into "commonly required skills and resources" and "Common organizational requirements". Commonly required skills and resources when implementing overall cost leadership are sustained capital investment and access to capital, process engineering skills, intense supervision of labor, products designed for ease in manufacture, and low-cost distribution systems. Common organizational requirements constitute of tight cost control, frequent, detailed control reports, structured organization and responsibilities, and incentives based on meeting strict quantitative targets.[25] According to Barney & Hesterley (2006), few layers in the reporting structure, simple reporting relationships, small corporate staff, and focus on narrow range of business functions are elements of organizational structure that allow firms to "realize the full potential of cost leadership strategies". Management control systems that support the implementation of cost leadership include tight cost control systems, quantitative cost goals, close supervision of labor, raw materials, inventory, and other costs, and a cost leadership philosophy. Examples of good compensation policies are rewards for cost reduction and incentives for all employees to be involved in cost reductions. [26]

[24] Barney & Hesterley (2006), p 129-135
[25] Porter (1988), p 40
[26] Barney & Hesterley (2006), p 136

Differentiation strategy

Differentiation consists in differentiating the product or service offered by the firm, in other words, creating something that is perceived industry-wide as being unique. Differentiation may be achieved in various ways, for example through design, brand image, technology, features, customer service, and dealer network. Bases of differentiation may be sorted into three categories. Firstly, to implement differentiation, a firm may focus directly on product (or service) attributes, i.e. product features, product complexity, timing of product introduction, or location. Secondly, a firm may focus on the relationship between itself and its customers, for example through product customisation, consumer marketing and product reputation. Finally, differentiation may be implemented by focusing on the linkage within or between firms, which includes linkage within functions of a firm, linkage with other firms, product mix, distribution channels and service support. Ideally, the firm should differentiate itself along several dimensions. [27] There may also be other ways for firms to differentiate than the examples mentioned above. In fact, Barney & Hesterley (2006) argues that, "product differentiation is ultimately an expression of the creativity of individuals and groups within the firms. It is limited only by the opportunities that exist, or that can be created, in a particular industry and by the willingness and ability of firms to creatively explore ways to take advantage of those opportunities.[28]

Benefits of differentiation. According to Porter differentiation may generate superior profitability for the reason that "[it] provides insulation against competitive rivalry because of brand loyalty by customers and resulting lower sensitivity to price. It also increases margins, which avoids the need for a low-cost position. The resulting customer loyalty and the need for a competitor to overcome uniqueness provide entry barriers. Differentiation yields higher margins with which to deal with supplier power, and it clearly mitigates buyer power, since buyers lack comparable alternatives and are thereby less price sensitive. Finally, the firm that has differentiated itself to achieve customer loyalty should be better positioned vis-à-vis substitutes than its competitors."[29] Besides reducing the five threats of entry, rivalry, substitutes, suppliers and buyers,

[27] Porter (1980), p 37
[28] Barney & Hesterley (2006), p 153
[29] Porter (1988), p 38

differentiation creates value by enabling a firm to charge a premium price that is greater than the extra cost incurred by differentiation.

As for overall cost leadership, successful differentiation requires that the strategy be rare and costly to imitate. And rare and costly bases for differentiation are sources of sustainable competitive advantage. As mentioned earlier, Barney & Hesterley (2006) mean "the rarity of a differentiation strategy depends on the ability of individual firms to be creative in finding new ways to differentiate their products." In short, creative firms will always manage to differentiate themselves from competitors. As rivals try to imitate these firms' last differentiation move, creative firm will already be working on new moves and therefore they always remain one step ahead of competition. In general, bases for differentiation that are costly to duplicate include links between functions, timing, location, reputation, distribution channels, and service and support. Product mix, links with other firms, product customisation, product complexity and consumer marketing may be costly to imitate depending on the circumstances.[30]

Organising to implement a differentiation strategy requires particular consideration to the organizational structure, management controls, compensation policies, and implementing cost leadership strategies. As mentioned previously, organizational arrangements and implementation tools should not only fit but also reinforce the strategy. Porter (1980) suggests that strong marketing abilities, product engineering, creative flair, strong capability in basic research, corporate reputation for quality or technological leadership, long traditional in the industry or unique combination of skills drawn from other businesses, and strong cooperation from channels are commonly required skills and resources for implementing differentiation. Common organizational requirements include strong coordination among functions in R&D, product development, and marketing, subjective measurement and incentives (instead of quantitative measures), and amenities to attract highly skilled labor, scientists, or creative people.[31] In addition, Barney & Hesterley (2006) suggest that an organizational structure supporting differentiation includes may be characterised by cross-divisional and cross-functional development teams, complex matrix structures and isolated pockets of intense creative efforts ("skunk works"). Broad management decision-making guidelines, managerial freedom within

[30] Barney & Hesterley (2006), p 158-163
[31] Porter (1988), p 41

guidelines, and policy of experimentation may be typical of a management control systems that support differentiation. Rewarding risk-taking (as opposed to punish failures), creativity, and multidimensional performance measures is an example of compensation policy that reinforces differentiation.[32]

Contrary to overall cost leadership, differentiation may imply a hinder to high market share. The reason is that differentiation typically requires a perception of exclusivity that is incompatible with high market share.[33]

Focus strategy

Considering that this paper focuses on the trade-off between overall cost leadership and differentiation, it does not serve the purpose of the thesis to describe the focus strategy in detail. In brief, the *focus* strategy aims at serving a particular target or segment of the industry well, as opposed to both overall cost leadership and differentiation strategies seek to achieve their objectives industry-wide. For example, a firm may choose to serve a particular buyer group, segment of the product line or geographic market. Thus a focus strategy sets out to achieve a low cost or differentiation position, or both, from the perspective of its narrow market segment. [34]

Trade-off

Porter means that three conditions explain firm success. First, a company must develop an internally set of consistent set of goals and functional policies that collectively define its position in the market. More specifically, strategy is seen as a way of integrating the activities of the diverse functional departments within a firm, including marketing, production, research and, procurement, finance and the like. An explicit and mutually reinforcing set of goals and functional policies is needed to counter the centrifugal forces that lead functional departments in

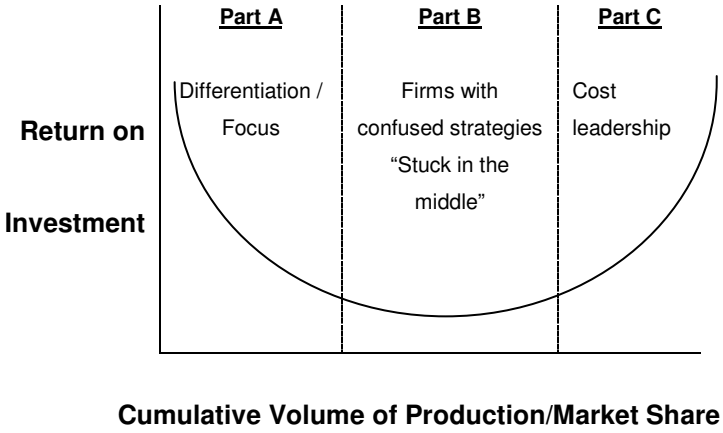
[32] Barney & Hesterley (2006), p 164
[33] Porter (1988), p 38
[34] See Porter (1980), p 38-39

different directions. The second condition for success is that this internally consistent set of goals and policies aligns the firm's strengths and weaknesses with the (external) industry opportunities and threats. Strategy is the act of aligning a company and its environment. And third, condition for success is that a firm's strategy be centrally concerned with the creation and explosion of its so-called 'distinctive competences'. Although there is not one way to position, (on the contrary, there may be several attractive positions), choice is essential. The challenge that a firm faces lies in choosing a distinct position from it rivals in order to avoid replication- a threat competitive advantage- whilst taking into account logical inconsistencies in pursuing several types of advantage or different scopes simultaneously.[35] The generic strategies proposed by Porter (1980) fulfil these conditions.

Although Porter did not coin the terms cost leadership and differentiation, he was the first to discuss the importance of choosing and focusing on one of the alternative.[36] Firms that fail to develop its strategy in at least one of the three directions are so called "stuck in the middle", a poor strategic situation, that almost guarantees low profitability: "[The firm stuck in the middle] either loses the high-volume customers who demand low prices or must bid away its profits to get this business away from low-cost firms. Yet it also loses high-margin businesses-the cream-to the firms who are focused on high-margin targets or have achieved differentiation overall."[37] This idea is illustrated by a U-shaped relationship between market share and profitability (Figure 2). Market-leading firms within overall cost leadership are the largest, while differentiation or focus strategy are the smallest, and stuck in the middle least profitable firms are medium sized. In effect, Porter argues that only under extreme circumstances can strategies be successfully reconciled; effectively implementing any of these generic strategies requires total commitment and supporting organizational arrangements that are diluted if there is more than one primary target and therefore it becomes vital for a firm to choose and adopt one of the three proposed generic strategies.[38]

[35] Porter (1991), p 96-98
[36] http://en.wikipedia.org/wiki/Business_strategy#Birth_of_strategic_management, 3 juni 2006, 17:49
[37] Porter (1980), p 41
[38] Porter (1980), p 35

Figure 2. Generic strategies and Porter's U-shaped relationship between market share and ROI



In the second edition of "*Competitive Strategy*" Porter explains: "Sometimes companies such as Microsoft get so far ahead that they seem to avoid the need for strategic choices, but this becomes their ultimate vulnerability."[39] Becoming "stuck in the middle" is no less a recipe for disaster.

Porter means that there are three reasons why trade-off is inevitable. The first reason is that there are inconsistencies in image or reputation between strategies. For example differentiation often requires a perception of exclusivity that is incompatible with high volumes and market share. Second, a trade-off may arise from the activities themselves because different positions require different product configurations, equipment, employee behavior, skills, resources, or management system. Different positions can also reflect inflexibilities, e.g. in machinery, people, or systems. Thirdly, there are limits on internal coordination and control, which implies that strategies are mutually exclusive. In general, if the activities required in achieving a successful differentiation position are inherently costly, i.e. extensive research, product design, high quality materials or intensive customer support, achieving a successful differentiation position will imply a trade-off with an overall cost leadership position.[40]

[39] Porter (1988), Introduction, p xiv
[40] Porter (1996), p 68-69

4. Literature Review

Despite their appeal, the generic strategies provoked a vigorous debate among strategist. Having introduced the topic in general and Porter's model in particular, a review of the existing literature on the fundamental trade-off between cost leadership and differentiation is undertaken in order to reflect this debate and thus the current state of the art of the topic. Three main differences have been identified between the two schools of thought and shall be synthesized according to the following disposition: 1.Conceptualisation of competitive strategies, 2.Competitive strategy and market share, 3.Mixed strategy and performance, 4.Summarizing table.

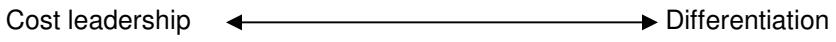
4.1. Conceptualization of competitive strategies

When examining the literature on the topic, there seem to be differences in the conceptualization of cost leadership and differentiation strategies between "Porter's school of thought", i.e. Porter and adherents of his theory and the "opposing school". This rises the question of whether differences in conceptualisation of strategies cause opinions on the (in)evitability of trade-off to differ. The differing conceptualizations will be describes next in order to gain a better understand of the causal relationship with trade-off.

Single continuum & broad strategic groups

Porter's conceptualisation of the two strategies implies that cost leadership and differentiation are viewed as opposite ends of a single continuum. For an illustration, see Figure 3.

Figure 3. Cost leadership and differentiation as opposite ends of a single continuum



If all firms were placed on the continuum, effective firms, that is, firms with an above-average profit, would be found at one of the ends of the continuum. Any location on the continuum, which is not one of the ends illustrates an unclear strategy, or "stuck in the middle". In other words, a trade-off is inevitable because a firm cannot move away from an end without its strategy become increasingly unclear, or "confused", which eventually will cause it to loose profits.

Porter's conceptualisation, however, lacks support even among adherents of Porter's school of thought. For example, Hambrick (1983) suggests: "It may be true, as Porter argues that efficiency and differentiation are generally incompatible, but they are not opposite ends of a single continuum."[41] With the exception of Akan et al (2006), the author has not identified any researchers that support Porter's conception. And not even Akan et al (2006) explicitely support the conception, the authors actually bring it up without rejecting it.[42]

Instead, the dominant conception within Porter's school of though is the one presented by Dess & Davis (1984). The authors suggest that competitive strategies represent broad types of strategic groups (or "designs"). That is, cost leadership makes out one group, gathering strategies that are similar and all have certain elements in common (elements that are generally associated with cost leadership). Differentiation makes out a second group and gathers strategies that are similar and all contain elements generally associated with differentiation, without necessarily being identical. Supporters of this conceptualisation (i.e. Dess & Davis, 1984; Roth, 1992; Green et al 1993) mean that choosing a strategy resembles choosing a strategic group membership: each group has its "essence" which are not reconcilable and thus a firm can become member in one strategic group only. Attempts to combine cost leadership and differentiation will fail because

[41] Hambrick (1983), p 689
[42] Akan, Allen, Helms & Spralls (2006), p 52

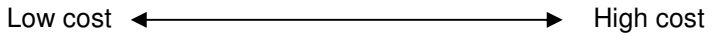
the two group's essences are incompatible. In other words, a trade-off is inevitable because strategies are mutually exclusive.

Cost and differentiation: Two dimensions of strategy

In a study of the Korean manufacturing market Kim & Lim (1988) found that differentiators also employed variables normally associated with cost leadership strategy, and cost leadership strategies also demonstrated traits generally linked to differentiators.[43] The researchers suggest that there are no "pure" strategies; both low cost and differentiation must be taken into account. This "two-dimensional" conceptualisation is the most commonly supported (Hall, 1980; Miller & Dess, 1993; Reddy, 1980; Kim & Lim, 1988; Miller & Friesen, 1986a; Jones & Butler, 1988; Reitsperger et al, 1993).

According to Jones & Butler (1988): "[…] the real underlying dimension is cost (low to high), not low cost vs. differentiation." Low cost and high cost, rather than low cost and differentiation are considered to be at opposite ends of the continuum. If a firm chooses to compete with a cost leadership strategy it approaches the low cost end of the continuum and if it chooses to pursue a differentiation strategy it approaches the high cost end of the continuum.[44] (Figure 4)

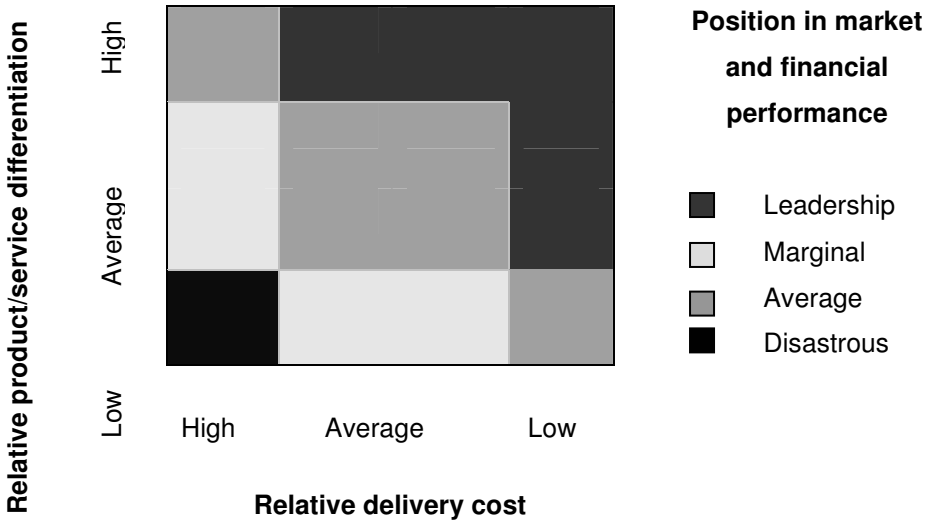
Figure 4. Jones & Butler's (1988) illustration of Porter's continuum[45]



There are various illustrations of the two-dimensional conceptualisation, the following, figure 5, is proposed by Hall (1980):

[43] Kim & Lim (1988), p 821
[44] Jones & Butler (1988), p 203
[45] Jones & Butler (1988), p 203

Figure 5. Hall's (1980) strategic profile analysis[46]



Reitsperger et al (1993) propose an interaction model. Note that the axis running from cost leadership strategy (4) to product differentiator (1) represents Porter's single continuum. Remaining corner strategies illustrate balanced strategies. (Figure 6). White (1986) presents a 2x2 matrix. (Figure 7).

Figure 6. Reitsperger et al's (1993) Integrative Model of manufacturing strategies[47]

Product Quality Focus	Product Differentiator	Strategic Integration
	Strategic Uncertainty	Cost Leader
		Cost control Focus

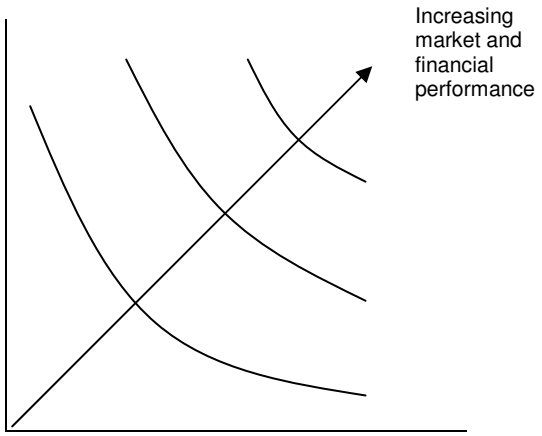
Figure 7. White's (1986) 2x2 matrix of generic Business strategies[48]

		Differentiation Position	
		Low	High
Cost Position	Low	Pure cost	Cost and differentiation
	High	No comparative advantage	Pure differentiation

[46] Hall (1980) p 80
[47] Reitsperger et al (1993), p 11
[48] White (1986), p 226

Karnani (1984) on the other hand uses iso-curves, explaining that: "Low cost position and high differentiation are two ways of gaining competitive advantage. The substitutability between the two is governed by a multiplicative relationship implying an interaction effect between the two dimensions. Therefore, a firm cannot afford to emphasis one dimensions at the cost of neglecting the other."[49] (Figure 8)

Figure 8. Karnani (1984) Iso-performance curves[50]



Summarizing "Conceptualization of competitive strategies"

In short, literature on the topic indicates that there are differences in the conception of cost leadership and differentiation strategies. Three main conceptions have been identified. Porter's proposition that the two strategies can be viewed as two different ends of a single continuum has little support. Dess & Davis (1984), Roth (1992) and Green et al (1993) argue that the two strategies make out two broad strategy groups, which are irreconcilable because they are essentially different. The "two-dimensional" conceptualisation dominates, suggesting that there is no pure strategy. Instead cost leadership and differentiation are two dimensions of strategy, which must both be taken into account. A firm's strategy contains more or fewer elements typically associated with either of the two strategies, yet always some elements of both. As expressed by Miller & Dess (1992): "The conceptualisation of Porter's model as three

[49] Karnani (1984), figure, p 378
[50] Karnani (1984), p 378

dimensions of strategic positioning rather than three types of strategies is what allows researchers to "explore the presence and viability of "combination" strategies [...]".[51] This thesis focuses on two (not three) strategies, nevertheless, Miller & Dess' (1992) argument holds true, meaning that there is a link between the conceptualization of strategies and the adherence to either of the two schools of though concerning the trade-off.

4.2. Competitive strategy and market share

The second element that distinguishes the two school of thought concerns the relationship between competitive strategy and market share. Similarly to the previous section, this rises the question of whether the nature of the relationship (positive or negative) between competitive strategy and market share determines the adherence to a school of thought (inevitable or possibly evitable trade-off). Next, the relationship between market share and differentiation shall be investigated, followed by an account on the relationship with trade-off.

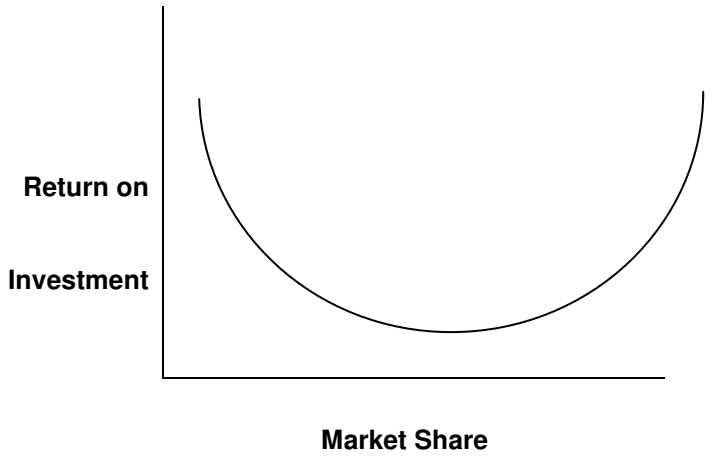
Differentiation hinders market share

Although differentiation comprises a large number of elements, e.g. guarantee of quality, uniquely tailored products, embodiment of identity and lifestyle, superior quality is probably the one element that is most frequently associated with differentiation. Following, superior quality is commonly used as a determinant of differentiation in tests and studies. Consistent with the traditional manufacturing notion "quality costs" or "quality is expensive", improving product quality is assumed to raise the cost of manufacturing. High-quality inputs, increased marketing expenditure, better after-sales services and better-trained employees are some of the direct costs associated with increased differentiation. Porter and adherents of his school of thought means that increased costs tend to reduce demand and consequently differentiation limits market share. In effect, the negative relationship between market share and differentiation does not affect profitability since increased costs justify premium prices (i.e. the profit margin is unchanged);

[51] Miller & Dess (1992), p 564

nevertheless, differentiation limits the potential for economies of scale and thus large market shares (Porter, 1980; Hambrick, 1983). As mentioned earlier, Porter describes the relationship between market share and return on investment (ROI) as "U-shaped". (Figure 9)

Figure 9. Porter's U-shaped relationship between market share and return on investment[52]



Differentiation and market share need not be negatively related

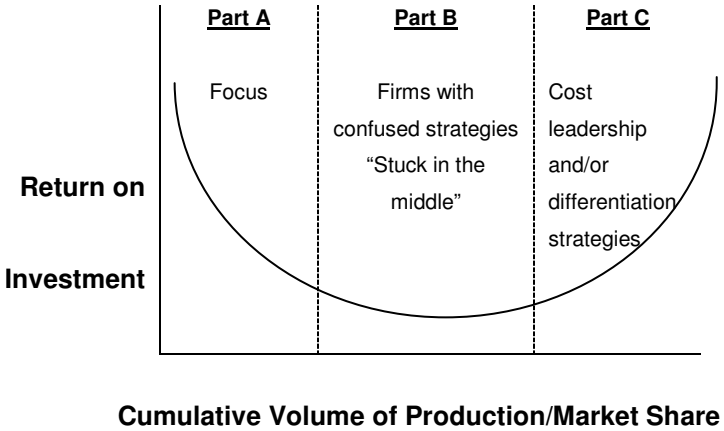
Opponents argue that differentiation and market share need not be negatively related (Reddy, 1980; Phillips et al, 1983; Karnani, 1984; Wright, 1987; Hill, 1988; Wright et al, 1991). The effect of an increase in differentiation on market share is dependent on two opposing forces. On the one hand, an increase in differentiation most likely leads to a high cost position independent of scale, which result in a high average cost position ("cost increasing effect"). On the other hand, improved differentiation generates competitive advantage, which leads to increased market share, and following, to a low average cost position.[53] Which one of the two forces dominates, and consequently, determines the total effect of improved differentiation on market share depends on the situation ("cost reducing effect").

Buzzell & Wiersema (1981a, 1981b) suggest that differentiation should be translated into product improvement in order for the cost reducing effect to dominate. The reason is that an

[52] see Porter (1988), p 43 for the original figure
[53] Karnani (1984), p 375

increase in product quality is believed to have beneficial effects on the relative product demand: When increased demand is addressed by mean of a raise in volumes, there may be indirect beneficial effects on relative direct cost position via a positive influence on market position. In other words, market share growth implies that economies may be achieved (e.g. economies of production, marketing, buying, distribution, finance.), which in turn results in reduce average costs. Among researchers of the opposing school of thought, this rasoning os strongly supported (Hill, 1988; Miller & Friesen, 1984; Jones & Butler, 1988; Wright et al, 1991[54]; Wright et al, 1990). Wright (1987) proposes a refinement of Porter's U-shaped relationship between market share and performance as an illustration.[55] (Figure 10)

Figure 10. Wright's (1987) refinement of Porter's U-shaped relationship between market share and ROI[56]



Differentiation as a mean to achieve a low cost position

Within the opposing school of thought, there are various suggestions as to why the traditional notion of "differentiation is costly" does not hold and differentiation is a mean to reduce costs. Fine (1986) examines the effects of quality-based learning and captures the idea that "production of high quality products can speed the rate of learning in the production system". The greater

[54] Wright, Kroll, Tu & Helms (1991)
[55] Wright (1987), Figure 3., p 100
[56] Wright (1987), p 98

increase in differentiation, the larger is its potential to reduce per unit costs as a result of learning effects.[57] This relationship is also supported by Murray (1988).

"Residual efficiency" also illustrates how differentiation can be a mean to reduce costs. At the essence of Japanese TQM and JIT methods, introduced at the beginning of the 1980s, lies the conviction that "quality is free"; quality and cost can be mutually supportive since better quality improves residual efficiency. Grant (2000) for example means that these methods "exploded the myth that there is a trade-off between high quality and low cost."[58] Others who support this argument are Wheelwright (1981), Fine (1986), Calori & Ardisson (1988), Murray (1988), Reitsperger & Daniel (1990), Wright et al (1990), Reitsperger et al (1993), and Ghemawat (1999). Although researchers mean that Japanese manufacturing companies in general evidence that trade-off need not emerge, Toyota and Canon are two specific examples mentioned in the literature.

Other researchers propose that product and system innovations have the potential to lower costs and increase differentiation through quality improvement efforts, process innovations, product innovations, and system innovations (e.g. Wright et al, 1991; Helms et al, 1997; Grant, 2005; Wright et al, 1990). Empirical evidence in support of this argument is provided by Oskarsson & Sjöberg (1994): A case study of Motorola and the mobile telephone industry revealed three technologies that are both cost and performance driving. Thereby Oskarsson & Sjöberg (1994) concluded that differentiation and cost leadership are not necessarily conflicting strategies.[59]

Moreover, due to price elasticity of demand, "differentiation need not translate into higher market share and scale economies […] in order to be beneficial for the firm."[60] As differentiation increases, customers tend to become less price-sensitive, which allows firms to increase prices

[57] Fine (1986), p 1302. The experience curve represents the relationship between cost and accumulated experience. Developed in 1968 by the Boston Consulting Group. According to Boston Consulting Group (1976), the unit cost of value added to a standard product declines by a constant percentage (20-30%) each time cumulative output doubles. If a firm expands its output more than its competitors it can move down the experience curve more rapidly than its rivals, opening up a cost differential. Consequently, market share should be its strategic goal.
[58] Grant (2005), p 244
[59] See Oskarsson & Sjöberg (1994), p 10-11 for a description of the three technologies.
[60] Wright, Nazemzadeh, Parnell & Lado (1991), p 15

without loosing sales. Provided that differentiation does not induce costs which are superior to the price increase, profit margins increase. (Wright et al, 1991[61]).

Finally, Karnani (1984) argues that differentiation does not need to be compromised by lower costs, provided that a firm can establish access to low labour costs, for instance by delocalising business units to low wage countries.[62] According to Wright et al (1991), the argument can be expanded to include other low cost inputs, e.g. low cost raw materials, energy, freight and semi-finished products. Gaining access to preferential distribution channels may also be a mean to pursue differentiation without necessarily increasing costs.

Besides Japanese manufacturing companies in general and already-mentioned Motorala, the firms that have been pointed out as evidence that strategies can be successfully reconciled (i.e. without trade-off emerging) includes Caterpillar, IKEA, Southwest Airlines, Dell, Philip Morris, Daimler Benz and Motorola.

Summarising "Competitive strategy and market share"

While Porter's school of thought supports a negative relation between market share and differentiation, the opposing school of though argues that differentiation does not necessarily lead to increased costs, on the contrary, it may serve to reduce cost, which implies that differentiation can be a mean to pursue a low cost position. In short, viewing differentiation and market share as positively related allows for differentiation to go hand-in-hand with cost leadership. Aspects of both are facilitated by large market share.

4.3. Mixed strategy and performance

Research has yielded extensive empirical evidence in support of a positive "strategy-performance link" which implies that strategy and performance are positively correlated seeing

[61] Wright, Nazemzadeh, Parnell & Lado (1991)
[62] Karnani (1984), p 375

that strategy generates competitive advantage.[63] However, the presented empirical evidence typically encompasses "pure" strategies, i.e., cost leadership differentiation (or focus). When it comes to the relationship between mixed strategy and performance, opinions diverge. Again, this raises the question of whether there is a link between the nature of the correlation of mixed strategy and performance (positive or negative) and adherence to either of the two trade-off related schools of thought.

Stuck in the middle strategy and performance

According to Porter, successfully adopting a "single" strategy necessitates total commitment, thus implementing two strategies requires an excessive effort. Chakraborty & Philip (1996) explain that the reason some firms follow a mixed approach is because of the difficulty in designing and implementing an effective long-term strategy based solely on one of the two approaches."[64] Because cost leadership and differentiation strategies require different resources, skills, organizational arrangements and managerial styles that are difficult and even incompatible to reconcile, attempts to reconcile the two inevitably lead to a trade-off. For example, competing with a cost leadership strategy involves resources and technologies of functional supports that emphasises cost cutting throughout "all the functional areas of the organization".[65] Campbell-Hunt (2000) means that organizational constraints actually represent the fundamental reason why cost- and differentiation-emphasis designs are believed to be mutually exclusive.[66]

Strategies are also vulnerable to different risk and therefore require different defences, which in turn may be incompatible or even opposed to each other (Wright & Parsinia, 1988). So, even if both strategies emphasise profits and performance, their approaches differ (Chakraborty & Philip, 1996). Deciding which strategy to adopt implies matching "strategic requirements" with the firm's resource, capabilities and limitations. However, since a firm has limited resources, it is rarely suited for all strategies (Porter, 1980; Wright & Parsinia, 1988; Barney, 2002). By trying

[63] Some examples of empirical studies supporting the strategy-performance link are Phillips et al (1983), Buzzell et al (1975), Schoeffler et al (1974), Karnani (1984), Miller & Friesen (1986a) and Woo (1984).
[64] Chakraborty & Philips (1996), p 57.
[65] Wright & Parsinia (1988), p 22
[66] Campbell-Hunt (2000), p 138

to be "all things to all customers", a firm risks becoming too broad and eventually answering to no customer or market segment (Porter, 1980; Akan et al, 2006; Chakraborty & Philip, 1996).

"Luck in the middle" strategy and performance

The opposing school reject the arguments presented by Porter and adherents of his school of though. Cost leadership and differentiation are believed to be reconcilable and even sought-after. Indeed some of the researchers suggest that a successful combined strategy generates superior profitability. This does not mean that a successful mixed strategy is easy to achieve; in fact, researchers of the opposing school of thought recognize the challenge. Successfully adopting a mixed strategy requires great effort and commitment (i.e. Reddy, 1980; Chakraborty & Philip, 1996; Wright et al, 1991; White, 1986; Grant, 2005). Grant (2005) for example calls it "one of the greatest strategic challenges of the 1990s".[67]

According to Murray (1988), the conditions that favour cost leadership are independent of conditions that favour differentiation and thereby there is no *a priori* reason to rule out the possibility of reconciling cost and differentiation based on external conditions. On the contrary, external conditions may actively favour mixed strategies, provided that differentiation serves as a mean to expand markets share. If the correlation between differentiation and market is positive, differentiation can generate economies of scale, which also means that higher differentiation and cost reductions are achieved simultaneously. As mentioned earlier, differentiators charge a premium price (initially justified by the higher production costs and product exclusivity). Thus, combining strategies successfully implies that a firm can charge a higher price (than cost leaders) while reducing costs (compared to differentiators), which leads to superior profits.

Other researchers mean strategies can be successfully reconciled (i.e. without trade-off) because firms can develop skills to adopt both strategies simultaneously. In fact, combined strategies are less vulnerable to risks associated with pure strategies, i.e. specialization (e.g. Miller, 1988; Wright et al, 1990, Wright et al, 1991). Quoting Miller (1988), strategic specialization may result

[67] Grant (2005), p 244

in "serious gaps or weaknesses in product offerings, ignore important customer needs, be easy for rivals to counter, and, in the long-run, cause inflexibility and narrow an organization's vision." Miller (1988) explains that Caterpillar initially attempted to become the highest-quality producer of earth-moving equipment in the world by focusing exclusively on durability and precision but failed to care about efficiency and economy.[68] In the long run, excessive focus on a single strength (or strategy) also risks reducing resilience and adaptability. Combination strategies on the other hand enhance flexibility and make it easier for firms to adapt to changes, such as advances in technology and industry changes (Miller, 1992; Parker & Helms, 1992).

Miller (1992), Barney (2002) and Barney & Hesterley (2006) propose that firms, which are successful in both cost leadership and product differentiation, may be expected to gain a sustained competitive advantage. In fact, combining cost leadership and differentiation strategies generates socially complex relations, e.g. among employees, between employees and the technology they use, and between employees and the firm for which they work. The reason is that mixed strategies engage more resources and organizational support. Thus, provided that the organizational strengths and weaknesses involved are rare and costly to imitate, the socially complex relations that emerge when reconciling strategies constitute a source of sustained competitive advantage (Miller, 1992; Barney, 2002; Barney & Hesterley, 2006).

Summarising "Mixed strategy and performance"

While Porter's school of thought argue that mixed strategy is a poor strategic choice, the opposing school mean that a trade-off does not need to be: mixed strategies may generate superior performance as they have the potential to create socially complex relations that make them rare and costly to imitate. This argument is valid on condition that the relationship between differentiation and market is positive, that is, differentiation should lead to reduced costs.

4.4. Summarising Table

[68] Miller (1992), p 37-38

Author	Empirical study Yes/no	Method	Trade-off yes/no	Findings	Arguments	Examples/ Observations
Porter (1980)	No	-	Yes	Stuck in the middle firms perform poorly	Organizational constraints: different resources and functional supports. Risk of becoming too broad	Few cases of successful mixed strategies. Only under extreme circumstances can strategies be reconciled
Hall (1980)	Yes	Strategic profile analysis	No	Single or mixed strategies perform the best: 3 of the 64 studied firms and 2 of the 16 leading companies employed mixed strategies.		Philip Morris & Daimler Benz, Caterpillar
Reddy (1980)	Yes	Case studies- four large U.S. manufacturing companies	No	Differentiation can be a mean for firms to establish a low-cost position	Quality improvement leads to cost reductions	Management style must assure a balanced approach that keeps all the objectives of quality, quantity and cost
Hambrick (1983)	Yes	Cluster Analysis (CA)	Yes	No successful mixed strategies identified Porter's strategic types are well-represented among high performers		
Phillips, Chang & Buzzell (1983)	Yes	Causal modelling methodology	No	Differentiation can be a mean for firms to establish a low-cost position	Quality exerts a significant positive effect on market share (consistent with the quality-learning curve) Economies of scale	
Dess & Davis (1984)	Yes	CA	Yes	No successful mixed strategies identified Stuck in the middle firms are outperformed by firms with single strategies. (Sales growth, ROA)		

Author	Empirical study Yes/no	Method	Trade-off yes/no	Findings	Arguments	Examples/ Observations
Fine (1986)	No	-	No	Differentiation can be a mean for firms to establish a low-cost position	Quality-based learning effects Japanese cost control methods	
Miller (1986)	No	-	Yes	Stuck in the middle" firms perform poorly"		
Miller & Friesen (1986a, b)	Yes	CA	No	Single or mixed strategies perform the best (ROI, GRMS)	Economies of scale (in production, advertising & sales). Cost leadership strategy in the beginning of the value chain, differentiation in the later part.	
White (1986)	Yes	Categorization [69]	No	Combined strategies have highest performance (ROI): 19 of the 69 studied firms	"Excellent companies may be able to combine seemingly contradictory organizational arrangements simultaneously [...]"[70] Sequential rather that simultaneous attention to the two strategies?	IBM, Caterpillar, Philip Morris. Only excellent firms succeed
Wright (1987)	No	-	Yes	Cost leadership and differentiation strategies are incompatible	Organizational constraints: different resources and technologies of functional support	
Calori & Ardisson (1988)	Yes	CA	No	Combined strategies have highest performance (GRMS)		Only excellent firms succeed

[69] White (1986) classified 69 business units from 2 different firms into four possible generic strategic groups (according to a 2x2 matrix)
[70] White (1986), p 230

Author	Empirical study Yes/no	Method	Trade-off yes/no	Findings	Arguments	Examples/ Observations
Hill (1988)	No	-	No	Differentiation can be a mean for firms to establish a low-cost position	Economies of scale	Only excellent firms succeed? Short-run (cost increase) vs. long-run (cost reduction)
Jones & Butler (1988)	No	Transaction cost approach	No	Differentiation can be a mean for firms to establish a low-cost position: Transaction cost approach	Economies of scale. Whether strategies are reconcilable also depends on the shape of the transaction cost curve and revenue considerations	
Karnani (1988)	No	Game-theoretic model of oligopolistic competition	No	Differentiation can be a mean for firms to establish a low-cost position	Two opposing forces influencing market share. 1.increased costs due to increased differentiation, 2.decreased costs due to economies of scale	Short-run (cost increase) vs. long-run (cost reduction)
Kim & Lim (1988)	Yes	CA	Yes	No successful mixed strategies identified	Stuck in the middle firms are outperformed by firms with single strategies. Need to commit to a clearly defined strategy	
Murray (1988)	No	-	No	Differentiation can be a mean for firms to establish a low-cost position	Economies of scale, cost control, Quality-based learning effects. Conditions that may favour leadership and differentiation are independent of each other	
Wright & Parsinia (1988)	No	-	Yes	Cost leadership and differentiation strategies are incompatible	Organizational constraints: different resources and functional supports (& defences)	

Author	Empirical study Yes/no	Method	Trade-off yes/no	Findings	Arguments	Examples/ Observations
Daniel & Rietsperger (1990)	No	-	No	Differentiation can be a mean for firms to establish a low-cost position	Japanese cost control methods	
Reddy (1990)	Yes	Case studies- four large U.S. manufacturing companies	No	Differentiation can be a mean for firms to establish a low-cost position	Quality improvement leads to cost reductions	Management style must assure a balanced approach that keeps all the objectives of quality, quantity and cost
Wright, Kroll, Kedia & Pringle (1990)	Yes	CA	No	Combined strategies have highest performance (ROI, RMS, GRMS): 10 of the 47 studied firms	Economies of scale, process and service innovations and cost control, reduced vulnerability to risks associated with single strategy	
Wright, Kroll, Tu & Helms (1991)	Yes	CA	No	Combined strategies have highest performance (ROI, GRMS): 10 out of 56 studied firms	Economies of scale, capacity utilization, process innovations	
Wright, Nazemzadeh, Parnell & Lado (1991)	No	-	No	Differentiation can be a mean for firms to establish a low-cost position	Price elasticity of demand. Low input costs	Possibly, only firms with "special talents and opportunities succeed
Miller (1992)	No	-	No	Differentiation can be a mean for firms to establish a low-cost position	Less vulnerable to risks associated with specialization. Greater flexibility. Imitation is more complex	Caterpillar, Computer Data Corp
Parker & Helms (1992)	Yes	Interviews	No	Single or mixed strategies perform the best (Relative net profit, ROA, Employment growth, sales growth/sales revenue growth)	Greater flexibility	

Author	Empirical study Yes/no	Method	Trade-off yes/no	Findings	Arguments	Examples/ Observations
Green, Lisboa & Yasin (1993)	Yes	Factor Analysis	Yes	No successful mixed strategies identified	Risk of becoming too broad: Stuck in the middle" attract neither high volume customers nor premium price customers	
Miller & Dess (1993)	Yes	Categorization[71]	No	Combined strategies have highest performance (ROI, AMS)		
Nayyar (1993)	Yes	Survey	Yes	No successful mixed strategies identified	Single strategies at product-level may give the illusion of mixed strategies at business-level	
Reitsperger, Daniel, Tallman & Chisman (1993)	Yes	CA	Yes	Combined strategies have highest performance	Relative technical or production efficiency	Toyota, IBM, P&G
Oskarsson & Sjöberg (1994)	Yes	Case study-Motorola	No	Differentiation can be a mean for firms to establish a low-cost position	Process, product and system innovations	Motorola
Chakraborty & Philip (1996)	No	-	Yes	Stuck in the middle firms are outperformed by firms with single strategies)	Cost leadership and differentiation strategies are incompatible: resource commitment	
Helms, Dibrell & Wright (1997)	Yes	CA	Yes	Combined strategies have highest performance (ROI)	Process, product and system innovations	
Parnell (1997)	Yes	Categorization[72]	No	Evidence of viable mixed strategies		

[71] Miller & Dess (1993) classified businesses strategies into seven different groups of strategic positions based on relative direct costs, relative product quality and breath of targeted market

Author	Empirical study Yes/no	Method	Trade-off yes/no	Findings	Arguments	Examples/ Observations
Grant (2005)	No	-	No	Differentiation can be a mean for firms to establish a low-cost position	Japanese cost control methods and, process, product and system innovations	Japanese manufacturing companies + Toyota, Dell and Canon, IKEA, Southwest Airlines
Akan, Allen, Helms & Spralls (2006)	Yes	Factor analysis	Yes	No successful mixed strategies identified	Risk of becoming too broad ("all things to all customers")	
Barney (2002)/ Barney & Hesterley (2006)	No	-	No	Differentiation does not necessarily need to be	Provided that the organizational strengths and weaknesses involved are rare and costly to imitate, the socially complex relations that emerge when reconciling strategies constitute a source of sustained competitive advantage.	

[72] Parnell (1997) adopted a categorization scheme that assigned strategies to organizations based on the degree of agreement (or disagreement) of five respondents from the same business unit. Four groups were used.

5. Interviews with Practitioners

The following section is a complement to the literature review. Four practitioners were interviewed with the objective of identifying whether they view and approach strategies as mutually exclusive or potentially reconcilable. The four practitioners interviewed were: Micael Dahlén, Associate Professor at the Center for Consumer Marketing at the Stockholm School of Economics, Stefan Georgi, Strategy Consultant at Strategic Leap Partners, Sophie Karlsson, Consultant at the Swedish Trade Council, and Torbjörn Persson, International Marketing & Sales Director at Sunnex Equipment AB. Findings of this "cross-check" study are presented next.

5.1. Mixed strategy and performance

To begin, respondents consent that profit maximization entails a preference for a strategy that simultaneously adopts low cost and premium prices if it results in superior profits. Had there been no trade-off, all practitioners should be adopting a combination rather than a single strategy. Evidently, this is not the case, which suggests that a trade-off exists. In fact, respondents unanimously believe that attempts to adopt cost leadership and differentiation strategy simultaneously tend to generate a trade-off. However, should a firm successfully reconcile both strategies, efforts will be compensated by superior performance.

5.2. Competitive strategy and market share

A priori, none of the respondents question the traditionally positive relationship between low cost and market share, meaning that increased emphasis on cost leadership is generally believed to result in greater market shares. Respondents also agree that differentiation strategy and market

share may be positively correlated, which is opposed to Porter's theory that differentiation restrains market share growth.

Sophie Karlsson and Micael Dahlén suggest: "Differentiation leads to greater market share, provided that the product appeals to customers. This implies that a firm must identify and pursue customer preferences if it wishes to gain increased market shares through differentiation. More specifically, when customer preferences are favourable (in terms of the firm's resources, skills, processes, history, etc), differentiation allows a firm to expand its market shares via decreased price elasticity of demand. Torbjörn Persson suggests an essentially similar explanation by explaining that differentiation allows a firm to offer a larger product portfolio, hence appeal to a broader market and consequently face superior demand (either through increase number of customers or number of purchases per customer). Again, this is conditional upon customer preferences and market and industry conditions.

What's more, there is a consensus that differentiation, when translated into increased product quality only, is insufficient as a mean to achieve a low cost position. Quoting Torbjörn Persson: "Competition from low-cost producing countries force firms to pay attention to flexibility and adaptability to industry- and market changes, differentiation strategy notwithstanding." Clearly, this reasoning is comparable to Karnani's (1984) "low input" argument, which suggests that by finding cheaper means to manufacture, market and distribute, firms have the opportunity to successfully achieve both high differentiation and low cost position.

5.3. Trade-off

All respondents except Stefan Georgi support a possible reconciliation of differentiation and cost leadership strategies. A trade-off exists and often occurs but is not necessarily inevitable, despite the fact that reconciling cost leadership and differentiation represents an enormous challenge in terms of managing requirements and conditions that are specific to respective strategy.

When discussing firms' potential to successfully reconcile cost leadership and differentiation answers differ further. While Micael Dahlén puts forward an existential philosophy suggesting that all firms have an equal opportunity to successfully reconcile strategies, Sophie Karlsson declares that "successfully combining cost leadership and differentiation is highly challenging, hence it is unlikely that more than a few companies in each industry (were a choice of strategy exists) succeed. Naturally, a firm that manages to avoid trade-off should be market leading." Torbjörn Persson adjoins that "far from all firms have the potential to do so since simultaneously adopting both strategies requires extensive experience and knowledge of the working of all functions, e.g. procuring inputs, manufacturing, stocking, marketing (in particular branding), distributions, recruitment & training of employees. What's more, firms must adapt to and successfully manage the new requirements and circumstances that emerge when reconciling cost leadership and differentiation."

Contrary to previous respondents, Stefan Georgi advocates an inevitable trade-off. "Low cost and differentiation may be reconcilable; in fact low cost can make out a differentiation strategy, as illustrated by Dell or Ryanair. Cost leadership and differentiation nevertheless remain two essentially different strategic choices. SAS and its low cost alternative Snowflake is a good example illustrating the strategies are incompatible. To meet the raising competition from low cost carriers, SAS took the decision to introduce Snowflake, its own low cost alternative. Despite recent years' extensive efforts to reduce costs, SAS has maintained its differentiation strategy and the attempt to integrate it with a cost leadership strategy has revealed unprofitable. The reason is that SAS is a differentiator and so the differentiation strategy is present in the whole company. Reducing costs increases margins and makes SAS to a better differentiator as long as the strategy remains clear. Attempting to integrate too many elements of cost leadership into its differentiation strategy however damages the initial strategy."

6. Analysis

Among the identified literature, the trade-off issue is typically studied as a subtopic when testing Porter's model of generic strategies, not as a main topic by itself. The literature is therefore limited and the topic not studied enough in depth. Practitioners have reflected a similar lack of depth in their argumentation. Nevertheless, provided that the thesis has served its purpose, it should have brought some insights into the topic. These findings shall be discussed next.

6.1. Interpreting findings on the trade-off

The main reason why Porter and adherents of his theory believe that a combination strategy is a poor strategic choice is that contradictory organizational requirements of cost leadership and differentiation strategies make a trade-off inevitable. It is also argued that the challenge is too complex and costly.

Opponents of Porter's theory believe that a trade-off does not need to be. The principal argument of the opposing school of thought is that differentiation may be a source of cost reduction (scale and learning economies, innovation processes), which implies that conditions that favour differentiation and cost leadership are not incompatible. Thus provided that differentiation leads to cost reductions or increased price premium or both, cost leadership and differentiation strategies can be combined without a trade-off. The literature review has revealed a number of explanations why differentiation may reduce costs. In addition it is argued that firms can develop management skills to reconcile cost leadership and differentiation strategy requirements. Evidence is provided by those empirical studies that have observed the existence of firms with mixed strategies and the studies that have measured performance of strategies and found that

firms with mixed strategies perform equally well or better than cost leaders and differentiators.[73] About two thirds of the empirical studies within the identified literature base support the argument in favour of reconcilable strategies.

In general, when examining the identified literature on the topic, a majority of the research adheres to the opposing school of thought (about two thirds of the studies identified. See table 1). Among interviewed practitioners, three out of four have suggested that a trade-off needs not necessarily be and, thereby, findings from the interviews seem to be rather consistent with findings from the literature review.

Moreover, the literature review has revealed that there are two main elements determining whether researchers adhere to Porter's school of thought or the opposing school: the conceptualisation of cost leadership and differentiation, and the opinion on the nature of the correlation between market share and performance. First, the conceptualisation of cost leadership and differentiation as two dimensions of strategic positioning rather than two types of strategies allows researchers to explore the existence of "combination" strategies. By viewing the two strategies as opposite ends of a single continuum or two different types of broad strategic groups, researchers rule out the possibility of reconciling strategies since moving closer to one end automatically implies moving farther away from another. Choosing to position between the two ends is equivalent to choosing a stuck in the middle strategy. Second, defenders of a positive relationship between market share and performance also mean that cost leadership and differentiation strategies may go hand-in-hand, as differentiation is a source of cost reductions. Respondents of the cross-check on the topic consent that differentiation may serve to achieve cost reduction and that the relationship between differentiation strategy and market share may be positive (although it is not inevitably the case). However, not all respondents agree that this "potentially positive relationship" implies that strategies may be reconciled. In fact, a cost reduction does not need to entail a fundamental change in strategy as explained by Stefan Viotti and the case of SAS and Snowflake.

[73] In terms of method, cluster analysis techniques as a mean to define strategic groups and the use of the PIMS database for collecting samples dominates the identified research studies. This is also observed by Campbell-Hunt (2000).

6.2. Lacking a definition of "mixed strategy"

The literature review has attempted to identify, present, and summarize the existing research of the topic in order to clarify what is being argued in the research field on the trade-off between cost leadership and differentiation. Identified literature has been classified according to school of thought, that is, whether strategies are believed to be mutually exclusive or potentially combinable. Yet a fundamental element to the discussion is the definition of the concept "combination strategy" (or "mixed" or "combined" strategy). Although it is presumed that a combined strategy contains both elements generally associated with cost leadership and with differentiation strategy, the definition remains vague and permits a range of interpretations. Occasionally it is specified that the two strategies must be adopted *simultaneously*, White (1986) on the other hand suggests that firms may externally focus on opportunities to differentiate while being internally oriented towards cost reduction; mixed strategies is achieve trough the "sequential rather than simultaneous attention to the different organizational requirements of these different business strategies."[74].

As discussed, the definition of "mixed strategy" or "combined strategy" may influences the compliance with either of the two schools of thought, and consequently, the lack of a consistent, clear, and specific definition makes research on the tropic a trick endeavour. Studies are difficult to compare and the accumulated weight of evidence is not assessable.

The problem with a lacking generally recognized definition, may be observed in the literature. In some cases, a company is presented as a successful cost leader or differentiator by a researcher, while another refers to the same firm as evidence that a trade-off may be avoided. This is the case of Wal-Mart: While Barney & Hesterley (2006) and Lumpkin, Droege & Dess (2002), Akan et al (2006) describe Wal-Mart as a remarkably successful cost leader while Barney (2002), for example, suggests that Wal-Mart successfully employs a combined strategy and thereby evidences the fact that a trade-off may be avoided. The case of Southwest makes out a second, similar example as some researchers mean that the airline is adopting a cost leadership strategy, e.g. Lumpkin, Droege & Dess (2002), while others argue that its strategy is a mix of cost

[74] White (1986), p 230

leadership and differentiation, e.g. Grant (2006). Despite the fact that Porter's definitions and theory underlie their studies, these researchers have proposed distinguishing observations and arguments, which illustrates that there is enough space for (mis)interpretation.

Ghemawat refers to McDonalds as evidences that firms can discover ways to produce superior products at lower costs, explaining that "McDonald's brand recognition and product consistency permitted it to charge a slight premium over competing fast-food vendor, even though its national scale, franchising relationships and rigorous standardization allowed it to incur lower costs than its rivals."[75] However, finding ways to produce superior products at lower costs is insufficient to create a mixed strategy. As indicated by the definitions of cost leadership and differentiation presented in the Theory section of this paper a firm should distinguish its strategy from rival's and develop a strategy which is rare and costly to imitate if it wishes to generate competitive advantage and superior profitability. A market cost leader, for example, is not necessarily the firm which sells at the absolute lowest costs. As discussed previously a strategy constitutes several elements; all elements and in particular the way they interact is what makes out the strategy. By developing its brand recognition and product consistency, McDonalds was able to charge a premium and in turn to outperform its competitors, as Porter's theory predicts. Thus owing to a remarkably successful cost leadership strategy, McDonald's became the cost leader per (Porter's) definition.

6.3. Strategy vs. Operational Effectiveness

According to Porter, failure to distinguish between strategy and operational effectiveness has led to confusions and misinterpretations by numerous managers.[76] What's more, it has led to confusions and misinterpretations by researchers. Employing TQM as empirical evidence in support of compatible strategies ("quality is free") without arguing that sustainable competitive advantages emerge is not valid. Differentiation may serve to reduce costs, but this does not necessarily mean that cost leadership and differentiation are reconcilable. In fact, management

[75] Ghemawat (1999), p 56
[76] Porter (1996), p 61

tools and techniques, i.e. TQM and JIT can lead to remarkable improvements in operational efficiencies, but they typically remain imitable by competitors and therefore fail to establish a sustainable competitive advantage. In other words, there is not necessarily a fundamental change in business strategy.

Similarly, some respondents have suggested that by finding cheaper means to manufacture, market and distribute, firms may reconcile differentiation and low cost. Karnani's (1984) "low input" argument, which states that by finding cheaper means to manufacture, market, and distribute, firm may successfully achieve both high differentiation and low average cost position. Again, operational effectiveness and strategy has been confused. Lindeberg, for example, may have moved its production to low cost countries, i.e. Morocco, China, Tukey and Taiwan, yet it has remained a differentiator.

6.4. The author's word on the topic

Having studied the literature on the topic thoroughly and discussed it with a small number of practitioners, the author is inclined towards Porter's initial proposition that simultaneously reconciling cost leadership and differentiation is accompanied by a trade-off. This represents a change compared to initial suppositions, which confidently rests on a deeper understanding of the topic and its issues. A lacking common definition, the risk of confusing strategy and operational efficiency and a desire to suggest that both strategies may be successfully combined risks leading to confusion and erroneous interpretations of arguments.

As it seems, a successful strategy concerns all functions and organisational elements of a firm. Competitive advantage emerges from the scores of interconnected relationships that result from successfully adopting a business strategy. The complexity of the scheme, which may be compared to a cogs mechanism, makes it difficult to identify all elements, functions and internal and external circumstances that interact. Failure to fully capture their interconnection renders imitation even more complex and in turn creates a sustainable competitive advantage. Introducing new and possibly contradictory elements into the scheme alters the whole scheme

and thus requires the understanding and management of a new set of relationships, rather than only the ones directly affected by the change. Avoiding a trade-off is therefore excessively complex and costly to be profitable and the few companies that may have succeeded to reconcile cost leadership and differentiation without a trade-off are exceptional.

7. Conclusions

This thesis set out to investigate the current state of art of research on the fundamental trade-off between cost leadership and differentiation strategies. Considering that no similar study has been conducted before (to the author's knowledge), the contribution is believed of value to the strategy field. In order to fulfil the purpose, a thorough attempt has been made to identify, gather and analyse the existing relevant literature. As a complement to the literature review, the trade-off was discussed with a few practitioners. Respondents were interviewed individually in order to obtain their input on the topic and potentially gain some insight into the relationship between theory and practice. Comparing practitioners' answers with findings from the literature indicates that theory and practice are seemingly consistent.

The relevant literature was classified according to two schools of thought. On the one hand, Porter and adherents of his theory advocate that cost leadership and differentiation strategies cannot be reconciled without an inevitable trade-off. On the other hand, the opposing school of thought argues that a trade-off need not be. Two elements determine adherence to either of these schools. First, the conceptualisation of competitive strategies which has revealed that a condition for exploring the possibility to reconcile cost leadership and differentiation is to view the strategies as two dimensions of strategic positioning, rather than opposing ends of a single continuum or two types of strategies. Second, the relationship between market share and differentiation: contrary to Porter's school, opponents believe that the relationship may be positive, which implies that that differentiation does not necessarily lead to increased costs since the strategy may serve to reduce costs and thereby cost leadership and differentiation are compatible. Further, if trade-off may be avoided, mixed strategies, per se, have the potential to yield superior profits.

An initial examination of the topic may produce the impression that a majority of researchers and practitioners support an evitable trade-off. Investigating the trade-off issue more thoroughly however reveals a number of confusions and misinterpretations that emerge first and foremost from the lack of a consistent definition and failure to distinguish between business strategy and

operational efficiency. Understanding these issues renders the arguments in support of an evitable trade-off invalid and Porter's theory withstanding.

Appendix A- Interview Questions

Following interview questions should be viewed pointers. Depending on each interview and the direction in which the discussion headed, some questions might have been left out and others asked. Nonetheless, an attempt was made by the author to receive an answer to these questions in order to obtain comparable answers.

”Conceptualization”

- Define the concepts cost leadership and differentiation strategy respectively in terms of a few elements or variables which you associate with each strategy
- ”Conceptualization”: How would you describe cost leadership and differentiation strategies in relation to each other? And low cost and differentiation?
    - Two types of reconcilable strategies
    - Two types of mutually exclusive strategies
    - One strategy; each containing elements of both cost leadership and differentiation only in different proportions

Strategy and cost

- Would you say that quality is costly or that quality is free?
- What is the nature of following relationships:
    - Low cost and market share
    - Differentiation and market share
    - Cost leadership strategy and costs
    - Differentiation strategy and costs
- Which costs increase or decrease respectively with differentiation strategy?
- Under what conditions/circumstances can differentiation lead to decreased costs?
- Under what conditions/circumstances can increased emphasis on differentiation lead to increased market shares?

“Combination strategy”

- “Luck in the middle” or “stuck in the middle”?

- A seemingly increased number of firms adopt cost leadership and differentiation strategies in combination (IKEA, South West Airlines, Caterpillar are a few frequently cited examples), are these firms exceptions?
- Can cost leadership and differentiation strategies be successfully reconciled? In other words, can a trade-off be avoided? Please specify.
- Under what conditions/ circumstances may cost leadership and differentiation strategies be reconciled?
- Do all firms have the same opportunity to adopt a combination strategy?
- What are the requirements?

8. Specification of sources & References

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