Table of Contents

Lecture 1: Important Concepts in Business Strategy

What are the Firm's Important Functions and Strategies?

- Selling strategy
- Production strategy
- Market equilibrium
- Market structure and rivalry
- Information
- Managerial operation

1. Selling Strategy
    - Companies need to know about consumers purchasing behaviour

   Ultimate goal is to maximize profits:

- Profit = Sales - Total Costs
- Sales = Price x Units Sold
- Total Costs = Unit Production Cost (Average Cost) x Number of Output

- **Demand curve:** Relationship between the quantity of a good that consumers are willing to buy and the price of the good.
- The demand curve, labeled D, shows how the quantity of a good demanded by consumers depends on its price. The demand curve is downward sloping; holding other things equal, consumers will want to purchase more of a good as its price goes down.
- The quantity demanded may also depend on other variables, such as income, the weather, and the prices of other goods. For most products, the quantity demanded increases when income rises.
- A higher income level shifts the demand curve to the right (from D to D′).

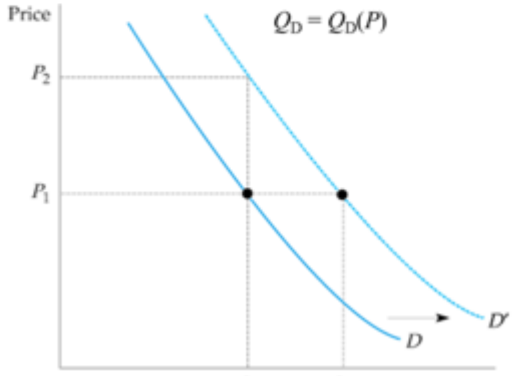

FIGURE 2.2

2. Production Strategy

- Production strategy relates to supply.
- **supply curve:** Relationship between the quantity of a good that producers are willing to sell and the price of the good.
- The supply curve, labeled *S* in the figure, shows how the quantity of a good offered for sale changes as the price of the good changes. The supply curve is upward sloping: The higher the price, the more firms are able and willing to produce and sell.
- If production costs fall, firms can produce the same quantity at a lower price or a larger quantity at the same price. The supply curve then shifts to the right (from *S* to *S*′).
- Two type of firms output decision: Short run vs long run decisions
- Supply curve is the marginal cost of the company
- should the firm continue producing even though loss?

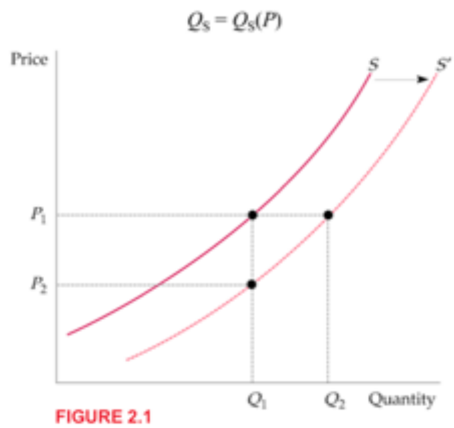

FIGURE 2.1

3. Market Equilibrium

- **Equilibrium** (or **market clearing**) **price:** Price that equates the quantity supplied to the quantity demanded.
- **Market mechanism:** Tendency in a free market for price to change until the market clears.
- **Surplus:** Situation in which the quantity supplied exceeds the quantity demanded.
- **Shortage:** Situation in which the quantity demanded exceeds the quantity supplied.

FIGURE 2.3

4. Market Structure and Rivalry

Types of Industry:

Perfectly Competitive
- Numerous small sellers and buyers in the market, similar products and consumers have complete and accurate information about their prices, perfect competitive markets have no single market leader or monopolistic firm
- E.g. Coffee Shop

Monopoly
- Monopoly industry infrastructure comprises a single producer or supplier of a product or a service that has no close substitutes
- E.g. local telephone companies and water companies

Oligopoly
- Market in which only a few firms compete with one another, and entry by new firms is impeded
- E.g. automobile manufacturers

5. (Asymmetric) Information
   - Information will effect in implications to managerial operation/selling
   - E.g. what if there is asymmetric information between owners and managers or between sellers and buyers

6. Managerial Operation
   - Managerial operation in organisation aspect of the firms
   - Institutional setting within which diverse entities interact and come into equilibrium

Linking Business Strategy and Microeconomics: Some Cases
1. How to Respond to Consumer's Behaviour?
   - E.g. Leather jacket industry vs Environmental protection
   - E.g. Accommodation cost in Gold Coast vs Terrorism
2. Market Positioning Strategy
   - E.g. Volvo's strategy focusing on safety in motor vehicle industry
3. Price Competition
   - E.g. Qantas vs Virgin Blue's competition
4. Cost of Production / Research and Development Investment
   - E.g. Dell company’s introduction of just-in-time delivery system to reduce inventory loading (managing inventory costs)
5. Business Type Strategy
   - E.g. Foreign direct investment vs Joint venture
   - E.g. Internal production vs Outsourcing

        - Should investment in a foreign company be done directly or indirectly or combined
6. Corporate Governance
    - Some argue that crony capitalism caused the Asian crisis in 1997
    - E.g. Collapse of HIH insurance in 2001
    - E.g. Ansett Airline 2002 - more than 16,000 Ansett jobs have been destroyed and another 60,000 are under threat in supplier companies and throughout the tourism industry
7. Implications of Asymmetric Information to Business Strategy
    - E.g. Product warranty, advertisement to assure quality of products
    - For example: Kirin, Sapporo and Asahi (Japanese Beer)

Goal: How to Outperform the Market?

- Firms can do well or poorly depending on their product positioning and product investment
- How organisations identify the market demand, adapt to changing environment and capitalizing the changing environment to increase profits
    - E.g. Toyota deciding to stop car manufacturing in Australia in 2017, bringing an end to car manufacturing in Australia, 2,500 workers lost jobs
    - BHP posts $7.8 billion loss, slashes dividends from $0.62 to $0.16

1. Big Decision / Commitment
    - Market positioning/pricing
    - Production/investment
    - Strategic (rivalry) decision
2. Organisation Strategy to Help the Organisation to Accomplish Goals
    - How to deploy the investment to be a valuable but not imitable resource

Why Microeconomics?

- Microeconomic Concept - provides basic function to analyse various kind of business strategy
- Microeconomics - concerned with the behaviour of individual economic units and their interactions
    - The two types of economic units typically considered are firms and consumers
    - The major type of interaction that is usually analysed is that of market interaction

How to Apply Microeconomic Principles to Actual Decision Making?

- Provides analytical techniques and underlying principles applicable to different strategic situations
    - E.g. analysis of optimization, given constraints, is crucial to understand consumers behaviour and the firms production decision
    - E.g. the firms big decision should be based on efficient resource allocation, which is the prime goal of microeconomics
    - E.g. Marginal Decision Making: marginal benefits vs marginal costs or marginal revenue vs marginal costs

Corporate Decision Making: The Toyota Prius

Hybrid cars are more energy efficient than cars with just a gasoline engine; the Prius, for example, can get 45 to 55 miles per gallon. The Prius was a big success, and within a few years other manufacturers began introducing hybrid versions of some of their cars. The design and efficient production of the Prius involved not only some impressive engineering, but a lot of economics as well. First, Toyota had to think carefully about how the public would react to the design and performance of this new product.

Consumer preference and demand, product positioning

Next, Toyota had to be concerned with the cost of manufacturing these cars.

Production costs and profit maximising choice of output

Toyota also had to design a pricing strategy and consider how competitors would react to it.

Pricing strategy, rivalry behaviours

Manufacturing the Prius required large investments in new capital equipment, Toyota had to consider both the risks and possible outcomes of its decisions

Investment decision

Finally, Toyota had to worry about organisational problems

Organisational strategy