

**Abstract.** The theoretical analysis dealing with the possibilities of supporting certain generic strategies is useful in order to guide the efforts needed to gain a competitive advantage at national level. Subsequently, the problem of this advantage can be taken into account at an international level. In parallel with the theoretical approach, it's important to make an evaluation of the existing situation from the point of view related to the preference for a certain type of strategy, and of the relation between the type of strategy and the level of profitability. An explicit modeling of the effort to define a certain strategy will be guided by the corroborated results of these analyses. The study aims at being a referential framework for an ampler discussion on the theme related to the sustainability of the generic strategies with an extreme positioning on the scale of competitive advantages provided by the cost and differentiation.

**Keywords:** differentiation strategy, generic strategies, low cost strategy.

## **DIFFERENTIATION VS. LOW COST STRATEGIES IN ROMANIA**

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## **1. Introduction**

One can appreciate that the nowadays competition systems present also a tendency of diversification in Romania, a tendency similar to the one manifested in the case of the states with developed economies. In the framework of these systems, the Romanian organizations own in practice a large set of strategic options. However, these options subscribe relatively easy to the theoretical framework constituted by the various classifications belonging to the renowned authors of strategic management. A number of basic strategic options, the so-called generic strategies, present a special interest for the manner of particularization in the Romanian area.

The cost leadership strategy generates a special interest for the East European countries, Romania included, because of the following reasoning: If a competitive advantage can be acquired by obtaining a product at a lower cost than that of the competitors, then some East European countries could be situated in a favourable position mainly due to the low labor cost, but also to other factors with contribute to the reduction of the total cost. In Romania for instance the average wages in many mature industries represent 10-15% compared to the wages in equivalent West European industries.

On the other hand, the generic strategy of differentiation is adopted in an increasing number of industries. The named strategy is mainly related to the quality. The attributes associated to the concept of „quality” play an essential role both in explaining the existence of a great number of differentiated products, and in explaining a great variety of strategic approaches related to the companies associated to these products.

One can consider an apparent paradox the coexistence of expensive products with superior performances with cheap products with inferior characteristics on the market, both categories having the same generic functionality. In other words, it seems that buyers are to be found for both the trademark products made in Western Europe, USA and Japan, and for the products made in Asian countries, which represent, in a way or another, the imitation or counterfeiting of certain products from the first group.

The evaluation related to the manner of manifestation dealing with the preference for the two generic strategies engenders a base of information, which can substantiate a coherent approach for the competition systems in various industries. In this manner, a strategic option of a certain organization has a greater probability to come into fact, in order to gain a certain advantage and the needed economic performance.

## **2. Theoretical background**

The present theory accepts the idea that a firm can use a number of so-called generic strategies whose results insure a competitive advantage. There are a large number of classifications based rather on conceptual differences than on empiric

evidence, classifications whose authors are academics or management consulting firms. Porter (1980) classification proposes three generic strategies: differentiation, overall cost leadership and focus based on the combination of the type of advantage – cost or differentiation, with the type of target – wide or narrow. The interesting part is the Porter's opinion that the choice of the type of advantage must be exclusive, either lower cost or differentiation, in order to be successful. Or in words that have become more controversial „a firm that engages in each generic strategy but fails to achieve any of them is «stuck in the middle»” (Porter, 1985).

Taking into account the enunciated asymmetry of representativity and purity, it is necessary that the „existence studies” concentrate on the cost leadership strategy. In Romania, for example, the studies are motivated by affirming that the low labor cost would be a premise to establish a competitive advantage by a firm with adopts a strategy mentioned type.

The leadership strategy based on costs appears as a reference strategy in the textbooks that discuss about business level strategies or Porter's generic strategies. Generally, many other textbooks on management refer to a strategy based on cost advantages, clearly connected to the economics or marketing theory.

The strategy based on cost advantages is associated directly to the homogeneity of the products. Also, it is supposed that the firm can't influence the price with anticompetitive individual interventions or in agreement with other firms or because of the natural monopoly structure in that industry. The public utilities presents this characteristic of homogeneity, but those industries are objects of price regulation.

In Romania's case, one can notice a lot of products whose economic utility is based on a single technical feature, which determines a reduced perception of the differences caused by other characteristics. This anomaly is probably determined both by the decrease of the purchasing power of the social categories depending on fixed income and by some consumption patterns inherited from the penury economy existing in Romania before 1990. Putting aside these remarks, the lack of differentiation of the products is very rare and it occurs as a result of the lack of imagination and marketing abilities of producers (Levitt, 1983).

The cost advantages strategies are based on the use of the following influencing factors: economies of scale, economies of scope, learning effects, low labor cost, low labor content low input costs.

The influence of these factors is differentiated according to a certain industry's intrinsic characteristics. In Romania, a set of additional characteristics is added, as a result of the historical process of these industries national development due to a political command. Many industries have developed by concentrating their production on a reduced number of producers, even one producer only in some cases, characterized by an advanced vertical integration. The obtainment of some scale or scope effects was thus had in view. As there were some natural local resources and a low labor cost, one assumes that there could occur some cost advantages associated to the inputs and having a significant effect on final cost.

The differentiation strategy is based on concepts belonging to the theory of the industrial economy. This strategy makes the distinction between the horizontal differentiation and the vertical differentiation of products. While the horizontal differentiation is based on the spatial distribution of providers, the reference pattern being the so-called „spatial duopoly” enounced by Hotelling in 1929, the vertical differentiation is based on the distinct quality, a number of essential theoretic landmarks being set by Schmalensee (1979) respectively by Shaked and Sutton (1982, 1983, 1987).

As a matter of fact, the simplifying patterns are hard to identify. The great majority of products belong to the „differentiated product” category. The most probable market structure in the case of a differentiated product is the one related to the oligopoly.

The competition behavior to be studied is interesting from the point of view of decisions related to price and quality, when is concerned the possibility related to the „natural” appearance of an alignment, or of a certain convergence associated to a given level of the product quality.

As a rule, the study of the competition behavior is made by simplifying the market structure, the starting point being the case of monopoly.

The subsequent empiric researches emphasized the study of combination possibilities, as there were obvious examples that demonstrated the possibility of combining the differentiation strategy with the cost leadership, without affecting the financial performance. The study results confirmed the fact that the strategies are not mutually exclusive (Hall, 1980, Hill, 1988).

If that are doubts about Porter’s argumentation, then an attentive analysis on the consistence of generic strategies and their consistency is required, especially for the firms belonging to other areas than USA, Japan and Western Europe. Studies for other areas are all the more necessary as the ones achieved in USA have shown a reality different from the initial theory.

On one hand, differentiation appears as a label for a large class of strategies, with a rich representation in the case of firms (Mintzberg, 1988). It originates in the non-homogeneity of the products, feature that can be noticed with the large majority of the today existing products in a market economy of the western type.

On the other hand, the cost leadership strategy is much rarer represented than its author hints at (Allaire and Firsirotu, 1998). Even a succinct analysis of the examples quoted in management textbook show that this kind of strategy is very rare in a pure form based on the initial description.

### **3. Method and findings**

This study has been made with a similar approach to that used by Porter when estimating the correlation between the performance of the firm and the level of the forces in his well-known five-force model analysis of the competitive environment

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(Porter, 1980). For a list of products the present study was focalized on the price level associated to the evolution of competitive advantage reflected in the market share between 2005-2009, compared to its level in 2000-'02. It is supposed that the price reflects relatively accurately the cost level.

The chosen products have the following essential characteristics:

- they are internally produced before 1990 as well
- they are made for the final consumption
- they are represented in the family budget
- for every product exist at least one new entrant after '90, like importer or owner of Romanian production facilities

The list of chosen products to be studied is:

- |                 |                           |                          |
|-----------------|---------------------------|--------------------------|
| - refrigerators | - medicines (general use) | - typographical products |
| - detergents    | - cars                    | - tourist services       |
| - beer          | - chocolate               | - textiles               |
| - soft drinks   |                           |                          |

Each of these products represents an industry with a different history of the evolution of the competitive background. For some of them, refrigerators, beer and cars, a short presentation could pinpoint the main characteristics and some important step in their history for an evaluation of the impact of a strategy based on cost, cost leadership or cost focus. The rest of products on the list have also their own history, with a lot of interesting features for a case study.

The products are appraised from the point of view of differentiation, differentiation based on price and the level of the competitive advantage based on cost. On suppose that the price follow the level of the cost, if the value is mediated during a period of 1-2 years.

The last decade of economic development in Romania is characterized, from the point of view of the previous theoretical theme, by a market in an accelerated process of differentiation.

The vertical differentiation of products is only a facet of the differentiation which guides, as a general strategy, the attempt of a certain company to gain a competition advantage.

From the point of view related to the theory of industrial economy, the elements of horizontal and vertical differentiation of products are easy to point out.

In the case of the first category, certain concretizations are remarked and remarkable, when associated to the spatial patterns of horizontal differentiation and to the products, in the case of retail services dealing with food and everyday products destined to the household use. The confrontation, in the sense of obtaining a significant discriminatory element, takes place through the medium of the price, after

a previous stage existed, associated to the choice of the most rewarding geographic position.

Product	Differentiation	Price Differentiation	Competitive Advantage Based on Cost
refrigerators	medium	medium	low
Detergents	low	medium	low
Beer	medium	high	low
soft drinks	low	high	medium
Medicines (for general use)	low	high	high
Cars	high	high	high
Chocolate	medium	high	medium
tourist services	medium	high	low
typographical products	low	low	low
Textiles	high	high	low

**Figure 1. Competitive advantage for different products**

The vertical differentiation of products is prominent due to the appearance of obvious signals that there is a „solvent demand” for products from „the superior part of the scale”. The everyday reality surprises by the apparently shocking coexistence of products having a very good quality, with the ones having an inferior quality, as a matter of fact providing certain characteristics deliberately chosen from the inferior part of the scale.

However, in the everyday reality there is a mixture of the two theoretical types of differentiation, which is characterized by the simultaneous use, as discrimination factors, of the quality, price and spatial positioning. To the „objective” elements resulted from the economic theory add the elements of subjective nature, generated and exploited using marketing strategies based on psycho-sociology. The vertical differentiation is amplified due to a differentiation of image, a vague border existing in between the two.

The majority of the products used nowadays present in fact a great number of benefits, generated by their technical characteristics, by the manner of providing them, or by the associated services, provided by the producer. Consequently, the economic products based on essential characteristic are applicable in a limited number of cases. The quality of the product appears in various forms of manifestation, multiplied by creating a segmentation of the market.

On the other hand, the economic integration of Romania in the European Union and the diminution related to the number of elements, which isolate the Romanian market as a distinct entity, have as a result the possibility of existence for a limited number of companies being in a non-cooperative equilibrium on the market of

a certain product which can be vertically differentiated. What can be observed is the great number of products existing on the market, having a representation in the extreme areas of quality. For instance, both the cars at prices under 10.000 Euros and the cars at prices over 100,000 Euros are being sold.

The strategic differentiation, as it is explained by Allaire and Firsirotu (1998), or the market differentiation, explained by Kotler (1997) are easy to point out in Romania after the adhesion to the European Union, especially in the form of a „dispersion” related to the quality of the products, on an extended scale of values.

#### **4. Conclusions**

The synthetic analysis, presented in the table 1, pinpoints the following findings:

- A small number of products present a positive linkage between the difference of the level of prices (compared with the prices of the products of new entrants) and the competitive advantage already existent, so the opinion that a strategy of cost leadership or cost focus are inconsistent, at least at this moment in Romania.
- For some products it is obvious that a differentiation strategy is chosen as well as one based on cost advantages, so the differentiation and low cost is not mutually exclusive.

The analysis related to the impact of the quality on the diversity of products on a certain market is guided by the theory of industrial economy, and the results correspond to the direct observations dealing with the concrete manifestations of the producers. The „classic” patterns related to the vertical differentiation explain why the coexistence of products belonging to the same type is possible, having certain characteristics associated to an inferior quality and to a superior quality. In fact, the theoretical foundations for the existence of certain brands are explained, related to the extremes of a quality scale.

During the last years, one can observe this differentiation in Romania because, as argued in the theory previously mentioned, a distribution of the incomes related to the consumers has appeared which allows the existence of competing companies with un-null profits and with products of different qualities. The differentiation is supported by the European economic integration, Romania becoming a part of a market having an income distribution, which also allows the accomplishing of other restrictive conditions associated to the existence of the oligopolies in a non-cooperative equilibrium, guided by certain options related to quality.

What today seems to be a shocking manifestation on the market, referred to the communist type market before 1989 – the differentiation based on quality and with an extreme dispersion of values – is a natural consequence of objective states of fact and easy to foresee on the grounds of the theory of industrial economy.

It is necessary to recognize the important limitations of the study. One of these is the smaller sample of products and the narrow base of comparison due to a differentiation strategy. Clearly additional research is needed to multiple the numbers of „generic” products.

The paper want to underline the necessity of empirical research for establish the real stage of generic strategies adopted in Romanian transition to a market economy.

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