

## **Abstract**

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*Cost leadership is one of the most significant strategies for the successful running of the business. This concept indicates manufacturing the product at that minimum cost, which competitors cannot do in the industry as a whole. Cost is the expenditure incurred in order to produce the product which includes cost of manufacturing, cost of selling and other expenses associated with the product and sales. Cost determines the price of a product. Cost control and cost reduction strategies and policies help the business organisations, to reduce the cost which helps the company in gaining competitive advantage. It also helps a company to pioneer in its industry, and to maximise the sales by attracting the customers. This can be achieved by the organisation when it adopts the best practices prevailing in the industry. The economies of scale centralised buying, integration and mergers, bargaining power with suppliers, effective utilisation of available resources, minimising the defective products and avoiding wastage are the factors contributing to achieve cost leadership. This article discusses in detail the cost leadership strategies followed in companies from varied industries and how they are benefited from it.*

**Keywords:** Cost Leadership, Economies of Scale, Integration, Cost control, Cost reduction.

## **Introduction**

### **Cost**

**I**n business, cost is usually a monetary valuation of effort, material, resources, time and utilities consumed, risks incurred, and opportunity forgone in production and delivery of a good or service. All expenses are costs, but not all costs are expenses like

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those costs which are incurred in acquisition of an income-generating asset.

### **Cost Leadership**

This is the strategy used by businesses to create a low cost of operation within their niche. The use of this strategy is primarily to gain an advantage over competitors by reducing operation costs below that of others in the same industry to increase the profit margin. Cost-leadership strategy is one that dictates the firm has the lowest costs for a given product. The concept explains that only one firm can be there as a cost leader. While there may be competition to obtain the position of lowest cost, only one firm can be the lowest. The low cost strategy means the firm has driven down its production and overhead costs to the bare minimum. These cost cuts can occur in various ways. Efficient facilities, experience, and control of customer accounts can help to decrease in the costs. This is in addition to the normal waste cutting that firms do. The goal is to have the lowest average cost per unit in the entire industry. Cost leadership is organising all resources around producing goods and services at the lowest cost possible. By having the lowest costs associated with providing the products, organisation can put its business in the unique position of being able to charge the customers at the lowest price in the market for those products. It should be noted that cost leadership and price leadership are two different concepts and it is also not necessary that a firm has both types of leadership.

### **Literature Review**

#### *Sustainable Price-Leadership*

According to Ben Baldaza it means 'Delivering More Than Low Cost'. He explained that an organisation should also give weight age to those factors which can affect the preferences of consumers.

#### *Cost Leadership & Strategy Marketing by,*

M. Scillyhas explored the cost leadership strategy position. Only one firm in an industry can have this strategy, implying all other firms should adopt the differentiation or focus strategies. There are tremendous advantages to having and maintaining the low cost position but there are also some big negatives. A low cost firm has to be constantly vigilant about the low cost position. If the low cost firm gets replaced, the firm must fight to maintain the position by cutting more costs or by changing its strategy completely.

#### *Shift from Cost Management to Cost Leadership*

This article explained about shifting of cost management to cost leadership. Cost leadership is reflected in a culture that, independent of macroeconomic circumstances, pursues a low cost high-quality, customer-centric approach to managing the business.

Cost leadership is characterised by the following primary criteria: (1) recognition as the lowest cost producer in one's industry, without compromise in quality or customer focus (2) dissemination of cost information with regard to customer, product, distribution channel, and the like that is timely, understandable, credible, and actionable and is made available to decision makers to fuel continuous improvement; and (3) aggressive and balanced performance targets are established across the value chain.

#### *Cost Leadership and Competitive Advantage*

Ian Linton in his article brings out importance of cost advantage to gain competitive advantage. Business can focus on different strategies, including leadership in cost, quality, innovation or customer service. Strongest advantage comes through leadership in a factor that is important to customers and difficult for competitors to match. Cost leadership means that firm the producer with the lowest costs in target market sector. That gives the ability to set lower prices than competitors while offering customers the same benefits.

#### *Price Leadership Helps Company Navigate Tough Economy*

*Trefis Team* discusses in the paper that a volatile and sluggish economic growth, customers have become more focused on product pricing in order to save money. Wal-Mart has been focused on managing its costs and has successfully passed on cost savings to its customers. This strategy has helped Wal-Mart to solidify and strengthen its presence as the largest retailer in the world.

### **Cost Leadership Strategies' Followed by Various Organisations**

#### **Wal-Mart**

Wal-Mart Stores Inc. has been successful using its strategy of everyday low prices to attract customers. The idea of everyday low prices is to offer products at a cheaper rate than competitors on a consistent basis, rather than relying on sales. It is able to achieve this due to its large scale and efficient supply chain. They source products from cheap domestic suppliers and from low-wage foreign markets, which allows the company to sell their items at low prices and to profit off thin margins at a high volume. It uses its enormous size and buying power to generate pressure on its suppliers to sell goods at low prices. In return, suppliers have an incentive to sell a large volume of goods. The company then passes these savings to its customers. The company enjoys a significant influence on its supplier enterprises, since they depend on it for a significant part of their sales. It has successfully influenced companies like General Mills to reduce costs by implementing redesigns of its products and packaging.

## **McDonald's**

The restaurant industry is known for yielding low margins that can make it difficult to compete with a cost leadership marketing strategy. McDonald's has been extremely successful with this strategy by offering basic fast-food meals at low prices. They are able to keep prices low through a division of labor that allows it to hire and train inexperienced employees rather than trained cooks. It also relies on few managers who typically earn higher wages. These staff savings allow the company to offer its foods for bargain prices. They have a very specific set of competitive advantages they try to achieve. They strive to be cost leaders and offer food at prices that cannot be matched with competitors. In order to do this, store must be efficient and keep everyday operations costs as low as possible. Doing so, they allow stores to be superior to other fast food restaurants because they can serve food at lower prices than any other fast food company. Another important competitive characteristic is speedy delivery of food. In order to maintain this advantage over other fast food chains, they make the processes of cooking food simple for all employees. It must be easy to learn and easy to execute with a low failure rate to ensure the quick production and delivery of food. These two competitive advantages comply directly with the vision of the company which is as follows: "McDonald's vision is to be the world's best quick service restaurant experience. Being the best means providing outstanding quality, service, cleanliness, and value, so that we make every customer in every restaurant smile." McDonald's competitive advantages are what make it stand out when compared to other companies. These are the aspects of McDonald's are what helped it become the number one fast food distributor in the world.

## **Ikea**

The Swedish furniture retailer Ikea revolutionised the furniture industry by offering cheap but stylish furniture. Ikea is able to keep its prices low by sourcing its products in low-wage countries and by offering a very basic level of service. Ikea does not assemble or deliver furniture; customers must collect the furniture in the warehouse and assemble at home themselves. While this is less convenient than traditional retailers, it allows Ikea to offer lower prices that attract customers. IKEA is a global brand in the home furnishing market with hundreds of stores across the world.

It has a clear mission: selling a wide range of furniture and accessories at a reasonable price so that most people can buy them. By offering a wide range of assortment the key word is functionality, consumers can find everything under one roof. Its success is based on the relatively simple idea of keeping the cost between manufacturers and customers down. In order to do so, IKEA customers have to assemble the bought products themselves. That creates innovation upstream, which helps suppliers to save costs, and downstream,

as self-assembly became a large cost saver for customers. According to the firm, low cost is always a priority. This applies to every phase of their activities. IKEA emphasises several activities to keep its costs low. Instead of relying primarily on third party manufacturers, the firm's engineers design low-cost, modular furniture ready for assembly by customers. It also positions its products in domestic settings. Typically, competitor's furniture stores display multiple varieties of a single item in separate rooms, means that their customers examine living room sofas in one room, tables in another room, chairs in another location, and accessories somewhere else entirely. In contrast, IKEA's customers can view different furniture combinations in a single setting, which eliminates the need for sales associates or decorators to help the customer imagine how a furniture arrangement would look when placed in the customer's home. This approach requires fewer sales personnel, allowing the company to keep its costs low.

A third practice that helps keep its costs low is expecting customers to transport their own purchases rather than providing a delivery service. Its concept relies on customers to choose, collect, transport and assemble IKEA products themselves. Customer involvement contributes to IKEA low prices. That is the idea behind: "You do your part. We do our part. Together we save money."

### **Southwest Airlines**

The airline industry has typically been an industry where profits are hard to come by without charging high ticket prices. Southwest Airlines challenged this concept by marketing itself as a cost leader. Southwest attempts to offer the lowest prices possible by being more efficient than traditional airlines. They minimise the time that their planes spend on the tarmac in order to keep them flying and to keep profits up. They also offer little in the way of additional thrills to customers, but pass the cost savings on to them. Working with the suppliers is an important part of managing the overall waste cycle. Every day, office products such as printer cartridges and toners can quickly accumulate and negatively impact on environment. Company is are devoted to finding Suppliers who meet their levels of Customer Service and high standards of efficiency and help them to achieve the commitment to Supplier Diversity.

Southwest's current strategy is to position itself as a cost leader with a focus strategy. The company's management and employees aim to cost-effectively and reliably fly large number of customers on short, non-stop flights, and to have fun doing it. They are devoted to making flying available to everyone. The company has been successful in implementing this strategy, having experienced strong growth and profitability. The main strategic issue facing Southwest at this time is to evaluate this strategy and determine its future course of action.

## Ford

Ford has chosen marketing strategy of Ford Focus – their flagship car. This will mean that the one car will be sold and promoted generically across the globe, rather than adapting the product and promotional material to suit local tastes. It is very unusual for a global firm to come out and state they are going to take a standardised approach. The company has adopted a global corporate strategy named 'One Ford' that has been adopted to make the company more efficient and benefit from cost-reducing economies of scale. Hence, the logic is simple enough: by producing just one standard product to satisfy all of their customer's needs – as ambitious as it sounds – there are substantial cost savings to be made. Economies of scale are not just about reducing operating costs. Marketing economies of scale are the benefits of having a large, simultaneous marketing strategy across the globe. It enables a more coherent message to be conveyed to consumers. And, in the case of the new Ford Focus, the benefit being sold to consumers is technology. The focus has been on improving processes. Low cost manufacture at Dagenham has been developed in a way which has greatly improved site competitiveness. In 1995, a specialist unit was introduced in the Dagenham plant called the Plant Vehicle Team (PVT). Its function was to concentrate on two key areas:

1. To examine all processes, evaluating the total cost of design, plant manufacturing processes and activities with a view to eliminating waste and reducing cost; and
2. To establish processes which focus on customer, address their concerns and implement permanent solutions, within 90 days.

The savings opportunities have been generated from many sources, like engineers evaluated a plant process involving the receipt of completed doors from Ford's Cologne Plant, due to damage in transit. It transpired that the completed doors were difficult to transport from Germany to Dagenham. The solution to improve the process was to ship in the components and weld at Dagenham. This resulted in improved pack density when transporting, reduced scrap and improved quality, which reduced the total cost of door manufacture. The PVT has proved to be so successful in improving value and improving quality, that it has been adopted by all Ford plants.

## Conclusion

To survive in this competitive world being a cost leadership is important strategy. In order to bring in the customer delight companies need to satisfy the customers in terms of quality as well as price. Cost – Leadership is one of the important strategies of the business organisations. In order to gain the competitive advantage in terms of cost the business organisations should minimise the cost from all the possible corners. Optimal utilisation of

all the resources in the organisation minimisation of wastage and defective products, quality management techniques all these factors help the business organisations to achieve cost leadership. Business organisations can achieve competitive advantage through low cost strategy. Lesser the cost more demand will be created, increase in demand leads to increased sales in turn increased revenue finally leads to increased profitability.

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