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Instructor's Manual for
Essentials of

STRATEGIC MANAGEMENT

The Quest for Competitive Advantage

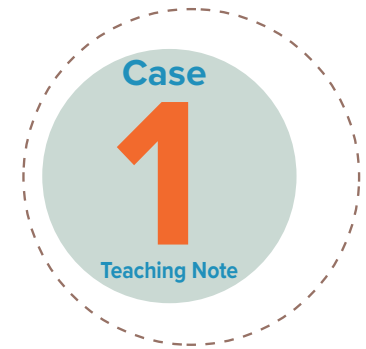


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Airbnb, Inc. in 2017*



Overview

Airbnb was founded in 2008 when Brian Chesky and a friend decided to rent their apartment to guests for a local convention. To accommodate the guests, they used air mattresses and referred to it as the ‘Air Bed & Breakfast.’ It was that weekend when the idea; and the potential viability; of a peer-to-peer room-sharing business model was born. While it was not yet a publicly traded company, by 2016 Airbnb had seen immense growth and success in its eight-year existence. The room-sharing company had expanded to over 190 countries had more than two million listed properties, and enjoyed a market valuation estimated at \$30 billion. Airbnb appeared to be disrupting the hotel and tourism industry through its business model that allowed hosts to offer spare rooms or entire homes to potential guests, in a peer-reviewed digital marketplace.

This case is meant to introduce students to the sharing economy. Students can evaluate and compare and contrast Airbnb’s business model with traditional models employed by bed and breakfast and hotel chain operators. Instructors should note that technology and the legal environment can lead to opportunities, as well as challenges for an upstart like Airbnb. The case opens and closes with quotes from CEO and co-founder Chesky, as a method to juxtapose for students how rapid advances in technology can lead to changes in competitive strategies for business, yet, how the legal environment can both lag behind, and be used to obstruct such strategies.

The case provides an overview of the accommodation market (i.e. hotels, motels and bed & breakfasts) to illustrate such strategic considerations as competitors; both large and small; and market segmentation, into recreational, business, and meetings. The case then presents the comparative costs of operating traditional hotels/motels to bed and breakfasts to illustrate Airbnb’s potential to attain and sustain competitive advantage using its technology-based business model. Yet Airbnb faces continuing challenges to obtain permits and overcome regulatory barriers. While it continues to demonstrate a growth trajectory that could result in an IPO, Airbnb will need to develop new strategic approaches to build out its model and surmount competitive forces.

Suggestions for Using the Case

Students should find Airbnb in 2017 an interesting case because of their own experiences with smartphones and companies such as Lyft or Uber or Airbnb. We recommend using the case immediately following your coverage of Chapter 1. As this case specifically addresses the sharing economy, it lends itself well to discussions of smartphones, technology and their impact on competitive positions for both new and incumbent competitors. It may also lead to discussion of disruptive innovation.

We believe that Airbnb in 2017 is an excellent leadoff case for the course (another good choice is Robin Hood)—which also requires that students draw upon the material covered in Chapter 1). The case is ideal for exploring the concepts of sustainable competitive advantage, competing differently, and business models. Instructors can drill students on such topics as customer value proposition and profit formula and compare and contrast Airbnb’s approaches with those of traditional lodging operators.

*This teaching note primarily reflects the thinking and analysis of Professor John D. Varlaro, Johnson & Wales University. We are most grateful for his insight, analysis and contributions to how the case can be taught successfully.

The assignment questions and teaching outline presented below reflect our thinking and suggestions about how to conduct the class discussion and what aspects to emphasize.

To provide students with guidance in what to think about and which analytical tools to utilize in preparing the Airbnb in 2017 case for class discussion, we strongly recommend providing class members with a set of study questions and insisting that they prepare good notes/answers to these questions in preparing for class discussion of the case.

To facilitate your use of study questions and to make them available to students, we have posted a file of the assignment questions contained in this teaching note for the Airbnb in 2017 case in the instructor resources section of the Connect Library. (We should also point out that there is a set of study questions posted in the student section of the OLC for each of the 12 cases included in the 6th Edition.)

You may also find it beneficial to have your class read the Guide to Case Analysis that is also posted in the instructor resources section of the Connect Library. Students will find the content of this Guide particularly helpful if this is their first experience with cases and they are unsure about the mechanics of how to prepare a case for class discussion, oral presentation, or written analysis.

Videos for Use with the Airbnb in 2017 Case. There are two videos that you may consider having students view prior to class discussion of the case (or you may choose to open the class discussion with one of the two videos). Both videos are posted at YouTube and can be accessed through the following links:

- Airbnb's International Growth Strategy is a 5:04 minute video posted at YouTube (<https://www.youtube.com/watch?v=QsF4VHriFFY>).
- Airbnb's VP of Product on Growth and Planning for the Future is a 6:40 minute video posted at YouTube (<https://www.youtube.com/watch?v=o1RMH8WQtAQ>).

Because the case is relatively short, it is well suited for use as a leadoff case on the first day of class, or for an in-class written case, or a final exam case. Our recommended questions for written assignments are as follows:

1. JW Marriott has asked you to assess the threat of Airbnb. Please prepare a 5-6 page report that includes a description of both Marriott's and Airbnb's business models, with an emphasis on an evaluation and comparison of disparate customer demands and user profiles. JW Marriott's management also asks that you make a recommendation as to how best to mitigate the growing appeal of Airbnb, and how to potentially reach millennials and other potential users of Airbnb.
2. As a new member of Airbnb's management team, you have been asked to prepare an analysis of its competitive position and potential threats. Your 2-3 page executive summary should list strategic issues confronting Airbnb and make recommendations to address both opportunities and challenges. The executive summary should be supported by your analysis of the lodging industry.

Assignment Questions

1. How would you illustrate and compare the business models for Airbnb, large hotels chains such as Marriott and Hilton, and bed & breakfast operators? Use the example chart in the textbook for business models as a guide (Concepts & Connections 1.1),
2. What are the general strengths and weaknesses of large, hotel chains such as Marriott and Hilton, bed & breakfasts, and Airbnb? Explain how you would compare and contrast those businesses.
3. In what ways has the lodging consumer changed, and how does Airbnb's customer value-proposition meet this change?

4. What key factors may determine the success or failure of Airbnb?
5. What recommendations would you make to Airbnb to improve its competitiveness in accommodation market while mitigating any current and future risks?

Teaching Outline and Analysis

1. How would you illustrate and compare the business models for large hotels chains such as Marriott and Hilton, bed & breakfast operators, and Airbnb? Use the example chart in the textbook for business models as a guide (Concepts & Connections 1.1),

Students should be able to identify the following:

	Chain Hotels/Motels	Bed & Breakfast (single proprietor)	Airbnb
Customer Value Proposition	<ul style="list-style-type: none"> • Familiar brands • International brands to which customers are accustomed and potentially feel affinity and loyalty • Global reach with loyalty programs 	<ul style="list-style-type: none"> • One location, offering unique, local accommodation • Intimate accommodation, with proprietor sometimes serving multiple roles, including ambassador to area • If in rural area, may be only accommodation 	<ul style="list-style-type: none"> • Use of technology to which users are familiar • Shorter, more intimate stays • Varying and different locales in which to stay, both local and international reach • Cheaper accommodations • Unique accommodations
Profit Formula	<ul style="list-style-type: none"> • Revenue generation dependent on renting rooms and overall occupancy • Cost structure extensive, composed of wages and high fixed costs associated with the purchase and upkeep of multiple physical assets/ locations • Other costs would include food and beverage, marketing, taxes, licenses • Global costs further complicate structure, including operating across multiple legal and physical jurisdictions 	<ul style="list-style-type: none"> • Revenue generation dependent on renting rooms and overall occupancy • Cost structure associated with operating brick and mortar physical location, food and beverages, marketing • Possibly wages if large enough to necessitate staff 	<ul style="list-style-type: none"> • Revenue generation transaction fee charged to users whom offer and rent accommodations through app • Cost structure associated with developing and updating software and technology, as well as marketing and wages for engineers, professional management and staff
Profit Margin	<ul style="list-style-type: none"> • Dependent on generating sufficient revenues across multiple locations to cover fixed and variable costs globally. Profitable locations may be used to offset losses and unprofitable locations 	<ul style="list-style-type: none"> • Dependent on generating revenues sufficient to cover fixed and variable costs. Lack of profitability several jeopardizes business as owned by sole proprietor 	<ul style="list-style-type: none"> • Not contingent upon the fixed costs associated with operating hotels/bed & breakfasts. Instead, profitability associated with percentage of revenue generated by all participating users offering accommodations

Students should be reminded that, as stated in Chapter 1 of the text:

- ***The appeal of a strategy or business model that yields a sustainable competitive advantage is that it offers the potential for an enduring edge over rivals.***
 - However, Chesky as CEO must be willing and ready to modify the strategy in response to the unexpected moves of competitors, shifting buyer needs and preferences, emerging market opportunities, new ideas for improving the strategy, and mounting evidence that the strategy is not working well.
 - Most of the time, a company’s strategy evolves incrementally as management fine-tunes various pieces of the strategy and adjusts the strategy to respond to unfolding events.

Here is a good opportunity to ask students to compare and contrast the strengths and weaknesses of Airbnb’s business model to those of its direct competitors.

2. What are the general strengths and weaknesses of large hotel chains such as Marriott and Hilton, bed & breakfasts, and Airbnb? Explain how you would compare and contrast those businesses.

Students should be able to identify the following:

	Large Hotel/Motel Chains	Bed & Breakfast (single proprietor)	Airbnb
Strengths	<ul style="list-style-type: none"> • Familiar, international brands • Brand loyalty • Global reach • Perception of safe, comfortable and/or reliable accommodations • Corporate accounts 	<ul style="list-style-type: none"> • One location, offering unique, local accommodation • Intimate accommodation, with proprietor sometimes serving multiple roles, including ambassador to area • If in rural area, may be only accommodation 	<ul style="list-style-type: none"> • No fixed costs associated with operating hotels, thus greatly reduced cost structure • Leveraging technology when consumers are more smartphone dependent • Market leader perception in technology • Ubiquitous, as user can access anytime through app • Offering both low-cost accommodations, as well as unique experiences
Weaknesses	<ul style="list-style-type: none"> • High cost structure, further exacerbated by global operations and presence • If consumer has bad experience with one location, all locations may be viewed as terrible • Need at times to compete on price through discount offerings 	<ul style="list-style-type: none"> • Revenue generation dependent on renting rooms and overall occupancy, highly associated with travel trends in the area • Cost structure which is highly sensitive to fluctuations, as a sole proprietor has very little room for shifts in revenue and costs 	<ul style="list-style-type: none"> • Perception of at times unsafe experiences • Users may be hesitant to use Airbnb in specific locations, opting for a more familiar brand • Legal exposure through individual users not following laws, such as anti-discrimination • Legal exposure as cities and towns determine if renting rooms through Airbnb is legal, and the potential for it to be illegal • Business model is relatively easy to copy, as demonstrated by Uber and Lyft in the ride-sharing space

Here is a good opportunity to recap Chapter 1 and also preview some concepts covered Chapter 2:

- ***In choosing among opportunities and addressing the hows of strategy, strategists must embrace the risks of uncertainty and the discomfort that naturally accompanies such risks.***
 - Bold strategies involve making difficult choices and placing bets on the future.
 - Good strategic planning is not about eliminating risks, but increasing the odds of success. In sorting through the possibilities of what the company should and should not do, managers may conclude some opportunities are unrealistic or not sufficiently attractive to pursue.
 - However, innovative strategy-making that results in a powerful customer value proposition or pushes the company into new markets will likely require the development of new resources and capabilities and force the company outside its comfort zone.

That an innovative strategy has its basis in a powerful customer value proposition leads nicely into the next question.

3. In what ways has the lodging consumer changed and how does Airbnb's customer value-proposition meet this change?

Students should be able to identify the following changes in the profile of lodging customers:

- ***Desire for unique experiences, not focused on ownership.*** Students should be able to discuss their experiences as consumers of the sharing economy (not only with Airbnb, but also Uber, Lyft, and other similar companies).
 - Airbnb provides customers with opportunities to experience multiple, unique accommodations not typically associated with larger chain brands.
 - Smaller sole proprietors such as bed & breakfasts may be accessed through the app.
 - Those offering accommodations share in the desire to not only have a unique experience with a guest, but also to invite a stranger into their own home or apartment.
- ***Desire to access experiences immediately through smartphone technology.*** Students should note that a company like Airbnb could only exist since the advent of Internet and smartphone technologies.
 - Apps and smartphones have provided the consumer the opportunity to have immediate access, such as purchasing songs immediately only after hearing them on the radio, or even the simple act of “googling” and looking-up information.
- ***Familiarity with apps and fluency with life/smartphone integration.*** Consumers—especially the Millennial age group (i.e. those consumers born between the early 1980s and the early years of the 21st century)—are less technology averse, use smartphones and apps, and are more willing to experiment and embrace the “experience economy” than previous generations, and this trend should continue to occur.
 - As younger generations whom have used smartphones from childhood age and get older, technology and businesses such as Airbnb will seem less unusual and more commonplace.

Students should conclude that these consumer changes position Airbnb very strongly to compete effectively, especially given its unique business model (as identified in Question #1).

4. What key factors may determine the success or failure of Airbnb?

Factors that are necessary for competitive success for Airbnb:

- **Mitigation of legal threats.** Any regulation that inhibits or prevents Airbnb users from offering their rooms on Airbnb represents a significant barrier. Students should observe that:
 - Both domestic and international legislation did not account for, and had yet to catch up to, more progressive and potentially disruptive business models utilized by companies like Airbnb.
 - Complicated legal issues existed at the local, state, and federal levels, both within the U.S. and outside the U.S.
 - Competitors, among them sole proprietor and large hotel chains, had already invested, and would most likely continue to invest in, lobbying to exclude Airbnb and create severe barriers to its expansion and growth.
 - While communities and jurisdictions might well bar or set quotas for the number of Airbnb permits to operators, Airbnb could promote the fact that its operators added to local revenues through occupancy taxes, as well as the probably economic multiplier effects that would also benefit local restaurants, retailers, and tourist attractions.
- **Use of smartphone and other technology for differentiation.** Due to its business model, Airbnb was already differentiated from traditional competitors. In addition, continuing innovations based on current and emergent technologies were essential to maintaining current users, while expanding into new users. Students should also recognize that user experience with the app, including ease of use, was an essential component of its competitive advantage. Students should be reminded that:
 - Most large hotel and motel chains as well as consolidators such as Priceline, HotelTonight, Hotel.com, and VRBO (Vacation Rental by Owner) also offered mobile apps that provided booking and ratings portals in direct competition to Airbnb.
 - According to case Exhibit 1, B&Bs in the United States catered primarily to domestic travelers in 2015, while 20% of recreational travelers coming from abroad apparently frequented hotel and motel chains, so Airbnb may have an opportunity to capture some of the international segment.
 - Inasmuch as Airbnb operates as a global enterprise, it is exposed to political and regulatory and currency risks that could impact fee revenue generation in both domestic and international markets.
- **Expansion of Users and Accommodations.** Overall expansion of users who offer accommodations and those who use Airbnb to book accommodations was critical to its success. Students should observe that:
 - While continued growth will be necessary to ensure profitability, it is not clear that Airbnb can sustain triple- or even double-digit growth rates over the long term.
 - Although Airbnb's estimated revenues were estimated to maintain a steady growth path out to 2017, growth in bookings was projected to decline at an incremental rate in 2016 and 2017 (exhibit 3).
- **Brand image.** Image was also a critical factor in helping consumers choose which accommodation to patronize. Included within this image was reliability, quality of stay and safety. Students should observe that:
 - Given the sheer immensity of the user base, and how each location represented a unique offering, Airbnb had a significant challenge in continually ensuring both quality and safety when consumers used Airbnb.

- While Airbnb achieved break-even profitability in 2016, it may want to revisit and revise upwards the expenses allocated to safety and quality as well as its efforts to prevent discrimination against customers and operators. (See exhibit 2 for the ranking of expenses incurred by B&B operators vs. hotel and motel chains).
- **Financial health.** Rapid growth businesses require capital. While case mentions a 2016 cash infusion of \$850 million in Airbnb and a pre-IPO valuation of about \$30 billion (see exhibit 4), the fact that the company only recently reached break-even signals the need for permanent capital to continue to scale its business model. Students should observe that:
 - It is unclear whether or not the \$30 billion valuation is realistic or due to a “tech bubble.” A severe downturn in the financial markets could result in the closing of the window for future IPOs and greatly impact Airbnb in its effort to scale.
 - Airbnb’s \$30 billion pre-market valuation still lags behind Marriott’s (\$40 billion), but Marriott is an established company (see exhibit 4) and is now growing by acquisition.
 - Students should note that Airbnb’s estimated revenues in exhibit 3, while slowing incrementally, remained strong.
 - Airbnb’s cost structure combined for a very solid competitive position.

Instructors may choose to foreshadow a key learning outcome from Chapter 2 here: A company’s vision, objectives, strategy, and approach to strategy execution are never final; managing strategy is an ongoing process, not an every-now-and-then task.

5. What recommendations would you make to Airbnb to improve its competitiveness in accommodation market while mitigating any current and future risks?

- Continue to lobby and advocate for friendly legislation as it did in 2015..
 - Identify business organizations, such as chambers’ of commerce, as large, pro-business groups could be leveraged to gain legislative support.
- Attract and enroll single-proprietor establishments, and devise methods to provide added value for such businesses, e.g. in utilizing Airbnb as a platform for marketing and offering accommodations.
 - Doing so could mitigate the legislative risk while growing the user base and potential future revenues.
 - Doing so could also enable Airbnb to leverage its investments in technologies such as yield management and dynamic pricing systems across a wider base of proprietors.
- Pursue the business traveler segment (exhibit 1), as it is an essential component of the market,
 - Business travelers and extended stay guests present opportunities for increased user base and revenue growth.
 - However, given Airbnb’s current position, it is not as business friendly as rival hotel/motel chains, has not developed a customer loyalty program, and would need potentially need to change its user interface and invoicing systems to accommodate corporate accounts.

- Make continued investments in technology to maintain its differentiation/focus generic strategy.
 - These investments will not only be in smartphone and computer interfaces, but also in emergent technologies that employ big data and customer preference algorithms.
 - For example, some students might discuss how virtual reality (VR) could be leveraged to market accommodations, or even improve brand aspects such as quality and safety.
- Find ways to mitigate competition between larger hotels and Airbnb. This can reduce legislative and competitive risk, while potentially expanding user base and revenues.
 - For example, students might suggest that Airbnb create a user interface that refers customers seeking lodging in high demand locations (such as resorts and cities) to established chain hotels during peak periods when regular Airbnb rooms are unavailable.
 - Students could argue that by doing so, Airbnb mitigates legislative risk and competitor retaliation, while also expanding into the business segment with minimal internal changes and investments.

Instructors can wrap-up the discussion by asking students if they strongly feel that CEO Chesky could well suffer from an “If it ain’t broke don’t fix it” mentality, that is, will Airbnb continue “business as usual,” and if its revenue and bookings growth rates continue on their current declining trajectories, will the company likely make slower progress towards its goal of achieving a competitive advantage and superior returns, as reflected in an IPO or possible sale to a rival technology or lodging firm?

Chesky and his team may also be betting on rather slim odds that:

- Other rivals in the online lodging industry will not identify the same emerging segments for “sharing economy” accommodations.
- Rivals will not copy Airbnb’s business model and then strive for a low cost provider strategy in Airbnb’s current niche.
- Rivals will not catch up and perhaps overtake Airbnb on service and prices to both buyers (guests) and sellers (proprietors of lodging establishments).

Remind students that Airbnb’s handling of the strategy implementation process can be considered successful *if* things go smoothly enough that the company meets or beats its strategic and financial performance targets and shows good progress in achieving management’s strategic vision.

Epilogue

More recent news on Airbnb can be found at: <https://press.atairbnb.com>.