Journal of Advanced Academic Research and Studies 高等学术研究期刊
Vol. 1, No.5, Mayl 2024 (pp. 1-6)
http://www.nlbaeai.org/

ISSN 3006-4007 (Print)
ISSN 3006-4015 (Online)

Seeking concentration or survival strategies for the next decade

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Received 01 December 2023, Revised 25 February 2024, Accepted 1 May 2024

Abstract

Purpose – Concentration could very probably become the prime strategy mode of the following decade. Technology is assuming a key role here. Many markets could become the ultimate domain of four or less players especially those where technology plays a key role. The trend is visible. Take key industries as semi-conductors and watch the concentration level according to the USA Census. Recent data reveal indeed a continuity of the trend and an even greater measures of concentration in industries as semi-conductors, electronic components and computing. The question arises, then, what is the conceptual framework of this concentration and what strategies lie behind it.
Design/Methodology/Approach – The article starts with an identification of the managerial and economic boundaries of the concept of concentration. It then proceeds to identify concentration strands and varieties. This is followed by an analysis of the strategies of concentration. The article provides a link between economic theory and strategic thinking. It further suggests a segmentation of concentrative behavior and a number of strategic tools for this. It further provides a number of examples of industries where this concentrative behavior have demonstrated results.
Findings – The article is qualitative research. Many of the resulting observations and deductions are hypotheses that could be supported by further research.
Research Implications – The article relies on classic work on oligopolistic competition and relates that to contemporary corporate strategic behavior as evidenced by case histories of identified key corporations.

Keywords: strategies,semi-conductors,concept of concentration,qualitative research
JEL Classifications: L2,G3,L1,O3

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I. Introduction

Concentration connotes the existence of a few major competitors within a given industry. Two measures of concentration are commonly cited: the concentration ratio and the Herfindal Index. Concentration ratios relate the combined market shares of the four largest firms in the industry to aggregate industry sales (or an identical measure of size variable relationship). The Herfindal-Hirschman Index squares the market shares of the respective firms and aggregates the squares. Whatever the measure, markets are ultimately segmented into competitive, moderately concentrated, concentrated and highly concentrated. (Scherer, 1970)

II. Concentration: a proposed conceptual framework.

1. Concentration as a derivative of kinked demand.

It is the authors contention that concentration can be expressed in terms of kinked demand curves.

Concentration is an expression of a state of oligopoly within an oligopolistic market structure. Oligopolistic competition, is that where players are few, profits are maximized, prices are set, entry and exit barriers are enhanced, non-price competition is potent and trust among the operators is lost.Nashs equilibrium construct illustrates the later (Nash, 1950). It is a distinctive state of interdependence where few large firms possess the ability to influence market conditions and keep other players in check. Oligopolistic markets are commonly represented by a kinked demand curve or a curve embodying two stages of price elasticity.The elastic segment implies a substantial revenue change in response to a measure of price adjustment. The inelastic or less elastic segment embodies the limited consequence of a price adjustment. The less elasticity segment of the kinked demand curve reflects the paralyzing power of reciprocity and fear from a dire retaliatory response by a key oligopolist. The "kink" represents the point where a shift occurs. It is a point where a competitive or a mildly concentrated industry becomes concentrated or highly concentrated.

A strategy of seeking concentration is that where the player or players embark upon moves that would limit the number of competitors to a specific high concentration norm and create, in the process, forbidding entry barrier.It is a strategy that moves the entire industry towards the inelastic slop of the kinked demand curve.

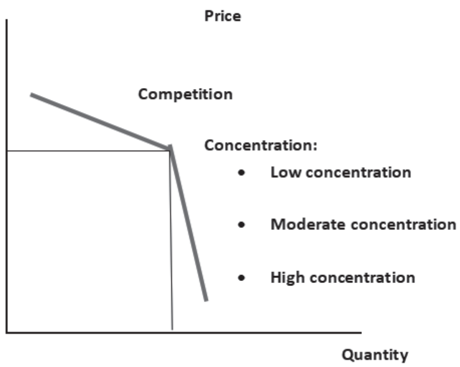

Figure1. A concentration-based kinked demand curve

Several industries demonstrate this propensity to concentrate in, specially, the United States. United States census of 2007 illustrates this high measure of concentration in the American industry. More recent data reflects the same state and, at times, an increase in the propensity. It goes without saying that search for concentration is usually motivated by a mix of goals from a desire for high returns to market dominance and technology superiority.

2.Observed patterns of concentration behavior

Concentrative behavior could take a variety of shapes. There is absolute concentration and partial concentration, reversible concentration and permanent concentration, dynamic concentration and static concentration.

2.1 Absolute vs. partial concentration.

Absolute concentration is a state of ultimate dominance within the respective industry. Absolute concentration has been, and still is, the favorite strategy for many a multinational corporation. The practice cuts across a wide variety of industries from Mittal Arcelors steel (scale concentration) to Gillette (market share concentration) and from Nokia (brand concentration) to Singapore airlines (capital resource concentration).

Absolute concentration could take any of the following states:

Capital resource concentration

Scale concentration

Brand concentration

Market share concentration.

Partial concentration is a concentration based on a specific strategic competitive advantage be it the product, the technology, the market segment or the market area. Partial concentration has many followers. There is Lehmans Mini Bond, a structured finance product (product concentration), Gillettes Mach 3 (technology concentration), Lenovos Chinese market desk top computer (market area concentration) and the emerging Shanghai Stock Market IPO dominance (market segment concentration). Partial concentration could take any of the following states:

Product concentration

Technology concentration

Market segment concentration

Market area concentration

2.2 Reversible vs. Irreversible Processes-permanent concentration

Reversible concentration is a state of temporary dominance followed by a return to the fragmentation that preceded the concentration event. Reversible concentration is, more frequently than not, an induced strategy emerging, most likely, as a consequence of events. As those events take a different turn the foundations of the concentration strategy unravel as the Sony Ericsson history proves. Sony and Ericsson alliance was based on a brand and technology synergy that worked for some time and ceased to work afterwards. Reversible concentration could take any of the following states:

Time bound concentration
Brand concentration
Fragile alliance concentration

Permanent concentration is a state of dominance that is likely to continue for an unforeseeable period of time. Dying industries provide a sound base for a permanent, or as permanent as the life span of the dying industry allows concentration. Capital based concentration could best be traced in the case of Apple or Singapore Airlines, for that matter. Both maintained dominances, and a high concentration, in their respective industry made very plausibly possible by abundant capital resource. Proprietary technology concentration existed for a long time in the case of Kodak and, prior to that, Polaroid. Permanent concentration could take any of the following states:

End game industry concentration
Proprietary technology concentration
Capital based concentration

2.3 Dynamic vs. static concentration

A state of dynamic concentration is that where concentration changes shape with the passage of time or the evolvement of events. A dynamic competency-based concentration could connote a shift from one type of competency concentration to the other or, alternatively, the combination of both. Dynamic concentration could take any of the following states:

Progressive concentration
Competency based concentration
Acquisition and divestment-based concentration

Static concentration is a permanent state of concentration that is unlikely to change in the medium term. Static concentration could take any of the following states:

Absolute competency advantage concentration
High entry barrier concentration
High exit barrier concentration

Summarizing, concentration strategy is a strategy with different dimensions depending on a variety of market, technology, function and capital conditions.

III. From concentration to strategic behavior

Seeking concentration connotes the search for strategic modes of dominance of an industry. Those modes could be "regular" or related to practices conducted in the course of day-to-day business or "innovative". Or modes based on an exploitation of unique events or opportunistic market conditions. Regular practices include merger and acquisition, be it markedly aggressive and distinctly expansive. Innovative modes would include opportunistic venues whose practice is directly tied to a narrow span of time or discontinuous market conditions.

Concentration strategies could follow any or all of the following strategies.

Aggressive acquisition

Invoking disruptive technology

Innovation.

Collusion

Several highly concentrated companies and industries demonstrate one or the other of those strategies.

US Search engines industry is one of those. Top four operators market share amounts to a near 98%, according to some estimates.

This industrys concentration has increased steadily driven by Googles growth and the parallel decline of smaller search engines like Ask.com and AOL It is difficult for new operators to enter the industry because of several factors including limited access to software and related hardware. Search engines require, moreover, substantial computing resources for ongoing operation and sophisticated software algorithms to handle indexing and relevancy tasks. The industry is continually investing in innovation by developing new features, new matching and relevancy algorithms, new tracking capabilities and new advertising performance measurement abilities.

Another example is soda drinks where top US three operators market share is put at a near 90% divided between Coca-Cola, Pepsi and Dr Pepper. Major players particularly Coca-Cola and Pepsi, engage in significant marketing and brand promotion to generate brand loyalty, which translates into significant market share and higher concentration. Additionally, Coca-Cola and Pepsi have gone through structural changes allowing for the incorporation of bottlers operations into their company structure. This bottler merger did and is increasing concentration.

A third example is the US lighting industry where top four operators market share adds up to more than 90% according to some estimates. General Electric, Philips and Siemens share this market share.

Global brand recognition, along with established relationships with major customers, has allowed this industry to be dominated by a few key players. Industry concentration has been on the rise due to mergers and acquisitions. In addition to the dominance of existing players, government regulation, resource constraints and, technological shifts made it difficult for new companies to enter the industry (Top 10 Highly Concentrated Industries IBISWorld Fri, Feb 10, 20).

IV. Concluding remark

Concentration is a complex process with several varieties and many strategic modes. It is the authors contention that concentration, as a strategy, will dominate as a result of the penetration of technologies that will alter the foundations of business. Artificial intelligence will render may driving forces of business dynamic and elusive. This will narrow business arenas and induce concentration.

V. Summary and conclusions

Concentration connotes the existence of a few major competitors within a given industry.

Concentration could very probably become the prime strategy mode of the following decade. There are several types and degrees of concentration from the partial to the complete and from the permanent to the reversable. Technology is assuming a key role in the emergence and continuity of concentration. Many markets could become the ultimate domain of four or less players especially those where technology plays a key role. The trend is visible. Take key US industries such as search engines and watch the concentration level. Take other industries as soda drinks and light bulbs and observe the pattern of concentration too. Recent data reveal indeed a continuity of the trend and an even greater measures of concentration in industries as semi-conductors, electronic components and computing.

The article suggests a conceptual and operational framework for this concentration and proposes a number of strategic behaviors leading to a level of concentration. Those include merger and acquisition and the advent of disruptive technology.

It is the authors contention that concentration, as a strategy, will dominate as a result of the penetration of technologies that will alter the foundations of business. Artificial intelligence will render may driving forces of business dynamic and elusive. This will narrow business arenas and induce concentration

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