Rolls-Royce

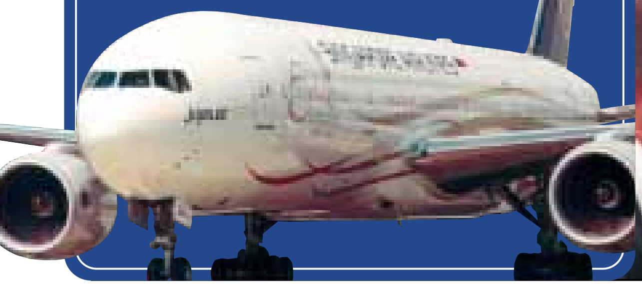
Competing within a changing world

INTRODUCTION

No business today operates in a complete vacuum unaffected by **market forces**. By their very nature business activities are competitive. Within a dynamic, rapidly changing business environment producers are constantly entering and leaving the market. At the same time, changing customer preferences provide signals for businesses to develop new strategies with different products and services. Some businesses will succeed by responding to and meeting market needs, while others may not perform quite so well.

Few markets have changed in recent years as much as civil aerospace. Ten years ago 950 million people travelled by air, five years ago they numbered 1.1 billion, and the total is set to climb to 2.5 billion by 2009. The aviation industry provides more than 24 million jobs worldwide, while its contribution to the world economy is estimated to rise to $1,800 billion by 2009. Today, one-third of the world's manufactured exports are transported by air. Twenty years ago the proportion was just one-tenth.

Growth in civil aviation markets has stimulated the competition between the businesses that operate in it such as the airlines. This has a knock-on effect on their suppliers – the aeroplane manufacturers and in turn on their suppliers – the engine manufacturers. Rolls-Royce is one of only three engine manufacturers in the world that has a proven capability to design, develop and produce large gas turbine aero-engines. In recent years the company has faced many challenges that have affected its position in the aero-engine industry. By providing an analysis of the competitive environment affecting Rolls-Royce, this case study illustrates how such information is being used by the company as it works towards its vision of becoming the world's first choice for power solutions for the new century.



Rolls-Royce plc

Rolls-Royce has not made motor cars since 1971. Rolls-Royce and Bentley Motor Cars Limited is owned by Volkswagon but exclusive rights to use the Rolls-Royce name for motor vehicles will pass to BMW in 2003.

The Rolls-Royce group is a **global business** with customers in 135 countries and production facilities in 14 countries. It employs around 40,000 people focused upon the present and future requirements of civil aerospace, defence, marine and energy markets. It has 56,000 aero engines in service with 300 airlines, 2,400 corporate and utility operators and supplies more than 100 armed forces. The engines are used in all sizes of commercial aircraft from business jets to the largest modern airlines made by the two main aeroplane manufacturers Airbus Industrie and Boeing.

As one of the most powerful brands in the world, Rolls-Royce symbolises a promise to deliver reliability, integrity and innovation to buyers and users.

The changing context

The commercial aero-engine business of Rolls-Royce operates within two distinct market sectors. These are:

- new engine sales to the two manufacturers such as Airbus Industrie and Boeing, as well as airlines;
- engine parts sales to airlines who service and maintain aircraft. Competitors in this secondary market include specialist maintenance companies.

The new engine market is the **primary market,** which provides access to the **secondary market** for the sales of engine parts.

During the 1970s, Rolls-Royce controlled less than 10 per cent of the civil aerospace market. The sector was characterised by intense commercial and technical competition from General Electric and Pratt & Whitney of the USA. Market share could only be increased by major investment in new engines, and developing an improved range of services for customers. This required the company to become focussed on service rather than products with services such as information management, inventory management and on and off wing maintenance.

The aero-engine market is **vertical** with a limited number of buyers. The customers of Rolls-Royce need to satisfy both their future and present needs. In the past, decisions about aero-engines were largely based upon cost and efficiency. However, in today's more competitive environment, Rolls-Royce's customers look for a much more complete service. Buying an aero-engine is a long-term decision. In this very competitive environment, a key element is **relationship marketing**. Through this process, Rolls-Royce and its staff have learned to develop activities and services that build good relationships with its customers.

Improving service

Customers are increasingly looking for a much more complete service. Although the product will always be important, customers expect higher levels of service such as the shipping of parts, after care service and total customer care. Where **total customer care** is successfully provided alongside efficient products, occasional customers become regular customers and then regular customers become advocates.

The Rolls-Royce share of the competitive secondary engine parts market has been growing. An emphasis upon total care is at the heart of the growth strategy. Rolls-Royce provides parts and a service for its customers that extends through the operational **product life-cycle**.

Analysing the external environment

One way in which staff within Rolls-Royce have focused their actions for responding to the changing role of the business, has been to use Porter's 'Five Forces' model of industry competition. It has helped them to develop a better understanding of the business environment so that business opportunities could be analysed. The model identifies four forces outside the industry:

- potential entrants and the threat of entrants
- power of buyers
- power of suppliers and threat of substitutes - as well as one within the industry – competitive rivalry.

Competitive rivalry

As described above three dominant players operate in this **oligopolistic** global industry. The industry is capital intensive and there is a requirement for high investment in advanced technology and research and development. No single manufacturer dominates the industry, so balance fuels the rivalry. Competition in the primary market for aero-engines is intensified by the link to the secondary market for engine part sales and services. Access to the secondary market is dependent on achieving the original sale of new engines. In recent years the intensity of competition has increased as each manufacturer has tried to improve its volumes and market share. Rivalry has also intensified because gas turbine engines are now essentially a mature product and the potential for technological **differential advantage** has been reduced.

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Power of buyers

The numbers of potential buyers of new aircraft are low. Buyers of aircraft engines are therefore essentially **price makers**, with the market price for new engines being largely set by the buyer. The power of buyers has further increased in recent years as many airlines have become ‘global carriers’. The decision to purchase a particular aircraft or engine combination is a long-term one. This means that failure to secure an order may prevent an engine manufacturer trading with a particular airline for more than a decade. The selection of one engine type can lead to a domino effect, with other competing buyers following the same selection. Airlines are increasingly seeking lifetime cost of ownership guarantees, and reduced repair costs.

Power of suppliers

The suppliers to the aero-engine manufacturer have limited power. There are many hundreds of different suppliers to the aero-engine industry. They supply all nature of components, from nuts and bolts to state-of-the-art electronic control systems costing hundreds of thousands of pounds. The power of many of the smaller companies, which represent most of the supplier base has been reduced. This is due to engine manufacturers adopting **dual sourcing** strategies, using a range of alternative sources of supply. The most powerful suppliers are those involved in the supply of high specification electronic control equipment.

Threat of entry

Although not unknown, entry to the aero-engine industry is extremely difficult. The highly specialised advanced nature of aero-engine design combined with the costs of research and development as well as the confidence of customers represent significant barriers to entry. New engines also need extensive testing before gaining airworthiness approval from the authorities. The market is also sensitive to the reputation of the engine manufacturer, where names such as Rolls-Royce represent a range of proven high-technology products.

Threat of substitutes

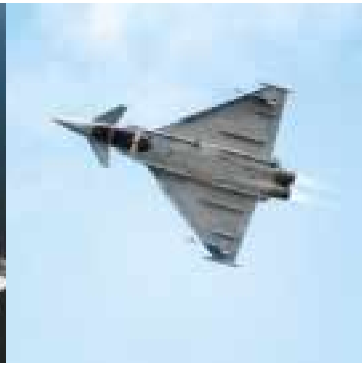
There is no substitute for an aero-engine and the threat of substitutes for air transport itself is minor. However, it is thought that the development of video conferencing capability will reduce some business travel and the growth of high speed train travel (e.g. Eurostar) will affect some travel decisions. However, both of these developments are taking place at a time when the demand for air travel is increasing.

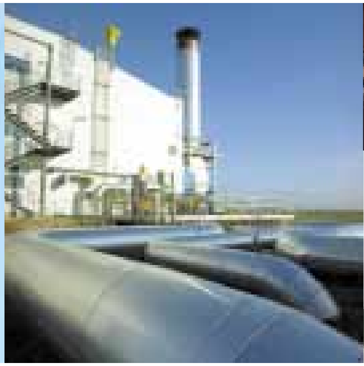
Summary of Five Forces analysis

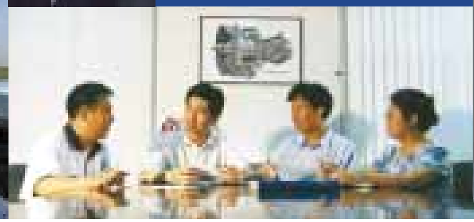
Five Forces analysis gives an improved understanding of the degree of competition within the business environment. The analysis shows that the commercial aero-engine business is highly competitive, with the buyer possessing and exerting a very powerful influence upon organisations. The high barriers to entry and the low threat of substitutes indicate that existing competitors will continue to share the business between them. However, a slow down in industry growth and the increasing maturity of products will intensify the degree of rivalry between the engine manufacturers.

Conclusion

In response to changes within its business environment Rolls-Royce has developed its orientation from that of engineering to become much more business and service focused. The organisation has had to become much more proactive, dealing with new ideas to create more services and customer focus. In the past, change was rare and slow, the company tended to follow the market trend. The structure of the organisation has been realigned to meet the needs of the new way of operating. **Organisational structures** define important relationships within the business, and create a mechanism for meeting business objectives. At the same time, it has been important to create a new **business culture**, within Rolls-Royce. A culture exists within the minds and hearts of the people of an organisation and contributes to the way they make decisions and develop business strategies. As an organisation changes from a product-focused organisation towards becoming a service-orientated culture, this requires more involvement of its people, with greater empowerment and rapid decision-taking. The **corporate identity** is the sum of the culture and its expression in behaviour and physical terms. Rolls-Royce has defined the identity that it needs to encourage, building on its past reputation and achievements for continuing success. As these changes take place, the organisation is also realigning its financial reporting framework and **corporate governance.** This will change how the whole business shapes its purposes and priorities.







GLOSSARY OF KEYWORDS

Business culture: Standards of behaviour within a business that affect attitudes, decision making and management style.

Brand: A unique combination of rational and emotional qualities associated with a product, service or business name or logotype. The brand is about image, perceptions and reputation.

Corporate governance: Meeting the needs of various stakeholders to an organisation.

Corporate identity: The ‘personality’ of a business as expressed in its behaviour, its visual representation and the views that people have of it.

Differential advantage: A key product or business advantage over competitors.

Dual sourcing: Buying parts or raw materials from more than one supplier.

Global company: A company that operates around the world.

Market forces: The interaction of buyers and sellers within a market.

Oligopolistic: A market in which there are a limited number of buyers or sellers.

Organisational structures: The ways in which an organisation is divided.

Price makers: Those who set a price rather than taking it

Primary market: The main market for a company which serves more than one market

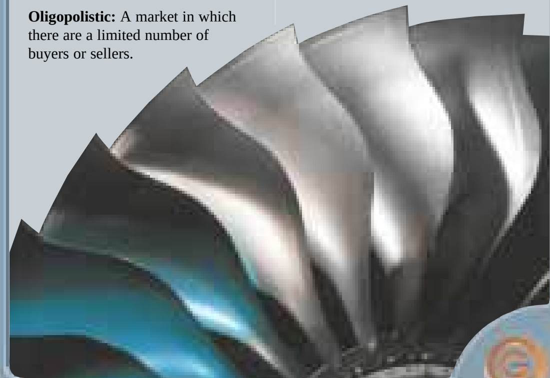
Product life-cycle: The duration for which a product appeals to customers.

Relationship marketing: The development of a relationship with customers through the selling process.

Secondary market: The alternative market for goods and services.

Total customer care: Focusing the whole business upon customer satisfaction through product integrity, including Customer Relationship Management and Total Care services.

Vertical: A market in which there are few customers.



QUESTIONS

1 Describe the difference between a primary and secondary market.

2 Compare the market structure for aero-engines with another market of your choice. Use the Five Forces analysis to undertake this activity.

3 Explain how
a) relationship marketing and
b) change management,
is helping Rolls-Royce to grow its market share.

4 Looking at the Five Forces analysis, identify and describe three problems faced by Rolls-Royce.

5 Using the case study, evaluate how Five Forces analysis could be used by a business organisation to develop a new strategic focus.

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