

Lenovo's Global Competition Strategy: the Driving Forces of Leadership

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The paper provides an overview and description of the Chinese economy in recent decades, taking into account the specifics of China's economic policy. The business activity of one of the most successful transnational Chinese company – Lenovo – was investigated in the paper. The article presents and analyzes the main business strategies that helped Lenovo to win in a short time competitive positions in the market of electronic equipment, gadgets and software products, not only on the national, but also on the world market. Particular attention in the study is given to the analysis of the company's financial performance by business groups and geographical units; the main indicators of the financial effectiveness of the company's business strategies; the effectiveness of the company's use of production resources is illustrated. Also, the paper analyzes the composition and elements of the global value chain formed by the company to realize competitive advantages and retain competitive positions in the world market.

Key words: asset, balance, profitability, investments, capital, competition, profit, product, market, strategy, global value chain.

Abbreviations:

PC – personal computer;

M&A – mergers and acquisitions.

УДК 338.2+338.4

JEL Codes: D12, D24, M21

Introduction. Before the start of reforms in 1978–1984, China had stagnating, badly centralized, largely inefficient economy that was isolated from the rest of the world. However, with the beginning of trade liberalization and market opening for foreign investment in 1979, China has shown the fastest economic growth, which the average annual rate over the last thirty years is almost 10 % [1].

Results of the research. The global economic crisis of 2008–2009 greatly affected on the economy of China: decreased volumes of import and export, decreased direct foreign investment (DFI), GDP growth slowed to 6–7 %, which caused a significant rising unemployment in the country (Fig. 1). The government of China responded to the crisis by the range of measures, including the implementation of the economic stimulus package with a total volume of US \$586 billion. The People's Bank of China mitigated monetary policy, allowed to increase Bank lending. These measures gave the possibility relatively painlessly relieved through the period of sharp fall in the world demand for products of Chinese exports, to maintain high economic growth.

Today the economic power of China is significant, also it is the determining factor of influence on the actions of key players on the global economic stage.

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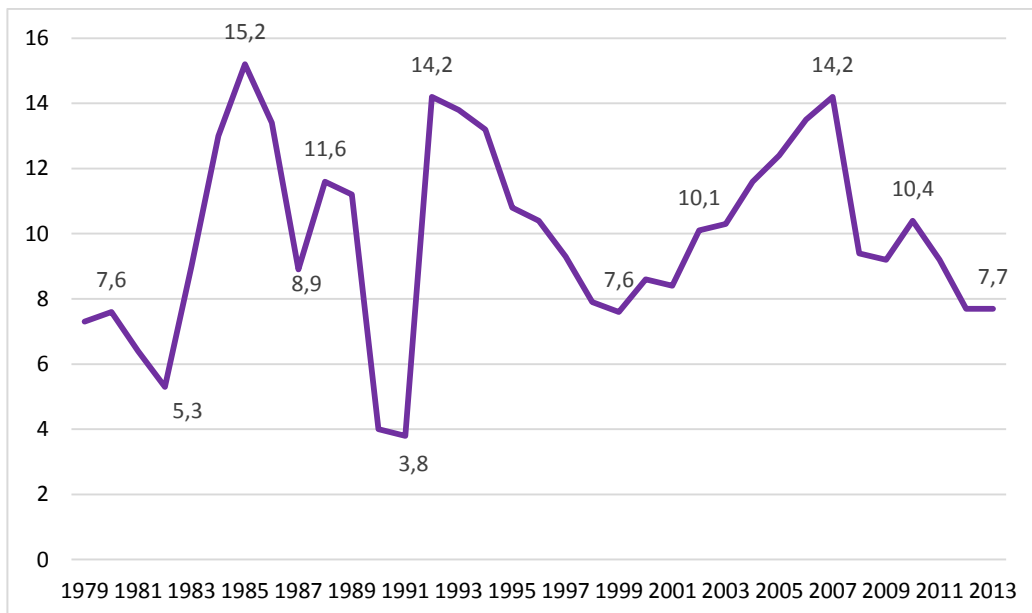


Figure 1. The growth rate of real GDP in China, 1979–2013, %

The factors of Chinese economic development.

One of the main factor of the Chinese economic “miracle” is the large-scale investments (as due to the large savings and foreign direct investment) and rapid productivity growth.

The second factor of economic growth is productivity growth, due to the relocation of labor resources in the sphere of its more efficient usage. Thus, agricultural reform freed labor from the earlier to the government-controlled agricultural sector, services and trade in favor of production.

In these conditions, flows of foreign direct investment rapidly increased: over the past three decades, China has made many efforts to build a favorable financial environment, achieved the full participation in the globalization process [2].

We will investigate one of the famous Chinese companies that is known all over the world.

Lenovo is one of the world’s leading personal technology companies, producing innovative PCs and mobile internet devices. Now it takes 202 place in fortune 500 list, Lenovo is the world’s largest PC vendor and the fourth largest smartphone company. While the Lenovo brand came into existence only in 2004, the company has a much longer history [4].

Today, Lenovo is a US \$47 billion personal technology company with more than 60000 employees (including joint ventures) in more than 60 countries serving customers and is represented in more than 160 countries. Lenovo has major research and manufacturing centers in countries around the world.

Lenovo has grown faster than the market for more than four years because of exceptionally engineered products. The customers use innovation to bring progress to the world, and company designs and builds the products with this in mind, taking inspiration from the drive and imagination of the people, who make things happen.

The company produces personal desktop computers, mobile phones, netbooks, servers, monitors, video projectors, video card, keyboard, mouse and kits, memory, optical drives, power supplies, accessories, bags and cases for laptops, as well as developing software for their products. The main trademarks under which the products are released are Lenovo, ThinkCentre, ThinkPad, ThinkVision, IdeaPad [11].

Market position strategy.

Lenovo's marketing position mainly considers the following three factors: take mainly to the high-end, middle and high-end combination of market positioning methods. Middle and high-end positioning can not only guarantee the consistency of Lenovo position in the market, also continue the image and status in consumer's mind, while the computer industry "present status such as the profits decline also decides the only choice for high-end positioning, will it be possible to maintain the long-term favorable market competitive position. Generally speaking, the high-end products" unit profits are 2–3 times more than low-end products, in the pressure of the rising cost situation, low-end products have no guarantee of profits, the profits of enterprises is the key to taking the high-end route [4].

The Product Strategy of Lenovo.

Lenovo's product strategy is the same as target market and positioning, mainly embodied as follows:

- middle and high-end market positioning – take Lenovo's personal computer as example, the market survey shows that its refrigerators mainly focus on middle and high end, Lenovo owns 70 % market share in high end products, while the middle end count for 40–50 % market share, the market share of low-end product is lower than 10 %;
- different competition of product development – through segmenting the market, tapping users' unmet demand, thereby pre-empt competitors to develop completely different products from the market, exclusive share the cake of segment market;
- according to the channels and the difference of segment markets, develop and design targeted products – as for the supermarket channel, Lenovo has designed relatively low prices of mid-level products, while high-end products on the electrical chain and retail sales channels [5].

Differentiation Strategy.

A differentiation strategy is based upon persuading customers that a product is superior to that offered by competitors. The major benefits to Lenovo of a successful differentiation strategy are:

- its products will command a premium price;
- demand or its product will be less price elastic than that for competitors' products;
- above average profits can be earned;
- it creates an additional barrier to entry new business wishing to enter the industry [6].

Focus Strategy.

A focus strategy is aimed at a segment of the market for a product rather than at the whole market or many markets. The major benefits of Lenovo's focus strategies are:

- it requires a lower investment in resources compared to a strategy aimed at an entire market or many markets;
- it allows specialization and greater knowledge of the segment being served;
- it makes enter to a new market less costly and much simpler [7].

Analysis of the value chain.

A value chain is a set of activities that a firm operating in a specific industry performs in order to deliver a valuable product or service for the market [8].

Then analyze the Lenovo's inside as well as outside processes and how the company creates own value.

Lenovo's production process.

Lenovo's product supply chain has been recognized in Gartner's Top 25 rankings the past three years. It plays a critical role in the development, manufacture, and delivery of our products. The supply chain begins with the management and control of a qualified supplier base, which provides qualified and secure components for use in development and manufacturing.

Critical, large volume components are tracked via barcodes, and controlled in the supplier's inventory and assembly process until receipt at Lenovo. Manufacturing takes place in a secure, controlled environment, including a secure physical facility, and a secure network. Completed products are then packaged with tamper-evident seals for boxes and pallets. Shipments are then tracked from origin to customer delivery.

The diagram below shows the complete product life cycle (Fig. 2). The Supply Chain involves the areas identified as Suppliers, and Lenovo Manufacturing and Test.

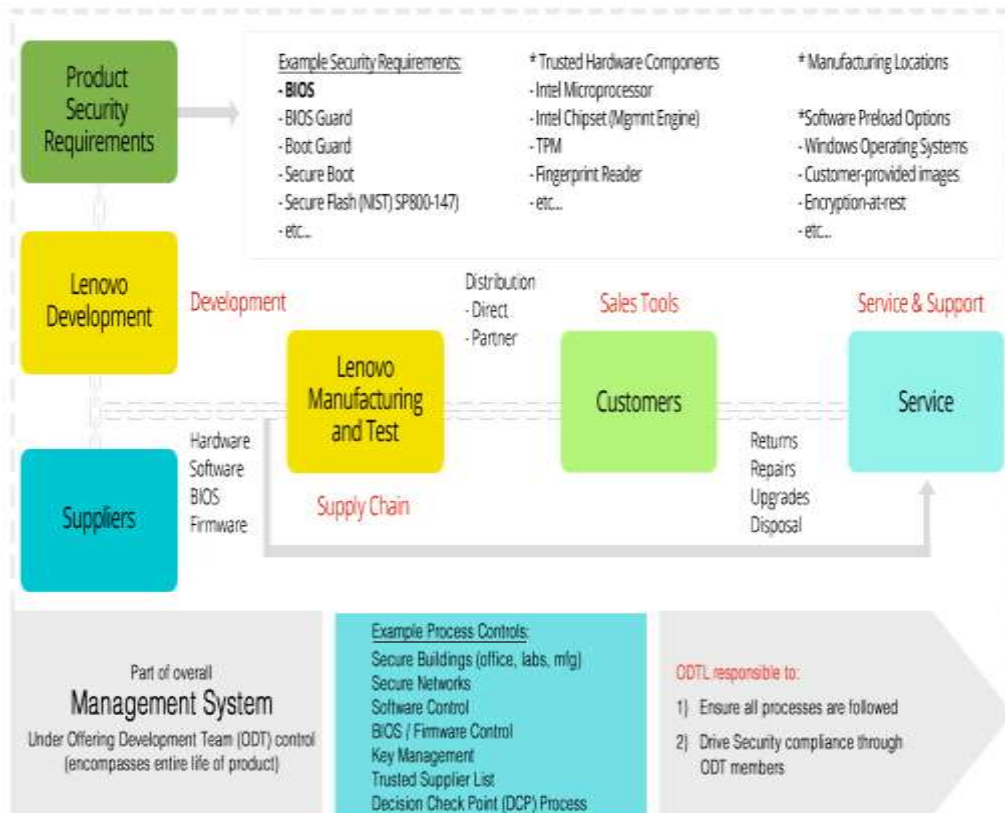


Figure 2. Product life cycle of Lenovo's products

In addition, there is technical work required to support the product throughout its life. Once the product is shipped, there is typically a need to qualify components to replace any end-of-life (EOL) parts, as well as a need to provide BIOS/firmware updates through a secure process. These are part of the overall Life Cycle Management and Support of the product [4].

The company evaluates its significant, material and environmental aspects. Once the significant aspects are identified, objectives and targets for each are set. Lenovo's significant aspects and objectives are provided in the table 1.

Table 1

Lenovo's significant aspects and objectives in the value creation

Significant aspect, compliance obligation, environmental risks or opportunity	Objectives
Supplier environmental performance	Monitor and drive good environmental management practices in the Lenovo Supply Chain. Minimize potential environmental impact of Lenovo's Category 1, 2 and 3 suppliers
Product materials	All products across all business units shall contain some Post-Consumer Recycled Content (PCRC). Sustain technological advances and maintain portfolio relative to low halogen products. Monitor and respond to market requirements in this area
Product energy consumption	Drive reduction in product energy use. Quantify and reduce lifecycle CO ₂ e emissions associated with the use of Lenovo products
Site energy consumption	Maximize energy efficiency and minimize CO ₂ e emissions associated with the development, manufacture and delivery of Lenovo products
Site air emissions	Absolute reduction in CO ₂ e emissions from Lenovo operations worldwide
Packaging	Minimize packaging material consumption while driving the use of environmentally sustainable materials
Transportation	Establish the foundation for driving future reductions in Lenovo international product transport carbon emissions
Waste management	Minimize environmental impacts associated with solid waste generated from Lenovo operations and products
Product end of life management	Ensure customer access to convenient, reliable and compliant product take back programs.

Lenovo recognizes that high-quality, long-lasting products not only satisfy customers, but also offers environmental benefits by delaying the need for recycling or disposal. Lenovo's global Quality Management System, which has earned ISO 9001 certification, aims to achieve customer satisfaction and deliver safe and superior products, solutions, and services while meeting customer requirements [9].

Effective use of company's resources.

Lenovo delivers profitable second quarter financial year 2016–2017 results:

- revenue was US \$11.2 billion, down eight percent year-over-year; up 12 % quarter-over-quarter;

- pre-tax income was US \$168 million, compared to US \$842 million loss in second quarter last year;
 - net income was US \$157 million, compared to US \$714 million loss in second quarter last year;
 - market conditions remain challenging and Lenovo is strongly executing its strategy;
 - three new industry leaders, experts in their fields, join the company.
- Further, we will analyze the company's revenues in geography (Fig. 3).

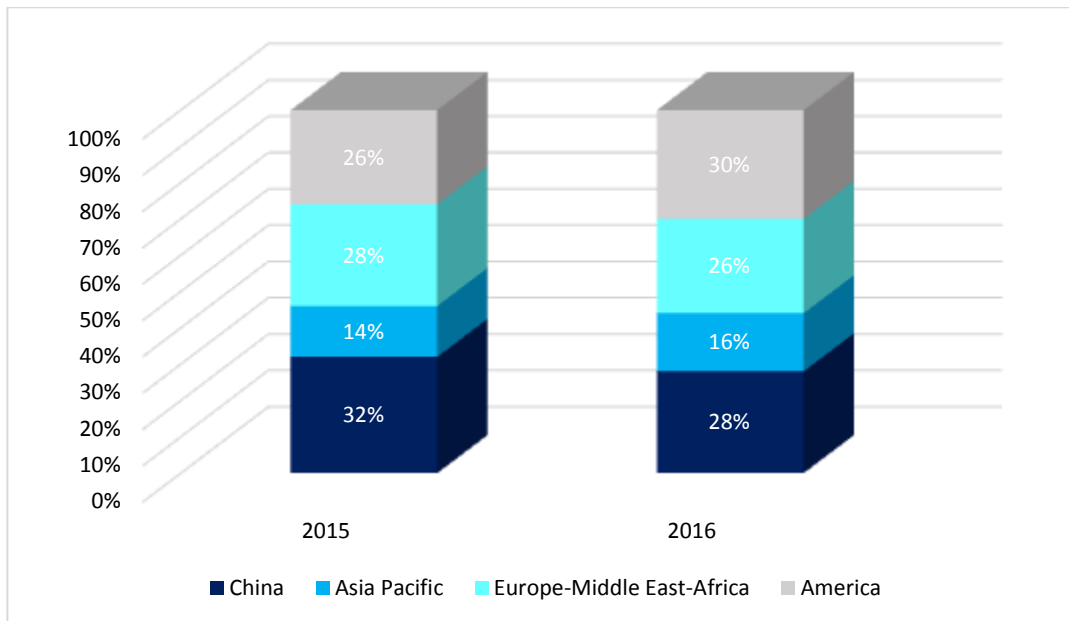


Figure 3. Revenue analysis by geography, %

As we may see, for the fiscal year ended March 31, 2016, the Lenovo revenue decreased by 3 % year-on-year to US \$44.912 million, due to currency fluctuation and the slower PC demand, while the company was building up the quality of its smartphone business.

In the previous year the highest share of the revenue had Chinese market and it had 32% in the total amount of revenue, but in 2016 the biggest share has belonged to American market that is because of the strengthening dollar positions in the global market. Also, the share of Asia-Pacific market has increased by 2 %. But what about Chinese market, for this year the share of revenue has decreased by 5 % that means that Lenovo is becoming stronger and stronger in the global market and captures more and more customers around the world.

What about the company revenue by business group, here the production of computers has the highest share almost three quarters, but for this fiscal year it has been decreased by 4 %. The reason of it is the increasing the share of mobile and enterprise productions by 2 and 4 % respectively. The share of Ecosystem and Cloud Service business group remains unchanged (2 %) (Fig. 4).

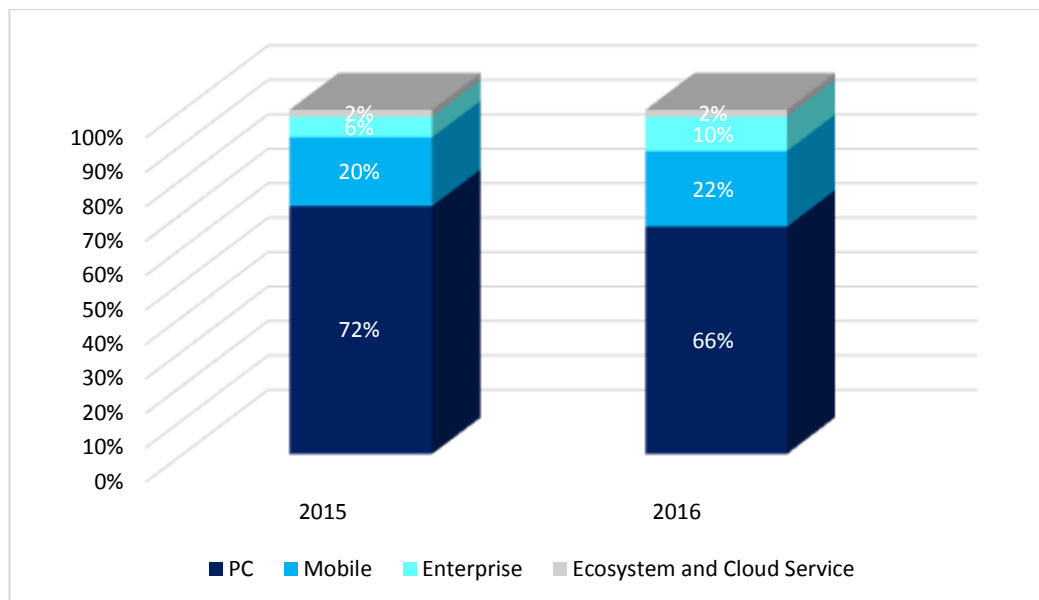


Figure 4. Revenue analysis by business group

Liquidity ratios are some of the most widely used ratios, perhaps next to profitability ratios. They are especially important to creditors. These ratios measure a firm's ability to meet its short-term obligations.

Table 2

Lenovo's liquidity ratios

Liquidity Ratios	2016	2015	2014	2013	2012	2011
Current Ratio	0,82	0,89	1	1,02	1	0,99
Quick Ratio	0,64	0,7	0,79	0,85	0,89	0,89
Cash Flow <i>per share</i>	0,03	0,02	0,14	0	0,19	0,1
Free Cash Flow <i>per share</i>	0,04	0,12	0,11	0,09	0,06	0,08

The current ratio has been decreasing from year to year; it is a bad trend, because the current assets can't cover its current liabilities. In 2016 Lenovo needs at least 18 % of current assets for covering its liabilities, in 2015 it needed for 7 % less and in 2014 the situation was better.

The situation with quick ratio is the same as with the first one ration. Lenovo's quick ratio has been decreasing too. From year to year it is starting to be less solvent than in the previous period. In 2014 company needs 21 % more for covering its current liabilities, in 2015 – 30 % and in this year it needs more than 35 %.

Financing ratios measure a company's ability to meet its longer-term obligations. Analysis of financing ratios provides insight on a company's capital.

Debt to equity ratio measures the amount of debt capital a firm uses compared to the amount of equity capital it uses.

Lenovo's debt to equity ratio also has had trend, but its value is valid and is less than 1 (Fig. 5). That means company has financial stability, but it was more stable before 2015. As we may see in 2016 this value has increased almost in 2 times and now it is a little bit more than 80 %. Lenovo uses own capital in production process at 20% more than loan capital. If trend will have the same tendency next year, company will lose its financial stability and will depend on other companies.

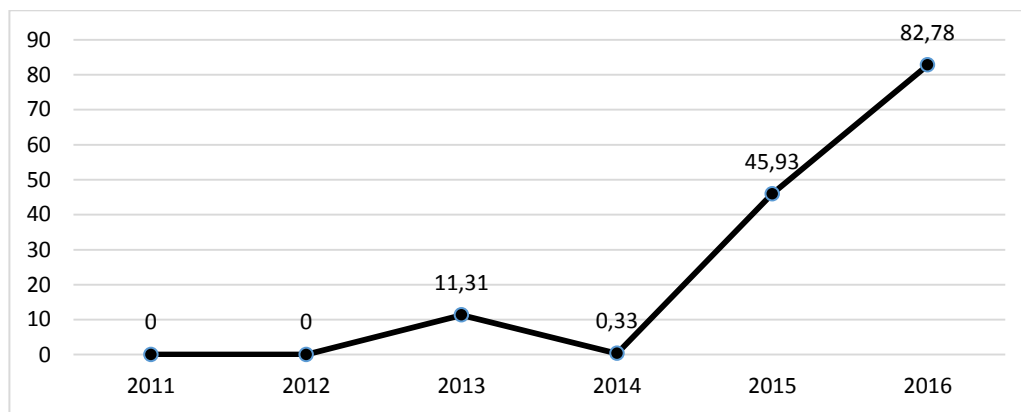


Figure 5. Trend of Lenovo's debt to equity ratio

Profitability ratios are arguably the most widely used ratios in investment analysis. These ratios include the ubiquitous "margin" ratios, such as gross, operating and net profit margins.

Gross Profit Margin shows that 13.08 % in 2014, 14.43 % in 2015 and 14.75% in 2016 of revenues were generated by the firm and are used to pay for the cost of goods sold. So, company has good revenue in this period. This table shows that gross profit margin has the positive tendency from year to year it is increasing.

Net profit margin from 2013 to 2015 was high: in 2013 – 86 %, in 2014 – 111 %, in 2015 – 81 %, which means that for every \$1 of revenue generated by the firm, \$1.86, \$1.11 and \$1.81 are created for the shareholders. But in this year the value of net margin rapidly decreased and \$1 of revenue generated by the firm only \$0.32 is created for the shareholders.

ROA (*the Return On Assets ratio*) in 2013 is 3.74, in 2014 – 4.45 and in 2015 – 3,05, its indicating that for every \$1 of company assets, the firm is generating \$3.74, 4.45 and 3.05 extra value to the year respectively. But as with net profit margin in 2016 year ROA has fallen and now \$1 of revenue generates losses.

ROE (*the Return On Equity*) to 2016 had the positive trend and was higher than 0, so it brought net income, but in 2016 Lenovo's situation became worthier, so this indicator is equal –4.78.

Regarding the loan money, it also has brought profit to Lenovo, but starting from this year company doesn't back loan money.

The Lenovo's gross profit for the fiscal year ended March 31, 2016 was US \$6.624 million, a decrease of 1 % year-on-year largely due to the revenue decline, while gross margin increased 0.4 % point year-on-year to 14.8 %. Operating expenses increased by 20 % year-on-year to US \$6.686 million, and the expenses-to-revenue ratio was 14.9 %. The increase was

mainly due to restructuring costs and one-time charges recorded in this fiscal quarter two, and the non-cash M&A accounting charges totaling US \$330 million booked in the fiscal year which included intangible asset amortization of two acquired businesses, namely Motorola Mobility and System X, and imputed interest expense of the three-year promissory note issued as part of the transaction to acquire Motorola Mobility. Excluding the restructuring costs and one time charges totaling US \$923 million and non-cash M&A accounting charges, the Group's run rate profit before taxation was US \$976 million, against US \$1,139 million of previous fiscal year. This decline was mainly due to slower PC demand and product transition of the Group's smartphone business. The decisive actions the Group took in fiscal quarter two to realign the business has started to show benefits in the second half of the fiscal year, and the Group's cost structure in the second half was enhanced with profitability improved. Including the restructuring costs, one time charges and non-cash M&A accounting charges, the Group reported a loss before taxation of US \$277 million, versus profit before taxation of US \$971 million in last fiscal year. The Group's net loss was US \$128 million, versus net income of US \$829 million of last fiscal year.

Conclusions. China's remarkable economic growth in the past 30 years has propelled it to become the third largest economy in the world, recently surpassing the United Kingdom and Germany.

The success of China is stipulated by: firstly, there will be sectoral and employment shifts in other economies, as some industries grow and others shrink; secondly, low prices for Chinese import products; thirdly, a sophisticated technical mix of export products and a policy focus on science and technology have resulted in a diverse set of determinants of international trade, with a great deal of provincial variability; fourthly, relatively cheap and high-quality labor forces. The continued growth and global integration of China will undoubtedly be of importance for the world economy, and countries will need to focus on their own competitiveness to benefit.

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Глобальна стратегія конкуренції компанії Lenovo: рушійні сили лідерства

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У статті наведено огляд і характеристику китайської економіки за останні десятиліття з урахуванням специфіки економічної політики Китаю. У роботі досліджена бізнес-діяльність однієї з найуспішніших транснаціональних китайських компаній – Lenovo. У статті наведено та проаналізовано основні бізнес-стратегії, які допомогли Lenovo завоювати за короткий час конкурентні позиції на ринку електронної техніки, гаджетів і програмних продуктів не тільки на національному, а й на світовому ринку. Особлива увага в дослідженні приділена аналізу фінансової діяльності компанії за бізнес-групами і географічними підрозділами; наведені основні показники фінансової ефективності реалізованих компанією бізнес-стратегій; проілюстрована ефективність використання компанією виробничих (матеріальних і нематеріальних) активів. Також у роботі проаналізовано склад і елементи глобального ланцюжка вартості, що формується компанією для реалізації конкурентних переваг і утримання конкурентних позицій на світовому ринку.

Ключові слова: актив, баланс, прибутковість, інвестиції, капітал, конкуренція, прибуток, продукт, ринок, стратегія, глобальний ланцюжок вартості.

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Глобальная стратегия конкуренции компании Lenovo: движущие силы лидерства

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Ключові слова: актив, баланс, доходність, інвестиції, капітал, конкуренція, прибуток, ринок, стратегія, глобальна ланцюжка вартості.

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