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Bestseller**

BLUE OCEAN STRATEGY

How to Create
Uncontested Market Space
and Make the Competition Irrelevant

W. Chan Kim • Renée Mauborgne

HARVARD BUSINESS SCHOOL PRESS

TLFeBOOK

Blue Ocean Strategy

Blue Ocean Strategy



*How to Create Uncontested Market Space and
Make the Competition Irrelevant*

W. Chan Kim
Renée Mauborgne

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*To friendship and to our families,
who make our worlds
more meaningful*



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Preface

THIS IS A BOOK about friendship, about loyalty, about believing in one another. It was because of that friendship, and that belief, that we set out on the journey to explore the ideas in this book and eventually came to write it.

We met twenty years ago in a classroom—one the professor, the other the student. And we have worked together ever since, often seeing ourselves along the journey as two wet rats in a drain. This book is not the victory of an idea but of a friendship that we have found more meaningful than any idea in the world of business. It has made our lives rich and our worlds more beautiful. We were not alone.

No journey is easy; no friendship is filled only with laughter. But we were excited every day of that journey because we were on a mission to learn and improve. We believe passionately in the ideas in this book. These ideas are not for those whose ambition in life is to get by or merely to survive. That was never an interest of ours. If you can be satisfied with that, do not read on. But if you want to make a difference, to create a company that builds a future where customers, employees, shareholders, and society win, read on. We are not saying it is easy, but it is worthwhile.

Our research confirms that there are no permanently excellent companies, just as there are no permanently excellent industries. As we have found on our own tumbling road, we all, like corporations, do smart things and less-than-smart things. To improve the quality of our success we need to study what we did that made a positive difference and understand how to replicate it systematically. That is what we call making smart strategic moves, and we have found that the strategic move that matters centrally is to create blue oceans.

Blue ocean strategy challenges companies to break out of the red ocean of bloody competition by creating uncontested market space that makes the competition irrelevant. Instead of dividing up existing—and often shrinking—demand and benchmarking competitors, blue ocean strategy is about growing demand and breaking away from the competition. This book not only challenges companies but also shows them how to achieve this. We first introduce a set of analytical tools and frameworks that show you how to systematically act on this challenge, and, second, we elaborate the principles that define and separate blue ocean strategy from competition-based strategic thought.

Our aim is to make the formulation and execution of blue ocean strategy as systematic and actionable as competing in the red waters of known market space. Only then can companies step up to the challenge of creating blue oceans in a smart and responsible way that is both opportunity maximizing and risk minimizing. No company—large or small, incumbent or new entrant—can afford to be a riverboat gambler. And no company should.

The contents of this book are based on more than fifteen years of research, data stretching back more than a hundred years, and a series of *Harvard Business Review* articles as well as academic articles on various dimensions of this topic. The ideas, tools, and frameworks presented here have been further tested and refined over the years in corporate practice in Europe, the United States, and Asia. This book builds on and extends this work by providing a narrative arc that draws these ideas together to offer a unified

framework. This framework addresses not only the analytic aspects behind the creation of blue ocean strategy but also the all-important human aspects of how to bring an organization and its people on this journey with a willingness to execute these ideas in action. Here, understanding how to build trust and commitment, as well as an understanding of the importance of intellectual and emotional recognition, are highlighted and brought to the core of strategy.

Blue ocean opportunities have been out there. As they have been explored, the market universe has been expanding. This expansion, we believe, is the root of growth. Yet poor understanding exists both in theory and in practice as to how to systematically create and capture blue oceans. We invite you to read this book to learn how you can be a driver of this expansion in the future.



Acknowledgments

WE HAVE HAD SIGNIFICANT HELP in actualizing this book. INSEAD has provided a unique environment in which to conduct our research. We have benefited greatly from the crossover between theory and practice that exists at INSEAD, and from the truly global composition of our faculty, student, and executive education populations. Deans Antonio Borges, Gabriel Hawawini, and Ludo Van der Heyden provided encouragement and institutional support from the start and allowed us to closely intertwine our research and teaching. PricewaterhouseCoopers (PwC) and the Boston Consulting Group (BCG) have extended the financial support for our research; in particular, Frank Brown and Richard Baird at PwC, and René Abate, John Clarkeson, George Stalk, and Olivier Tardy of BCG have been valued partners.

While we had help from a highly talented group of researchers over the years, our two dedicated research associates, Jason Hunter and Ji Mi, who have worked with us for the last several years, deserve special mention. Their commitment, persistent research support, and drive for perfection, were essential in realizing this book. We feel blessed by their presence.

Our colleagues at the school have contributed to the ideas in the book. INSEAD faculty members, particularly Subramanian Rangan and Ludo Van der Heyden, helped us to reflect upon our ideas and offered valuable comments and support. Many of INSEAD's faculty have taught the ideas and frameworks in this book to executive and M.B.A. audiences, providing valuable feedback that sharpened our thinking. Others have provided intellectual encouragement and the energy of kindness. We thank here, among others, Ron Adner, Jean-Louis Barsoux, Ben Bensaou, Henri-Claude de Bettignies, Mike Brimm, Laurence Capron, Marco Ceccagnoli, Karel Cool, Arnoud De Meyer, Ingemar Dierickx, Gareth Dyas, George Eapen, Paul Evans, Charlie Galunic, Annabelle Gawer, Javier Gimeno, Dominique Héau, Neil Jones, Philippe Lasserre, Jean-François Manzoni, Jens Meyer, Claude Michaud, Deigan Morris, Quy Nguyen-Huy, Subramanian Rangan, Jonathan Story, Heinz Thanheiser, Ludo Van der Heyden, David Young, Peter Zemsky, and Ming Zeng.

We have been fortunate to have a network of practitioners and case writers across the globe. They have contributed greatly in showing how the ideas in this book apply in action and helping to develop case material for our research. Among many people, one deserves special mention: Marc Beauvois-Coladon, who has worked with us from the start and made a major contribution to chapter 4 based on his field experiences practicing our ideas in companies. Among the wealth of others, we would like to thank Francis Gouillart and his associates; Gavin Fraser and his associates; Wayne Mortensen; Brian Marks; Kenneth Lau; Yasushi Shiina; Jonathan Landrey and his associates; Junan Jiang; Ralph Trombetta and his associates; Gabor Burt and his associates; Shantaram Venkatesh; Miki Kawawa and her associates; Atul Sinha and his associates; Arnold Izsak and his associates; Volker Westermann and his associates; Matt Williamson; and Caroline Edwards and her associates. We also appreciate the emerging cooperation with Accenture as kicked off with Mark Spelman, Omar Abbosh, Jim Sayles, and their team. Thanks are also due to Lucent Technologies for their support.

During the course of our research, we have met with corporate executives and public officers around the world who generously gave us their time and insight, greatly shaping the ideas in this book. We are grateful to them. Among many private and public initiatives for putting our ideas into practice, the Value Innovation Program (VIP) Center at Samsung Electronics and the Value Innovation Action Tank (VIAT) in Singapore for the country's government and private sectors have been major sources of inspiration and learning. In particular, Jong-Yong Yun at Samsung Electronics and all the Permanent Secretaries of Singapore Government have been valued partners. Warm thanks also to the members of the Value Innovation Network (VIN), a global community of practice on the Value Innovation family of concepts—especially to those we were unable to mention here.

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PART ONE



Blue Ocean Strategy

Creating Blue Oceans

A ONE TIME ACCORDION PLAYER, stilt-walker, and fire-eater, Guy Laliberté is now CEO of Cirque du Soleil, one of Canada's largest cultural exports. Created in 1984 by a group of street performers, Cirque's productions have been seen by almost forty million people in ninety cities around the world. In less than twenty years Cirque du Soleil has achieved a level of revenues that took Ringling Bros. and Barnum & Bailey—the global champion of the circus industry—more than one hundred years to attain.

What makes this rapid growth all the more remarkable is that it was not achieved in an attractive industry but rather in a declining industry in which traditional strategic analysis pointed to limited potential for growth. Supplier power on the part of star performers was strong. So was buyer power. Alternative forms of entertainment—ranging from various kinds of urban live entertainment to sporting events to home entertainment—cast an increasingly long shadow. Children cried out for PlayStations rather than a visit to the traveling circus. Partially as a result, the industry was suffering from steadily decreasing audiences and, in turn, declining revenue and profits. There was also increasing sentiment against the

use of animals in circuses by animal rights groups. Ringling Bros. and Barnum & Bailey set the standard, and competing smaller circuses essentially followed with scaled-down versions. From the perspective of competition-based strategy, then, the circus industry appeared unattractive.

Another compelling aspect of Cirque du Soleil's success is that it did not win by taking customers from the already shrinking circus industry, which historically catered to children. Cirque du Soleil did not compete with Ringling Bros. and Barnum & Bailey. Instead it created uncontested new market space that made the competition irrelevant. It appealed to a whole new group of customers: adults and corporate clients prepared to pay a price several times as great as traditional circuses for an unprecedented entertainment experience. Significantly, one of the first Cirque productions was titled "We Reinvent the Circus."

New Market Space

Cirque du Soleil succeeded because it realized that to win in the future, companies must stop competing with each other. The only way to beat the competition is to stop *trying* to beat the competition.

To understand what Cirque du Soleil has achieved, imagine a market universe composed of two sorts of oceans: red oceans and blue oceans. Red oceans represent all the industries in existence today. This is the known market space. Blue oceans denote all the industries *not* in existence today. This is the unknown market space.

In the red oceans, industry boundaries are defined and accepted, and the competitive rules of the game are known.¹ Here, companies try to outperform their rivals to grab a greater share of existing demand. As the market space gets crowded, prospects for profits and growth are reduced. Products become commodities, and cutthroat competition turns the red ocean bloody.

Blue oceans, in contrast, are defined by untapped market space, demand creation, and the opportunity for highly profitable growth.

Although some blue oceans are created well beyond existing industry boundaries, most are created from within red oceans by expanding existing industry boundaries, as Cirque du Soleil did. In blue oceans, competition is irrelevant because the rules of the game are waiting to be set.

It will always be important to swim successfully in the red ocean by outcompeting rivals. Red oceans will always matter and will always be a fact of business life. But with supply exceeding demand in more industries, competing for a share of contracting markets, while necessary, will not be sufficient to sustain high performance.² Companies need to go beyond competing. To seize new profit and growth opportunities, they also need to create blue oceans.

Unfortunately, blue oceans are largely uncharted. The dominant focus of strategy work over the past twenty-five years has been on competition-based red ocean strategies.³ The result has been a fairly good understanding of how to compete skillfully in red waters, from analyzing the underlying economic structure of an existing industry, to choosing a strategic position of low cost or differentiation or focus, to benchmarking the competition. Some discussions around blue oceans exist.⁴ However, there is little practical guidance on how to create them. Without analytic frameworks to create blue oceans and principles to effectively manage risk, creating blue oceans has remained wishful thinking that is seen as too risky for managers to pursue as strategy. This book provides practical frameworks and analytics for the systematic pursuit and capture of blue oceans.

The Continuing Creation of Blue Oceans

Although the term *blue oceans* is new, their existence is not. They are a feature of business life, past and present. Look back one hundred years and ask yourself, How many of today's industries were then unknown? The answer: Many industries as basic as automobiles, music recording, aviation, petrochemicals, health care, and

management consulting were unheard of or had just begun to emerge at that time. Now turn the clock back only thirty years. Again, a plethora of multibillion-dollar industries jumps out—mutual funds, cell phones, gas-fired electricity plants, biotechnology, discount retail, express package delivery, minivans, snowboards, coffee bars, and home videos, to name a few. Just three decades ago, none of these industries existed in a meaningful way.

Now put the clock forward twenty years—or perhaps fifty years—and ask yourself how many now unknown industries will likely exist then. If history is any predictor of the future, again the answer is many of them.

The reality is that industries never stand still. They continuously evolve. Operations improve, markets expand, and players come and go. History teaches us that we have a hugely underestimated capacity to create new industries and re-create existing ones. In fact, the half-century-old Standard Industrial Classification (SIC) system published by the U.S. Census was replaced in 1997 by the North America Industry Classification Standard (NAICS) system. The new system expanded the ten SIC industry sectors into twenty sectors to reflect the emerging realities of new industry territories.⁵ The services sector under the old system, for example, is now expanded into seven business sectors ranging from information to health care and social assistance.⁶ Given that these systems are designed for standardization and continuity, such a replacement shows how significant the expansion of blue oceans has been.

Yet the overriding focus of strategic thinking has been on competition-based red ocean strategies. Part of the explanation for this is that corporate strategy is heavily influenced by its roots in military strategy. The very language of strategy is deeply imbued with military references—chief executive “officers” in “headquarters,” “troops” on the “front lines.” Described this way, strategy is about confronting an opponent and fighting over a given piece of land that is both limited and constant.⁷ Unlike war, however, the history of industry shows us that the market universe has never been constant; rather, blue oceans have continuously been created over

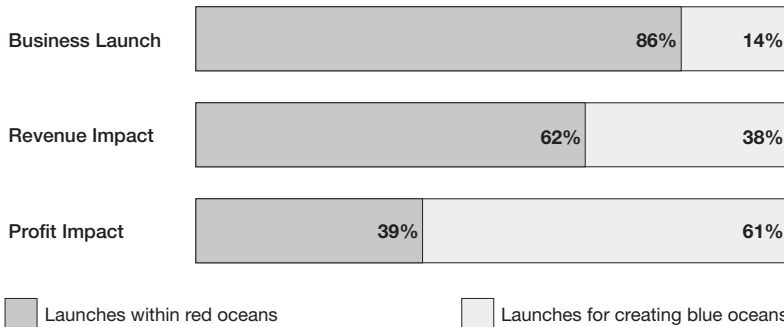
time. To focus on the red ocean is therefore to accept the key constraining factors of war—limited terrain and the need to beat an enemy to succeed—and to deny the distinctive strength of the business world: the capacity to create new market space that is uncontested.

The Impact of Creating Blue Oceans

We set out to quantify the impact of creating blue oceans on a company’s growth in both revenues and profits in a study of the business launches of 108 companies (see figure 1-1). We found that 86 percent of the launches were line extensions, that is, incremental improvements within the red ocean of existing market space. Yet they accounted for only 62 percent of total revenues and a mere 39 percent of total profits. The remaining 14 percent of the launches were aimed at creating blue oceans. They generated 38 percent of total revenues and 61 percent of total profits. Given that business launches included the total investments made for creating red and blue oceans (regardless of their subsequent revenue and profit consequences, including failures), the performance benefits of creating

FIGURE 1-1

The Profit and Growth Consequences of Creating Blue Oceans



blue waters are evident. Although we don't have data on the hit rate of success of red and blue ocean initiatives, the global performance differences between them are marked.

The Rising Imperative of Creating Blue Oceans

There are several driving forces behind a rising imperative to create blue oceans. Accelerated technological advances have substantially improved industrial productivity and have allowed suppliers to produce an unprecedented array of products and services. The result is that in increasing numbers of industries, supply exceeds demand.⁸ The trend toward globalization compounds the situation. As trade barriers between nations and regions are dismantled and as information on products and prices becomes instantly and globally available, niche markets and havens for monopoly continue to disappear.⁹ While supply is on the rise as global competition intensifies, there is no clear evidence of an increase in demand worldwide, and statistics even point to declining populations in many developed markets.¹⁰

The result has been accelerated commoditization of products and services, increasing price wars, and shrinking profit margins. Recent industrywide studies on major American brands confirm this trend.¹¹ They reveal that for major product and service categories, brands are generally becoming more similar, and as they are becoming more similar people increasingly select based on price.¹² People no longer insist, as in the past, that their laundry detergent be Tide. Nor will they necessarily stick to Colgate when Crest is on sale, and vice versa. In overcrowded industries, differentiating brands becomes harder in both economic upturns and downturns.

All this suggests that the business environment in which most strategy and management approaches of the twentieth century evolved is increasingly disappearing. As red oceans become increasingly bloody, management will need to be more concerned with blue oceans than the current cohort of managers is accustomed to.

From Company and Industry to Strategic Move

How can a company break out of the red ocean of bloody competition? How can it create a blue ocean? Is there a systematic approach to achieve this and thereby sustain high performance?

In search of an answer, our initial step was to define the basic unit of analysis for our research. To understand the roots of high performance, the business literature typically uses the company as the basic unit of analysis. People have marveled at how companies attain strong, profitable growth with a distinguished set of strategic, operational, and organizational characteristics. Our question, however, was this: Are there *lasting* “excellent” or “visionary” companies that continuously outperform the market and repeatedly create blue oceans?

Consider, for example, *In Search of Excellence* and *Built to Last*.¹³ The bestselling book *In Search of Excellence* was published twenty years ago. Yet within two years of its publication a number of the companies surveyed began to slip into oblivion: Atari, Chesebrough-Pond’s, Data General, Fluor, National Semiconductor. As documented in *Managing on the Edge*, two-thirds of the identified model firms in the book had fallen from their perches as industry leaders within five years of its publication.¹⁴

The book *Built to Last* continued in the same footsteps. It sought out the “successful habits of visionary companies” that had a long-running track record of superior performance. To avoid the pitfalls of *In Search of Excellence*, however, the survey period of *Built to Last* was expanded to the entire life span of the companies while its analysis was limited to firms more than forty years old. *Built to Last* also became a bestseller.

But again, upon closer examination, deficiencies in some of the visionary companies spotlighted in *Built to Last* have come to light. As illustrated in the recent book *Creative Destruction*, much of the success attributed to some of the model companies in *Built to Last* was the result of industry sector performance rather than the

companies themselves.¹⁵ For example, Hewlett-Packard (HP) met the criteria of *Built to Last* by outperforming the market over the long term. In reality, while HP outperformed the market, so did the entire computer-hardware industry. What's more, HP did not even outperform the competition within the industry. Through this and other examples, *Creative Destruction* questioned whether "visionary" companies that continuously outperform the market have ever existed. And we all have seen the stagnating or declining performance of the Japanese companies that were celebrated as "revolutionary" strategists in their heyday of the late 1970s and early 1980s.

If there is no perpetually high-performing company and if the same company can be brilliant at one moment and wrongheaded at another, it appears that the company is not the appropriate unit of analysis in exploring the roots of high performance and blue oceans.

As discussed earlier, history also shows that industries are constantly being created and expanded over time and that industry conditions and boundaries are not given; individual actors can shape them. Companies need not compete head-on in a given industry space; Cirque du Soleil created a new market space in the entertainment sector, generating strong, profitable growth as a result. It appears, then, that neither the company nor the industry is the best unit of analysis in studying the roots of profitable growth.

Consistent with this observation, our study shows that the strategic move, and not the company or the industry, is the right unit of analysis for explaining the creation of blue oceans and sustained high performance. A strategic move is the set of managerial actions and decisions involved in making a major market-creating business offering. Compaq, for example, was acquired by Hewlett-Packard in 2001 and ceased to be an independent company. As a result, many people might judge the company as unsuccessful. This does not, however, invalidate the blue ocean strategic moves that Compaq made in creating the server industry. These strategic moves not only were a part of the company's powerful comeback in the mid-1990s but also unlocked a new multibillion-dollar market space in computing.

Appendix A, “A Sketch of the Historical Pattern of Blue Ocean Creation,” provides a snapshot overview of the history of three representative U.S. industries drawn from our database: the auto industry—how we get to work; the computer industry—what we use at work; and the cinema industry—where we go after work for enjoyment. As shown in appendix A, no perpetually excellent company or industry is found. But a striking commonality appears to exist across strategic moves that have created blue oceans and have led to new trajectories of strong, profitable growth.

The strategic moves we discuss—moves that have delivered products and services that opened and captured new market space, with a significant leap in demand—contain great stories of profitable growth as well as thought-provoking tales of missed opportunities by companies stuck in red oceans. We built our study around these strategic moves to understand the pattern by which blue oceans are created and high performance achieved. We studied more than one hundred fifty strategic moves made from 1880 to 2000 in more than thirty industries, and we closely examined the relevant business players in each of these events. Industries ranged from hotels, the cinema, retail, airlines, energy, computers, broadcasting, and construction to automobiles and steel. We analyzed not only winning business players who created blue oceans but also their less successful competitors.

Both within a given strategic move and across strategic moves, we searched for convergence among the group that created blue oceans and within less successful players caught in the red ocean. We also searched for divergence across these two groups. In so doing, we tried to discover the common factors leading to the creation of blue oceans and the key differences separating those winners from the mere survivors and the losers adrift in the red ocean.

Our analysis of more than thirty industries confirms that neither industry nor organizational characteristics explain the distinction between the two groups. In assessing industry, organizational, and strategic variables we found that the creation and capturing of blue oceans were achieved by small and large companies, by young and

old managers, by companies in attractive and unattractive industries, by new entrants and established incumbents, by private and public companies, by companies in low- and high-tech industries, and by companies of diverse national origins.

Our analysis failed to find any perpetually excellent company or industry. What we did find behind the seemingly idiosyncratic success stories, however, was a consistent and common pattern across strategic moves for creating and capturing blue oceans. Whether it was Ford in 1908 with the Model T; GM in 1924 with cars styled to appeal to the emotions; CNN in 1980 with real-time news 24/7; or Compaq, Starbucks, Southwest Airlines, or Cirque du Soleil—or, for that matter, any of the other blue ocean moves in our study—the approach to strategy in creating blue oceans was consistent across time regardless of industry. Our research also reached out to embrace famous strategic moves in public sector turnarounds. Here we found a strikingly similar pattern.

Value Innovation: The Cornerstone of Blue Ocean Strategy

What consistently separated winners from losers in creating blue oceans was their approach to strategy. The companies caught in the red ocean followed a conventional approach, racing to beat the competition by building a defensible position within the existing industry order.¹⁶ The creators of blue oceans, surprisingly, didn't use the competition as their benchmark.¹⁷ Instead, they followed a different strategic logic that we call *value innovation*. Value innovation is the cornerstone of blue ocean strategy. We call it value innovation because instead of focusing on beating the competition, you focus on making the competition irrelevant by creating a leap in value for buyers and your company, thereby opening up new and uncontested market space.

Value innovation places equal emphasis on value and innovation. Value without innovation tends to focus on *value creation* on

an incremental scale, something that improves value but is not sufficient to make you stand out in the marketplace.¹⁸ *Innovation* without value tends to be technology-driven, market pioneering, or futuristic, often shooting beyond what buyers are ready to accept and pay for.¹⁹ In this sense, it is important to distinguish between value innovation as opposed to technology innovation and market pioneering. Our study shows that what separates winners from losers in creating blue oceans is neither bleeding-edge technology nor “timing for market entry.” Sometimes these exist; more often, however, they do not. Value innovation occurs only when companies align innovation with utility, price, and cost positions. If they fail to anchor innovation with value in this way, technology innovators and market pioneers often lay the eggs that other companies hatch.

Value innovation is a new way of thinking about and executing strategy that results in the creation of a blue ocean and a break from the competition. Importantly, value innovation defies one of the most commonly accepted dogmas of competition-based strategy: the value-cost trade-off.²⁰ It is conventionally believed that companies can either create greater value to customers at a higher cost or create reasonable value at a lower cost. Here strategy is seen as making a choice between differentiation and low cost.²¹ In contrast, those that seek to create blue oceans pursue differentiation and low cost simultaneously.

Let’s return to the example of Cirque du Soleil. Pursuing differentiation and low cost simultaneously lies at the heart of the entertainment experience it created. At the time of its debut, other circuses focused on benchmarking one another and maximizing their share of already shrinking demand by tweaking traditional circus acts. This included trying to secure more famous clowns and lion tamers, a strategy that raised circuses’ cost structure without substantially altering the circus experience. The result was rising costs without rising revenues, and a downward spiral of overall circus demand.

These efforts were made irrelevant when Cirque du Soleil appeared. Neither an ordinary circus nor a classic theater production,

Cirque du Soleil paid no heed to what the competition did. Instead of following the conventional logic of outpacing the competition by offering a better solution to the given problem—creating a circus with even greater fun and thrills—it sought to offer people the fun and thrill of the circus *and* the intellectual sophistication and artistic richness of the theater at the same time; hence, it redefined the problem itself.²² By breaking the market boundaries of theater and circus, Cirque du Soleil gained a new understanding not only of circus customers but also of circus noncustomers: adult theater customers.

This led to a whole new circus concept that broke the value-cost trade-off and created a blue ocean of new market space. Consider the differences. Whereas other circuses focused on offering animal shows, hiring star performers, presenting multiple show arenas in the form of three rings, and pushing aisle concession sales, Cirque du Soleil did away with all these factors. These factors had long been taken for granted in the traditional circus industry, which never questioned their ongoing relevance. However, there was increasing public discomfort with the use of animals. Moreover, animal acts were one of the most expensive elements, including not only the cost of the animals but also their training, medical care, housing, insurance, and transportation.

Similarly, while the circus industry focused on featuring stars, in the mind of the public the so-called stars of the circus were trivial next to movie stars. Again, they were a high-cost component carrying little sway with spectators. Gone, too, are three-ring venues. Not only did this arrangement create angst among spectators as they rapidly switched their gaze from one ring to the other, but it also increased the number of performers needed, with obvious cost implications. And although aisle concession sales appeared to be a good way to generate revenue, in practice the high prices discouraged audiences from making purchases and made them feel they were being taken for a ride.

The lasting allure of the traditional circus came down to only three key factors: the tent, the clowns, and the classic acrobatic

acts such as the wheelman and short stunts. So Cirque du Soleil kept the clowns but shifted their humor from slapstick to a more enchanting, sophisticated style. It glamorized the tent, an element that, ironically, many circuses had begun to forfeit in favor of rented venues. Seeing that this unique venue symbolically captured the magic of the circus, Cirque du Soleil designed the classic symbol of the circus with a glorious external finish and a higher level of comfort, making its tents reminiscent of the grand epic circuses. Gone were the sawdust and hard benches. Acrobats and other thrilling acts are retained, but their roles were reduced and made more elegant by the addition of artistic flair and intellectual wonder to the acts.

By looking across the market boundary of theater, Cirque du Soleil also offered new noncircus factors, such as a story line and, with it, intellectual richness, artistic music and dance, and multiple productions. These factors, entirely new creations for the circus industry, are drawn from the alternative live entertainment industry of theater.

Unlike traditional circus shows having a series of unrelated acts, for example, each Cirque du Soleil creation has a theme and story line, somewhat resembling a theater performance. Although the theme is vague (and intentionally so), it brings harmony and an intellectual element to the show—without limiting the potential for acts. Le Cirque also borrows ideas from Broadway shows. For example, it features multiple productions rather than the traditional “one for all” shows. As with Broadway shows, too, each Cirque du Soleil show has an original score and assorted music, which drives the visual performance, lighting, and timing of the acts rather than the other way around. The shows feature abstract and spiritual dance, an idea derived from theater and ballet. By introducing these new factors into its offering, Cirque du Soleil has created more sophisticated shows.

Moreover, by injecting the concept of multiple productions and by giving people a reason to come to the circus more frequently, Cirque du Soleil has dramatically increased demand.

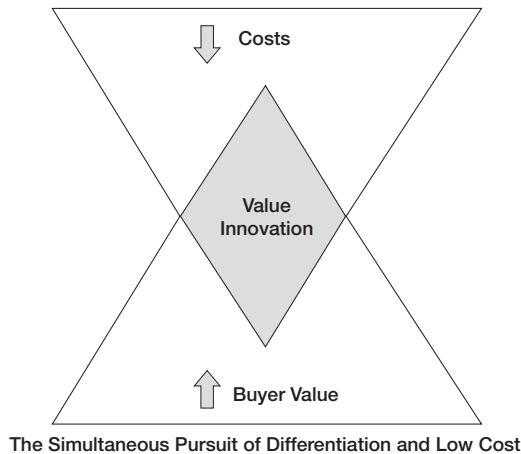
In short, Cirque du Soleil offers the best of both circus and theater, and it has eliminated or reduced everything else. By offering unprecedented utility, Cirque du Soleil has created a blue ocean and has invented a new form of live entertainment, one that is markedly different from both traditional circus and theater. At the same time, by eliminating many of the most costly elements of the circus, it has dramatically reduced its cost structure, achieving both differentiation and low cost. Le Cirque strategically priced its tickets against those of the theater, lifting the price point of the circus industry by several multiples while still pricing its productions to capture the mass of adult customers, who were used to theater prices.

Figure 1-2 depicts the differentiation–low cost dynamics underpinning value innovation.

FIGURE 1-2

Value Innovation: The Cornerstone of Blue Ocean Strategy

Value innovation is created in the region where a company's actions favorably affect both its cost structure and its value proposition to buyers. Cost savings are made by eliminating and reducing the factors an industry competes on. Buyer value is lifted by raising and creating elements the industry has never offered. Over time, costs are reduced further as scale economies kick in due to the high sales volumes that superior value generates.



As shown in figure 1-2, the creation of blue oceans is about driving costs down while simultaneously driving value up for buyers. This is how a leap in value for both the company and its buyers is achieved. Because buyer value comes from the utility and price that the company offers to buyers and because the value to the company is generated from price and its cost structure, value innovation is achieved only when the whole system of the company's utility, price, and cost activities is properly aligned. It is this whole-system approach that makes the creation of blue oceans a sustainable strategy. Blue ocean strategy integrates the range of a firm's functional and operational activities.

In contrast, innovations such as production innovations can be achieved at the subsystem level without impacting the company's overall strategy. An innovation in the production process, for example, may lower a company's cost structure to reinforce its existing cost leadership strategy without changing the utility proposition of its offering. Although innovations of this sort may help to secure and even lift a company's position in the existing market space, such a subsystem approach will rarely create a blue ocean of new market space.

In this sense, value innovation is more than *innovation*. It is about *strategy* that embraces the entire system of a company's activities.²³ Value innovation requires companies to orient the whole system toward achieving a *leap* in value for both buyers *and* themselves. Absent such an integral approach, innovation will remain divided from the core of strategy.²⁴ Figure 1-3 outlines the key defining features of red and blue ocean strategies.

Competition-based red ocean strategy assumes that an industry's structural conditions are given and that firms are forced to compete within them, an assumption based on what the academics call the *structuralist* view, or *environmental determinism*.²⁵ In contrast, value innovation is based on the view that market boundaries and industry structure are not given and can be reconstructed by the actions and beliefs of industry players. We call this the

FIGURE 1-3

Red Ocean Versus Blue Ocean Strategy

Red Ocean Strategy	Blue Ocean Strategy
Compete in existing market space.	Create uncontested market space.
Beat the competition.	Make the competition irrelevant.
Exploit existing demand.	Create and capture new demand.
Make the value-cost trade-off.	Break the value-cost trade-off.
Align the whole system of a firm's activities with its strategic choice of differentiation or low cost.	Align the whole system of a firm's activities in pursuit of differentiation and low cost.

reconstructionist view. In the red ocean, differentiation costs because firms compete with the same best-practice rule. Here, the strategic choices for firms are to pursue either differentiation or low cost. In the reconstructionist world, however, the strategic aim is to create new best-practice rules by breaking the existing value-cost trade-off and thereby creating a blue ocean. (For more discussions on this, see appendix B, “Value Innovation: A Reconstructionist View of Strategy.”)

Cirque du Soleil broke the best practice rule of the circus industry, achieving both differentiation and low cost by reconstructing elements across existing industry boundaries. Is Cirque du Soleil, then, really a circus, with all that it eliminated, reduced, raised, and created? Or is it theater? And if it is theater, then what genre—a Broadway show, an opera, a ballet? It is not clear. Cirque du Soleil reconstructed elements across these alternatives, and, in the end, it is simultaneously a little of all of them and none of any of them in their entirety. It created a blue ocean of new, uncontested market space that as of yet has no agreed-on industry name.

Formulating and Executing Blue Ocean Strategy

Although economic conditions indicate the rising imperative of blue oceans, there is a general belief that the odds of success are lower when companies venture beyond existing industry space.²⁶ The issue is how to succeed in blue oceans. How can companies systematically maximize the opportunities while simultaneously minimizing the risks of formulating and executing blue ocean strategy? If you lack an understanding of the opportunity-maximizing and risk-minimizing principles driving the creation and capture of blue oceans, the odds will be lengthened against your blue ocean initiative.

Of course, there is no such thing as a riskless strategy.²⁷ Strategy will always involve both opportunity and risk, be it a red ocean or a blue ocean initiative. But at present the playing field is dramatically unbalanced in favor of tools and analytical frameworks to succeed in red oceans. As long as this remains true, red oceans will continue to dominate companies' strategic agenda even as the business imperative for creating blue oceans takes on new urgency. Perhaps this explains why, despite prior calls for companies to go beyond existing industry space, companies have yet to act seriously on these recommendations.

This book seeks to address this imbalance by laying out a methodology to support our thesis. Here we present the principles and analytical frameworks to succeed in blue oceans.

Chapter 2 introduces the analytical tools and frameworks that are essential for creating and capturing blue oceans. Although supplementary tools are introduced in other chapters as needed, these basic analytics are used throughout the book. Companies can make proactive changes in industry or market fundamentals through the purposeful application of these blue ocean tools and frameworks, which are grounded in the issues of both opportunity and risk. Subsequent chapters introduce the principles that drive

the successful formulation and implementation of blue ocean strategy and explain how they, along with the analytics, are applied in action.

There are four guiding principles for the successful formulation of blue ocean strategy. Chapters 3 to 6 address these in turn. Chapter 3 identifies the paths by which you can systematically create uncontested market space across diverse industry domains, hence attenuating *search risk*. It teaches you how to make the competition irrelevant by looking across the six conventional boundaries of competition to open up commercially important blue oceans. The six paths focus on looking across alternative industries, across strategic groups, across buyer groups, across complementary product and service offerings, across the functional-emotional orientation of an industry, and even across time.

Chapter 4 shows how to design a company's strategic planning process to go beyond incremental improvements to create value innovations. It presents an alternative to the existing strategic planning process, which is often criticized as a number-crunching exercise that keeps companies locked into making incremental improvements. This principle tackles *planning risk*. Using a visualizing approach that drives you to focus on the big picture rather than to be submerged in numbers and jargon, this chapter proposes a four-step planning process whereby you can build a strategy that creates and captures blue ocean opportunities.

Chapter 5 shows how to maximize the size of a blue ocean. To create the greatest market of new demand, this chapter challenges the conventional practice of aiming for finer segmentation to better meet existing customer preferences. This practice often results in increasingly small target markets. Instead, this chapter shows you how to aggregate demand, not by focusing on the differences that separate customers but by building on the powerful commonalities across noncustomers to maximize the size of the blue ocean being created and new demand being unlocked, hence minimizing *scale risk*.

Chapter 6 lays out the design of a strategy that allows you not only to provide a leap in value to the mass of buyers but also to build a viable business model to produce and maintain profitable growth for itself. It shows you how to ensure that your company builds a business model that profits from the blue ocean it is creating. It addresses *business model risk*. The chapter articulates the sequence in which you should create a strategy to ensure that both you and your customers win as you create new business terrain. Such a strategy follows the sequence of utility, price, cost, and adoption.

Chapters 7 and 8 turn to the principles that drive effective execution of blue ocean strategy. Specifically, chapter 7 introduces what we call *tipping point leadership*. Tipping point leadership shows managers how to mobilize an organization to overcome the key organizational hurdles that block the implementation of a blue ocean strategy. It deals with *organizational risk*. It lays out how leaders and managers alike can surmount the cognitive, resource, motivational, and political hurdles in spite of limited time and resources in executing blue ocean strategy.

Chapter 8 argues for the integration of execution into strategy making, thus motivating people to act on and execute a blue ocean strategy in a sustained way deep in an organization. This chapter

FIGURE 1-4

The Six Principles of Blue Ocean Strategy

Formulation principles	Risk factor each principle attenuates
Reconstruct market boundaries	↓ Search risk
Focus on the big picture, not the numbers	↓ Planning risk
Reach beyond existing demand	↓ Scale risk
Get the strategic sequence right	↓ Business model risk
Execution principles	Risk factor each principle attenuates
Overcome key organizational hurdles	↓ Organizational risk
Build execution into strategy	↓ Management risk

introduces what we call *fair process*. Because a blue ocean strategy performance represents a departure from the status quo, this chapter shows how fair process facilitates both strategy making and execution by mobilizing people for the voluntary cooperation needed to execute blue ocean strategy. It deals with *management risk* associated with people's attitudes and behaviors.

Figure 1-4 highlights the six principles driving the successful formulation and execution of blue ocean strategy and the risks that these principles attenuate.

Chapter 9 discusses the dynamic aspects of blue ocean strategy—the issues of sustainability and renewal.

Let's now move on to chapter 2, where we lay out the basic analytical tools and frameworks that will be used throughout this book in the formulation and execution of blue ocean strategy.