## CHAPTER 2: THE ESSENCE OF MANAGEMENT CONSULTING FIRMS

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Chapter 2: The essence of management consulting firms

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SYNOPSIS

This chapter sets out the context within which management consultant work. It defines the practice of consultancy, puts this into a historical framework, explains the structure of the consultancy industry and its markets, profiles the major consultancies and then takes a look at the changes and developments affecting the smaller MCF. It analyses the various factors that influence the existence of the smaller MCF and consider Porter’s five forces model to obtain competitive advantage. It concludes by returning to the present and suggesting where this industry is heading.

The above-mentioned focus areas support objective 1: to conduct an overview of the essence of MCFs, by pursuing a strategic approach to obtain a competitive advantage and the strategic implications thereof.
2.1 INTRODUCTION

There are almost as many definitions of consultancy as there are consultants and each consultant and consultancy has their own slant on the work they do. In recent years, consultancy has become such an all-embracing pursuit, for a variety of reasons, that it is impossible to define consultancy as precisely. According to Sadler (2002:29) there are three definitions that together sum up what consultancy is all about.

Definition 1 states: the rendering of independent advice and assistance about management issues. This typically includes identifying and investigating problems and/or opportunities, recommending appropriate action and helping to implement those recommendations.

Definition 2 states: the service provided to business, public and other undertakings by an independent and qualified person or persons in identifying and investigating problems concerned with policy, organisation, procedures and methods, recommending appropriate action and helping to implement those recommendations.

Definition 3 states: management consulting is an advisory service contracted for and provided to organisations by specially trained and qualified persons who assists, in an objective and independent manner, the client organisation to identify problems, analyse such problems, recommend solutions to these problems and help, when requested, in the implementation of solutions.

Consultants have also been called ‘company doctors’ who is apt because the very term ‘management consultant’ appears to have originated from the medical profession. The word consultant first came to mean someone whose advice you sought and it was then a short step to creating the term management consultant, that is, someone to whom you looked in order to counsel a client on managing a business (Sadler 2002:30).

Implicit in all the definitions the notion is that the consultant advises and encourages but never actually manages. There is one exception to this: outsourcing. When a management consultant takes on an outsourcing contract, they are very clearly...
entering the realms of management. Whether outsourcing is part of management consultancy is still being questioned but what cannot be denied is that outsourcing is what management consultancies are increasingly offering.

A firm’s asset or competency that is capable of being the competitive basis of many of its businesses is termed a core asset or competency and can be a synergistic advantage (Aaker 2001:141). Prahalad & Hamel (1990:79) suggest a tree metaphor, in which the root system is the core asset or competency, the trunk and major limbs are core products, the smaller branches are business units, and the leaves and flowers are end products. Therefore a smaller MCF may not recognise the strength of a competitor if it simply look at its end products and fail to examine the strength of its root system. Core competence represents the consolidation of firm-wide technologies and skills into a coherent thrust. A core asset, such as brand name or a distribution channel, merits investment and management that span business units.

Loewen (1999:59) argues that consultants do not have a strategy in their heads. Their role is to set up the process around people and all of their experiences, and to tease out innovative thinking, and not to do their thinking for them. In other words, strategists should be the facilitators, matchmakers or catalysts, but not the thinkers. This chapter address the relationships and influential factors that influence the innovative thinking and the impact of the five forces on MCFs.

### 2.2 OVERVIEW OF MANAGEMENT CONSULTING FIRMS

The origins of management consultancy are essentially Anglo American (Sadler 2002:33). The industry was founded by pioneers in the United States of America in the late nineteenth and early twentieth centuries and by leading management thinkers and businessmen in the United Kingdom from the 1920s onwards. The first management consultants came into being between 1870 and 1914 in the United States of America and their main role was to help manufacturing companies to become more productive and more efficient. These companies were especially active in the steel and engineering companies in the north-west of America. Among the early pioneers were Charles Sampson, Frederick Taylor, Frank and Lillian Gilbreth, Arthur D Little and...
Edward Booz. They were all American and were management researchers just as much as they were management consultants (Sadler 2002:33).

Frederick Taylor left a particular legacy and his prescriptions have caused him to be called the father of "scientific management." Taylor was essentially concerned with what was later called organisation and method studies. Frank and Lillian Gilbreth are also important in the history of consultancy and were fascinated by the interplay between man and machine; more often than not by the apparent lack of interplay. Unlike Taylor, their starting point was the human factor rather than the mechanical one. They were enthusiasts and evangelists for their ideas and their sheer exuberance had a profound effect on the development of management consultancy (Sadler 2002:34).

After World War I, management consultants played a big part in the development and restructuring of the American industry. Consultancy boomed in the 1960s in response to a rapidly changing industrial and economic structure. During the 1970s, all previous assumptions about management of a business have been shattered because of the oil price crisis. Between 1973 and 1978 world oil prices were twice raised to unheard of heights. These price rises dramatically shifted business priorities. The financial performance became the top concern. When financial return on capital became much more critical, it was natural for the accountants to start offering consultancy advice in a significant way. During the 1970s, accountancy firms began to take the consultancy market seriously and by the end of the 1970s the accountancy firms had a sizeable share of the market. During the 1980s there was a series of developments in management thinking that affected the consultancy world (Sadler 2002:36).

The internationalisation of business has helped to create a whole new segment of the consultancy market, namely culture change management. The management of international companies with diverse systems, cultures and products has proved extremely complex. In these large enterprises the cultural changes that they were experiencing were both externally and internally generated. These companies cut across different functions and their effects are often subtle but powerful (Sadler 2002:37).
Porter was an early exponent of the need for firms to add value. In particular, Porter introduced the concept of the value chain, where each activity performed by a firm can be analysed in order to show how it interacts with other activities. Porter (Sadler 2002:38) states “A firm gains competitive advantage by performing these strategically important activities more cheaply or better than its competitors.”

Since the 1990s the Internet has begun to make a considerable impact on the world of management consultancy. The rise of e-commerce has led to the new opportunities for management consultancies as their clients seek to exploit this new medium of business. At the same time it has encouraged the development of e-consultancies, specifically set up to address the needs of e-business. Some of these consultancies will fall by the wayside or be acquired by the older, more traditional firms. Only a selected number will survive as independent entities. What is beyond doubt is that the e-consultancy is here to stay and will become increasingly important.

These newer developments mean that management consultancies are having to review their own operations and practices in order to survive and prosper in the 21st century. They have many issues to consider such as core competences, recruitment and training. For many MCFs the key issues are identity and purpose. What are they in business for? What should their role be? And how should they adapt to a new future? The essence of smaller MCFs needs to address these questions in order to survive.

## 2.3 FACTORS INFLUENCING THE EXISTENCE OF SMALLER MANAGEMENT CONSULTING FIRMS

MCFs have extensive relationships with the world’s leading companies and governments and work with organisations of all sizes. Using the industry and business-process knowledge, the service offering expertise and the insight into and access to existing and emerging technologies, MCFs identify new business and technology trends and formulate and implement solutions for clients under demanding time constraints. Specifically, MCFs help clients to:
• identify and enter new markets;

• increase revenues in existing markets;

• improve operational performance;

• deliver products and services more effectively and efficiently.

The MCF business is structured around operating groups, which together comprise of various industry groups serving clients in major industries. The management consulting industry focus provide an understanding of industry evolution, business issues and applicable technologies, enabling to deliver innovative solutions tailored to each client or, as appropriate, standardised capabilities that they offer to multiple clients.

MCFs develop a full spectrum of services and solutions that address business opportunities and challenges common across industries. The business process outsourcing, businesses provide function-specific and/or industry-specific business services to multiple clients on an outsourced basis through standard operating models. Client engagement teams typically consist of industry experts, capability specialists and professionals with local market knowledge. The MCF client teams are complemented by professionals in the delivery centres, who capture replicable components of methodologies and technologies to create client solutions quickly, predictably and cost-effectively.

Because research and innovation have been major factors in achieving success, MCFs spend huge amounts of money every year on research and development. MCFs use the investment in research to help create, commercialise and disseminate innovative business strategies and technology to develop market-ready solutions for their clients. The research and innovation programme is designed to generate early insights into how knowledge can be harnessed to create innovative business solutions for clients and to develop business strategies with significant value.
As the management consultants have moved into newer areas, such as strategic marketing, information technology and outsourcing, other professional groups are moving into consultancy and will have an affect on the existence of smaller MCFs, they are:

- *designers and technologists:* are offering product development and design consultancy.
- *corporate identity companies:* are offering marketing and communications consultancy.
- *advertising and marketing agencies:* are also providing consultancy services in marketing, advertising strategy and brand management.
- *executive search companies and employment agencies:* are offering consultancy advice on human resource management.
- *environmental consultancies:* are providing consultancy advice that inevitably overlaps with the kind of work that consultants provide in manufacturing.

Source: Sadler (2002:43)

The following factors have an influence on the existence of smaller MCFs:

- *Economic factors:* the economic growth has produced consulting opportunities in the areas of capital markets, strategic planning, finance, marketing, human resources development, organisational development, feasibility studies and system installation.

- *Globalisation:* because more multinational firms are interested in gaining a niche in the market, consultancy assistance in the following fields are needed: joint ventures, franchising, cross cultural management, and international standardization.

- *Technology:* consulting opportunities are incurred by developments in information technology, automation, software application, and bio-technology.
- **Socio-economic factors**: consultancy services are needed in solving problems related to: rapid developments in urbanisation; need for vocational training; and fierce competition in penetrating new export markets;

- **Political factors**: changes in government policies introduce new opportunities for consulting firms.

- **Environmental management**: consulting opportunities abound in companies concerned in energy conservation, pollution control, and industrial waste control. Opportunities are also present in the conduct of environmental impact assessments for various companies.

- **Managerial needs**: because of the transformation of business leadership structure for ownership to professional management, consulting services are needed in the areas of business management tools, and future work planning.

2.4 **STRATEGIC MANAGEMENT APPROACH: PORTER’S FIVE FORCES ANALYSIS**

"Business strategy is now the single most important management issue and will remain so for the next few years"

Loewen 1999:9

"What is an opportunity can only be decided if there is a strategy"

Drucker 2003:43

Strategy is defined in the Oxford English Dictionary as "The art of war or the art of planning and directing larger military movements … or war" (Strydom et al. 2000:254). Strategy thus has a definite military connotation. Army commanders make tactical decisions, combine them in a strategy and then implement the strategy in order to outwit and overcome the enemy. In the business environment, this concept have been proved to be popular, especially in a competitive, dynamic situation where smaller
MCFs continually have to formulate strategies in order to ensure survival and their profitable existence.

Porter sees strategy as necessarily deductive and deliberate, as if strategic planning and emergent strategy do not exist. (Mintzberg et al. 1998:119). According to Porter (1997:162 & 163) “… if strategy is stretched to include employees and organisational arrangements, it becomes virtually everything a company does or consists of. Not only does this complicate matters, but it obscures the chain of causality that runs from competitive environment to position to activates to employee skills and organisation.”

Loewen (1999:110) said that focusing on competition is a good spur to keep you going, but it is not what will carry you to victory. But by focusing on the client, the firm will get the victory. “Strategy is first and foremost about your customer. Yet ‘how do I beat my competition?’ is typically what most people think strategy is about, and is the ‘most frequently cited concern’ of the majority of business leaders. Beating your competition is the outcome of a good strategy.” Porter (2002:34) contends “Competitive strategy must grow out of a sophisticated understanding of the structure of the industry and how it is changing.”

Michael Porter has demonstrated that, although the competitive pressures in various industries are never precise, the competitive process works similarly enough to use a common analytical framework, in gauging the nature and intensity of competitive forces. The state of competition in an industry is a composite of the five competitive forces according to Porter (in Thompson & Strickland 2001:80). Whether it is domestic or international, the nature of competition is embodied in these forces, namely:

- the rivalry among competing sellers in the industry;
- the potential entry of new competitors;
- the market attempts of companies in other industries to win customers over to their own substitute products;
- the competitive pressures stemming from supplier-seller collaboration and bargaining;
- the competitive pressures stemming from seller-buyer collaboration and bargaining.
Porter’s five competitive forces are more refined way to assess environments, according to Griffin (1996:84). Anthony & Govindarajan (2003:64) states that every business unit should develop a competitive advantage in order to accomplish its mission.

The five forces model determine industry profitability because they shape the prices businesses can charge, the costs businesses have to bear, and the investment required to compete in an industry. The threat of new entrants limits the overall profit potential in the industry, because new entrants bring new capacity and seek market share, pushing down margins. Powerful buyers or suppliers bargain away to the profits for themselves. Fierce competitive rivalry erodes profits by requiring higher costs of competing or by passing on profits to customers in the form of lower prices. The presence of close substitute product limits the price competitors can charge without inducing substitution and eroding industry volume.

According to Miller & Dess (1993:64) the competitive environment refers to the situation facing the business within its specific competitive arena. The competitive arena combines the forces that are relevant to a business strategy, which includes competitors, customers and suppliers. The five forces model can be utilised as an analytical tool for examining the competitive environment. A business can survive and succeed in the long term if it develops strategies successfully to confront the five forces, which shape the structure of competition in an industry, according to O’Brien (1996:402). A business can develop a variety of competitive strategies to confront these competitive forces.

According to Porter (1979:137-145), the five forces model is “… a powerful tool for systematically diagnosing the principal competitive pressures in a market and assessing how strong and important each one is.” It is also argued by Thompson & Strickland (2001:80) the five forces model is not only the most widely used technique for competition analysis, but also relatively easy to understand and apply. The collective strength of these five forces determines the competitiveness in the industry and therefore its profitability (Smit & Cronje 1999:73). According to Pearce & David
(1997:109) contend that, every industry has underlying structures that give rise to these five competitive forces. A business wanting to cope best with its industry environment or to influence that environment in its favour must learn what makes the environment tick. MCFs must understand how the five forces work in the management consulting industry, and how they affect the company in its particular situation.

The Five Forces Model is a key analytical tool for diagnosing the competitive environment of MCFs. Porter’s five forces model is very orderly and structured. It explains neatly why some industries are more attractive than others. In a way that at least give managers confidence in their judgement, even if it did not make them feel better about being in a dead loss market (Pitt 2000:20). The five forces can relate to business and management issues, such as customers and suppliers, barriers to entry and substitute products and firm-firm competition.

The traditional view of strategy in MCFs has been that it is possible to understand fully the environment in which the MCF functions and therefore to plan for the future accordingly. However, as the environment is changing so swiftly, smaller MCFs need to adapt and plan their strategies accordingly. Pitt (2000:20) expresses that “The kinds of innovations that we are talking about are not simple improvements, rather we are referring to what have become known as killer applications.” This killer application is not merely an innovation that improves the way something is done but is one that changes the way society itself works and functions.

According to Robert (1997:123) successful companies are those that can leverage their unique set of capabilities (driving force and areas of excellence) across the largest number of products and markets. Thus, MCFs that can spread the heartbeat of the business and their accompanying strategic capabilities across as many business units as possible are those that will assist that business units in surviving and prospering. Figure 2-1 illustrates Porter’s five forces responsible for competition in a particular industry.
Figure 2-1: Porter’s Five Forces Model

FIRMS IN OTHER INDUSTRIES OFFERING SUBSTITUTE PRODUCTS

Competitive pressures coming from the market attempts of outsiders to win buyers over to their products

SUPPLIERS OF RAW MATERIALS, OR OTHER RESOURCE INPUTS

Competitive pressures stemming from supplier-seller collaboration and bargaining

RIVALRY AMONG COMPETING SELLERS

Competitive pressures created by jockeying for better market position and competitive advantage

BUYERS

Competitive pressures stemming from seller-buyer collaboration and bargaining

POTENTIAL NEW ENTRANTS

Competitive pressures coming from the threat of entry of new rivals

Source: Adapted from Porter 1979:137-145; Thompson & Strickland 2001:81
2.5 CLOSURE

The strength of each of the five competitive forces is a function of industry structure or the underlying economic and technical characteristics of an industry (Porter 2002:38). The buyer power is a function of the number of buyers, how much of a MCF sales are at risk to any one buyer and whether a product is a significant fraction of buyer’s own costs which leads to price sensitivity. The threat of entry depends on the extent of barriers to entry, such as brand loyalty or economies of scale. Therefore a smaller MCF needs a strategy that reduces entry barriers and nullifies the competitor’s advantages.

Porter’s five forces model is critical because it influences the price, costs, and required investments of firms in a given industry. The strength of the five forces varies from industry to industry and their collective strength will determine the profitability of firms in that industry.

A smaller MCF needs to first analyse the competition in order to understand the competitive pressures associated with each of the above forces. Secondly, it must determine whether these pressures result in a strong or weak competitive force in the market. Thirdly, it should think strategically about what sort of competitive strategy the smaller MCF would need to employ, given the rules of competition in the industry.

The smaller MCF must employ a strategy to insulate the business as much as possible from the five competitive forces, influence the industry’s competitive rules in its favour and lastly, to gain a competitive edge over competitors. The peculiarities of each of these five forces may explain why businesses adopt a particular strategy. The essence of smaller MCFs is to gain a competitive edge if the smaller MCF can cope with the five forces better than their rivals.