

FUNDAMENTALS OF STRATEGIC ANALYSIS

What is Strategy?

Strategy: A strategy is a plan or method aimed at achieving a goal.

Tactics: The means used to put a strategy into action and achieve a set of objectives.

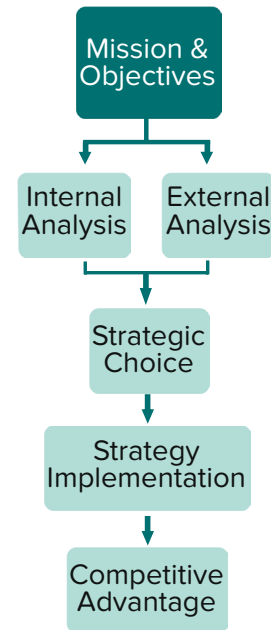
Strategic management process: A sequence of analyses and choices that helps a firm ensure it's on the right track. The process is composed of four steps:

Setting the mission and objectives: A company first determines its main purpose and aspirations. Then it sets **objectives**, or specific performance targets, to determine how well it's fulfilling its mission.

Strategic analysis: A company performs an **internal analysis** to evaluate their strengths and weaknesses, and an **external analysis** to assess the competitive environment.

Strategic choice: A decision made by a firm in order to achieve a competitive advantage.

Strategic implementation: The firm implements certain tactics to carry out its strategy.



Porter's Five Forces Model

Industry: A group of providers of a product category.

Porter's five forces model: A framework used to describe and evaluate the competitive forces at play in an industry. It consists of:

Rivalry among existing firms: The force defined by the effects of competition between companies.

Threat of new entrants: The force of new entrants threatening to offer something not easily replicated by others and reduce profits for the already established firms.

Threat of substitutes: The force consisting of the threat that products from outside the industry could offer similar benefits or be used interchangeably.

Bargaining power of suppliers: The force of suppliers being able to set prices for in-demand items.

Bargaining power of customers: The force created by customers being able to switch between products or firms at a low cost and make demands collectively.



Applying Porter's Five Forces

Barriers to entry: These prevent new players from being competitive. As barriers increase, interest in entering the industry decreases and lowers the threat of new entrants.

Already established companies make it more difficult for new companies to enter the industry because of the incumbents brand reputation, supplier relationships, customer loyalty, and ability to achieve economies of scale.

The bargaining power of customers increases when there are few buyers and many sellers and when switching between products is easy for the customer.

The bargaining power of suppliers increases when there are fewer suppliers, the supplier's business is important to the industry, and there are not substitutes readily available.

PESTEL Analysis

Macroenvironment: The external factors that influence the firm's choices and performance.

PESTEL analysis: A systematic way to evaluate the most important macroenvironmental elements that might affect a firm's performance. The components of PESTEL are:

Political: Factors concerning governments and government policies.

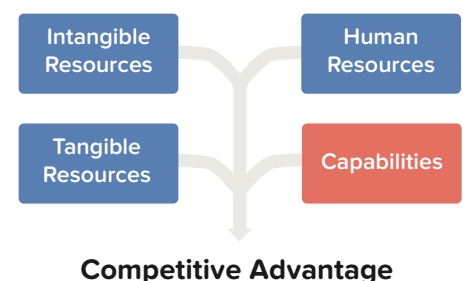
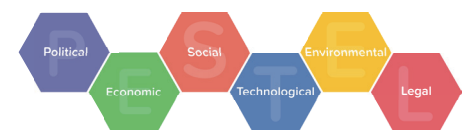
Economic: Factors that impact purchasing power.

Social: Factors that impact market size and customer needs.

Technological: Factors that relate to the rate of technological change and the overall level of research and development activity.

Environmental: Factors related to weather and the climate.

Legal: Factors concerning laws and legislations.



The Resource-Based View

Resource-based view (RBV): An inventory of the resources a firm owns and its existing capabilities for leveraging those resources into a competitive advantage.

There are three types of resources that the RBV model examines:

Tangible resources: Any tangible assets that can create customer value and which can be seen or quantified.

Intangible resources: Any assets that are not explicitly visible or documented, like brand reputation.

Human resources: The productive efforts, skills, and expertise of the employees.

Organizational capabilities: The ability of a firm to mobilize its resources.

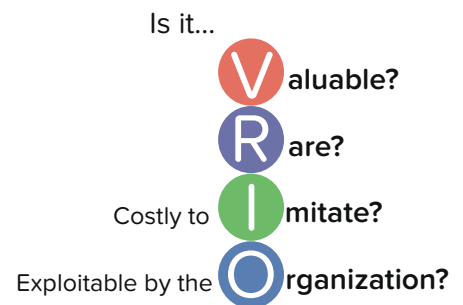
VRIO framework: Strategists determine which resources to include in an RBV by using the VRIO tool. It consists of four questions to ask about a resource or capability.

Is it **valuable**? A valuable resource is one that enables a firm to enhance its competitive advantage.

Is it **rare**? A rare resource is only controlled by a small number of firms.

Is it costly to **imitate**? A resource that's costly to imitate means other firms face a cost disadvantage in getting it.

Is the firm **organized** in a way to exploit it? An appropriately organized firm can maximize the utility of a resource.



Building a Competitive Advantage

Competitive advantage: An edge a company holds when it generates more economic value than rival firms.

Business-level strategy: A set of actions or plan used to gain and sustain a competitive advantage in a single market or industry.

Porter's generic strategies: A theory that lists three main ways a company can gain competitive advantage. These are:

Cost leadership: A business-level strategy that centers on keeping costs of operation low.

Economies of scale: A strategy that involves scaling up so the per-unit cost of production drops.

Diseconomies of scale: When the per-unit cost of production increases after scaling up too much.

Differentiation strategy: It is centered on enhancing the perceived value of a company's products or services relative to other firms' offerings so that customers will pay more.

Technological leadership: Investing in particular technologies early on. This includes preemptively buying assets valuable to the new technology and making it costly for customers to switch to substitute products.

Focus strategy: There are two variants of this strategy: cost focus and differentiation focus, which apply cost leadership and differentiation to niche markets, respectively.

Stuck in the middle: When a firm chooses to pursue multiple strategies and does not excel at any of them. The firm may still be profitable, but may not outperform its rivals.

