

# Intro to Strategy - Mgmt 654

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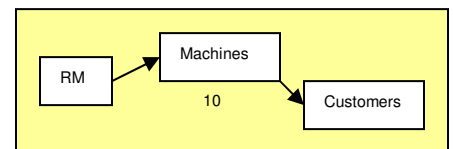
## I. Background

- **classis competitive strategy** – competitive position w/i attractive industry (focus) + outperform competition (goal) + 5 force / value chain / generic strategies (tools)
- **Value Innovation** – move industry boundaries / create competitive space (focus) + make comp irrelevant (goal) + value curves / 6 paths (tools)
  - e.g., - Cirque de Soliel – lowered costs + raised revenues / WTP
- **business strategy** – how to compete in a given industry (~ requires sustainable competitive advantage)
  - this is Industry Analysis + Competitive Analysis below (??)
- **corporate strategy** – which industries to compete in (~ scope + resources / capabilities + etc)

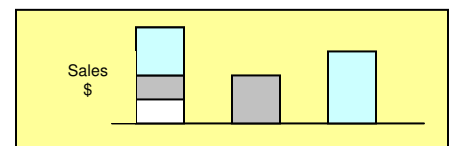
## II. Industry Analysis

- **General**
  - **why do this** – eval industry attractiveness + understand economics for developing strategy + identify opps to improve industry structure
  - **industry types** –
    - perfect competition – many firms + no BtE + homogeneous products + perfect info
    - oligopoly – few firms + significant BtE + potential differentiation + imperfect info
    - duopoly – two firms + significant BtE + potential differentiation + imperfect info
    - monopoly – one firm + high BtE + potential differentiation + imperfect info
  - **profitability** ~ driven by value of product + competition (presence / possible entry) + supply chain bargaining power
  - **consider** - can industry participants shape industry (e.g., Coke / Pepsi)
- **Tools** –
  - **A) Industry History**
    - **used to** – identify trends + prior successful / failed strategies
    - **consider** –
      - ◆ historical analysis must be consistent with 5 Force
      - ◆ collusion among competitors? (Coke v. Pepsi)

- **B) Supply Chain**
  - **used to** – identify key players + flow of goods
  - **consider** - how can it be improved

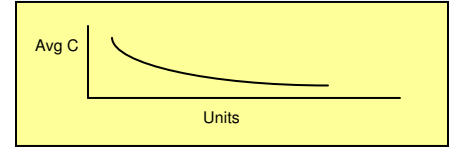


- **C) Channel Analysis**
  - **what is it** - inter-company comparative bar chart breaking out revenues by product
  - **used to** – compare relative importance of products to each firm
  - **consider** – sales / costs m/b on comparable basis (~ recognize price premium / discount affects actual volumes)



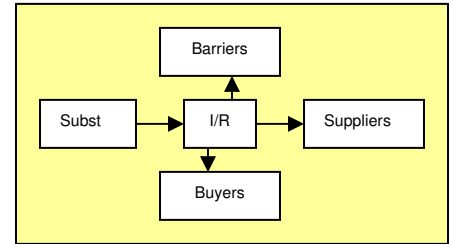
➤ **D) Economies of Scale**

- **used to** – identify position sustainability of market position
- **consider** –
  - ◆ **basic point** – significance of EoS depend on market size
  - ◆ **advanced point** – basic point assumes fixed costs are given, BUT firms can choose the level of their fixed costs to better adapt to EoS



➤ **E) 5 Force Analysis**

- **used to** – evaluate appeal of entering a market
- **components** –
  - ◆ **i) Substitutes**
    - > defn ~ our  $Q_D$  falls if its (P falls) / (performance rises)
    - > factors – performance + availability + consumer choice / lifestyle (Coke)
  - ◆ **ii) Supplier Power** –
    - > consider – 5 force analysis on upstream suppliers to measure power
    - > diminished by – use of commodities + ability to vertically integrate
  - ◆ **iii) Industry Rivalry** –
    - > depends on industry structure + past mgmt of comp relationships
    - > identify industry structure?
    - > How do members compete? P, Advert / Brand, differentiation, distribution
  - ◆ **iv) Barriers to Entry** –
    - > Generally - Brand + low cost mfr + product differentiation + fixed cost EoS + Capital Required
    - > **switching costs** – reduce entry incentive / viab of subst + gives supplier more power
    - > Coke ~ contracts / relationships + Advertising EoS
    - > Invacare - Aggressive incumbent
  - ◆ **v) Buyer Power** (by channel / end consumer) –
    - > factors – fragmentation + channel power (~ McDonalds v Coke)

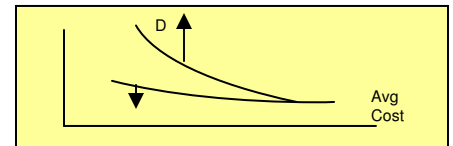


➤ **F) Trends Analysis**

- **used to** – evaluate longevity of strategy + identify potential entries / exits + look for changes to competitor products + identify future market changes (Sunrise's aging population)
- **look at** – Share P + RoS + number of competitors + et al

➤ **G) Market Size**

- **used to** – evaluate appeal of a market + identify how to increase market size / decrease costs
- **consider** – network externalities = explosive growth



➤ **H) Game Theory (BSB)**

- **used to** – identify reactions of rational competitors + find ways to change competitive rules (commit to market) + assess trade-offs
- **consider** –
  - ◆ Real options – limit downside risk
  - ◆ competitor analysis ~ resources / capabilities + strategy + assumptions + goals + entry deterrence
  - ◆ weakness ~ uncertainty of outcomes + cannot expect numerical outcomes

• **Remember**

- industries that compete on P are less attractive than those that compete on product differentiation

• **Cases** –

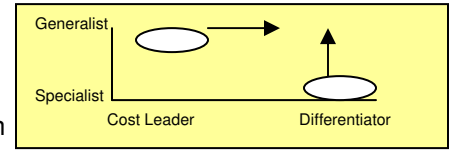
- Dell – computer industry is unattractive due to competitive convergence

### III. Competitive Advantage

- Tools –

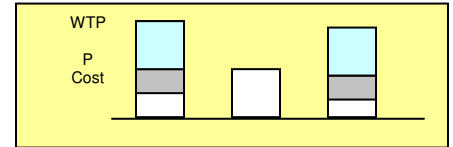
- **A) Strategic Groups**

- **used to** – identify relative market position / trends of companies / products based on competitively important attributes
- **attributes** -
  - ◆ Market – product; geography; channels; product differentiation
  - ◆ Supply – production process; R&D capability
  - ◆ **generic strategies** -
    - > **cost leader** – competitive advantage from lower costs (thru EoS, experience curves, innovation, etc.)
    - > **differentiator** – comp advantage from superior performance generating high willingness to pay that offsets costs (but watch for cost leader innovation)
    - > **stuck in the middle** – trying to do both and getting out competed
- **consider** –
  - ◆ what trends are present
  - ◆ who is cost leader - sales / costs m/b on comparable basis (~ recognize price premium / discount affects actual volumes)



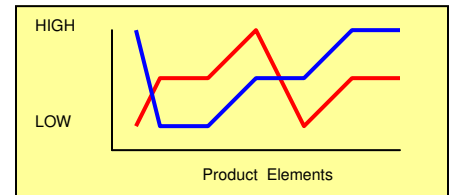
- **B) Competitive Advantage** –

- **used to** – compare value to customers / compare willingness to pay
- **consider** –
  - ◆ what is P premium earned by each firm?
  - ◆ **value added** = (Avg WTP – Avg Cost) \* Volume
  - ◆ **value capture** ( $\pi$ ) = (Avg P – Avg Cost) \* Volume



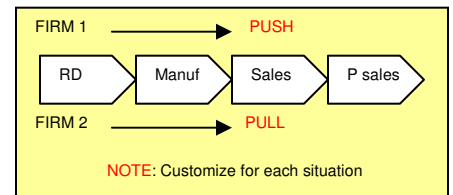
- **C) Value Curves** –

- **used to** – compare relative value to customer of **product** features
- **consider** –
  - ◆ draw curve for both (i) customers and (ii) distributors
  - ◆ to discover new curve →
    - > **i)** eliminate factors industry takes for granted
    - > **ii)** raise factors above industry standard
    - > **iii)** create factors that industry has not considered
    - > **iv)** reduce factors below industry standard where possible



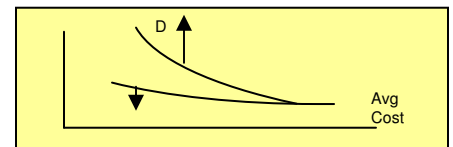
- **D) Value Chain** –

- **used to** – identify relative market position of companies / products
- **consider** -
  - ◆ customize steps based on specifics of each organization
  - ◆ are sales **pushed** or **pulled**?
  - ◆ key question – do policies fit internally across chain
- **Dell** –
  - ◆ by cutting out middleman → competes with both mfr & resellers
  - ◆ knows where its model fits best (large corp clients + developed markets geographically)



- **E) Value Creation**

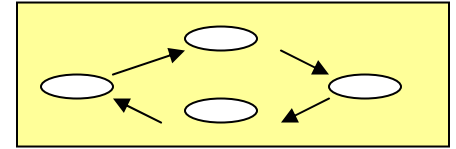
- **used to** – identify relative market position of companies / products
- **consider** -
  - ◆ identify important compliments
  - ◆ combine old elements in new ways (~ Cirque de Soleil)
  - ◆ focus on different part of buyer chain (Bloomberg IT dept → traders)
  - ◆ reverse functional / emotional focus (Swatch – functional → emotional)
  - ◆ slopes – to evaluate . . .
    - > Demand – consider elasticity



- > Supply – consider Scale and Fixed Costs
- value creation process –
  - ◆ i) visual awakening – value chain / value curve identifies common understanding of industry
  - ◆ ii) visual exploration – develop new value curves (see above)
  - ◆ iii) visual strategy fair – seek input from all parties potentially impacted
  - ◆ iv) visual communication – prep new value curve + communicate up / down / out
- evaluation process (~Wal-Mart) –
  - ◆ i) compare relative costs b/w firms – note that costs m/b on same basis
  - ◆ ii) assess WtP → value curves / volume information
  - ◆ iii) identify competitive advantages → value chain

➤ **F) Sustainability –**

- consider – Any threats other than imitation? - forex + innovation
- comes from
  - ◆ i) BtE at industry level (~ 1<sup>st</sup> mover advantages from strong increasing returns) - Brand + relationships + EEs / culture + EoS + complexity + Time
  - ◆ ii) Btl ~ levq resources / capabilities to create competitive advantage
- break by – leapfrog through innovation



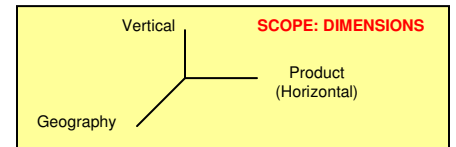
**IV. Corporate Strategy**

• Remember

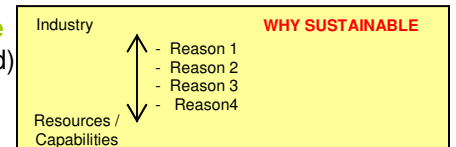
- Key Message ~ Scope of corporation must reflect value creation
- Corp Strategy Key skills ~ identify Econ of Scope + compare internalization v. market transactions + manage multi business firm (~ minimize value destruction)

• Analysis Process (Class 8)

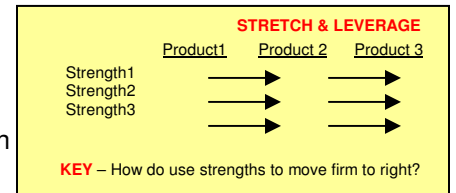
- i) **Scope** - identify scope of business
  - what does firm do? – customers + products + geography + activities in supply chain



- ii) **Competitive Advantage**
  - a) identify sources of sustainable competitive advantage – see III above
  - b) explain why advantage is sustainable (ask why it will not be sustained)

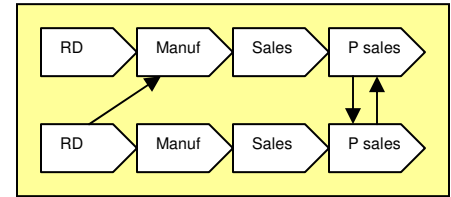


- iii) **Resources & Capabilities** –
  - a) What are they?
  - b) How can these be exploited?
    - ◆ A) stretch – develop new resources / capabilities
      - > without stretch – core strength → core rigidity
    - ◆ B) leverage -
      - > Barriers to limit – can make it hard to leverage for growth
      - > exploit existing / new resources and capabilities to achieve growth



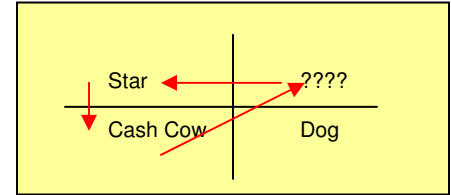
- ◆ C) vertical integration – two decisions . . . [Value Chain + Strategic Groups]
  - > i) make v. buy –
    - ↳ make benes – BtE + neutralize buyer / supplier power + better inter-activity mgmt
    - ↳ buy benes – greater EoS / learning + market efficiencies (flexible to choose different supplier) + Econ of Specialization
  - > ii) how structure relations for externalized processes –

- ◆ **D) diversification** (Disney) ~ all about transferring capabilities b/w Value Chains of businesses
  - > i) define **value chain**
  - > ii) identify competitive (dis)advantages at each step in chain
  - > iii) look for **Economies of Scope** (~ shared activities or resources / capabilities) from inter-relationships b/w value chains of businesses



- ◆ **E) portfolio analysis** (Ciba Geigy) -

- > remember
  - industry analysis is more than **growth**
  - comp advert is more than **market share**
- > inherent problem – ignores other sources Econ of Scope
- > pros – rationalizes tough decisions (tho arbitrary) + non-financial resources may be scarce as well
- > cons – only works if resource constrained (breaks if can allocate resources to invest in positive NPV projects)



➤ **iv) Identify Strategy's Value –**

- **a) superior performance requires** – all of

- ◆ **1) Value creation / Value added** ~  $(\text{Avg WTP} - \text{Avg Cost}) * \text{Volume}$ 
  - > create ability to earn more ~ value to society / not S/H
  - > industry → usually simply assumed to occur + grow Market
  - > company / positioning → comp advantage + value innovation + adjusting value chain
- ◆ **2) Value capture (profit)** ~  $(\text{Avg P} - \text{Avg Cost}) * \text{Volume}$ 
  - > ~ value to S/H
  - > industry → 5 forces + analyze competitive pressures
  - > company / positioning → sustainability (barriers to imitation)
- ◆ **3) Recognition of Demand / Supply side effects on Market Size**
  - > demand – subst + complim + demographics + elasticity
  - > supply – innovation + input costs + scale econ + gov't regs
- ◆ **4) Limit value destruction** – killing a cash cow? + Bureaucratization

- **b) measurement** ~ DCF

- ◆ account for scope economies (O/W why internalize)
- ◆ agency problems will effect C/F estimates
- ◆ uncertainty in C/F → **real options** (~ value increases with more uncertainty)
  - > real option value ~ (lost option to wait) + NPV option to abandon + NPV growth options

➤ **v) Compare strategy value to next best alternative** – sell out / spin off