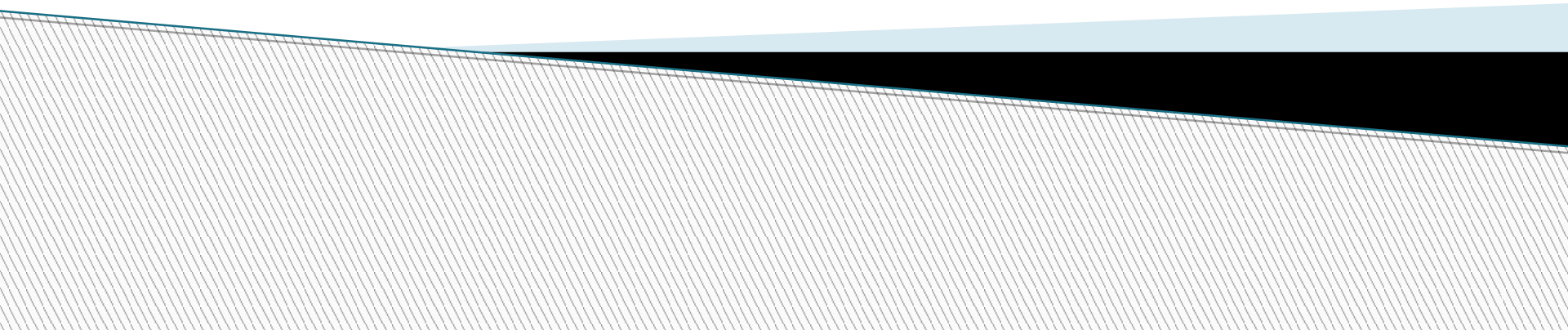


Module 2

Strategic Intent: External Environment Analysis



What we will cover

External Environment Analysis

Analysis of General Environment

Analysis of Industry Environment

Porter's 5 Forces Model

Driving Forces Analysis

Strategic Grouping

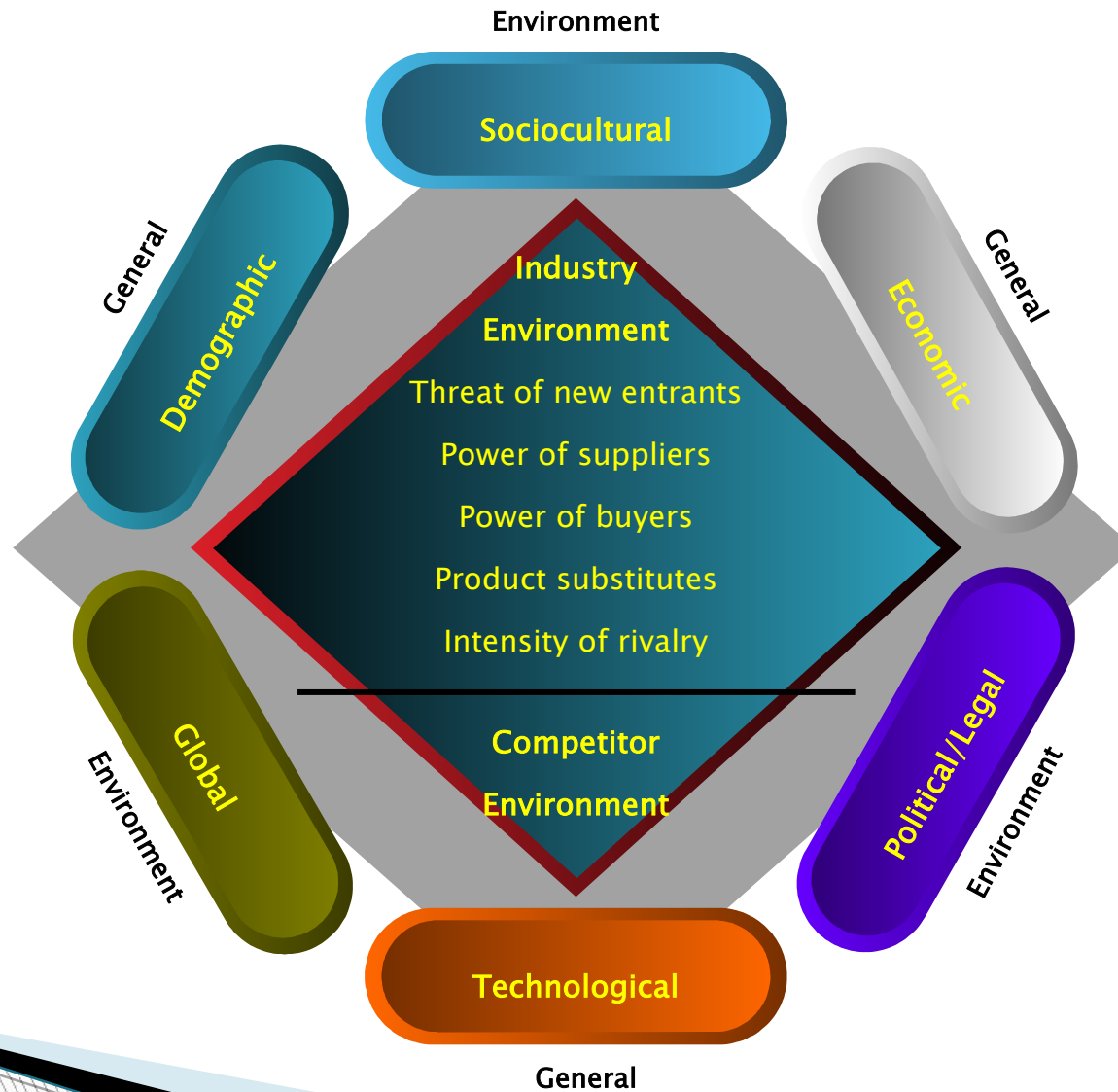
External Factors Evaluation (EFE) Matrix

Competitor Analysis

External Environment Analysis



The External Environment



The External Environment

- ▶ A firm's external environment creates
 - **Opportunities**
 - Any General environmental condition which if exploited helps a firm to achieve strategic competitiveness
 - **Threats**
 - General environment condition that may hinder a company's efforts to achieve strategic competitiveness

Collectively, Opportunities and Threats affect a firm's strategic actions

External Environment Analysis

Scanning



Identifying early signals of environmental changes and trends

Monitoring



Detecting meaning through ongoing observations of environmental changes and trends

Forecasting



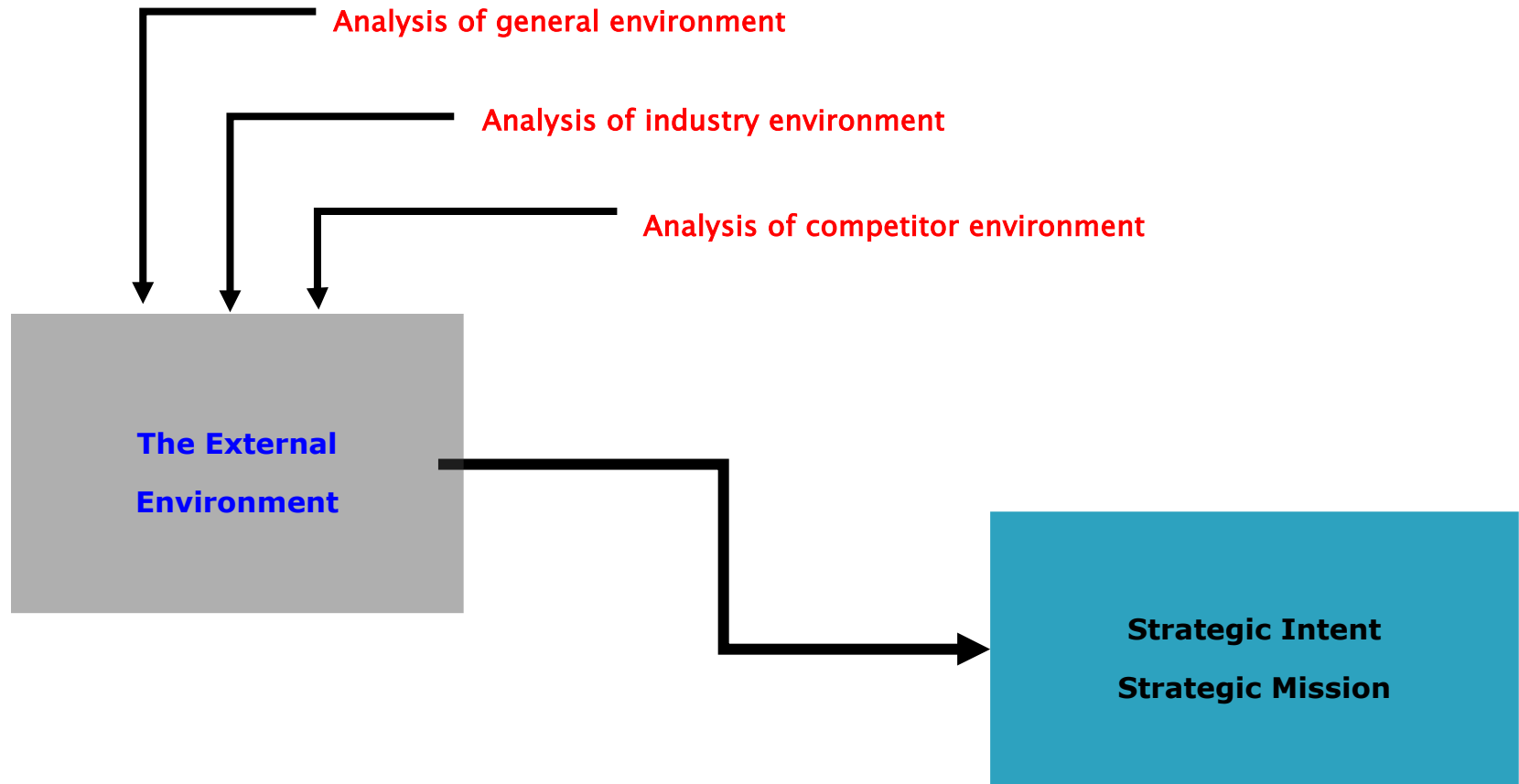
Developing projections of anticipated outcomes based on monitored changes and trends

Assessing



Determining the timing and importance of environmental changes and trends for firms' strategies and their management

External Environment Analysis



A Firm's strategic actions are influenced by conditions in all the above three environments

Some Important Definitions

- **General Environment**

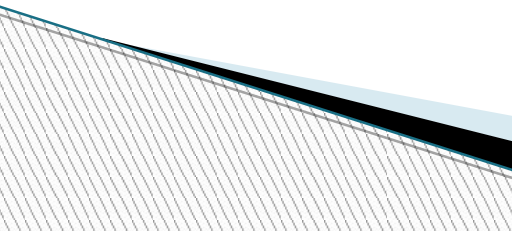
Dimensions in the broader society that influence an industry and the firms within it

- **Industry Environment**

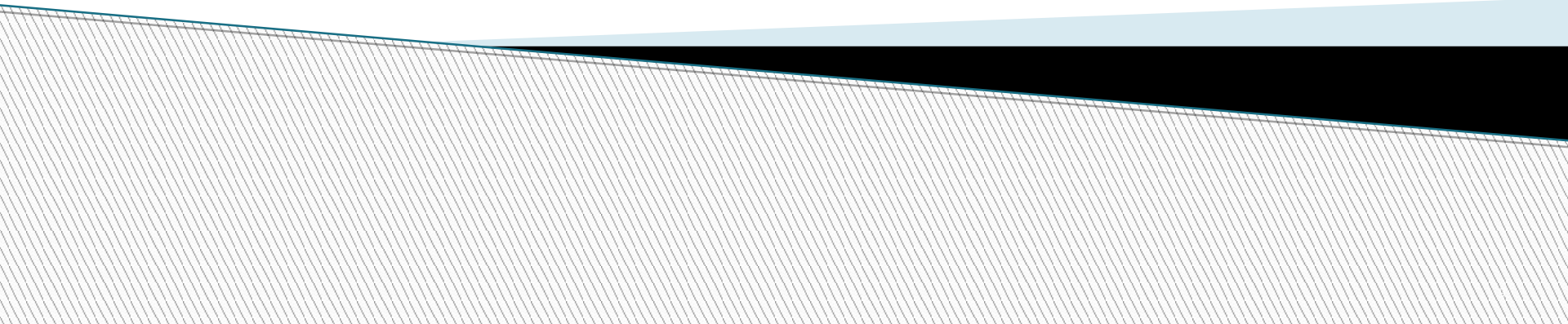
Set of factors that directly influences a firm and its competitive actions and response

- **Competitor Environment**

Focuses on each company against which a firm directly competes

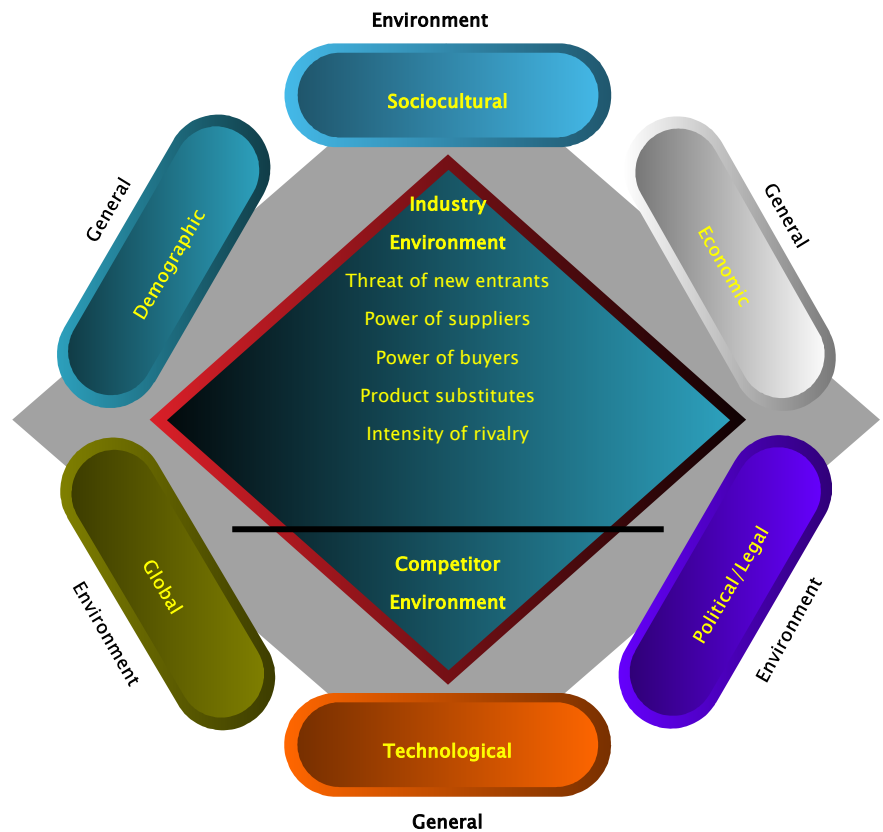


Analysis of General Environment



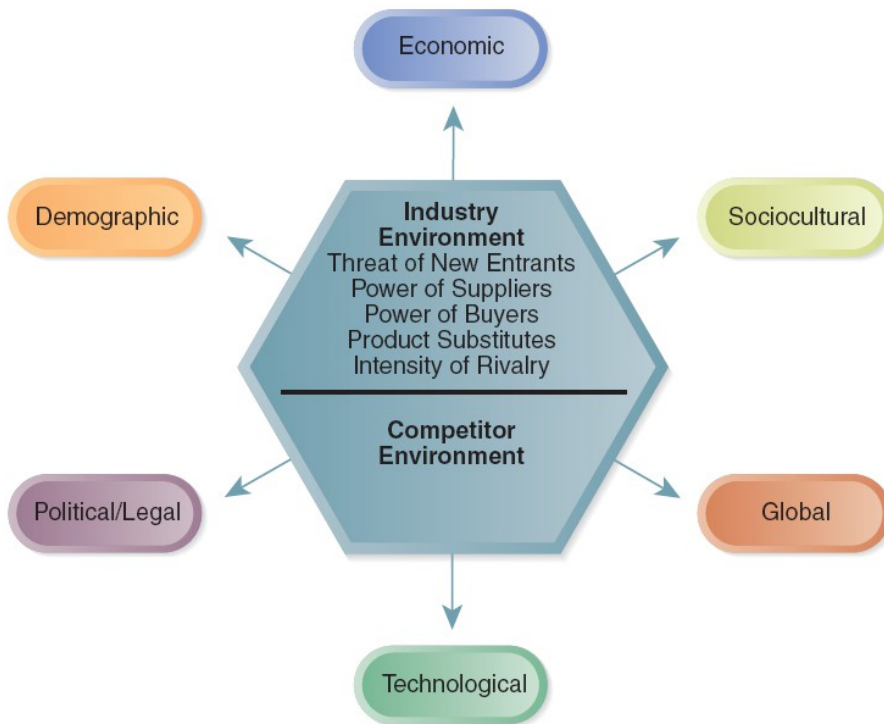
General Environment Analysis

- ▶ Dimensions in the broader society that influence and industry and the firms within it
 - Economic
 - Sociocultural
 - Global
 - Technological
 - Political/legal
 - Demographic



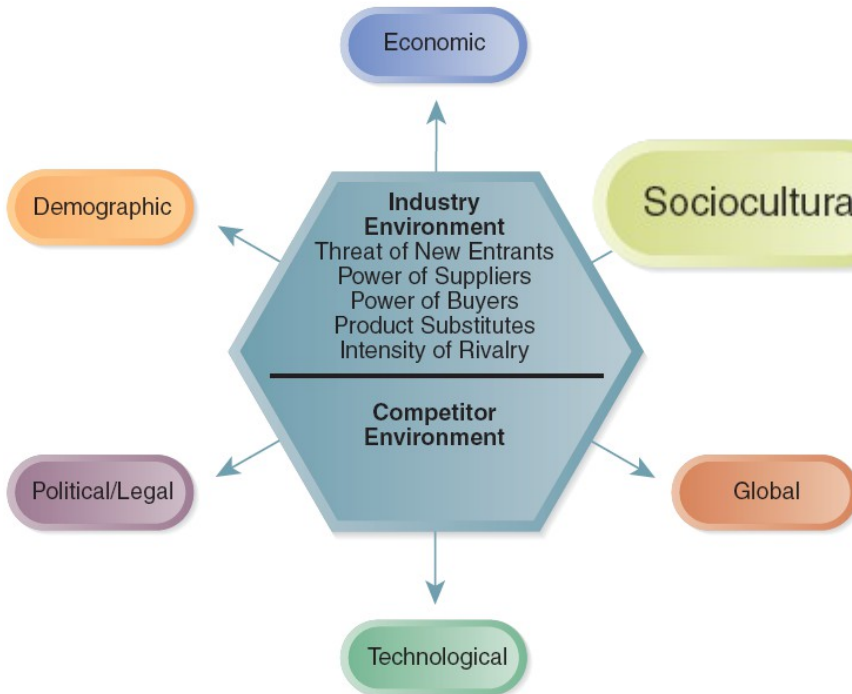
•PESTLE/ SLEPT/ PEST/ STEEP

GeneralEnvt– Economic Factors



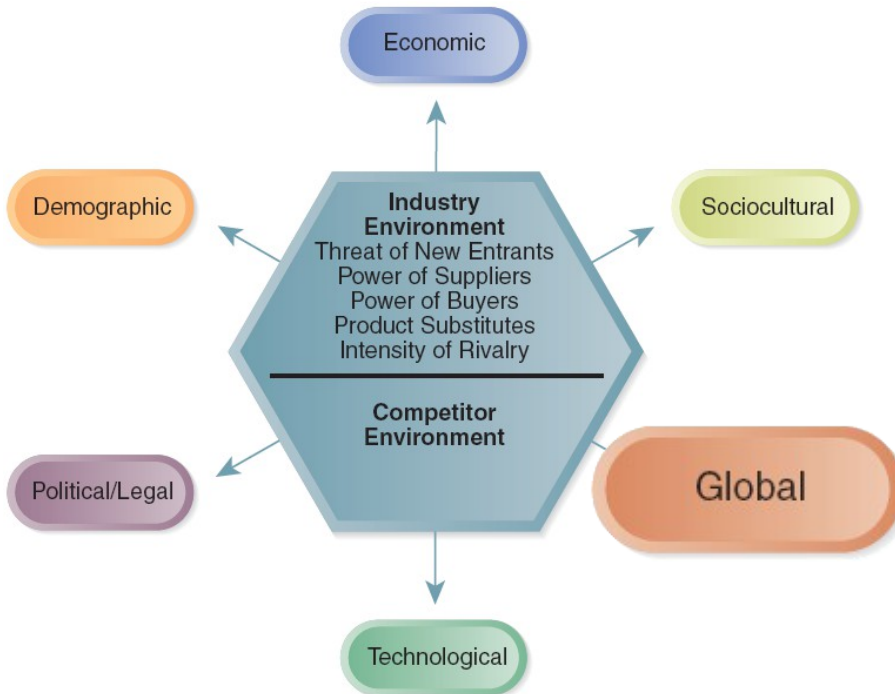
- Inflation rates
- Interest rates
- Trade deficits or surpluses
- Budget deficits or surpluses
- Personal savings rate
- Business savings rates
- Unemployment levels
- Energy availability and cost
- Energy alternatives

GeneralEnvt- Sociocultural Factors



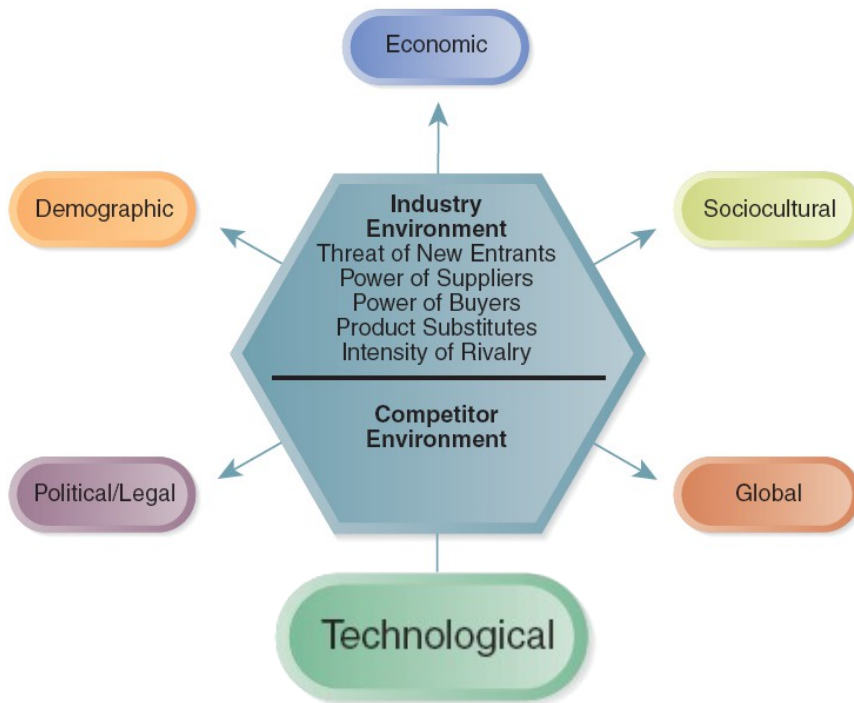
- Women in the workplace
- Workforce diversity
- Attitudes about quality of work life
- Concerns about environment
- Shifts in work and career preferences
- Shifts in product and service preferences

GeneralEnvt- Global Factors



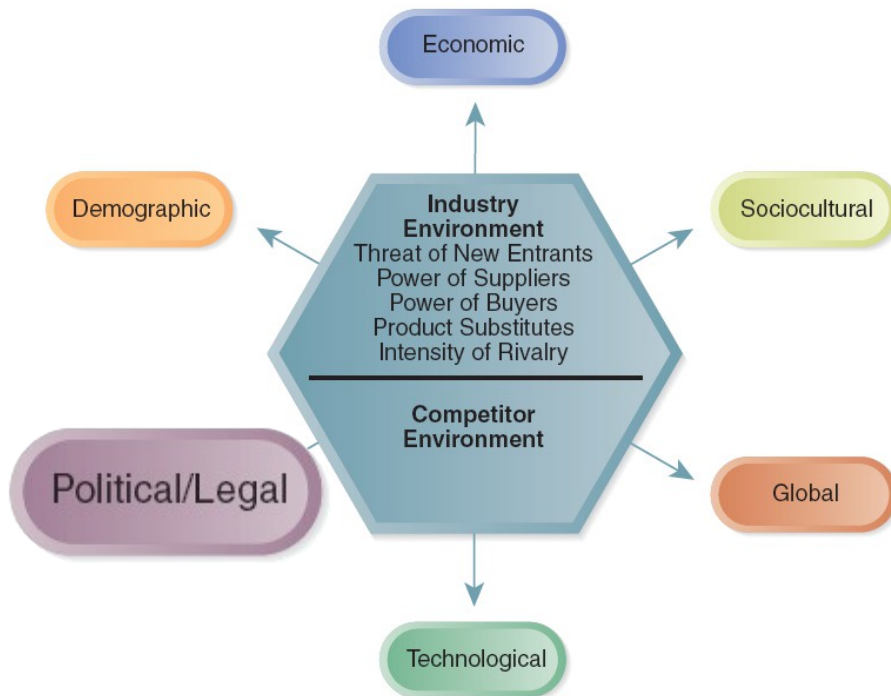
- New global markets
- Changing existing markets
- Important international events
- Critical cultural and institutional characteristics of global markets

GeneralEnvt– Technological Factors



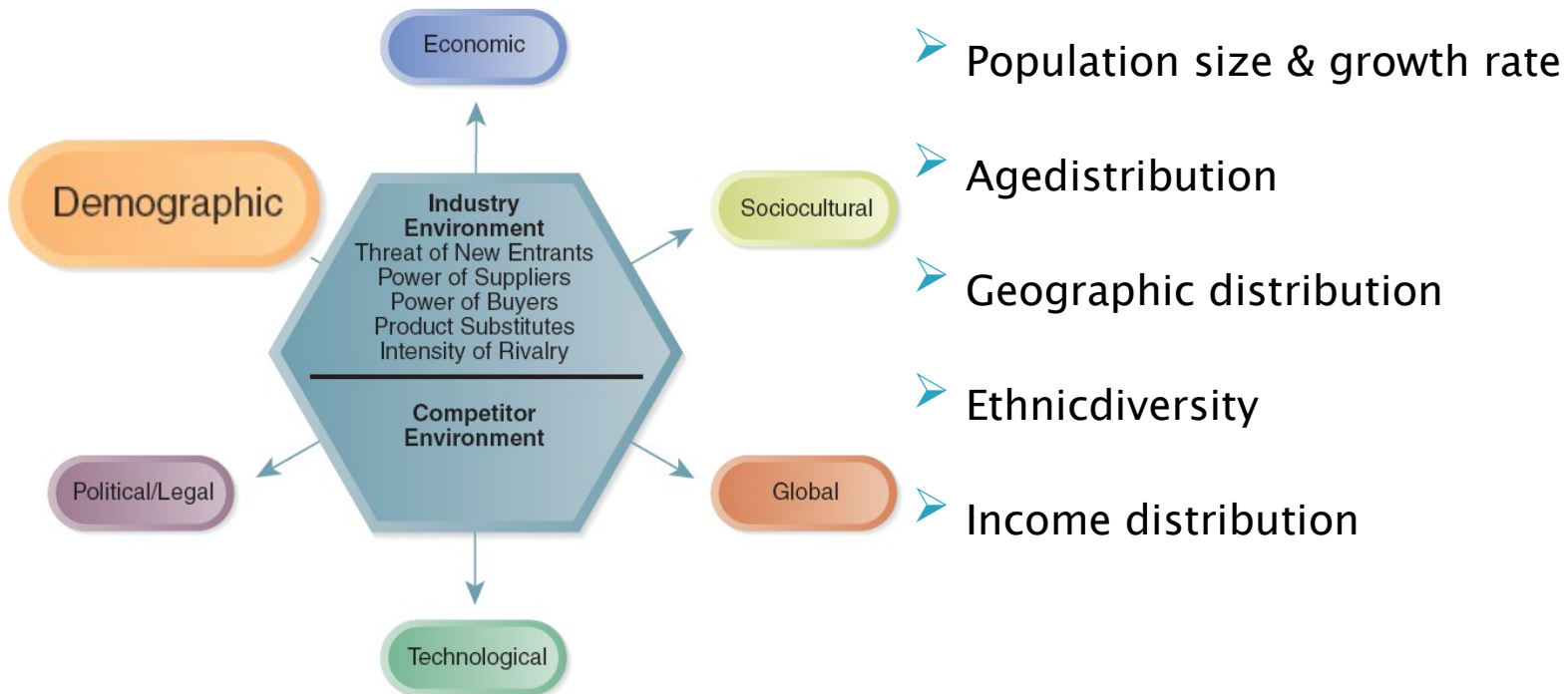
- Product and process innovations
- Focus of private and government-supported R&D expenditures
- New communication technologies
- Productivity improvements through automation
- Internet availability
- Telecommunications infrastructure

GeneralEnvt- Political/ Legal Factors



- Govtpolicies towards business
- Investment incentives
- Antitrustlaws
- Taxation laws
- Deregulation philosophies
- Laborlaws
- Educational philosophies and policies

GeneralEnvt- Demographic Factors



How to identify the strategic factors in the External Environment

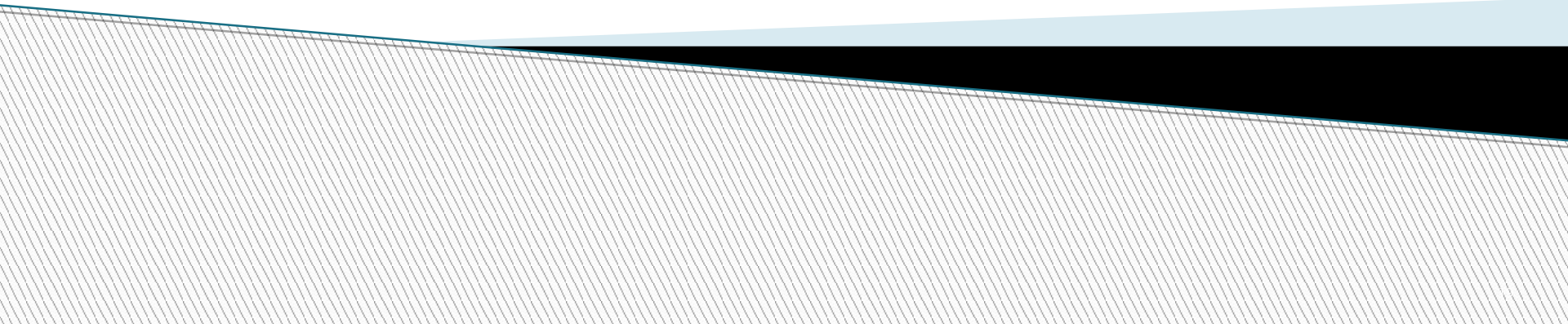
- ▶ List the major trends or developments emerging in each of the areas of the firm's environment
- ▶ Estimate the likely impact of these trends on the primary stakeholders – creditors, competitors, vendors etc
 - These are the strategic issues likely to impact future environment
- ▶ Plot these strategic on a Issues Priority Matrix

Issues Priority Matrix

		Probable Impact on Corporation		
		High	Medium	Low
Probability of Occurrence	High	High Priority	High Priority	Medium Priority
	Medium	High Priority	Medium Priority	Low Priority
	Low	Medium Priority	Low Priority	Low Priority

- ▶ The Issues Priority matrix can be used to help managers decide which environmental trends should merely be scanned and which should be monitored as strategic factors
- ▶ Those issues having **high probability of occurrence** and a **high impact** are the **strategic factors** for a firm
- ▶ These factors can be classified as Opportunities or Threats

Analysis of Industry Environment



Industry Environment Analysis

- ▶ An INDUSTRY is a group of firms that produce similar products or offer similar services that are close substitutes
- ▶ Compared to the General Environment, the Industry Environment has a more direct impact on the firm's
 - **STRATEGIC COMPETITIVENESS**
 - **ABILITY TO EARN ABOVE AVERAGE RETURNS**

Tools for Industry Environment Analysis

Porter's 5 Forces Model of Competition

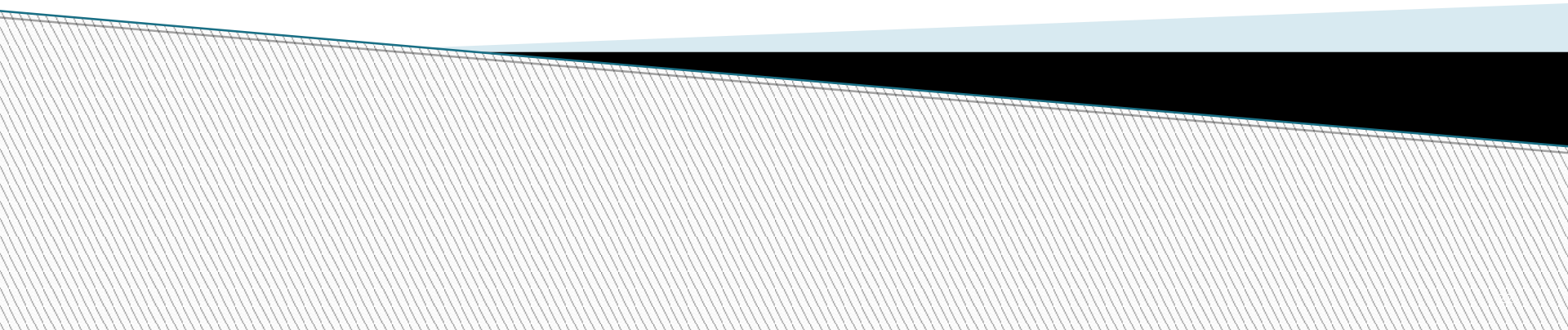
Driving Forces Analysis

Strategic Grouping

External Factor Evaluation Matrix (EFE)

Industry Analysis

Porter's 5 Forces Model of Competition



Porter's 5 Forces Model of Competition



Threat of New Entrants

- ▶ Function of 2 factors
 - Barriers to Entry
 - Expected Retaliation
- ▶ Can threaten market share of existing firms
- ▶ May stimulate additional production capacity
- ▶ May force existing firms to be more efficient and to learn to compete on new dimensions
- ▶ Entry barriers make it difficult for new firms to enter an industry
 - May place the new firms at a competitive disadvantage even if they are able to enter
- ▶ High entry barriers tend to increase the returns for the existing players and may allow some firms to dominate the industry
- ▶ Existing players would want to maintain high entry barriers so as to discourage new entrants

Threat of New Entrants – Barriers to Entry

Economies of Scale

Product Differentiation

Capital Requirements

Switching Costs

Access to Distribution Channels

Government Policy

Expected Retaliation

Bargaining Power of Suppliers

- ▶ A supplier group is powerful when
 - It is dominated by a few large companies
 - Satisfactory substitute products are not available to industry firms
 - Industry firms are not a significant customer for the supplier group
 - Suppliers' goods are critical to buyers' marketplace success
 - Effectiveness of suppliers' products has created high switching costs
 - Suppliers are a credible threat to integrate forward into the buyers' industry

Bargaining Power of Buyers

- ▶ Buyers are powerful when
 - They purchase a large portion of an industry's total output
 - The sales of the product being purchased account for a significant portion of the seller's annual revenues
 - They could easily switch to another product
 - The industry's products are undifferentiated or standardized, and buyers pose a credible threat if they were to integrate backward into the seller's industry

Threat of Substitute Products

- ▶ Product substitutes are a powerful threat when
 - Customers face few switching costs
 - Substitute product's price is lower
 - Substitute product's quality and performance capabilities are equal to or greater than those of the competing product

Rivalry amongst Competing Firms

- ▶ Intensity of rivalry is stronger when competitors
 - Are numerous or equally balanced
 - Experience slow industry growth
 - Have high fixed costs or high storage costs
 - Lack differentiation
 - Have high exit barriers

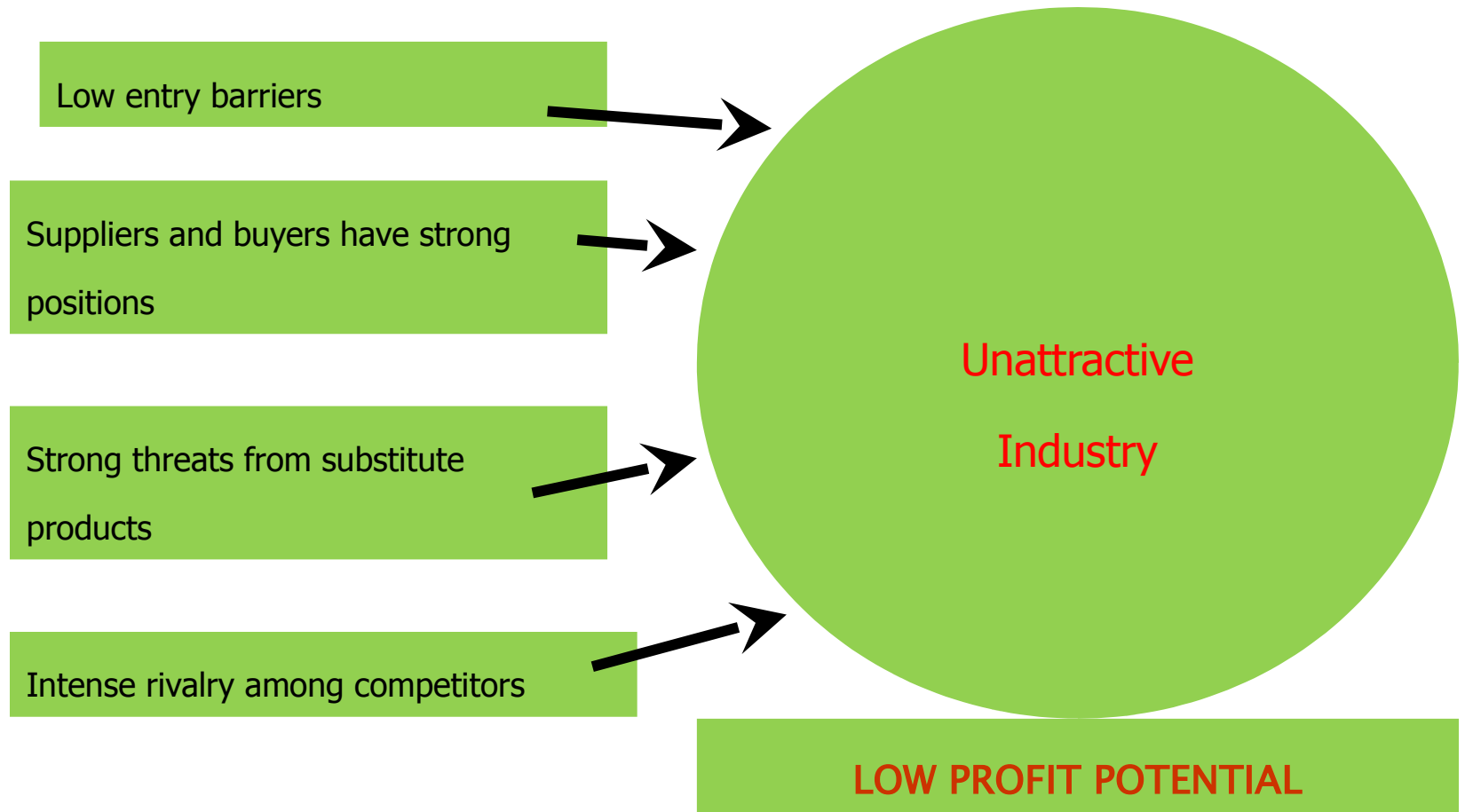
Rivalry amongst Competing Firms

- ▶ Competitors are rarely homogenous
- ▶ They differ in resources and capabilities
- ▶ They seek to differentiate themselves in ways that customers value and in areas where firms have a competitive advantage
- ▶ Common rivalry dimensions
 - Price
 - Quality
 - After sale service
 - Innovation

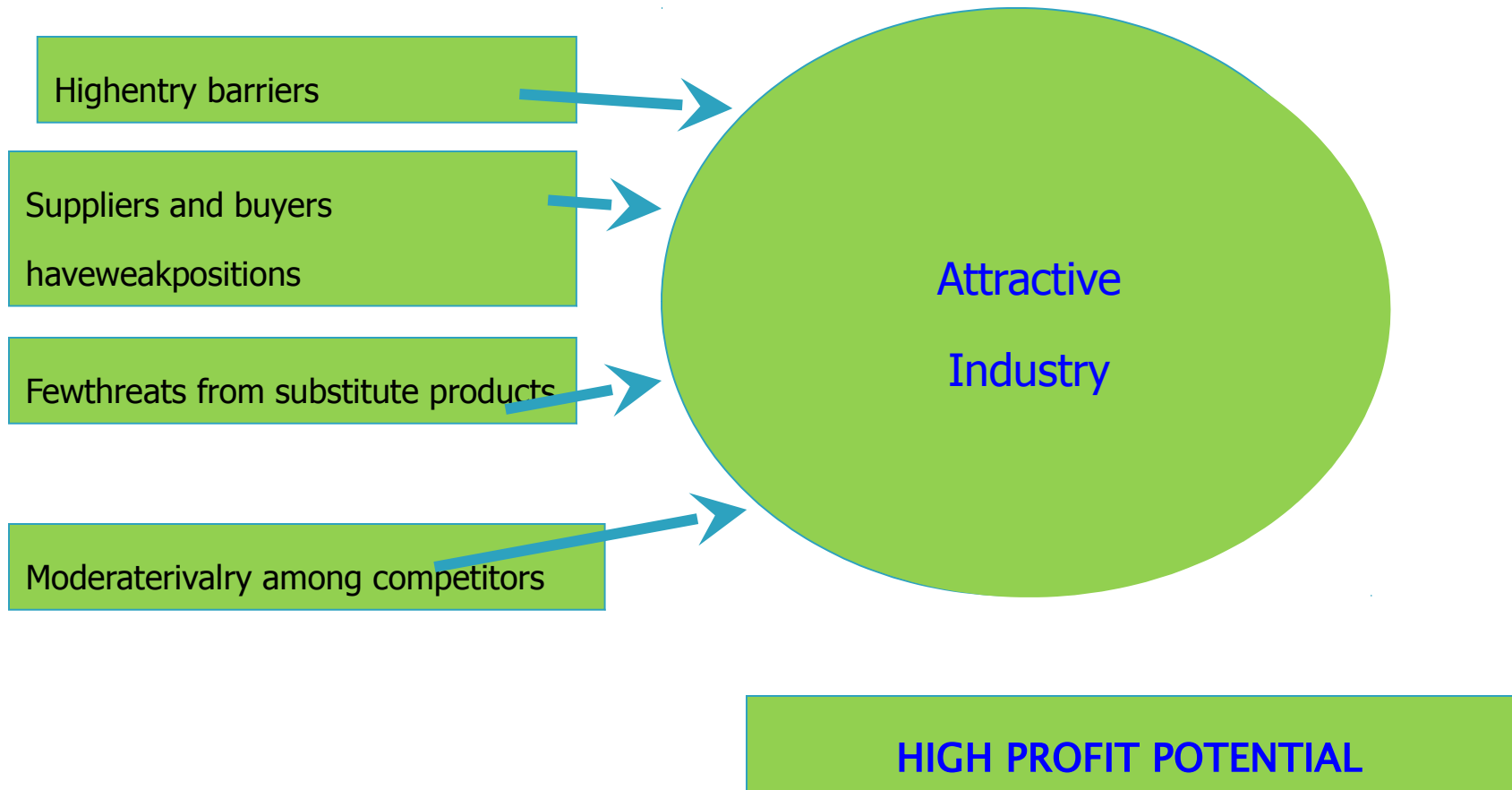
Rivalry amongst Competing Firms – Exit Barriers

- ▶ High Exit Barriers prevent competitors from leaving the industry
- ▶ Examples of High Exit Barriers
 - Specialized Assets – Assets with values linked to a particular business
 - Fixed costs of Exit – Labour agreements
 - Strategic Interrelationships – relationships of mutual dependence, such as those between one business and other parts of a company's operations, including shared facilities and access to financial markets
 - Emotional Barriers
 - Government and Social restrictions

Interpreting the Industry Analysis



Interpreting Industry Analysis

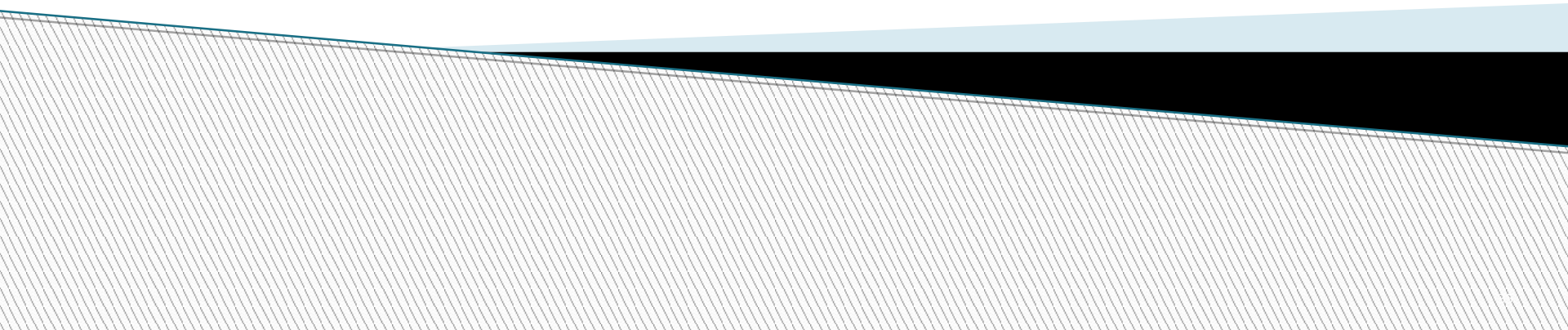


Class Activity: Applying Porter's 5 Forces Model to a few Companies

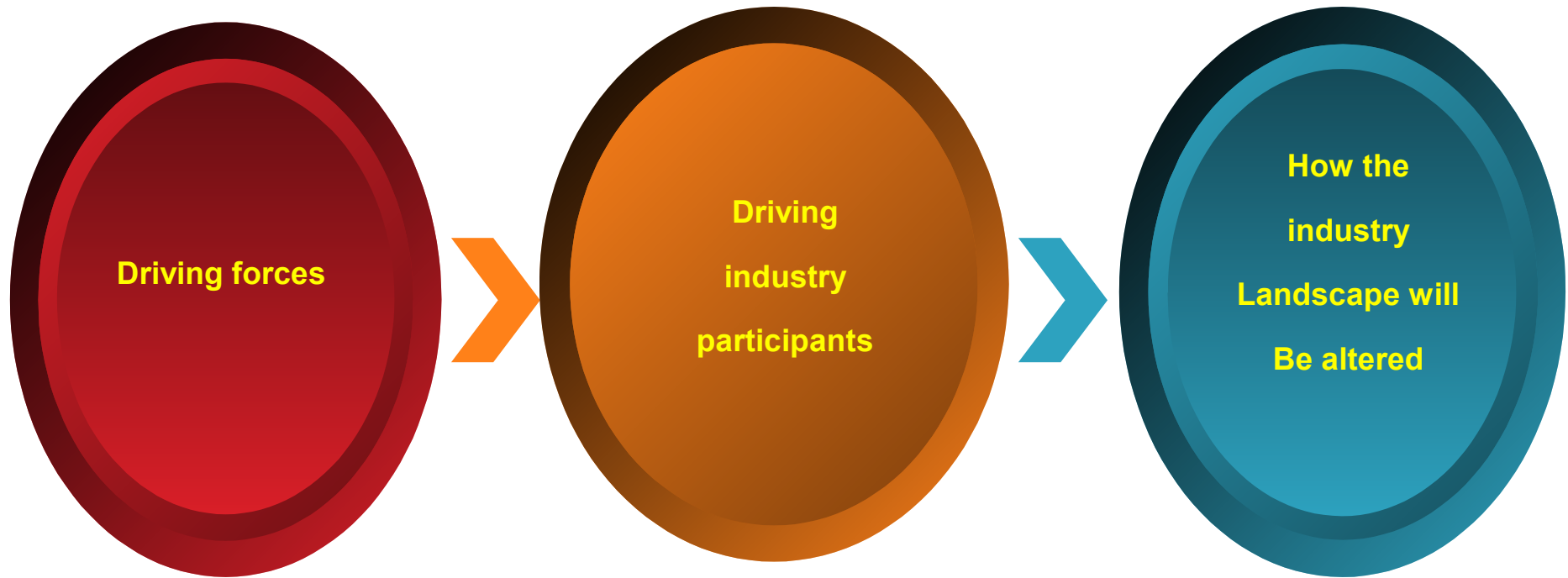
1. McDonalds
2. Apple
3. Coca Cola
4. Starbucks

Industry Analysis

Driving Forces Analysis



Driving Forces Analysis



Driving Forces

Change in the long term industry growth rate

Increasing Globalization

Emerging new Internet capabilities and applications

Change in who buy the product and how they use it

Product Innovation

Technological change and Manufacturing process innovation

Marketing Innovation

Driving Forces

Entry or exit of major firms

Diffusion of technical knowhow across more companies/ countries

Changes in cost structures and efficiencies

Growing buyer preferences

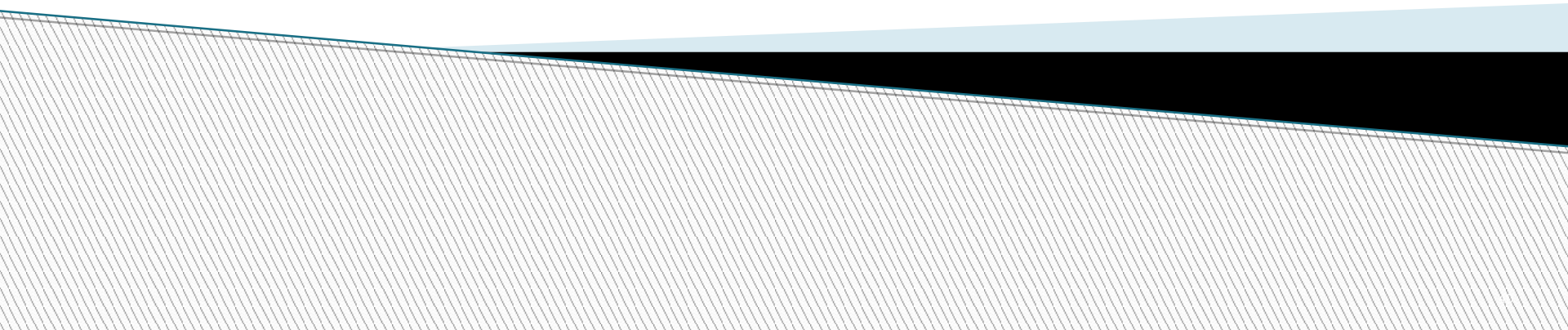
Regulatory influences and change in government policy

Changing attitudes and lifestyles

Driving Forces Analysis

- ▶ Identifying what the driving forces for your industry are
- ▶ Assessing whether the driving forces are making the industry more or less attractive
- ▶ Determining what strategy changes are needed to prepare for the impact of the driving forces

Industry Analysis Strategic Grouping



What is a Strategic Group

- ▶ A Strategic group is a group of firms in an industry following the same or similar strategy
- ▶ Can be a useful tool for analyzing an industry and its competitive structure
- ▶ Can also be helpful in diagnosing competition, positioning and the profitability of a firm within an industry

Strategic Group Characteristics

- ▶ Firms in the same strategic group have two or more competitive characteristics in common
 - Have comparable product line breadth
 - Sell in same price/quality range
 - Emphasize same distribution channels
 - Use same product attributes to appeal to similar types of buyers
 - Use identical technological approaches
 - Offer buyers similar services
 - Cover same geographic areas

How to construct a Strategic Group Map

Step 1

Identify competitive characteristics that differentiate firms in an industry from one another

Step 2

Plot firms on a two-variable map using pairs of these differentiating characteristics

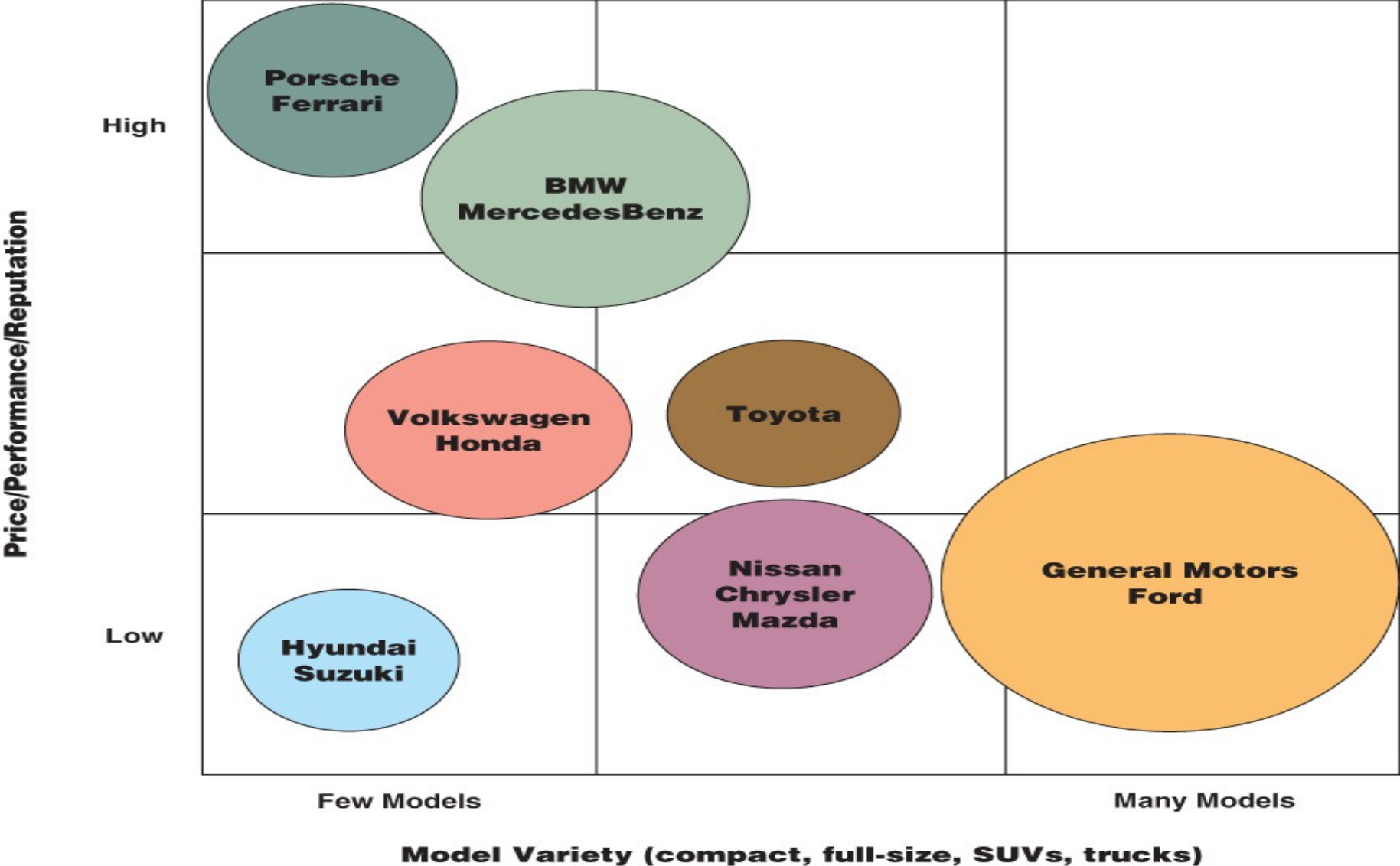
Step 3

Assign firms that fall in about the same strategy space to same strategic group

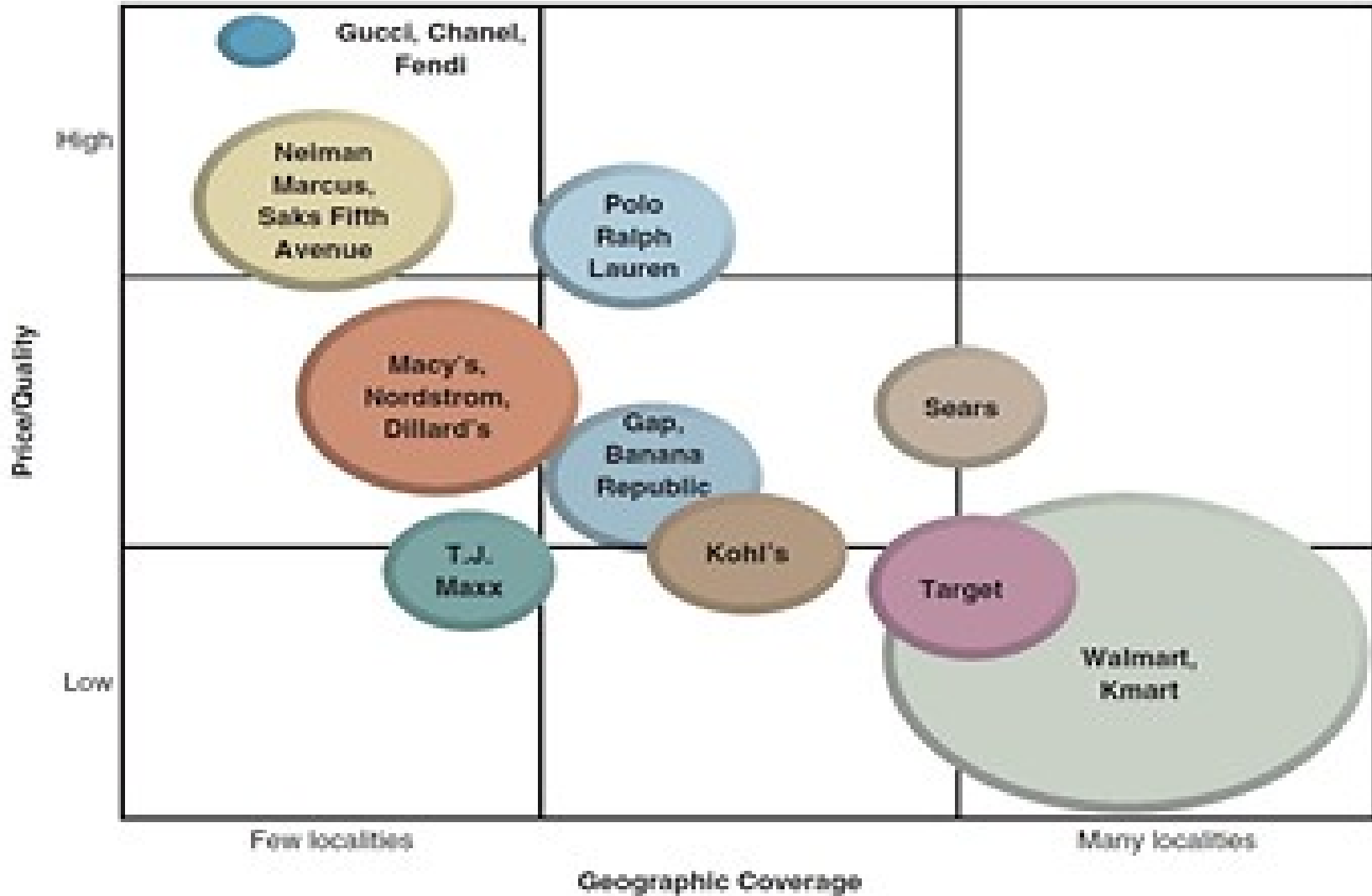
Step 4

Draw circles around each group, making circles proportional to size of group's respective share of total industry sales

Strategic Grouping of World Automobile Industry



Strategic Grouping of World Retail Chains



Interpreting the Strategic Group Analysis

- ▶ The closer the strategic groups on the map, the stronger the cross-group competitive rivalry
- ▶ Because firms within a group compete (offer similar products) rivalry can be intense – the greater the rivalry the greater the threat to each firm's profitability
- ▶ Helps with positioning and in the identification of direct and indirect competitors
- ▶ It can illustrate how easy or difficult it is to move from one strategic group to another
- ▶ It may help identify future opportunities

Class Activity

Developing a Strategic Group Map

1. Fast Food Industry in India
2. Mobile Handset Industry in India
3. Two wheeler (Bike) Industry in India