

**BUS359**

# **Contemporary Strategic Analysis**

Lecture 3: Macro-Environment Analysis and Industry Analysis

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# Recap:

## Goals, values, and performance

### Think-pair-share (5 minutes):

- What are the three dimensions of value?
- Why is profit used to measure value?
- How can analysis of profit performance guide strategy?
- What is the paradox of value?
- What is sustainable value?

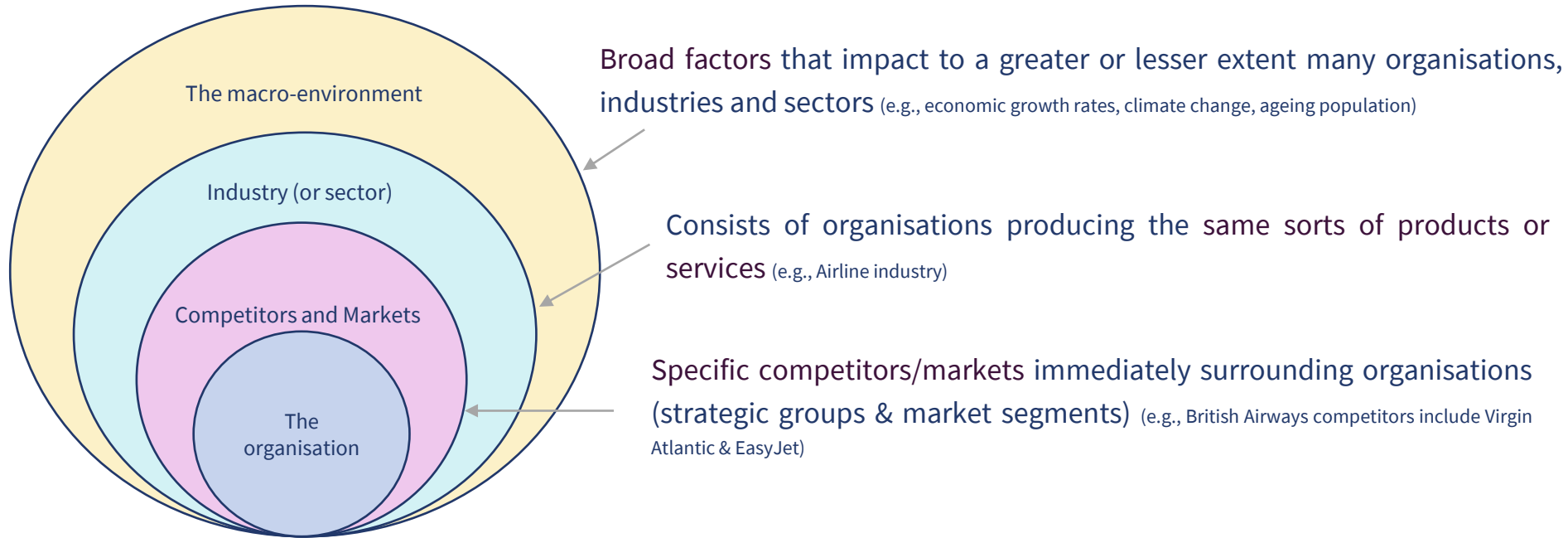
# Common elements in successful strategy



# Outline

- PESTEL analysis
- From macro-environment to industry environment
- Porter's Five Forces
- How industry structure determines competition

# The layers of the competitive environment



**Class activities**

# PESTEL analysis

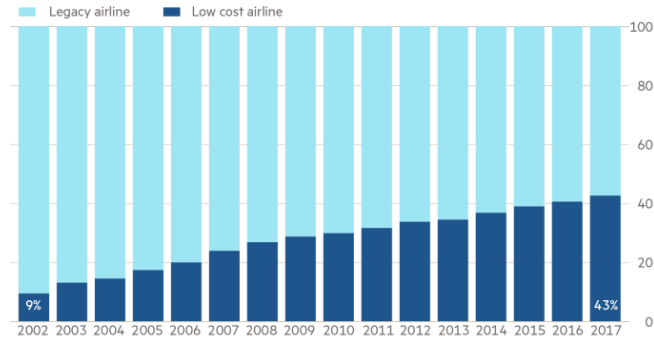
<b>P</b> olitics	Determines extent to which government may impact organisation (e.g., government policy, foreign trade policy, tax policy, labour law, environmental law, trade restrictions, etc.)
<b>E</b> conomics	The economy and its performance impacts how an organization does business and its profitability (e.g., economic growth, interest rates, unemployment rates, raw material costs exchange rates, inflation, disposable income, etc.)
<b>S</b> ocial	Social & cultural trends and patterns that impact customer needs & size of markets (e.g., age distribution, population growth rate, education & career trends, religious beliefs, social classes, etc.)
<b>T</b> echnological	Considers the rate of technological innovation and development that could affect a market or industry (e.g., digital or mobile technology, automation, new methods of distribution, manufacturing and logistics, etc.)
<b>E</b> cological	Influence of the natural environment & ecological aspects (e.g., climate change, recycling procedures, waste disposal, etc.)
<b>L</b> egal	What is legal and allowed within the territories they operate in? (note: crossover with political factors, but difference is political = government-led, legal = must be complied with). (e.g., employment legislation, consumer law, health and safety, etc.)

# PESTEL analysis

Class activities: Individual reflection (4 minutes)

Low cost airlines are relentlessly eating up European market share

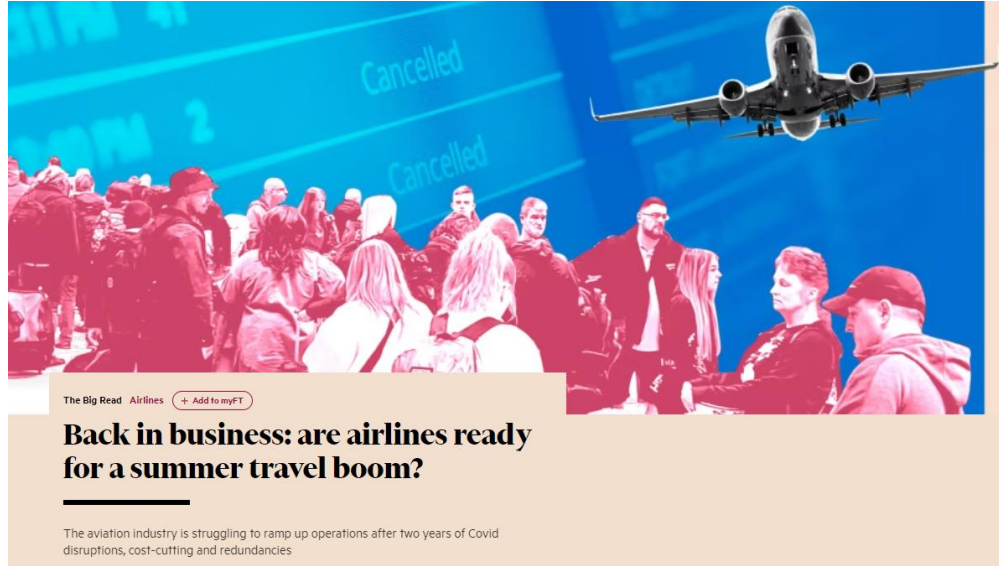
Market share, western Europe (%)



Source: OAG  
© FT

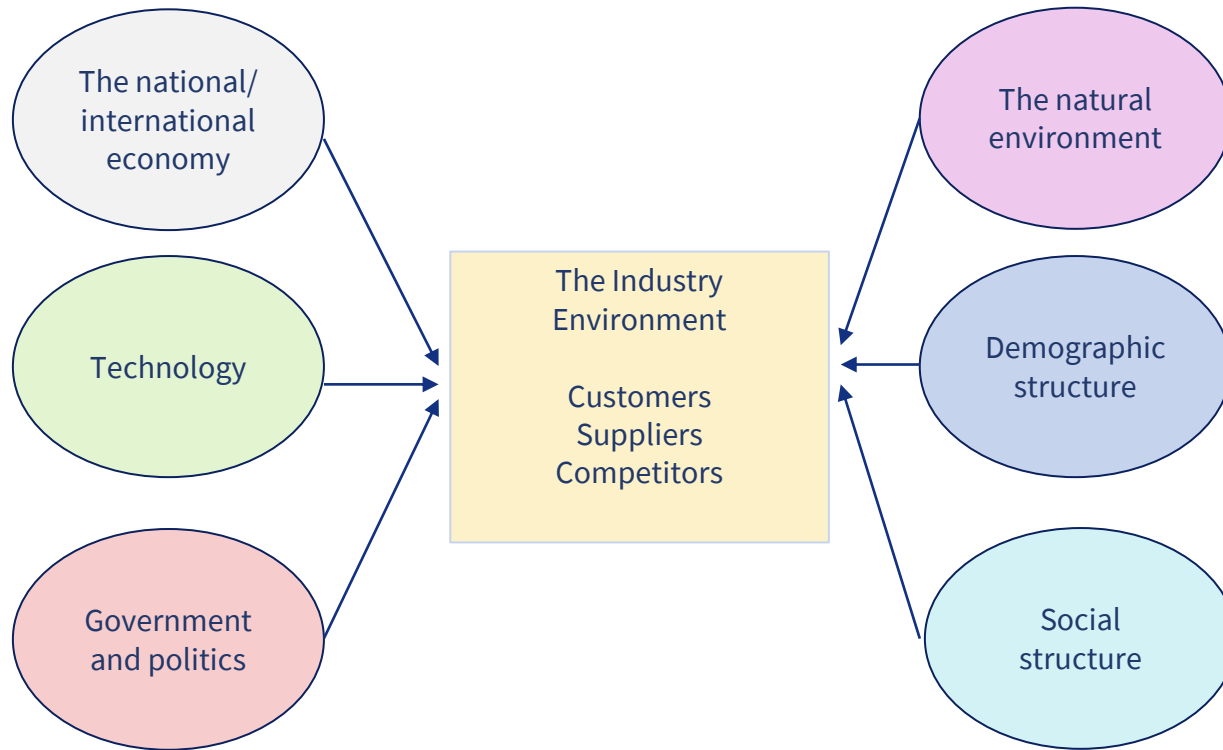
(Source: [Financial Times](#))

Apply a PESTEL analysis to the European Airline Industry



(Source: [Financial Times](#))

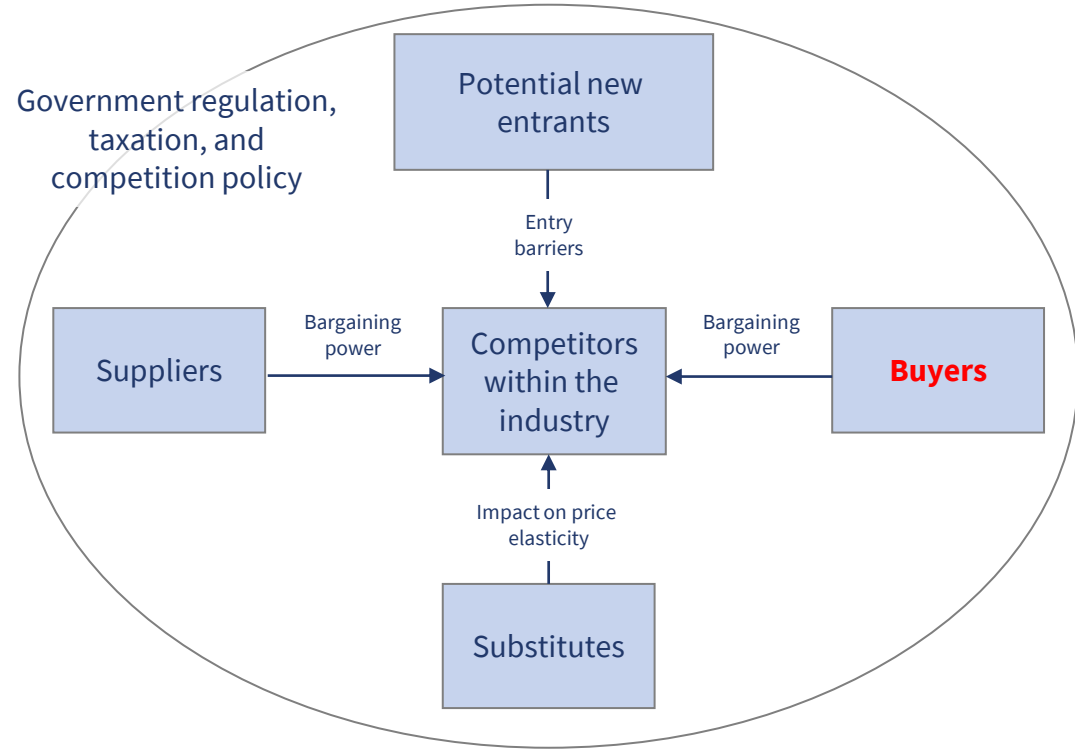
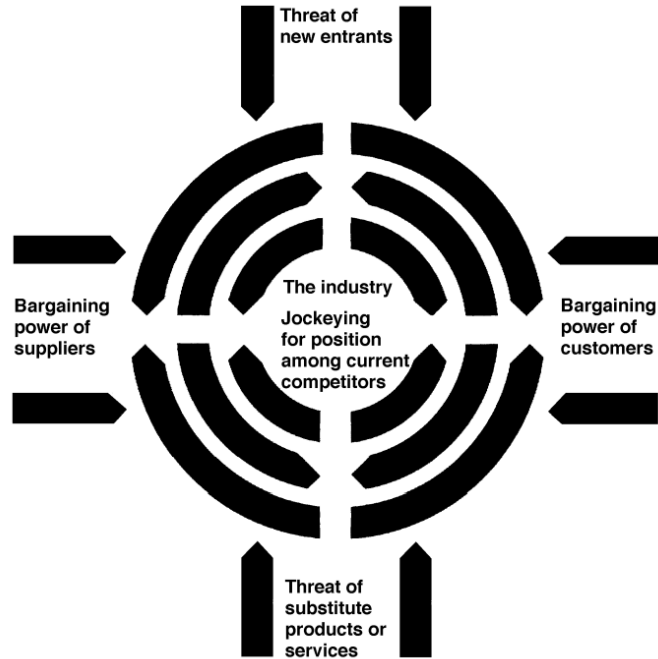
# From macro-environment analysis to industry analysis



- Macro-environment analysis is costly and may result in information overload.
- The industry environment lies at the core of the macro-environment.
- The Macro-environment impacts the firm through its effect in the industry environment.

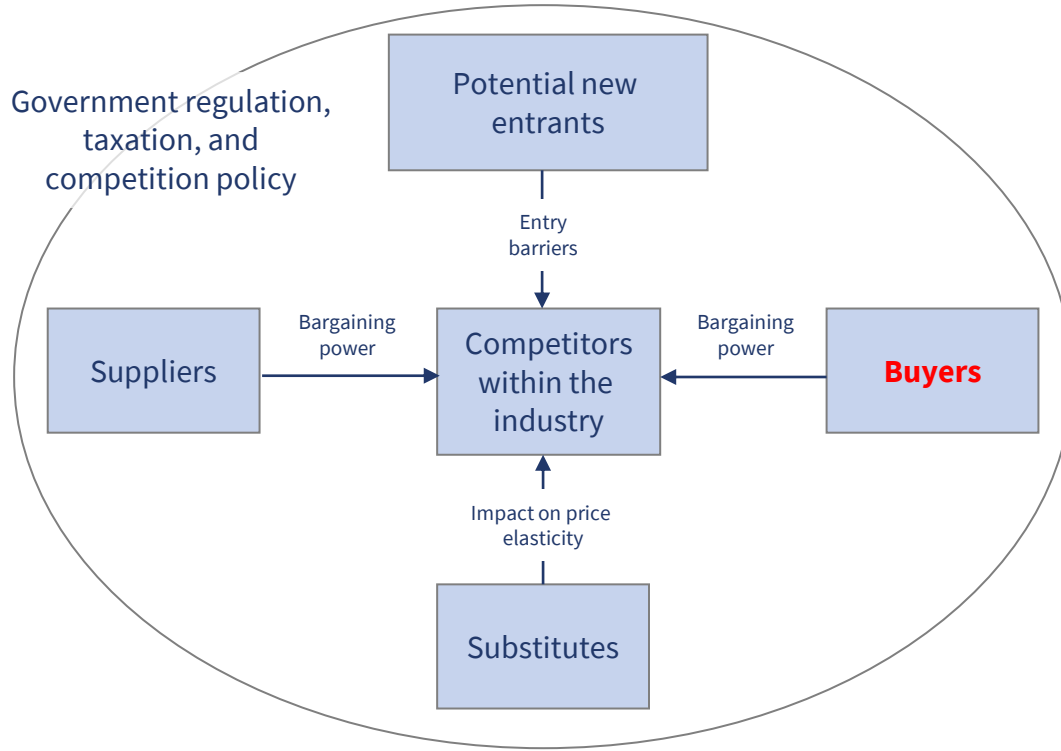


# Porter's Five Forces



Porter, M. (1979). How competitive forces shape strategy Harvard Business Review, March/April 1979. *Gross & Gold*, 174.

# Porter's Five Forces



## Attractive industry – high profits:

- High barriers to enter
- Weak suppliers bargaining power
- Weak buyers bargaining power
- Few substitute products or services
- Low competition

## Unattractive industry – low profits:

- Low barriers to enter
- Strong suppliers bargaining power
- Strong buyers bargaining power
- Many substitute products or services
- Intense competition

# The threat of entry

- Successful firm's attract other firms
- Entrants' threat to industry profitability depends upon the height of barriers to entry
- The principal barriers to entry include:
  - Capital requirements
  - Economies of scale
  - Absolute cost advantage
  - Product differentiation
  - Access to channels of distribution
  - Legal & regulatory barriers
  - Retaliation

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# Threat of substitutes

- The extent to which substitutes affect an organisations profitability depends upon:
  - Buyers' propensity to substitute between alternatives
  - The price-performance characteristics of substitutes
- Availability of alternatives to customers:
  - Absence of close substitutes = customers are relatively insensitive to price
  - Presence of close substitutes = customers switch according to price



# Rivalry between established competitors

- Rivalry between established competitors:
  - Concentration (number & size distribution of firms)
  - Diversity of competitors (characteristics of top management mindset, cost structure, strategy)
  - Product differentiation
  - Excess capacity & exit barriers
  - Cost conditions
    - Extent of scale economies
    - Ratio of fixed to variable costs



# Bargaining power of buyers & suppliers

## Buyer's price sensitivity

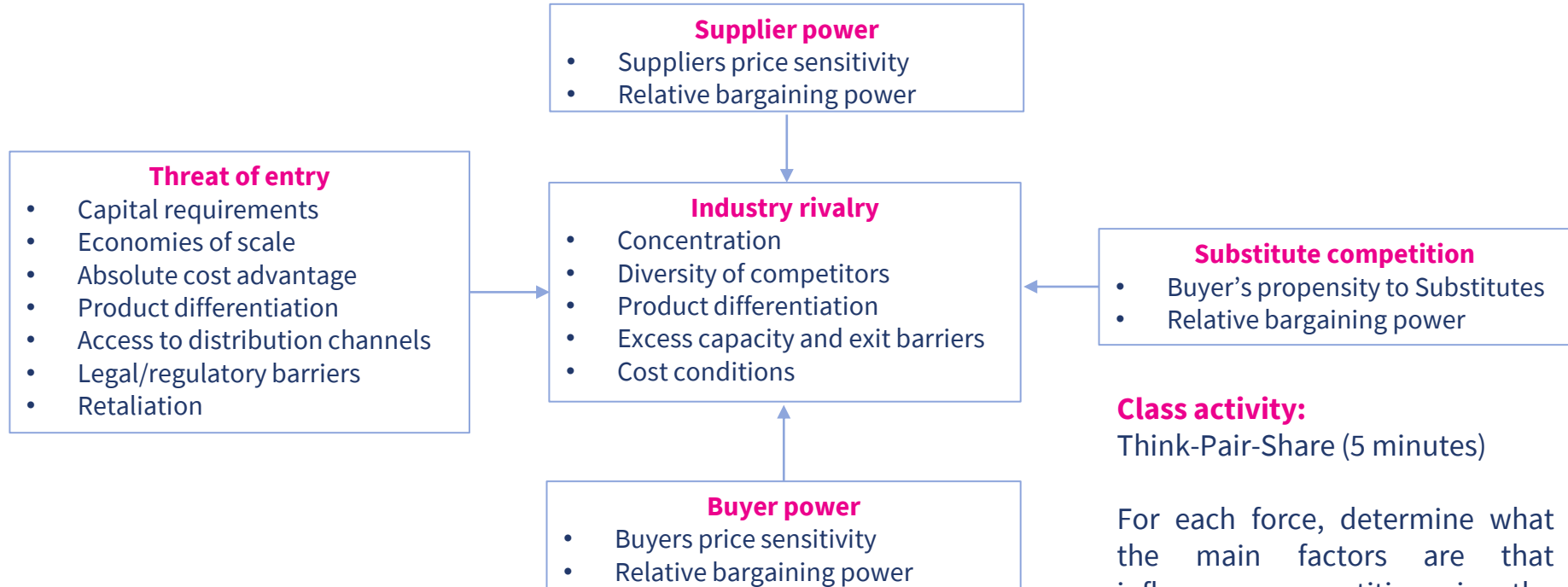
- Cost of purchases as % of buyers total costs
- How differentiated is the purchased item?
- How intense is competition between buyers?
- How important is the item to quality of the buyers own output?

## Relative bargaining power

- Size & concentration of buyers relative to sellers
- Buyer's information
- Ability to backward integrate

**Note:** Analysis of supplier power is symmetric to buyer power

# The structural determinants of competition



## Class activity:

Think-Pair-Share (5 minutes)

For each force, determine what the main factors are that influence competition in the European Airline Industry.

# Applying Industry analysis

## Part A: Identifying industry structure

- Who are the main stakeholders? (e.g., producers, customers, input suppliers, & producers of substitute goods)
- What are the characteristics of each stakeholder that will determine competition & bargaining power?

## Part B: Forecasting industry profitability

- Current profitability is a poor indicator of future profitability (e.g., newspaper industry).
- If we can forecast changes in industry structure – through observations of structural trends in an industry – we can predict likely impacts on competition & profitability.
  - Examine how the industry's current and recent levels of competition & profitability are a consequence of its present structure
  - Identify trends that are changing the industry's structure – Is it consolidating? Are products becoming more differentiated?
  - Identify how these structural changes will affect the five forces of competition & resulting profitability of the industry – Will changes cause competition to intensify or weaken?

## Use the above knowledge to develop strategies that...

### ...Alter industry structure

What structural variables are depressing profitability?

Which one can be changed by individual or collective strategies?

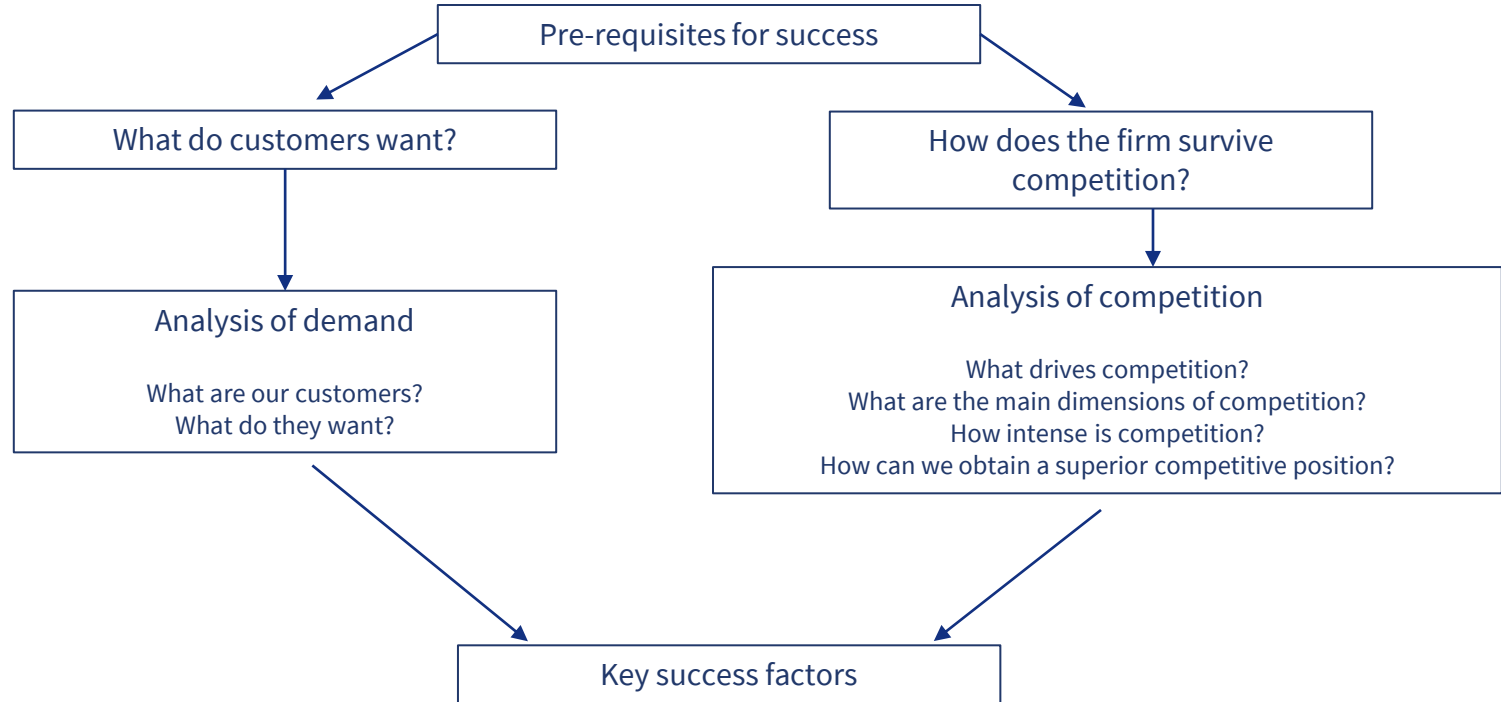
### ...Positioning the company

What are the weakest competitive forces?

Anticipate changes in competitive forces likely to affect the industry



# Identifying key success factors



# Summary and next week

## Recap

- Macro-environment analysis
- Industry analysis - Porter's Five Forces
- Applying industry analysis
- Identifying key success factors

## Forthcoming:

- Lecture 4: Further topics in industry analysis.
- Applying Porter's Five Forces.
- Dynamic competition.

## Seminar session 3:

Required reading: The case study.

Discussion questions, refer to the QMplus module page.



Queen Mary

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