INDUSTRY AND COMPETITOR ANALYSIS

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INDUSTRY ANALYSIS

- An **industry** is a group of firms producing a similar product/ service
- When studying an industry, an entrepreneur must answer three questions before pursuing the idea of starting a firm:
  - Is the industry accessible or is it a realistic place for a new venture to enter?
  - Does the industry contain markets that are ripe for innovators or are underserved?
  - Are there positions in the industry that will avoid some of the negative attributes of the industry as a whole?
- It is useful for a new venture to think about its **position** at both – the company level and the product/ service level.
- **Competitive landscape:** what an industry is???
- Recognized in fourth century B.C. by **Sun-tzu**, a Chinese philosopher, in his book ***The Art of War***…..to help generals prepare for battle (ideas in the book help managers prepare their firms for the competitive wars of the marketplace).

- Entrepreneurs must be **"familiar with the face of the country"** i.e. until they understand the industry they plan to enter and in which they intend to compete, they are not adequately prepared to start their businesses
- **Still 8% – 30% of variation in firm profitability is directly attributable to the industry in which a firm competes.**

Studying Industry Trends

- **Environmental Trends:**

  economic, social, technological advances, political & regulatory

- **Business Trends:**

  outsourcing manufacturing or service functions to lower-cost foreign labor markets;

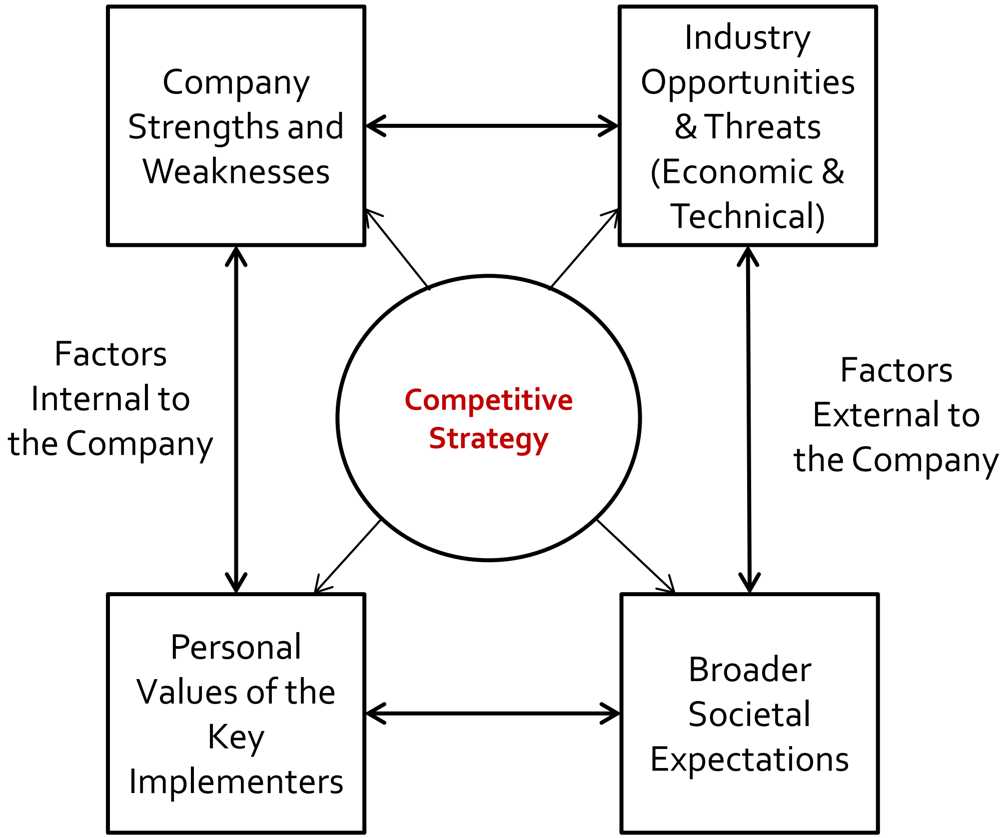
  move customer procurement and service functions online at considerable cost savings

THE CLASSIC APPROACH TO FORMULATION OF STRATEGY

The Wheel of Competitive Strategy

- Developing a competitive strategy is developing a broad formula for how a business is going to compete, what its goals should be, and what policies will be needed to carry out those goals.
- Competitive strategy is a combination of the ***ends*** (goals) for which the firm is striving and the ***means*** (policies) by which it is seeking to get there.
- The **"Wheel of Competitive Strategy,"** is a device for articulating the key aspects of a firm's competitive strategy.
- In the hub of the wheel are the firm's goals, which are its broad definition of how it wants to compete and its specific economic and noneconomic objectives.
- The spokes of the wheel are the key operating policies with which the firm is seeking to achieve these goals.
- Under each heading on the wheel a succinct statement of the key operating policies in that functional area should be derived from the company's activities.
- Depending on the nature of the business, management can be more or less specific in articulating these key operating policies; once they are specified, the concept of strategy can be used to guide the overall behavior of the firm.
- Like a wheel, the spokes (policies) must radiate from and reflect the hub (goals), and the spokes must be connected with each other or the wheel will not roll.

CONTEXT IN WHICH COMPETITIVE STRATEGY FORMULATED



- The company's strengths and weaknesses are its profile of assets and skills relative to competitors, including financial resources, technological posture, brand identification.
- The personal values of an organization are the motivations and needs of the key executives and other personnel who must implement the chosen strategy.
- Strengths and weaknesses combined with values determine the internal (to the company) limits to the competitive strategy a company can successfully adopt. The external limits are determined by its industry and broader environment.
- Industry opportunities and threats define the competitive environment, with its attendant risks and potential rewards.
- Societal expectations reflect the impact on the company of such things as government policy, social concerns, evolving mores, and many others.

A. What is the Business Doing Now?

1. Identification

What is the implicit or explicit current strategy?

2. Implied Assumptions

What assumptions about the company's relative position, strengths & weaknesses, competitors, and industry trends must be made for current strategy to make sense?

B. What is Happening in the Environment?

1. Industry Analysis

What are key factors for competitive success and important industry opportunities & threats?

2. Competitor Analysis

What are capabilities and limitations of existing and potential competitors,& their probable future moves?

3. Societal Analysis

What important governmental, social, and political factors will present opportunities or threats?

4. Strengths and Weaknesses

Given an analysis of industry and competitors, what are the company's strengths and weaknesses relative to present and future competitors?

C. What Should the Business be Doing?

1. Tests of Assumptions and Strategy

How do the assumptions embodied in the current strategy compare with the analysis in B above?

2. Strategic Alternatives

What are the feasible strategic alternatives given above analysis? (Is current strategy one of these?)

3. Strategic Choice

Which alternative best relates the company's situation to external opportunities and threats?

The outline of questions gives an approach to developing the optimal competitive strategy.

THE FIVE FORCES MODEL

Threat of Substitutes

Threat of New Entrants

Rivalry among Existing Firms

Bargaining Power of Suppliers

Bargaining Power of Buyers

- Framework for understanding the structure of an industry was developed by Harvard Professor **Michael Porter**
- Five forces determine industry profitability
- Impacts the average rate of return on invested capital for the firms in an industry by applying pressure on industry profitability
- Well-managed firms try to position to avoid or diminish these forces (in an attempt to beat the avg. rate of return for the industry)

➢ Industries differ fundamentally in their ultimate profit potential as the collective strength of the forces differs; the forces range from intense in industries like tires, paper & steel – where no firms earns spectacular returns – to relatively mild in industries like oil-field equipment & services, cosmetics, and toiletries – where high returns are quite common

Threat of New Entrants: barrier to entry

- Economies of Scale
- Product Differentiation
- Capital Requirements
- Cost advantages independent of size
- Access to distribution channels
- Government and legal barriers

Rivalry among Existing Firms

- Number and balance of competitors
- Degree of difference between products
- Growth rate of an industry
- Level of fixed costs

Bargaining Power of Suppliers

- Supplier concentration
- Switching costs
- Attractiveness of substitutes
- Threat of forward integration

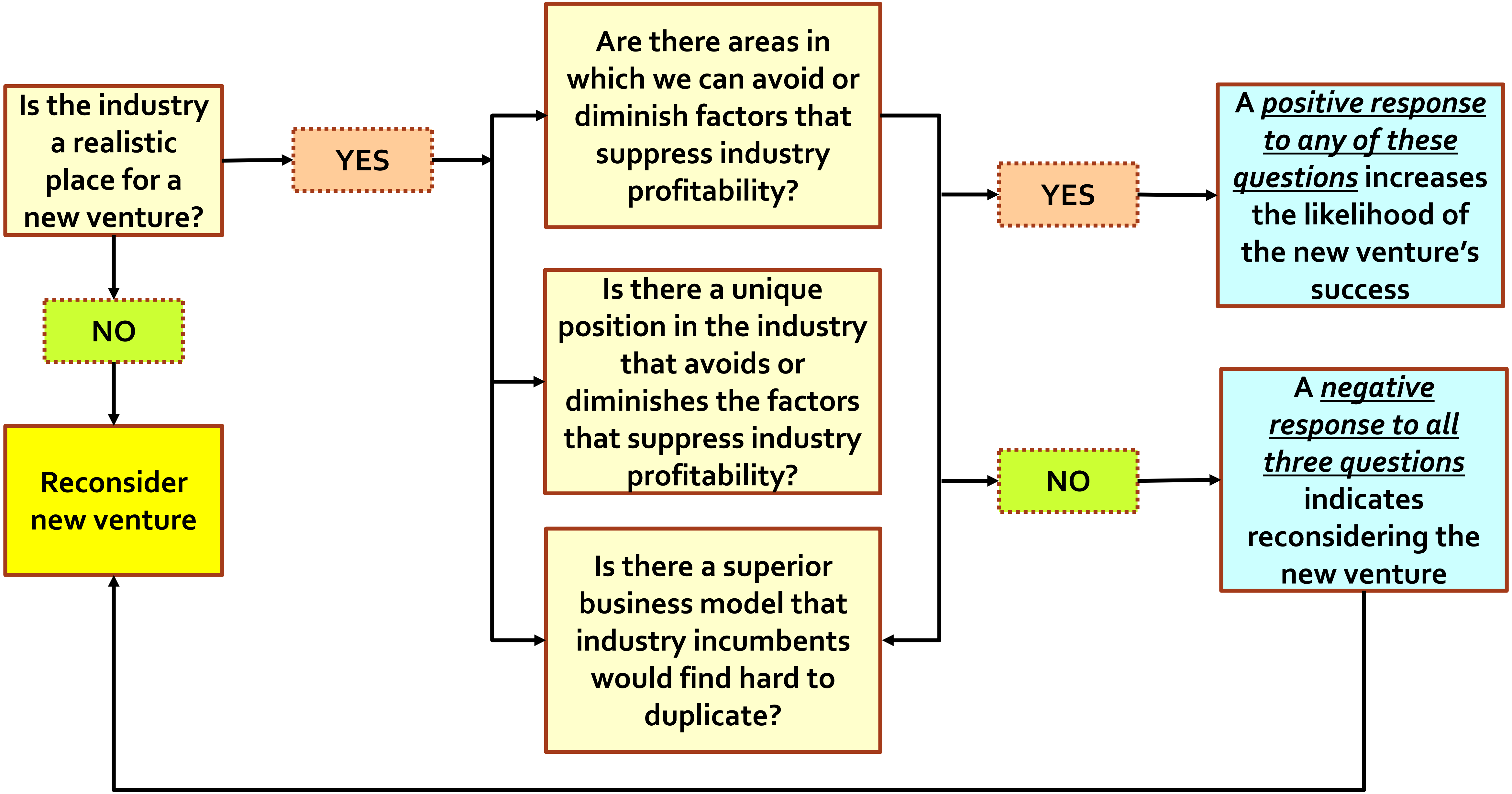
Bargaining Power of Buyers

- Buyer group concentration
- Buyer's costs
- Degree of standardization of supplier's products
- Threat of backward integration

THE VALUE OF THE FIVE FORCES MODEL

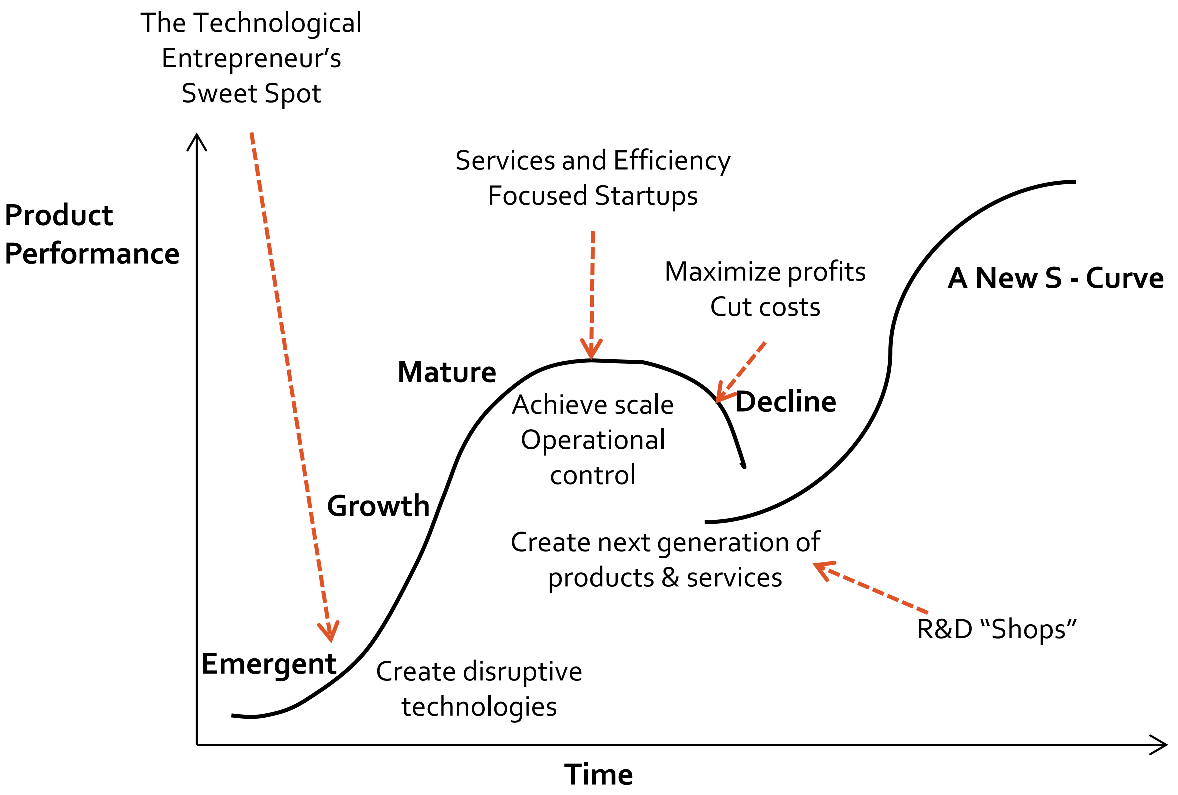
1. To help a firm determine whether it should enter a particular industry
2. Whether it can carve out an attractive position in that industry

Competitive Force	Threat to Industry Profitability		
	Low	Medium	High
Threat of substitute Threat of new entrant Rivalry among existing firms Bargaining power of suppliers Bargaining power of buyers			
Instructions: Step 1 : Select an industry Step 2 : Determine the level of threat to industry profitability for each of the forces Step 3 : Use the table to get an overall feel for the attractiveness of the industry (low, medium, high) Step 4 : Use the table to identify the threats that are most often relevant to industry profitability			



TO DETERMINE THE POTENTIAL SUCCESS OF A NEW VENTURE USING FIVE FORCES MODEL

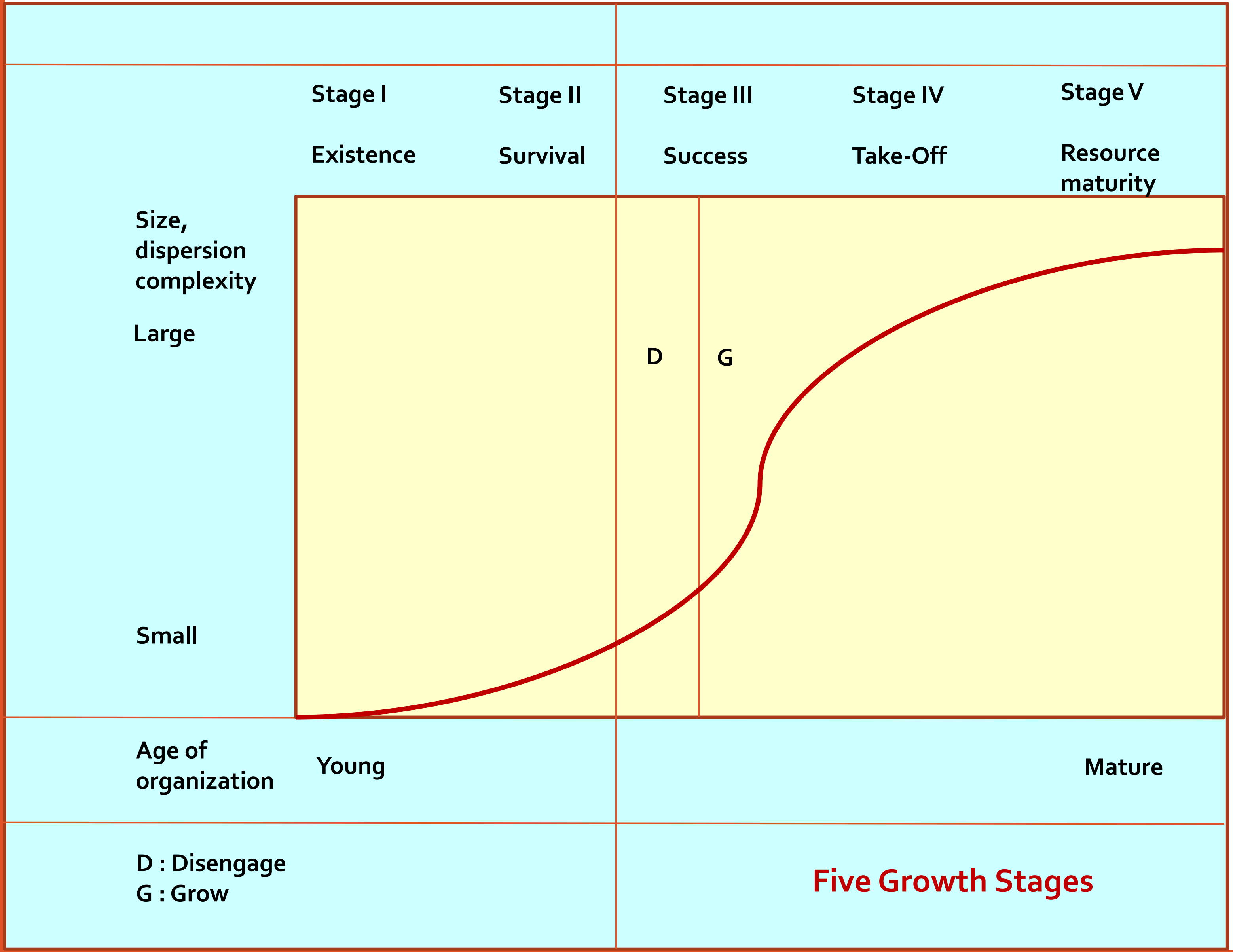
Industry Life Cycles: S – Curve Unfolding Over Time



- Experience shows that technology-based ventures enjoy the greatest success when they enter the field ***near the beginning*** of the growth stage
- This is the **Entrepreneur's Sweet Spot** as customers are aware of the new technology; have money to spend; and anxiously waiting for new solutions
- **Too early in the game**, entrepreneur has to wait for years to technology to ripen and **too late**, you are up against well-established players. Jump to a **new S-curve** and you are back in the research game

- The initial or emergent stage is a period of slow revenue growth, with few direct competitors. Many ventures are still forming product/ service concept. A credible market may not exist yet. **Nanotechnology**
- The next stage is characterized by rapid growth where products/ services really clicks with customers. **Cell phone**
- Eventually, growth markets become saturated, the rocketing curve tapers off & competitors find themselves in the maturity stage. Many companies resort to incremental changes, price discounts, other mechanisms to generate revenues and poach customers from competitors. Weaker firms are forced out of the industry and few remains. **Office productivity segment of Software industry**
- Lastly, when traditional industry paradigm stagnates, it goes into decline. This opens door for an entirely new generation of technology and an entirely new S – curve. The new pioneer work to disrupt old products and business models. **Apple**

FIVE STAGES OF SMALL BUSINESS GROWTH

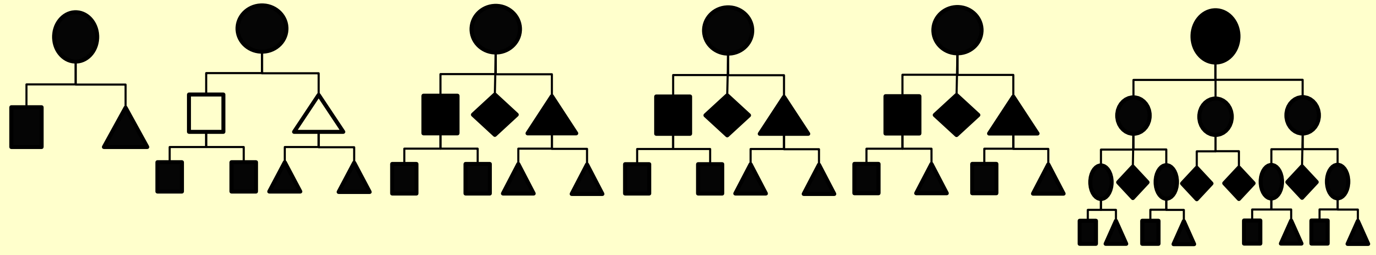
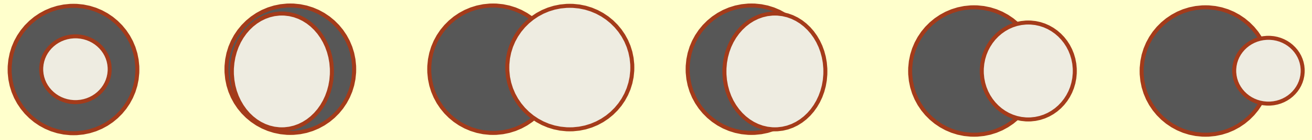


- Models using business size as one dimension and company maturity or the stage of growth as second dimension are inappropriate for small businesses

1. Assume company must grow & pass through all stages of development or die
2. Models fail to capture important early stages in a company's origin & growth
3. Characterize company size largely in terms of annual sales (also no. of employees) & ignore factors – value added, no. of locations, complexity of product line, rate of change in products or production technology

- Framework for small & growing businesses has five stages – characterized by index of size, diversity, & complexity and described by five management factors: managerial style; organizational structure; extent of formal systems; major strategic goals, & the owner's involvement in the business

CHARACTERISTICS OF SMALL BUSINESS AT EACH STAGE OF GROWTH

	Stage I Existence	Stage II Survival	Stage III - D Success - D	Stage III - G Success - G	Stage IV Take-Off	Stage V Resource maturity
Management Style	Direct supervision	Supervised supervision	Functional	Functional	Divisional	Line and Staff
Organization						
Extent of Formal Systems	Minimal to nonexistent	Minimal	Basic	Developing	Maturing	Extensive
Major Strategy	Existence	Survival	Maintaining profitable status quo	Get resources for growth	Growth	Return on Investment
Business & Owner*						

*Smaller circle represents owner.
Larger circle represents business.

Stage I: problems in obtaining customers and delivering the product or service contracted for

- Firm simple, owner does everything & directly supervises subordinates

Stage II: workable business entity, enough satisfied customers. Problem shifts to generate enough cash flows to breakeven, to cover repair or replacement of capital assets, to finance growth and stay in business

- Firm simple, limited no. of employees supervised by a manager carrying out orders of owner

Stage III: whether to exploit firm's accomplishments and expand (substage III-G) or keep the firm stable & profitable, providing a base for alternative owner activities i.e., completely or partially disengage from the firm (substage III-D)

Stage IV: how to grow rapidly & how to finance that growth. Problems are: **delegation** and **cash**. Firm is decentralized and partly divisionalized – in either sales or production

Stage V: concerns are to consolidate and control the financial gains due to rapid growth and secondly to retain the advantages of small size, including flexibility of response and entrepreneurial spirit. Eliminate inefficiencies & professionalize company.

BARRIERS TO ENTRY

Of the many barriers faced by industry outsiders, three are particularly important for new ventures:

- ***Capital and Time***
  - **Entry to some industry segments/ niches requires huge amount of capital – amount that few entrepreneurs can raise**
  - **Years of R&D are needed to develop marketable products**
- ***Manufacturing***
  - **Certain manufacturing industries require particular types of machines to produce a given category of products.** For building products, complex woodcutting, forming, & assembly machines are needed; for certain plastics and food products – specially built extrusion machines are required
  - **An entrepreneur who insists on entering capital-intensive industry needs to consider external manufacturing options- often called contract or co-manufacturers- to source his products**
- ***Distribution***
  - **Marketing is the third major barrier to entry that an entrepreneur needs to consider**
  - **Gaining access to large retailers can be difficult and costly**
  - **But if you've got something good and you have confidence to say it, the big players may very well want your wares**

INDUSTRY TYPES & OPPORTUNITY THEY OFFER

Industry Type	Description	Industry Characteristics	Opportunities	Entrepreneurial firms (exploiting opportunities)
Emerging Industries	High uncertainty; barriers to entry low; no established pattern of rivalry	Recent change in demand or technology; new industry standard operating procedures have yet to be developed	First mover advantage	• Apple • Windspire • PharmaSecure
Fragmented Industries	Geographic roll-up strategy; position as industry leader	Large number of firms of approximately same size	Consolidation	• Starbucks • 1-800-GOT-JUNK? • Geeks on Call
Mature Industries	Occasionally new product innovation to revitalize the industry	Slow increases in demand, numerous repeat customers, & limited product innovation	Process and after sale service innovation	• InstyMeds • Fresh Health Vending • Daisy Rock Guitars
Declining Industries	Leadership, niche and cost reduction strategy	Consistent reduction in industry demand	Leaders, niche, harvest & divest	• Nucor • JetBlue
Global Industries	Multi-domestic and global strategy	Significant international sales	Multinational & global	• PharmaJet • d.light

THREE GENERIC COMPETITIVE STRATEGIES

In coping with the five competitive forces, there are three potentially successful generic strategic approaches to outperforming other firms in an industry:

1. OVERALL COST LEADERSHIP:

- Requires aggressive construction of efficient-scale facilities, pursuit of cost reductions from experience, tight cost and overhead control, avoidance of marginal customer accounts, and cost minimization in areas like **R&D,** service, sales force, advertising, and so on. A great deal of managerial attention to cost control is necessary to achieve these aims.
- Low-cost position yields the firm **above-average returns** in its industry despite strong competitive forces. Lower costs mean that it can still earn returns after its competitors have competed away their profits through rivalry.
- Defends firm against powerful buyers as they drive down prices to the level of next most efficient competitor. Low cost provides a defense against powerful suppliers by providing more flexibility to cope with input cost increases. Factors that lead to a low-cost position usually also provide substantial entry barriers in terms of scale economies or cost advantages. Places the firm in a favourable position vis-a-vis substitutes relative to its competitors.
- Protects firm against all five competitive forces because bargaining can only continue to erode profits until those of the next most efficient competitor are eliminated, and because the less efficient competitors will suffer first in the face of competitive pressures. Achieving a low overall cost position often requires a high relative market share or other advantages, such as favorable access to raw materials.
- It may well require designing products for ease in manufacturing, maintaining a wide line of related products to spread costs, and serving all major customer groups in order to build volume. In turn, implementing the low-cost strategy may require heavy up-front capital investment in state-of-the art equipment, aggressive pricing, and start-up losses to build market share. High market share may in turn allow economies in purchasing which lower costs even further. Once achieved, the low-cost position provides **high margins** which can be reinvested in new equipment and modern facilities in order to maintain cost leadership. **Reinvestment may be a prerequisite to sustaining a low-cost position.**
    - Harnischfeger is in the midst of a daring attempt to revolutionize the rough-terrain crane industry in 1979. Starting from a 15 percent market share, Harnischfeger redesigned its cranes for easy manufacture and service using modularized components, configuration changes, and reduced material content. It then established subassembly areas and a conveyorized assembly line, a notable departure from industry norms. It ordered parts in large volumes to save costs. All this allowed the company to offer an acceptable quality product and drop prices by 15 percent. Harnischfeger's market share has grown rapidly to 25 percent and is continuing to grow. Says Willis Fisher, general manager of Harnischfeger's Hydraulic Equipment Division: We didn't set out to develop a machine significantly better than anyone else but we did want to develop one that was truly simple to manufacture and was priced, intentionally, as a low cost machine.' Competitors are grumbling that Harnischfeger has "bought" market share with lower margins, a charge that the company denies.

2. DIFFERENTIATION

- Differentiating the product or service offering of the firm is creating something that is perceived ***industrywide*** as being unique. Approaches to differentiating can take many forms: **design or brand image** (Fieldcrest in top of the line towels and linens; Mercedes in automobiles), **technology** (Hyster in lift trucks; Macintosh in stereo components; Coleman in camping equipment), **features** (Jenn-Air in electric ranges); **customer service** (Crown Cork and Seal in metal cans), **dealer network** (Caterpillar Tractor in construction equipment), or other dimensions.
- Ideally, the firm differentiates itself along several dimensions. **Caterpillar Tractor**, for example, is known not only for its dealer network and excellent spare parts availability but also for its extremely high-quality durable products, all of which are crucial in heavy equipment where downtime is very expensive.
- It should be stressed that the differentiation strategy **does not allow the firm to ignore costs**, but rather they are not the primary strategic target. Differentiation, if achieved, is a viable strategy for earning above-average returns in an industry because it creates a defensible position for coping with the five competitive forces, albeit in a different way than cost leadership.
- Differentiation provides insulation against competitive rivalry because of brand loyalty by customers and resulting lower sensitivity to price. It also increases margins, which avoids the need for a low-cost position. The resulting **customer loyalty** and the need for a competitor to overcome **uniqueness** provide ***entry barriers***. Differentiation yields **higher margins** with which to deal with supplier power, and it clearly mitigates buyer power, since buyers lack comparable alternatives and are thereby less price sensitive.
- Finally, the firm that has differentiated itself to achieve customer loyalty should be better positioned vis-a-vis substitutes than its competitors.
- Achieving differentiation may sometimes preclude gaining a high market share. It often requires a perception of exclusivity, which is incompatible with high market share. More commonly, however, achieving differentiation will imply a trade-off with cost position if the activities required in creating it are inherently costly, such as extensive research, product design, high quality materials, or intensive customer support.
- Whereas customers industrywide acknowledge the superiority of the firm, not all customers will be willing or able to pay the required higher prices (though most are in industries like earthmoving equipment where despite high prices Caterpillar has a dominant market share). In other businesses, differentiation may not be incompatible with relatively low costs and comparable prices to those of competitors.

3. FOCUS

- The final generic strategy is focusing on a particular buyer group, segment of the product line, or geographic market; as with differentiation, focus may take many forms.
- Although the low cost and differentiation strategies are aimed at achieving their objectives industrywide, the entire focus strategy is built around serving a particular target very well, and each functional policy is developed with this in mind.
- The strategy rests on the premise that the firm is thus able to serve its narrow strategic target more effectively or efficiently than competitors who are competing more broadly. As a result, the firm achieves either differentiation from better meeting the needs of the particular target, or lower costs in serving this target, or both.
- Even though the focus strategy does not achieve low cost or differentiation from the perspective of the market as a whole, it does achieve one or both of these positions vis-a-vis its narrow market target.
- The firm achieving focus may also potentially earn above-average returns for its industry.
- Focus may also be used to select targets least vulnerable to substitutes or where competitors are the weakest. For example, Illinois Tool Works has focused on specialty markets for fasteners where it can design products for particular buyer needs and create switching costs. Although many buyers are uninterested in these services, some are.
- Fort Howard Paper focuses on a narrow range of industrial-grade papers, avoiding consumer products vulnerable to advertising battles and rapid introductions of new products.
- Porter Paint focuses on the professional painter rather than the do-it-yourself market, building its strategy around serving the professional through free paint-matching services, rapid delivery of as little as a gallon of needed paint to the worksite, and free coffee rooms designed to provide a home for professional painters at factory stores. An example of a focus strategy that achieves a low-cost

DEFINING INDUSTRY FOCUS AND TYPE OF BUSINESS TO START

Work Experience

- Position, type and depth of experience gained
- Other work experience

Educational Experience

- University, skills gained
- Other education, skills gained

Family Experience

- Family business, experience gained, source of finance, access to channels & suppliers

Personal Passions

- Personal goals and interests

The Industry Segment or Niche

- First is self-assessment of your personal factors; in the middle, your cogent industry analysis; and last an initial definition of the type of business you want to start given your interests and the target industry segment or niche

Your Industry Analysis

Pros

Cons

Challenges

The Type of Business You Want to Start

- A product venture
- A systems venture
- A services venture
- Combination/ Hybrid
- A pure distribution venture

- Last step defines the scope of a venture: deciding what type of business to be in terms of creating and providing products, systems, services, a hybrid combination thereof, or a pure distribution play
- It is not unusual to find customers in the same industry being served by different companies focusing on different things

DIFFERENT TYPES OF BUSINESS OPPORTUNITY IN THE SAME INDUSTRY

Suppose we want to start a venture in the supply chain management industry, with a focus on mass market retailers. Those retailers, led by Big Bazar, want to track every product they sell from suppliers' factories to their store shelves. Now let's consider how different business "types" created by entrepreneurs could serve the needs of Big Bazar and others needing next-generation supply chain management solutions.

- ***Products:*** We might create RFID sensors and readers capable of tracking products in transit by item and by pallet. The venture will obtain patents on its sensor technology and find third party manufacturers to produce its sensors & readers. We could be selling RFID tags and tag readers.
- ***Systems:*** We might create software based systems to acquire data from other vendors' RFID readers in real time, communicate those data to central services armed with sophisticated workflow management software, and use software applications to inform customers of the status of products in production, in transit any place, in the warehouse, or in the store. Customers will use these data to optimize inventory planning and distribution center operations. We are selling "systems" and support services for those systems.
- ***Services:*** We take other companies' sensors, RFID readers, and server software, package it all together and provide to the implementation and customization services needed to tune these technologies for specific situations. We are selling our expertise and forms – in other words, a systems integration and consulting services firm.

Type of Business	Cost Implications	Operating Profit	Point of Leverage
Product	For every $100 revenues: $30 - $40 spent on manufacturing, another $25 - $40 on selling, marketing, R&D, and administration	Net operating profit margin in the range of $15 - $25	To design a great set of products and manufacture large quantity at a low cost per unit. Outsourcing can be a real advantage of "lean" startups
Systems	For every $100 revenues: $20 - $30 might be spent on R&D, and another $10 - $20 on sales, marketing, and administration	Net operating profit margin of $50 or more	To hire the smartest programmers, have them create fantastic software, and then ship it electronically with virtually no cost
Services	For every $100 revenues: spends a third on labor; a third on technology, marketing and administration	Net operating profit margin of $33 or more	The design of the service, the people who deliver the service, and the technology that helps them deliver the service efficiently & effectively
Pure Distribution	Distribution channel – people, trucks, information technology, innovative distribution models	Tend to make about 5% - 8% operating profit	Key success is Logistics with that information technology

COMPETITOR ANALYSIS

- ❑ **Direct competitors:** businesses that offer products identical or similar to those of the firm in the analysis. They attempt to acquire the same customers as the new firm
- ❑ **Indirect competitors:** offer close substitutes to the product the firm sells.
- ❑ **Future competitors:** that are not yet direct or indirect competitors but could move into one of these roles at any time

- ❖ Identifying 5 – 10 direct and indirect competitors makes it easier for the firm to complete its competitive analysis grid
- ❖ Creating meaningful value and sharp differentiation from competitors are actions small firms in crowded industries can take to remain competitive & gain market share.

OPENING PROFILE

ELEMENT BARS

www.elementbars.com

(Occupying a Unique Position in a Difficult Industry – and Thriving)

- Jonathan Miller started tinkering with making energy bars in his kitchen, at the same time his wife Jennifer was working with Maria Sutanto doing the same thing. Jennifer put Jonathan and Maria together, how to make energy bars at home. Both were energy bar eaters but were dissatisfied with the unhealthy ingredients contained in many of them in the market.
- Miller & Sutanto met in December 2007. Miller was an MBA student (Marketing specialization) at Kellogg School of Management while Sutatnto was a PhD candidate in molecular nutrition.
- Led to **Element Bars'** basic value proposition - *offering fresh nutritious energy bars that could be "customized" by its customers*.

- Sales would be made online and through special arrangements with businesses like Spas and Fitness centres that wanted to brand their own speciality energy bars.
- Customers log onto Element Bars' website and in five steps can "build" their own energy bar like first is to pick a base texture, with options such as chewy; crispy; datey
- Then to add their choice of fruits, nuts, sweet, and boosts – a nutrition label on the screen changes as ingredients are added – so the creator can see how different ingredients affect the calories or the grams of saturated fat in the bar. Finally to name the bar whatever customer wants. Bar is made and shipped in few days.
- A helpful twist – *while users are free to build any energy bar of their choice but the site warns them if one of their choices will result in a poor outcome in terms of taste /texture*
- Bars run $36 for a pack of 12, though a discount of $6 is given for the purchase of bars listed under the popular section of the site.
- Shortly after Element Bars launched, a third cofounder was added.
- The novel way the bars are made & sold, combined with the "freshness" factor of shipping just in few days, describes Element Bars position in the $3 billion per year energy bar industry.

Element Bars envisions a bright future, for two reasons:

1. Website is easy to navigate and five steps look simple

    however, the technology behind the website was not simple to create;

    there are trade secrets embedded in the functionality of the site, along with how the bars are baked & shipped in such an expedient manner

   Co. believes that sufficient barriers to entry are in place

2. The energy bar market has tremendous upside potential.

    only about 15% of the population regularly buys them

    Element Bars doesn't necessarily have to take sales from large competitors as it can appeal to growing population of health-conscious consumers to bring new customers into the energy bar industry

COMPETITIVE ANALYSIS GRID: ELEMENT BARS

Name	Element Bars	Power Bar	Cliff Bar	Balance Bar	Larabar
Nutritional value	Advantage	Even	Even	Even	Even
Taste	Even	Disadvantage	Even	Even	Disadvantage
Freshness	Advantage	Disadvantage	Disadvantage	Disadvantage	Disadvantage
Price	Disadvantage	Advantage	Advantage	Advantage	Advantage
Packaging	Advantage	Even	Even	Even	Even
Branding	Disadvantage	Advantage	Advantage	Even	Even
Customizable	Advantage	Disadvantage	Disadvantage	Disadvantage	Disadvantage