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9B18M059

STUDENT GUIDE TO THE CASE METHOD: note 7—USING common tools for case analysis

Susan J. Van Weelden and Laurie George Busuttil wrote this note solely to assist students with understanding and using the case method. The authors do not intend to illustrate either effective or ineffective handling of a managerial situation. The authors may have disguised certain names and other identifying information to protect confidentiality.

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A *case* or *case study* is a real business story that requires you to step into the role of a manager or a member of the management team that faces a dilemma, or the role of a consultant assisting an organization that faces a dilemma. Acting in that role, you are tasked with resolving the issues or problems that the profiled organization is facing at a particular moment in time. Alternatively, you are asked to evaluate and choose among opportunities that exist for the organization at a specific point in time. Those issues and opportunities may be confined to a specific discipline in business, such as accounting, marketing, human resources, or strategic management. However, the challenges often involve several disciplines, reflecting the multi-faceted nature of business in practice.

The case method involves learning by doing. It provides you with an opportunity to apply your knowledge and skills to real-life and realistic situations. Listening to class lectures, reading about various business subjects, and performing quantitative and qualitative analyses to solve well-defined problems are all valuable learning tools; however, management skills and knowledge cannot be developed by these methods alone. Management requires more than applying a storehouse of prepackaged solutions or standard answers. Each situation faced by management has its own variables unique to the situation. Using the case method provides you with valuable opportunities to develop and practise skills you will need in those situations.

1. **Introduction to Common Tools for Case Analysis**

The method for a basic case analysis presented in Note 2 of the Case Guide Series—“Performing a Case Analysis,” No. 9B18M054—can be used for various purposes: discussing the case in class, writing a report, making a presentation, or writing a case exam. This note provides you with a few of the more popular tools used in case analysis and guides you in using those tools.

The guidelines in this note are for general use. You should always defer to your instructor’s requirements, which may differ or be more specific.

1. **horizontal Analysis**

The data presented by the case author(s) in figures and exhibits will provide you with some of the best opportunities for value-added analysis. Reorganize and summarize the data. Perform additional calculations. Draw new comparisons. In doing so, you will be able to interpret existing information in new ways and provide support for new findings.

When data are presented in numerical form, a logical first step in analyzing the data is to compute percentage changes from one year to the next, or to assess the magnitude of the differences between one company and the next. Look for trends such as whether the company is gaining or losing market share compared with its competitors, and whether sales are growing or shrinking, and the rate of change.

When calculating year-over-year percentage changes, the earlier year’s number forms the base:

For example, suppose you are given the following numbers:

|  |  |
| --- | --- |
| **Year** | **Sales** |
| 2015 | $184,700 |
| 2016 | $182,500 |
| 2017 | $179,800 |

The percentage decrease in sales from 2015 to 2016

The percentage decrease in sales from 2016 to 2017

For the two-year period:

The percentage decrease in sales from 2015 to 2017

From the above horizontal analysis, you can conclude that sales are declining at an increasing rate.

1. **VERTICAL ANALYSIS**

Vertical analysis or common size analysis expresses each item on a financial statement in terms of a percentage of a base amount. The base for income statement items is usually sales. For example, you can calculate cost of goods sold (COGS) or other expenses as a percentage of sales. Potential bases for statement of financial position (balance sheet) items are total assets or total liabilities. For example, you can calculate inventory as a percentage of total assets, or you can calculate current liabilities as a percentage of total liabilities.

Vertical analysis facilitates comparison between one business and its competitors of different sizes. It also allows a business to compare its own results from one year to the next. For instance, if sales were higher, one would expect COGS to also be higher. By expressing COGS as a percentage of sales, we can determine whether sales price increases are keeping pace with cost increases.

For example, suppose you are given the sales numbers in Section 2.1 and the following numbers:

|  |  |
| --- | --- |
| **Year** | **COGS** |
| 2015 | $85,800 |
| 2016 | $84,500 |
| 2017 | $86,200 |

|  |  |
| --- | --- |
| **Year** | **% of Sales** |
| 2015 | 46.4 |
| 2016 | 46.3 |
| 2017 | 47.9 |

You might note that for 2015 and 2016, COGS as a percentage of sales was fairly steady, but in 2017 the percentage rose significantly to 47.9 per cent. Referring back to Section 2.1, you might also note that sales had declined from the previous two years, leading to questions about not only the drop in sales but also the reasons for the sharp increase in COGS.

1. **RATIO ANALYSIS**

In many cases, it is beneficial to analyze an organization’s financial performance by performing ratio analysis. Ratios show the relationship among selected items of financial statement data, as expressed by a percentage, rate, or proportion.

Ratios are useful only if they are compared to ratios of prior years, ratios of competitors, industry standards, and forecast ratios. Be judicious in both your calculation and interpretation of ratios to ensure that your financial statement analysis adds value to your report. The most valid external comparisons involve companies within the same industry, or industry benchmarks produced by such organizations as J.D. Power or Deloitte. General benchmarks, known as “rules of thumb” are sometimes available; however, industry benchmarks take precedence over general benchmarks since ratios can be expected to vary considerably from one industry to the next.

When a ratio mixes balance sheet (statement of financial position) values and income statement (statement of earnings) values, use an average of the balance sheet values. (This approach is used because an income statement provides information about a company’s performance over a period of time, whereas a balance sheet is comprised of values at one point in time.) When the value at the beginning of the time period is unavailable (e.g., when only two years’ data are available and you are calculating comparison ratios for two years), use year-end values as a proxy for the average. However, the more asset values fluctuate over that period of time, the more use of a year-end value distorts the picture.

The following formula is used to calculate the average of balance sheet values:

where one year’s beginning value is the prior year’s ending value.

Provided below are the formulas and brief interpretations of three types of ratios—profitability or activity ratios, liquidity ratios, and solvency ratios.

* 1. **Profitability or Activity Ratios**

Profitability ratios measure a business’s ability to generate earnings from providing goods and services. Profitability ratios can be useful for comparing a business’s present and past performance, or comparing a business with that of its competitors or industry benchmarks during the same period in time. The three main profitability ratios are return on assets (ROA), return on equity (ROE), and earnings per share (EPS). As will be shown below in Sections 4.12 through 4.18, changes to ROA can be explained by calculating other ratios.

* + 1. Return on Assets

Return on assets (ROA) indicates the profitability of a business relative to the assets invested in the business. An ROA of 10 per cent indicates that for every dollar invested in assets, the business earns 10 cents in profit. Instead of net income (also referred to as profit or earnings), income from continuing operations can be used to provide a better benchmark for future comparison, since discontinued operations will no longer be available to generate profit.

ROA depends on two factors: profit margin and asset turnover. Thus, the equation for ROA can also be stated as follows:

* + 1. Profit Margin

Profit margin indicates the profitability of a business relative to its sales revenue, and reflects how well a business is controlling its various expenses. Expressing net income relative to sales revenue provides a more meaningful comparison of the business’s performance from one year to another than merely comparing net income in the two years. A profit margin of 12 per cent indicates that for every dollar of sales revenue, the business has 12 cents left in profit after all expenses are deducted.

Profit margin, in turn, can be dissected to analyze how well individual expenses are being controlled.

* + 1. Gross Profit Margin

Gross profit is a preliminary measure of profitability. It measures a company’s ability to maintain an adequate selling price above its cost of goods sold (COGS). Gross profit also measures the company’s ability to pay operating and other expenses. If the gross profit margin is 30 per cent, the business has 30 cents left from every dollar of sales revenue to pay operating and other expenses. In other words, for every dollar in sales revenue, it costs the business, on average, 70 cents to make or buy the products it is selling, leaving 30 cents to pay operating expenses, such as wages and rent, and other expenses, such as interest. A declining gross profit margin is a sign that selling prices are not keeping up with increases in COGS.

* + 1. Expense Ratios

Expense ratios measure the portion of income that is spent on specific expenses. An expense ratio that is higher this year than the previous year could indicate that the company has potential problems with controlling costs in individual expense categories such as selling expenses, administrative expenses, and interest expenses. However, increasing the amount spent on expenses could also be the key to future growth, as would be the case, for example, if the business significantly increased its advertising and promotion expenditures or added new salespeople in an effort to increase sales.

Note that although you can calculate an expense ratio using COGS, the result would be the complement of the gross profit margin (i.e., if the gross profit margin is 34 per cent, then COGS is 66 per cent of the net sales).

* + 1. Asset Turnover

The asset turnover ratio, the second main determinant of ROA, measures how well a business uses its assets to generate sales. If the asset turnover ratio is 8.33 per cent, the business is generating 8.33 cents in sales for every dollar invested in assets. Thus, the two keys to improving a company’s ROA are to improve the profitability of each sale of a good or service and to sell more goods and services in the first place.

* + 1. Inventory Turnover

The inventory turnover ratio measures the average number of times inventory is sold during the period. The higher this ratio, the more quickly inventory is being sold and, therefore, the more efficiently inventory is being used to generate sales.

The days in inventory ratio measures the average age of the inventory—the average number of days products remain in inventory, measured from the time the company produces or purchases the product to the time the product is sold to customers.

Days in inventory is an easier ratio to interpret than inventory turnover, but calculating days in inventory relies on first computing inventory turnover.

* + 1. Receivables Turnover

The receivables turnover ratio measures the number of times, on average, that receivables are collected during the year.

The average collection period shows the average number of days it takes a business to collect accounts receivables from customers. The average collection period should be evaluated in relation to the business’s credit terms; for many businesses, accounts are due within 30 days.

The average collection period is the easier of the two ratios to interpret, but it cannot be calculated without first computing the receivables turnover.

* + 1. Return on Equity

Return on equity (ROE) is the second main ratio that helps to assess the profitability of a business. It measures the return on shareholders’ equity—the profit relative to the investment of common shareholders (the true owners of the corporation). Because preferred dividends are reserved for and are paid out to preferred shareholders, they do not belong to the common shareholders and are subtracted from income before calculating ROE.

A ratio of 17 per cent indicates that for every dollar invested by common shareholders, the corporation earns 17 cents in profit. ROE is affected by two factors: ROA and debt to total assets. Thus, to improve its ROE, a firm can improve its ROA, increase its use of debt financing (known as increasing the use of leverage), or both. However, more reliance on debt financing also increases the risk that the organization will be unable to make interest and principal repayments.

* + 1. Earnings per Share

The third main measure of profitability is earnings per share (EPS), which looks at profitability from the perspective of common shareholders, who are the residual owners of the corporation. It expresses net income on a per share basis. EPS is widely used to compare profitability from one year to the next or to compare actual profitability against expected profitability. The calculation looks simple, but several accounting rules are applied to determine both the numerator (the income available to common shareholders) and the denominator (the weighted average number of common shares).

EPS is the only ratio that public companies are required to publish in their financial statements. Announcements of expected or actual EPS can cause stock prices to fluctuate, as the market reacts to the company’s initial projections and its subsequent performance against those goals. However, because companies each have widely varying numbers of common shares, EPS cannot be used for intercompany comparisons.

* + 1. Price-Earnings Ratio

The price-earnings (P/E) ratio looks at the market price of shares compared with earnings expressed on a per share basis. A P/E ratio of 10 indicates that an investor is willing to pay $10 for every $1 the share currently earns.

The P/E ratio is a measure of investors’ beliefs about the company’s future earnings potential. A high ratio indicates investors have confidence in the company and expect significant growth in profitability. Therefore, they are willing to pay a higher price for shares. It might also indicate that the shares are overvalued in the marketplace, making it a good time to sell those shares. A decreasing ratio indicates declining investor confidence.

The average P/E ratio over the past 80 years has ranged between 14 and 15.

* 1. **Liquidity Ratios**

Liquidity ratios evaluate a company’s ability to pay its short-term debts as they come due. The ratios can be used within a company to track a business’s performance by comparing the ratios over periods of time. The ratios can also be used to assess a company’s performance compared with the performance of another company or compared with industry benchmarks.

* + 1. Current Ratio

Current assets are assets that are expected to be converted into cash, sold, or used up within one year of the organization’s financial statement date.

Current liabilities are debts that are expected to be paid within one year of the organization’s financial statement date.

The current ratio measures a company’s current assets against its current liabilities. A current ratio of 1.8 means that for every dollar of current liabilities, the business has $1.80 in current assets. A general rule of thumb is that this ratio should be at least 1.5 to 2.0, although as noted earlier, industry benchmarks always take precedence over general rules of thumb.

* + 1. Acid Test Ratio (Quick Ratio)

The acid test ratio assesses a company’s ability to pay its current liabilities with short-term assets that can be quickly converted to cash. An acid test ratio of 0.9 means that for every dollar a company has in current liabilities, it has 90 cents in highly liquid assets to pay those current debts. As a rule of thumb, a minimum healthy ratio is 0.9 to 1.0.

The current ratio and the acid test ratio both measure a business’s short-term ability to pay its current debts as they come due. However, the acid test ratio is a more accurate measure of liquidity because it excludes current assets that are not quickly turned into cash (e.g., inventory) or intended to be turned into cash (e.g., prepaid insurance and supplies).

The inventory turnover and accounts receivable turnover ratios, discussed earlier as activity ratios (see Sections 4.1.6 and 4.1.7), are also liquidity ratios because a business’s ability to pay off its own current liabilities depends to a great extent on how quickly it can sell its inventory and, in turn, how quickly it can collect payment from its customers. For example, if days in inventory is 53 days and the collection period is 45 days, the business needs to wait a total of 98 days (days in inventory + collection period) before cash is available to pay its own suppliers and to pay other operating expenses.

* 1. **Solvency Ratios**
     1. Debt Ratio

The debt to total assets ratio (also referred to as the debt ratio) measures the percentage of a business’s assets that are financed by creditors. The ratio indicates how heavily a business relies on debt financing. A ratio of 0.55 means that for every dollar of assets, 55 cents is financed by debt; or, expressed another way, 55 per cent of a business’s assets are financed by debt.

The level of debt that a business can handle depends on its earnings. As well, more capital intensive industries generally use more debt financing. However, in general, as the percentage of debt to total assets increases, the risk also increases that the business may be unable to meet its maturing obligations and ongoing interest payments. In general, 0.60 to 0.70 is an acceptable level.

* + 1. Debt to Equity Ratio

The debt to equity (D/E) ratio is a variation of the debt ratio. Where the debt to total assets ratio measures how much of a company’s assets are financed by debt, the D/E ratio measures how much of a company’s debt is covered by shareholders’ equity (including retained earnings). A ratio of 0.7 means that for every dollar of shareholders’ equity, there is 70 cents in liabilities. A high D/E ratio usually means that a company is being aggressive in using debt financing to leverage growth.

Both the debt to assets and debt to equity ratios are sometimes calculated using long-term liabilities instead of total liabilities.

* + 1. Times Interest Earned

Where EBIT refers to earnings before interest and taxes.

The times interest earned ratio (also known as the interest coverage ratio) is one measure of a corporation’s ability to generate sufficient earnings to make interest payments as they come due. An acceptable range is typically 2.0 to 3.0, although, again, the suitability of this range varies by industry.

1. **Assessing Profitability**

If you are asked to evaluate the profitability of a specific alternative course of action, your approach should depend on the level of detail provided in the case facts. A simple measure of profitability is to calculate the contribution margin (CM) of individual products.

Variable costs are those costs that vary directly, on a total basis, with increases or decreases in sales, such as labour or materials. As production volume increases, total variable costs increase proportionately; as production volume decreases, total variable costs decrease proportionately. Fixed costs are those costs that do not vary, on a total basis, with changes in sales; rather, they need to be paid regardless of the level of business activity. Total fixed costs remain the same, as long as sales fall within a relevant range of production. Examples of fixed costs include rent, insurance, utilities, and property taxes.

Variable costs per unit do not change as production volume changes, while fixed costs per unit do change as production volume changes.

You can calculate the contribution margin to compare the profitability of different services or products. Obviously, the larger the margin, the better for the company; but in any event, a positive contribution margin is required to help cover the fixed costs associated with production and distribution.

Another simple measure of profitability is to calculate the gross profit margin (see Section 4.1.3). Contribution margin is the better measure of profitability for decision making purposes—especially because it can be used to perform break-even analysis—but it requires having sufficient information from the case to distinguish between variable and fixed costs. Calculating the gross profit does not require the same detail.

Finally, if sufficient information is available in the case, pro forma (forecast) income statements should be prepared for each alternative course of action you are evaluating.

1. **Break-even Analysis**

One of the most helpful management accounting tools for case analysis is break-even analysis. While the goal of a business is not to just break even (i.e., earn zero profit), knowing the break-even point for a specific product or a group of products helps to measure how risky a given new product venture might be. If expected sales do not exceed the break-even point, a business will need to reconsider the product’s price, find ways to reduce costs, or both.

A helpful variation on break-even analysis is to calculate the sales (in units or dollars) required to reach a target level of profit.

1. **Market Potential and Market Share**

Market potential (MP) is an estimate of the revenue a company can expect to make from a product or service it plans to market.

Where N = total number of customers

P = average selling price

Q = average annual consumption quantity

MS = market share, which is the actual percentage of industry sales captured by a company

1. **SWOT Analysis**

A SWOT analysisis an evaluation of the strengths (S), weaknesses (W), opportunities (O), and threats (T) faced by an organization. It is a popular tool for analyzing an organization’s internal and external environments to identify various issues. A SWOT analysis can also be used to generate pros and cons when evaluating alternative courses of action.

Although strengths and weaknesses are listed first in the acronym, the assessment of opportunities and threats (i.e., the external analysis) is usually performed before the internal analysis.

*Opportunities* represent conditions in the external environment that an organization can take advantage of (by formulating and implementing appropriate strategies) to enhance its competitiveness, profitability, and overall success. Opportunities should not be confused with alternatives. For example, an increase in the demand for dark chocolate because of its cancer-fighting antioxidants and heart-healthy properties represents an opportunity (a favourable environmental condition). To take advantage of this opportunity, a confectionery company might consider alternatives such as switching some of its milk chocolate production capacity to dark chocolate or acquiring a company that specializes in the manufacture of dark chocolate.

*Threats* represent conditions in the external environment that endanger the competitiveness, profitability, and success of the organization. For example, the increasing incidence of obesity and diabetes pose threats to a confectionery company.

Opportunities represent possibilities, while threats pose constraints. Both are conditions that are outside an organization’s control.

*Strengths* are activities the organization does very well or characteristics that enhance its competitiveness. Strengths can be found in skills, expertise, physical assets, human assets, or competitive advantages.

*Weaknesses* are activities the organization does poorly (compared with its competitors), resources it lacks, or internal conditions that make the organization vulnerable. These are areas that an organization can improve on; for example, a retail business is vulnerable if it does not have an online sales presence but its competitors do.

1. **PESTLE Analysis**

A PESTLE analysis (see Figure 1) identifies changes and trends in six segments of the general, societal, or macro environment: political (P), economic (E), socio-cultural (S), technological (T), legal (L), and environmental (E). The analysis is also variably referred to as PESTEL (or PEST analysis if only the first four factors are considered). It evaluates the potential impact of changes and trends in the environment on both the industry and the organization, considering how the changes and trends affect supply, demand, competition, and each element of the company’s value chain.

A PESTLE analysis can be used as a stand-alone tool, or it can be used in conjunction with a SWOT analysis to enhance the thoroughness of external analysis by more methodically identifying opportunities and threats.

**Figure 1: PESTLE Analysis**

|  |  |
| --- | --- |
| Force | Examples |
| Political | Tariffs,trade agreements, and special interest groups that promote or oppose specific products (e.g., tobacco) or marketing practices (e.g., promotion of healthy body image) |
| Economic | Interest rates, inflation rates, stock market trends, unemployment rates, gross domestic product, productivity levels, disposable income levels, government deficits, monetary policies, tax policies |
| Socio-cultural | Society’s values, beliefs, attitudes, lifestyles, and demographics; e.g., having children later in life, desire to live in the suburbs, attitudes toward saving and investing, attitudes toward leisure and careers, desire for healthy lifestyle; gender, age, and income distribution; ethnic makeup; education levels |
| Technological developments | Developments that lead to new or improved products or services, and changes in how products are delivered and marketed; e.g., social media, computer-aided manufacturing, artificial materials |
| Legal | Laws and regulations; e.g., competition, labour, taxation, intellectual property, product safety, corporate governance |
| Environmental | Trends related to pollution, global warming, and sustainable development; e.g., recycling programs, packaging, energy conservation, and reforestation |

In the body of a report, use PESTLE to identify only the most important external forces. For example, for an automobile manufacturer, the most relevant forces might be abandonment of free trade agreements (P); increasing interest rates for car loans (E); pressure to use rapid transit systems (S); development of self-driving cars (T); higher damage awards for product safety violations (L); and lower emissions requirements (E). If it adds value to your report, a more extensive description of external forces can be put in an appendix.

1. **Porter’s Five Forces Framework[[1]](#footnote-1)**

Porter’s five forces framework (see Figure 2) is used to evaluate five competitive forces that influence an industry’s profit potential or attractiveness, and to identify where economic profit lies in an industry’s value chain (see Section 133.1). A five forces analysis can also be used to identify specific opportunities and threats in the industry, such as introduction of a substitute product or increased competitive rivalry.

**Figure 2: Porter's Five Forces**

Bargaining Power of Suppliers

Bargaining Power of Buyers

Threat of New Entrants

Intensity of Rivalry between Competing Firms

Threat of Substitute Products

*The threat of new entrants* increases when barriers to entry are low, for example, when

* there are no economies of scale related to production, marketing, or distribution;
* product differentiation is low, so new firms do not have to spend heavily on branding;
* capital requirements are low, which makes entry into an industry less risky;
* switching costs are low, so new firms do not need to offer major improvements to get a customer to switch brands; or
* firms have easy access to distribution channels.

*Intensity of industry rivalry* increases, for example, when

* the number of competitors increases;
* competitors are equal in size and capability;
* demand for the product is growing slowly; or
* customers’ costs to switch brands are low.

*Threat of substitutes* (products that provide similar benefits) is high, for example, when

* the relative price of substitute products decreases; or
* customer switching costs are low.

*Supplier power* is high, for example, when

* a supplier group is dominated by few companies;
* the supplier group’s product is unique;
* there are no or few substitute inputs; or
* suppliers pose a credible threat of integrating forward into the organization’s business.

*Buyer power* is high, for example, when

* the buyer group is concentrated or buyers purchase in large volumes;
* products purchased are undifferentiated;
* buyers earn low profits, which creates pressure to lower purchasing costs; or
* buyers pose a credible threat of integrating backward to make the organization’s product.

In the body of a report, Porter’s five forces analysis should be used judiciously to highlight key forces that make an industry attractive or unattractive to enter. For example, in analyzing whether a restaurant should expand into catering, an organization would encounter an unattractive industry characterized by high threat of new entrants (capital requirements are relatively low and product differentiation is hard to achieve); fierce rivalry (many restaurants are doing catering, and demand for catered meals is growing slowly); high supplier power (there are only a few commercial food service companies); high buyer power (there are many caterers for buyers to choose from, and often they offer the same type of food); and a moderately high threat of substitutes (going to a restaurant, cooking yourself). A more completePorter’s five forces can be placed in an appendix, if you deem this to be value-added.

1. **Stakeholder Analysis**

A stakeholder analysis identifies the relevant internal and external stakeholders (e.g., customers, shareholders, employees, distributors, suppliers, and the local community) and what they need or expect from an organization as it pertains to the dilemma under consideration.

After identifying potential stakeholders and their interests, a company can either align its actions to meet the interests and needs of the stakeholders, or it can manage its relationships with stakeholders by addressing the consequences of the company’s actions on the stakeholders.

A grid similar to that shown in Figure 7 for resource gap analysis can be used to summarize the existing preferences of various stakeholders, the new required preferences (i.e., to align with a particular alternative), major gaps between stakeholder expectations and corporate actions, and ways to reduce those gaps.

1. **Industry Key Success Factors**

Industry key success factors (KSFs) identify what a company needs to succeed or win in the industry. KSFs include product qualities, organizational capabilities, resources, and market achievements that combine to create value for customers and are critical for long-term competitive success in the industry. An industry usually has only two or three KSFs; rarely are there more than five or six.

Identifying KSFs allows a company to assess its performance against industry KSFs. A company wants to perform well on all KSFs and be distinctively better on one or two to develop a competitive advantage.

1. **Value Chain Analysis**
   1. Industry Value Chain

An industry value chain[[2]](#footnote-2) (see Figure 3) consists of the activities that contribute to the process of firms within an industry providing a valuable product or service. Most businesses buy products or supplies from another company, transform them, and then sell them to customers. Therefore, an industry value chain includes the firms’ own value chains as well as the value chains of their suppliers and distributors.

**Figure 3:** **Industry Value Chain**

Inbound Logistics

Operations

Outbound Logistics

Marketing & Sales

Service

Firm Infrastructure

Human Resource Management

Technology Development

Procurement

Margin

**13.2 Organization Value Chain**

An organization can use a value chain analysis to systematically identify its own capabilities and competitive advantages. Part of a sample value chain analysis for an organization is provided in Figure 4. The analysis is designed to evaluate the value chain of Birks Group, a Canadian jewellery company. Analyzing Birks’ value chain identifies where the company’s primary and supporting activities can be leveraged and integrated to add value and build an advantage over a competitor.

**Figure 4: Value Chain Analysis, Birks Group**

|  |  |
| --- | --- |
| Primary Activities | |
| Operations | Jewellery factory: making models of jewellery, casting metals, mounting and setting jewels, polishing completed jewellery  Watch factory: limited reassembly and customization of watches |
| Outbound logistics | Shipping of jewellery and watches |
| Marketing and sales | 38 corporate stores in 15 Canadian markets |
| Service | Polishing and repairing of jewellery and watches |
| **Secondary Activities** | |
| Human resource management | Internationally renowned, award-winning, in-house design team |
| Firm infrastructure | Head office support by 62 managers in Montreal |
| Procurement | Sourcing metal and jewels for jewellery  Sourcing watch components for limited reassembly |

1. **Competitive Position Matrix**

A competitive position matrix identifies competitive dimensions that add value and are important to the customer. Potential dimensions include price, delivery, price/quality mix, product/service characteristics, product/service scope, and geographical scope. The matrix uses these dimensions to compare the positions of competitors in an industry (see Figure 5). Competitors with similar characteristics and market positions can be grouped to make competitive analysis more manageable.

**Figure 5: Competitive Position Matrix, Canadian Furniture Retail**

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
|  | Geographical Scope | Price Relative  to Quality | Selection | Service and Delivery |
| IKEA | National, in urban centres | Low to moderate | Low—only knock-down furniture | Low—consumers transport and assemble |
| The Brick | National | Low to moderate | High | Moderate—includes financing |
| Hudson’s Bay (Home Outfitters) | National | Low to moderate | Moderate to high | Moderate to high |
| Independents | Local | Moderate to High | Low to high | High |

1. **Strategic Cluster Map**

A strategic cluster map (or strategic group map) provides a convenient visualization of the competitive position of various firms in the industry, but the map limits the choice of competitive dimensions to two (see Figure 6).

**Figure 6: Strategic Cluster Map, Canadian Furniture Retail**

*High*

*Low*

*Full-Line Mass Merchandiser*

*Full-Line*

*Specialty*

**Width of Product Line, Range of Merchandise Mix**

**Price Relative to Quality**

1. **Resource Gap Analysis**

A resource gap analysis identifies an organization’s major gaps in resources and skills. It can be used to analyze issues and to develop the pros and cons for alternative courses of action.

In Figure 7, a partially completed template for a resource-gap analysis identifies gaps in a university’s ability to serve adult learners through a continuing education program.

**Figure 7: Resource Gap Analysis**

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| Resource Category | Required Resources | Available Resources | Resource Gaps | Ways to Reduce Resource Gaps |
| Human Resources | Course instructors | Existing full-time and part-time faculty; alumni with experience in a variety of fields | Instructors who have experience with adult learners | Hire and train instructors |
| Operations | Curriculum | Existing courses | Material tailored to an adult audience with on-the-job experience | Have faculty adjust existing course material; have faculty develop new course material |

1. **Core Competencies**

Core competencies are skills and capabilities that an organization uses exceptionally well, such as developing curriculum for a diverse audience or delivering instructional content using user-friendly online platforms. Analysis of an organization’s core competencies can be used to identify strengths, as part of a SWOT analysis. When core competencies involve competitively important value chain activities, the competencies can evolve into competitive advantages.

1. **Competitive Advantage Analysis: VRIO[[3]](#footnote-3)**

The VRIO framework developed by Jay Barney suggests that resources and capabilities may offer a competitive advantage if they are valuable (V), rare (R), and inimitable (I) (i.e., difficult to imitate), and the firm is organized (O) to capitalize on those resources and capabilities.

Resources are *valuable* if they contribute to meeting customers’ needs at the price that customers are willing to pay. Resources are also valuable if they enable a company to develop alternatives to exploit opportunities, mitigate threats, and improve efficiency or effectiveness.

Resources and capabilities are *rare* if only a few competing firms possess them.

Resources and capabilities are *inimitable* if they are costly and difficult to imitate. Resources could be inimitable because they are physically unique; have been built up over time based on specific experiences (e.g., unique historical conditions); result from interpersonal relationships, group norms, or culture (social complexity); or because it is difficult to identify the resource, its value, or its competitive advantages (causal ambiguity).

Finally, resources and capabilities provide a competitive advantage only if the firm is *organized*—that is, the firm has thenecessary structure, such asthe appropriate employees, management, organization, control systems, reward systems, and culture—to capitalize on its resources and capabilities.

1. **Case Analysis and Academic Integrity**

Because case analysis is complex, it may often seem helpful to discuss the case informally or formally with other students before participating in a class discussion, writing a report, or making a presentation. Managers and consultants often discuss problems with other people, within the constraints allowed by confidentiality. Therefore, your instructor may allow, encourage, or even require such discussion. However, ***to ensure academic integrity and to avoid plagiarism, unless your instructor has specifically indicated that some degree of discussion is permissible, you should consult with your instructor before engaging in any collaboration***. This restriction on outside discussion is especially necessary when preparing reports and presentations.

It may also seem helpful to search the Internet for teaching notes for cases or for case reports or slide presentations prepared by other students. Academic integrity requires that you refrain from using such resources, in full or in part. Any attempt to use the work of others and to pass it off as your own is plagiarism. If the instructor is suspicious that plagiarism might be involved, you may be asked to upload a copy of your case report through Turnitin.com.

While using the work of others may appear to provide a shortcut to a good grade, the quality of online sources and the work of other students is often suspect, at best. Most importantly, you deprive yourself of the learning opportunities the case method offers.

1. Michael E. Porter, “How Competitive Forces Shape Strategy,” *Harvard Business Review*, March 1979, 137–145; Michael E. Porter, “The Five Competitive Forces That Shape Strategy,” *Harvard Business Review*, January 2008, 57–71. Available from Ivey Publishing, product no. R0801E. [↑](#footnote-ref-1)
2. Based on Michael E. Porter, *Competitive Advantage: Creating and Sustaining Superior Performance* (New York, NY: Free Press, 1985). [↑](#footnote-ref-2)
3. Jay Barney, “Firm Resources and Sustained Competitive Advantage,” *Journal of Management* 17, no. 1 (1991): 99–120. [↑](#footnote-ref-3)