An	Introd	ucti	on	to
Str	ategic	Ana	alys	sis



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What is Business Strategy?

"Strategy is the pattern of decisions in a company that determines and reveals its objectives, purposes, or goals, produces the principal policies and plans for achieving those goals, and defines the range of business the company is to pursue, the kind of economic and human organization it is or intends to be, and the nature of the economic and noneconomic contribution it intends to make to its shareholders, employees, customers, and communities."

Kenneth Andrews, The Concept of Corporate Strategy (Homewood, IL: Richard D. Irwin, 1971).

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A Simple Strategy Schema	
Strategic Mission	
A firm's values and purpose and the scope of its operations in product and market terms.	
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Strategic Plan How a firm positions itself in the market and	
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Strategic Plan How a firm positions itself in the market and	
How a firm positions itself in the market and develops and leverages internal resources and capabilities to accomplish its strategic mission.	
Strategic Actions Individual actions taken to execute the strategic plan in pursuit of the strategic mission.	
Strategic Analysis	
What is Strategic Analysis?	
Definition: The assessment of an organization's current competitive position and the identification of future valuable competitive positions and how	
to achieve them	

What is Strategic Analysis?	
From a generalist's perspective	
(integrative, foundational) • Using strategic reasoning (rivalry,	
dynamics, complexity)	
Grounded in analytics and data Applying appropriate tools and	
frameworks	
	-
Who does Strategic Analysis?	
Someone who formulates and	
implements strategy • CEO or President	
■ Entrepreneur/Owner	
VP Strategic Planning General Manager of a	
Business Unit	
Who does Strategic Analysis?	
Someone who evaluates strategy	
InvestorsFinancial Analysts	
Someone who recommends future	
strategic actions Consultants	
Secondary Stakeholders	

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The Strategist's Challenge	
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The Strategist's Challenge	
Values	
Mission Statements	
• The mission of The Walt Disney	
The mission of The Walt Disney Company is to be one of the world's	
leading producers and providers of entertainment and information.	
Google's mission is to organize the world's information and make it	
universally accessible and useful.	

Mission Statements	
Dell's mission is to be the most successful computer company in the world at	
delivering the best customer experience in	
markets we serve.	
Our goal for Citigroup is to be the most	
respected global financial services	
company. Like any other public company, we're obligated to deliver profits and	
growth to our shareholders. Of equal	
importance is to deliver those profits and	
generate growth responsibly. Source: http://www.misionstatements.com	
Mission Chahamanha	
Mission Statements	
At the heart of the Chevron way is our vision to be the global energy company	
most admired for its people,	
partnership and performance.	
McKesson: Our mission is to provide	
comprehensive pharmacy solutions	
that improve productivity, profitability	
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The Strategist's Challenge	
Values Values	
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The Strategist's Challenge



The Strategist's Challenge



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The Strategist's Challenge



The Strategist's Challenge	
Values	
Opportunities Capabilities	
The Strategist's Challenge	
Values	
Opportunities Capabilities	
The Strategist's Challenge	
Values Valuable	
Competitive Position	

The Fundamental	
Principle of Busine	SS
Strategy	

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The Fundamental Principle of Business Strategy

"If everyone can do it, it's difficult to create and capture value from it."

The Fundamental Principle	
of Business Strategy	
"If everyone can do it, it's difficult to create and capture value from it."	
or, alternatively	
"In a perfectly competitive market, no firm realizes economic profits (rents)."	
Economic Profits (or Rents)	
Economic Profits (of Refits)	
Definition: economic profits (rents) are returns in excess of what an investor	
expects to earn from investments of similar risk (i.e., in excess of the	
opportunity cost of capital)	
Economic Profits (or Rents)	
1	
IBM 56,328.00 \$2,541.00	
Microsoft \$4,490.00	
\$3,776.00	
General Motors \$2,956.00 \$(5,525.00)	
Accounting Profits Economic Profits	
All data in US 5 millions from 1998. Abstracted from S. Oster, "Modern Competitive Analysis". Oxford University Press. 1999.	

Measuring Economic Profit	
Tobin's Q Ratio of a firm's market value to its	
asset replacement value Directly measures "rents" above those	
to physical inputs Difficult to calculate because it	
requires knowledge of assets' replacement value	
Measuring Economic Profit	
Discounted Cash Flow (DCF)	
Measures value of firm going forward	
 Discount rate reflects return to equity (i.e., opportunity cost) Positive NPV indicates rents over and 	
Positive NPV indicates rents over and above returns to all inputs	
Competitive Markets	
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The Fundamental Principle

"In a perfectly competitive market, no firm realizes economic profits (rents)."

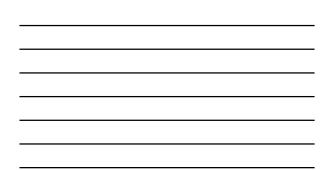
• The existence of economic profits suggests some type of market inefficiency.



Competitive Markets

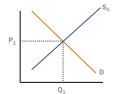
An Industry





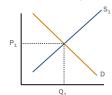
Competitive Markets

An Industry



Competitive Markets

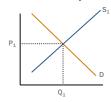
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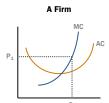




Competitive Markets

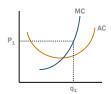
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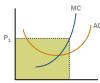
Competitive Markets

A Firm



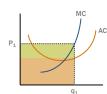
Competitive Markets

A Firm



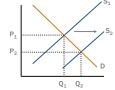
Competitive Markets

A Firm

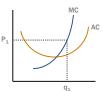


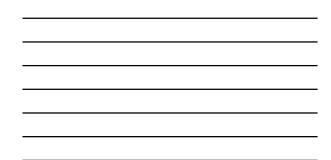
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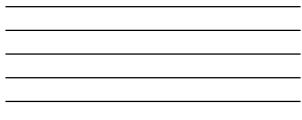
An Industry



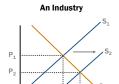


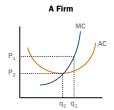




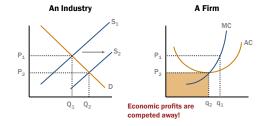


Competitive Markets





Competitive Markets



A Little Calculus

Competitive Markets	
A Firm	
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P ₁	
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A Little Colonius	
A Little Calculus	
Profits = Revenues - Variable	
Costs – Fixed Costs	
A Little Calculus	
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Costs - Fixed Costs	
$\pi = P_1 q_1 - c(q_1) - c_f$	

A Little Calculus	
Profits = Revenues - Variable	
Costs - Fixed Costs	
$\pi = P_1 q_1 - c(q_1) - c_f$	
$\delta \pi / \delta \mathbf{q_1} = \delta (\mathbf{P_1} \mathbf{q_1} - \mathbf{c}(\mathbf{q_1}) - \mathbf{c_f}) / \delta \mathbf{q_1} = 0$	
A Little Calculus	
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Costs - Fixed Costs	
$\pi = P_{1}q_{1} - c(q_{1}) - c_{f}$	
$\delta \pi / \delta q_1 = \delta (P_1 q_1 - c(q_1) - c_f) / \delta q_1 = 0$	
$P_{\mathtt{1}}-c'(q_{\mathtt{1}})=0$	
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A Little Calculus	
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A Little Calculus Profits = Revenues - Variable Costs - Fixed Costs $\pi = P_1 q_1 - c(q_1) - c_f$ $\delta \pi / \delta q_1 = \delta(P_1 q_1 - c(q_1) - c_f) / \delta q_1 = 0$	

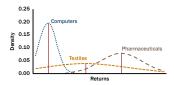
Competitive Markets	
A Firm	
MC / AC	
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Two Perspectives on	
Economic Rents	
The Fundamental Principle	
"In a perfectly competitive market, no	
firm realizes economic profits (rents)."	
The existence of economic profits suggests some type of market	
inefficiency. The strategist's task is to identify ways	
in which firms may capitalize on these market imperfections.	

Are	Markets	S Perfectly
Con	npetitive	?

• Facts:

- Average industry returns vary even after controlling for risk.
- Returns among companies within industries vary even more.
- Returns for individual companies vary over time.

Are Markets Perfectly Competitive?



Analyzing Economic Profits

"When you are presented with a project that appears to have a positive NPV, don't just accept the calculations at face value. They may reflect simple estimation errors in forecasting cash flows. Probe behind cash flow estimates and try to identify the source of economic rents. A positive NPV for a new project is believable only if you believe that the company has some special advantage."

From the chapter, "Where Positive Net Value Comes From" Brealey & Myers, *Principles of Corporate* Finance

Two Perspectives on Rents	
Monopoly Rents	
(Industrial Organization View)	
Р 8	
Q D	
Barriers to entry Industry structure matters	
Two Perspectives on Rents	
Ricardian Rents (Resource Based View)	
MC_1 MC_2 AC_2	
ACL	
$\ensuremath{q_1}\ensuremath{q_2}$ - Barriers to imitation - Firm structure matters	
Module Lessons	

Madula Laggara	
Module Lessons	
A business' strategy is embodied in its	
mission, plan, and actions	
Strategic analysis is useful for assessing the viability of a business strategy	
Strategic analysis is not just the purview of the CEO	
The strategist's challenge is to balance	
values, opportunities, and capabilities to identify desirable competitive positions	
that create and sustain value.	
Module Lessons	
The Fundamental Principle – In perfectly	
competitive markets, no firm realizes economic profits.	
Economic profits are returns in excess of the opportunity cost of capital.	
In the real world, product markets are rarely	
perfect and firms often have competitive advantage.	
Broadly speaking, firms may capture economic profits when there are either barriers to	
competition or barriers to imitation.	
The Strategist's Toolkit:	
SWOT Analysis	
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The Strategist's	Toolkit
SWOT Analysis	



The Strategist's Toolkit: Competitor Analysis

The Strategist's Toolkit: Competitor Analysis

	Performance Metrics	Capabilities	Objectives/ Values	Strategy
Focal Firm				
Competitor 1				
Competitor 2				
Competitor 3				
Competitor 4				
Competitor 5				

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The Strategist's Toolkit: Competitor Analysis	
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The Strategist's Toolkit:	
Competitor Analysis	
Performance Metrics Capabilities Objectives/ Values Strategy	
Competitor 1 Competitor 2	-
Competitor 3 Competitor 4	
Competitor 5	
	-
The Strategist's Toolkit:	
Environmental Analysis	

1	The Strategist' Environmental	s Toolkit:		
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	Demographic Socio-Co Trends Influe	ultural Technological nces Developments		
N	Macroeconomic Political Impacts Pressi	-Legal Global Trade ures Issues		
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Environmental Analysis							
	Demographic Trends		Socio-Cultural Influences		Technological Developments		



The Strategist's Toolkit: Environmental Analysis



The Strategist's Toolkit: Environmental Analysis

