

# An Introduction to Strategic Analysis



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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."**

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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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## A Simple Strategy Schema

### Strategic Mission

A firm's values and purpose and the scope of its operations in product and market terms.



### Strategic Plan

How a firm positions itself in the market and develops and leverages internal resources and capabilities to accomplish its strategic mission.

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## A Simple Strategy Schema




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## Strategic Analysis

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## 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

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### 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

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### Who does Strategic Analysis?

- Someone who formulates and implements strategy
  - CEO or President
  - Entrepreneur/Owner
  - VP Strategic Planning
  - General Manager of a Business Unit

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### Who does Strategic Analysis?

- Someone who evaluates strategy
  - Investors
  - Financial Analysts
- Someone who recommends future strategic actions
  - Consultants
  - Secondary Stakeholders

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## The Strategist's Challenge

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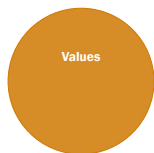
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## The Strategist's Challenge



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## Mission Statements

- 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.

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## 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.missionstatements.com>

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## 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 and result in superior patient care and satisfaction.

Source: <http://www.missionstatements.com>

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## Mission Statements

- **Ford**: We are a global family with a proud heritage passionately committed to providing personal mobility for people around the world.
- **Facebook's** mission is to give people the power to share and make the world more open and connected.

Source: <http://www.missionstatements.com>

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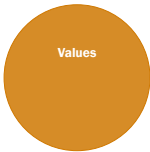
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The Strategist's Challenge



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The Strategist's Challenge



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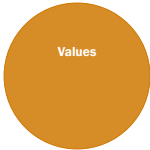
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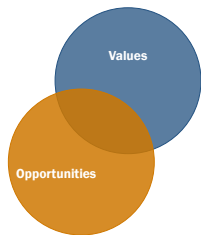
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The Strategist's Challenge



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The Strategist's Challenge



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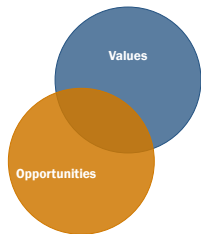
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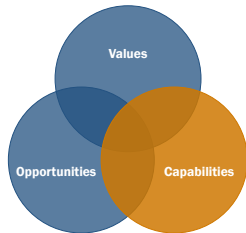
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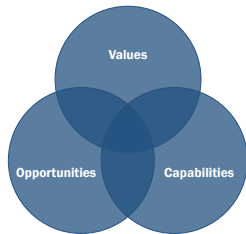
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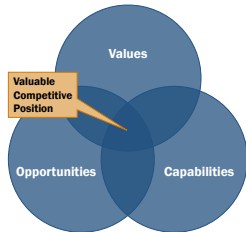
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The Strategist's Challenge



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## The Fundamental Principle of Business Strategy



Image Credit: By Jacob Bættar from Copenhagen, Denmark (Flickr) [CC BY 2.0] ([http://commons.wikimedia.org/wiki/File:Jacob\\_Baettar.jpg](http://commons.wikimedia.org/wiki/File:Jacob_Baettar.jpg)) via Wikimedia Commons

### 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)."

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## Economic Profits (or Rents)

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)

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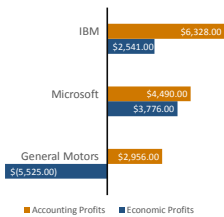
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## Economic Profits (or Rents)



All data in US \$ millions from 1998. Abstracted from S. Orlitz, "Modern Competitive Analysis", Oxford University Press, 1999.

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## 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

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## 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 above returns to all inputs

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## 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.

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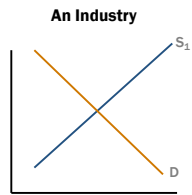
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### Competitive Markets



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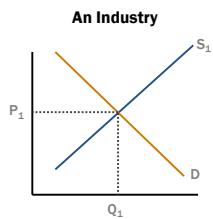
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### Competitive Markets



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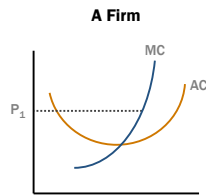
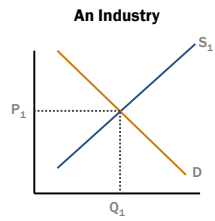
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**Competitive Markets**

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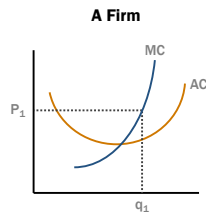
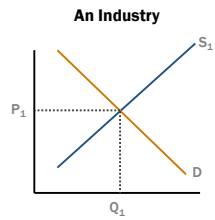
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**Competitive Markets**

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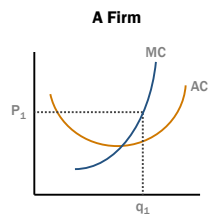
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**Competitive Markets**

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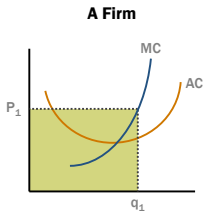
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Competitive Markets



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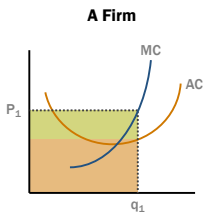
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Competitive Markets



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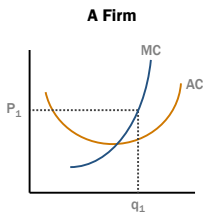
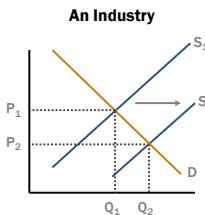
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Competitive Markets



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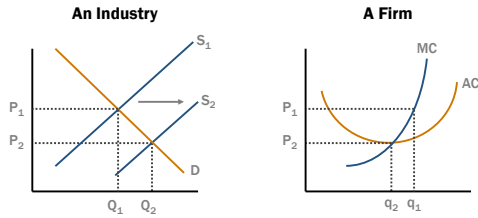
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## Competitive Markets




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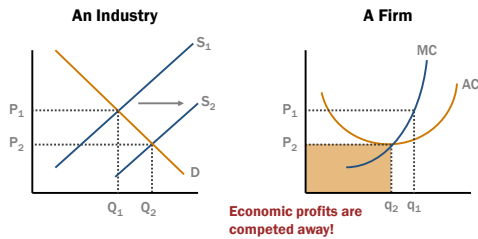
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## Competitive Markets




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## A Little Calculus

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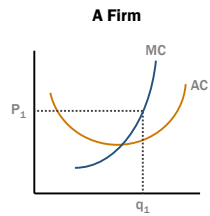
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## Competitive Markets




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## A Little Calculus

Profits = Revenues – Variable  
Costs – Fixed Costs

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## A Little Calculus

Profits = Revenues – Variable  
Costs – Fixed Costs

$$\pi = P_1 q_1 - c(q_1) - c_f$$

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### A Little Calculus

Profits = Revenues – Variable  
Costs – Fixed Costs

$$\pi = P_1 q_1 - c(q_1) - c_f$$

$$\delta\pi/\delta q_1 = \delta(P_1 q_1 - c(q_1) - c_f)/\delta q_1 = 0$$

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Profits = Revenues – Variable  
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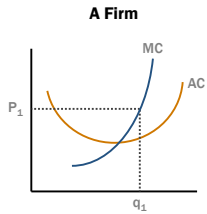
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$$P_1 - c'(q_1) = 0$$

$$P_1 = c'(q_1) = MC$$

## Competitive Markets



## 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 Perfectly Competitive?

### • 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.

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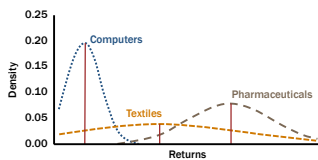
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## Are Markets Perfectly Competitive?




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## 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*

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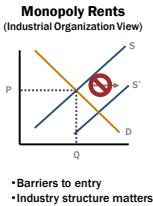
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Two Perspectives on Rents



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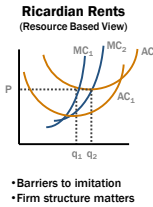
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Two Perspectives on Rents



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Module Lessons

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## 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.

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## 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.

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## The Strategist's Toolkit: SWOT Analysis

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The Strategist's Toolkit:  
SWOT Analysis



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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
Focal Firm				
Competitor 1				
Competitor 2				
Competitor 3				
Competitor 4				
Competitor 5				

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The Strategist's Toolkit:  
Environmental Analysis

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Environmental Analysis



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