

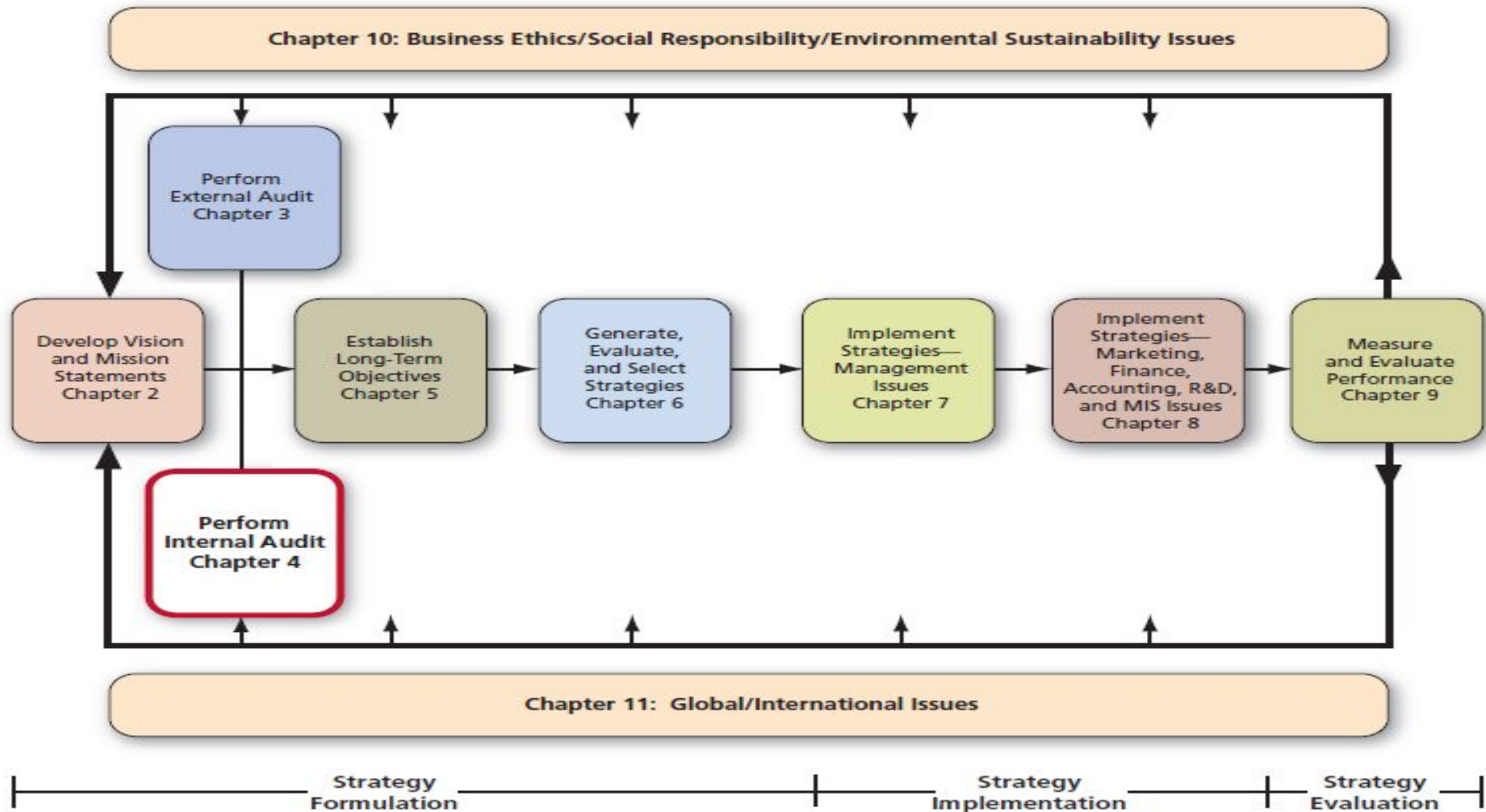
CHAPTER FOUR

THE INTERNAL ENVIRONMENT

A Comprehensive Strategic-Management Model

FIGURE 4-1

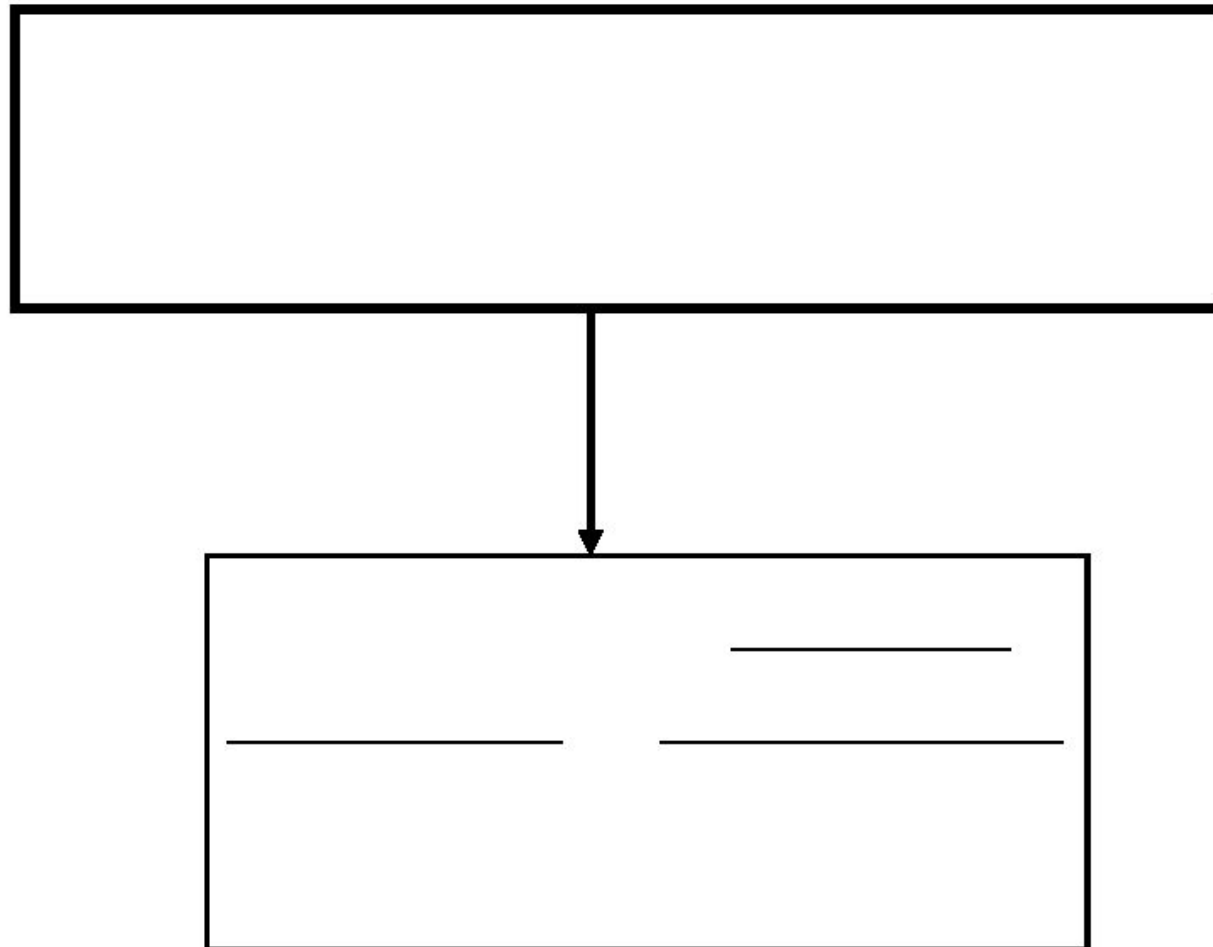
A Comprehensive Strategic-Management Model



“If you are not faster than your competitor, you are in a tenuous position, and you are only half as fast, you are terminal.”

George Salk

Environmental Analyses



Key Internal Forces

- ◆ **Distinctive competencies**
 - A firm's strengths that cannot be easily matched or imitated by competitors
- ◆ Building competitive advantages involves taking advantage of distinctive competencies.

FIGURE 4-2

The Process of Gaining Competitive Advantage in a Firm

Weaknesses \Rightarrow Strengths \Rightarrow Distinctive Competencies \Rightarrow Competitive Advantage

Competitive advantage

- ❖ Why do some companies outperform others?
What is (are) the basis of their competitive advantage?
 - In retail industry, Wal-Mart has consistently outperformed Kmart.
 - In the global auto industry Toyota has consistently outperformed General Motors for most of the last twenty years

Competitive advantage...

- ❖ A firm outperform its rivals due to the prevalence of superior efficiency, superior quality, superior innovation and superior responsiveness to the market.
- ❖ We refer to *efficiency, quality, innovation, and customer responsiveness* as the four generic building blocks of competitive advantage.
- ❖ This days *information technology and environmental issues* are also generating a competitive advantage for global firms.

Competitive advantage

- ❖ For a company to outperform its rivals, it must have unique strengths, or distinctive competences, in at least one of these building blocks.
 - For example, Wal-Mart outperforms its rivals in the discount retail industry because it is more efficient and more responsive to its customers.

Internal analysis

- ❖ Internal environment analysis enables an organization to determine *what it can do-* *that is*, the actions permitted by its unique resources, capabilities and core competencies.
- ❖ The proper matching of **what a firm can do with what it might do** allows the development of strategic intent, the pursuit of strategic mission and formulation of strategies.

Internal analysis

- Is a way of looking the firms internal capabilities to determine its internal strengths and weaknesses
- Internal analysis helps the firm:
 - Determine if its resources and capabilities are likely sources of competitive advantage
 - Establish strategies that will exploit any resources of competitive advantage

Internal Analysis ... cont'd

STRENGTHS:

- Strength is a resource, skill, or other advantage relative to competitors and the needs of the markets a firm serves or expects to serve.
- It is a distinctive competence that gives the firm a comparative advantage in the market place.
- Strengths may exist with regard to financial resources, image, market leadership, buyer/supplier relations etc.

Internal Analysis cont'd ...

WEAKNESSES:

- ❖ Weakness is a limitation or deficiency in resource, and capabilities that seriously impedes a firm's effective performance.
- ❖ Lack of facilities, financial resources, management capabilities, marketing skills, and brand image can be source of weaknesses.

Internal Analysis ... cont'd

The process of internal analysis of an organization involves four basic steps:

1. Developing a profile of financial; physical, organizational, & human; & technological
2. Determining the key success requirement of the product/market segments in which the organization competes or might compete
3. Comparing the resource profile to the key success requirements to determine the strengths & weaknesses
4. Comparing the strengths & weaknesses of the organization with those of its major competitor's

Group Discuss

❖ SW Analysis (Internal Environment)

Instructions:

- ❖ List the major strengths and weaknesses of your organization as you see them. Identify of these strengths and weaknesses that will be most critical to your organization's future success.

Strengths	Weaknesses

The Resource-Based View (RBV)

◆ The Resource-Based View (RBV) approach

- contends that internal resources are more important for a firm than external factors in achieving and sustaining competitive advantage

The Resource-Based View (RBV)

- ✓ Proponents of the RBV contend that organizational performance will primarily be determined by internal resources that can be grouped into three all-encompassing categories:
 - ❖ physical resources,
 - ❖ human resources, and
 - ❖ organizational resources

RBV - Resources Vs. Capability

❖ Resources

- Tangible and intangible assets of a firm
- Used to conceive and implement strategies

❖ Capabilities

- A subset of resources that enable a firm to take full advantage of other resources
 - E.g. marketing skill, cooperative strategies

Assumptions of RBV

- Two critical assumptions of RBV:
 - Resource heterogeneity
 - d/t firms may have d/t resources
 - Resource Immobility
 - It may be costly for firms without resources to acquire or develop
 - Some resources may not spread from and to a firm without substantial cost

What do these assumptions really mean?

- ❖ If one firm has resources that are valuable and other firms don't
- ❖ If other firms cannot imitate these resources without incurring costs
- ❖ The firm possessing the valuable resources will likely gain a sustained competitive advantage

Internal Analysis-RBV

❖ There are four indicators of the potential of a firm's competitive advantage with respect to its resources and capabilities. These are:

- **Valuable**
- **Rare**
- **Costly to imitate**
- **Non-substitutable**

Internal Analysis (RBV)

❖ A resource or bundle of resources is subjected to each question to determine their competitive implications.

❖ The questions of Value

- Does the resource enable the firm to exploit an external opportunity or neutralize a threat

Internal Analysis (RBV)

◆ The question of rarity

- If a resource is not rare, then perfect competition dynamics are likely to be observed (i.e. no competitive advantage, no above normal profits)
- A resource must be rare enough so that perfect competition has not set in
- If a resource is not rare there is no difference between the focal firm and other firms

Internal Analysis (RBV)

● The question of imitability

cost of imitation might be high due to:

- Unique historical condition
- Causal ambiguity
 - Causal links b/n resources and competitive advantage may not be understood
 - Bundles of resources may cause the causal links

□ Patents

- Patents may be a two edged sword
 - Protection –benefit
 - Disclosure –cost

Internal Analysis (RBV)

❖ The question of substitutability

- There should not be a substitutable resource to be used by business rivalries

❖ The question of organization

- A firms structure and control mechanism must be aligned so as to give people ability and incentive to exploit firms resources – formal and informal structure, management control and relationships

Integrating Strategy and Culture

- ❖ Organizational culture significantly affects business decisions and thus must be evaluated during an internal strategic-management audit.
- ❖ If strategies can capitalize on cultural strengths, such as a strong work ethic or highly ethical beliefs, then management often can swiftly and easily implement changes.

Integrating Strategy & Culture

Organizational Culture

Pattern of behavior developed by an organization as it learns to cope with its problem of external adaptation and internal integration...is considered valid and taught to new members

Integrating Strategy & Culture

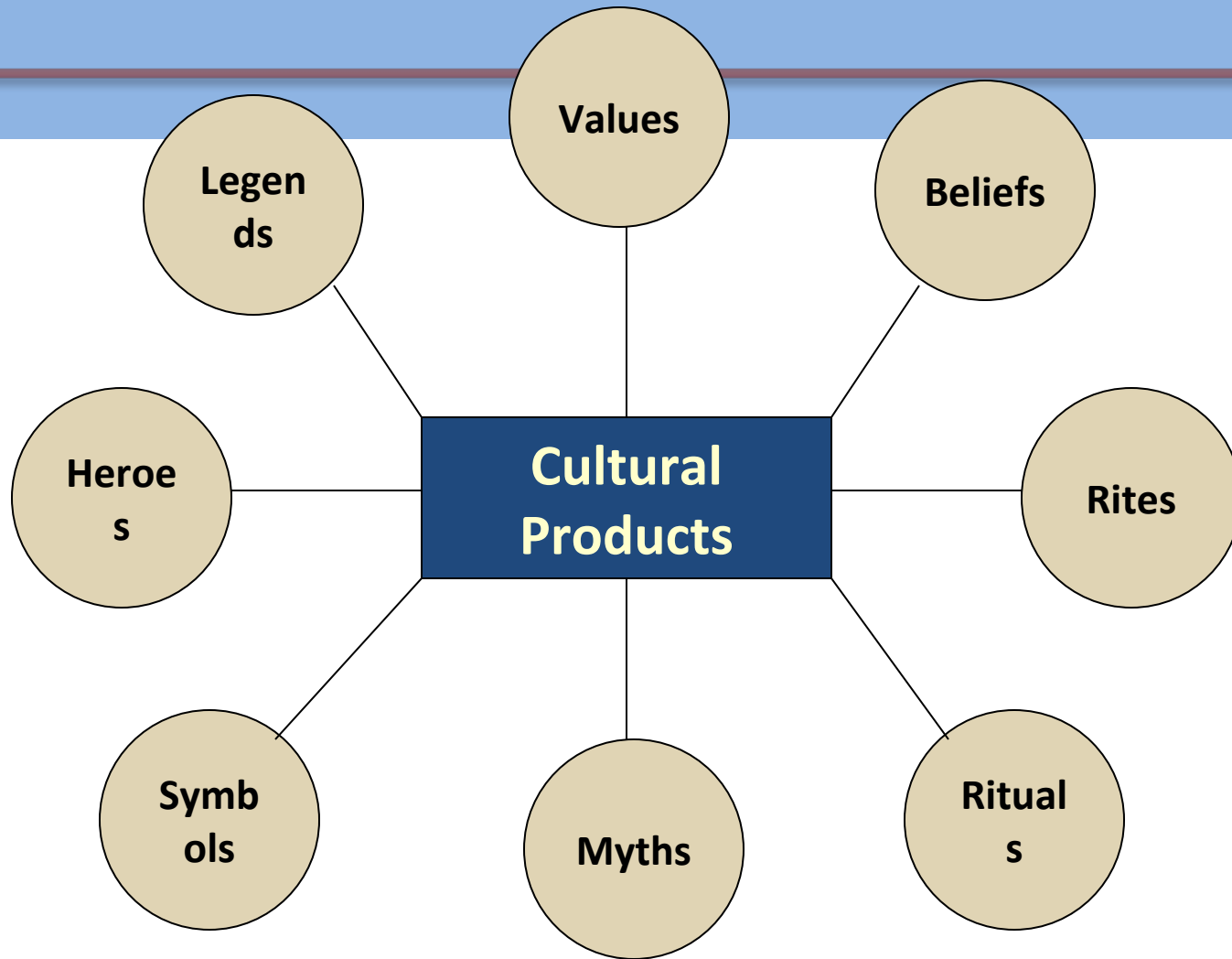


TABLE 4-1

Cultural Products and Associated Definitions

Rites	Relatively elaborate, dramatic, planned sets of activities that consolidate various forms of cultural expressions into one event, carried out through social interactions, usually for the benefit of an audience
Ceremonial	A system of several rites connected with a single occasion or event
Ritual	A standardized, detailed set of techniques and behaviors that manage anxieties, but seldom produce intended, technical consequences of practical importance
Myth	A dramatic narrative of imagined events, usually used to explain origins or transformations of something. Also, an unquestioned belief about the practical benefits of certain techniques and behaviors that is not supported by facts
Saga	A historical narrative describing the unique accomplishments of a group and its leaders, usually in heroic terms
Legend	A handed-down narrative of some wonderful event that is based on history but has been embellished with fictional details
Story	A narrative based on true events, sometimes a combination of truth and fiction
Folktale	A completely fictional narrative
Symbol	Any object, act, event, quality, or relation that serves as a vehicle for conveying meaning, usually by representing another thing
Language	A particular form or manner in which members of a group use sounds and written signs to convey meanings to each other
Metaphors	Shorthand words used to capture a vision or to reinforce old or new values
Values	Life-directing attitudes that serve as behavioral guidelines
Belief	An understanding of a particular phenomenon
Heroes/Heroines	Individuals whom the organization has legitimized to model behavior for others

Source: Adapted from H. M. Trice and J. M. Beyer, "Studying Organizational Cultures through Rites and Ceremonials," *Academy of Management Review* 9, no. 4 (October 1984): 655.

Management

- ❖ The *functions of management* consist of five basic activities: planning, organizing, motivating, staffing, and controlling.
- ❖ These activities are important to assess in strategic planning because an organization should continually **capitalize** on its management strengths and **improve** on its management weaknesses.

The Basic Functions of Management

TABLE 4-3 The Basic Functions of Management

Function	Description	Stage of Strategic-Management Process When Most Important
Planning	Planning consists of all those managerial activities related to preparing for the future. Specific tasks include forecasting, establishing objectives, devising strategies, developing policies, and setting goals.	Strategy Formulation
Organizing	Organizing includes all those managerial activities that result in a structure of task and authority relationships. Specific areas include organizational design, job specialization, job descriptions, job specifications, span of control, unity of command, coordination, job design, and job analysis.	Strategy Implementation
Motivating	Motivating involves efforts directed toward shaping human behavior. Specific topics include leadership, communication, work groups, behavior modification, delegation of authority, job enrichment, job satisfaction, needs fulfillment, organizational change, employee morale, and managerial morale.	Strategy Implementation
Staffing	Staffing activities are centered on personnel or human resource management. Included are wage and salary administration, employee benefits, interviewing, hiring, firing, training, management development, employee safety, affirmative action, equal employment opportunity, union relations, career development, personnel research, discipline policies, grievance procedures, and public relations.	Strategy Implementation
Controlling	Controlling refers to all those managerial activities directed toward ensuring that actual results are consistent with planned results. Key areas of concern include quality control, financial control, sales control, inventory control, expense control, analysis of variances, rewards, and sanctions.	Strategy Evaluation

Management Audit Checklist of Questions

1. Does the firm use strategic-management concepts?
2. Are company objectives and goals measurable and well communicated?
3. Do managers at all hierarchical levels plan effectively?
4. Do managers delegate authority well?
5. Is the organization's structure appropriate?
6. Are job descriptions and job specifications clear?
7. Is employee morale high?
8. Are employee turnover and absenteeism low?
9. Are organizational reward and control mechanisms effective?

Marketing



Marketing

- the process of defining, anticipating, creating, and fulfilling customers' needs and wants for products and services

Functions of Marketing

Customer analysis

Selling products/services

Product and service planning

Pricing Distribution

Marketing research

Opportunity analysis

Cost/Benefit Analysis

Three steps are required to perform a cost/benefit analysis:

1. compute the total costs associated with a decision,
2. estimate the total benefits from the decision,
3. compare the total costs with the total benefits.

Marketing Audit Checklist of Questions

1. Are markets segmented effectively?
2. Is the organization positioned well among competitors?
3. Has the firm's market share been increasing?
4. Are present channels of distribution reliable and cost effective?
5. Does the firm have an effective sales organization?
6. Does the firm conduct market research?

Marketing Audit Checklist of Questions

7. Are product quality and customer service good?
8. Are the firm's products and services priced appropriately?
9. Does the firm have an effective promotion, advertising, and publicity strategy?
10. Are marketing, planning, and budgeting effective?
11. Do the firm's marketing managers have adequate experience and training?
12. Is the firm's Internet presence excellent as compared to rivals?

Finance/Accounting Functions

The *functions of finance/accounting* comprise three decisions:

- 1.the investment decision
- 2.the financing decision
- 3.the dividend decision

Finance/Accounting Functions

◆ **Investment decision**

- the allocation and reallocation of capital and resources to projects, products, assets, and divisions of an organization

◆ **Financing decision**

- determines the best capital structure for the firm and includes examining various methods by which the firm can raise capital

Finance/Accounting Functions

◆ Dividend decisions

- concern issues such as the percentage of earnings paid to stockholders, the stability of dividends paid over time, and the repurchase or issuance of stock
- determine the amount of funds that are retained in a firm compared to the amount paid out to stockholders

Finance/Accounting Functions

1. How has each ratio changed over time?
2. How does each ratio compare to industry norms?
3. How does each ratio compare with key competitors?

Finance/Accounting Audit Checklist

1. Where is the firm financially strong and weak as indicated by financial ratio analyses?
2. Can the firm raise needed short-term capital?
3. Can the firm raise needed long-term capital through debt and/or equity?
4. Does the firm have sufficient working capital?
5. Are capital budgeting procedures effective?

Finance/Accounting Audit Checklist

7. Are dividend payout policies reasonable?
8. Does the firm have good relations with its investors and stockholders?
9. Are the firm's financial managers experienced and well trained?
10. Is the firm's debt situation excellent?

Production/Operations

❖ **Production/operations function**

- consists of all those activities that transforms inputs into goods and services

❖ Production/operations management deals with inputs, transformations, and outputs that vary across industries and markets.

The Basic Functions (Decisions) Within Production/Operations

TABLE 4-7 The Basic Functions (Decisions) Within Production/Operations

Decision Areas	Example Decisions
1. Process	These decisions include choice of technology, facility layout, process flow analysis, facility location, line balancing, process control, and transportation analysis. Distances from raw materials to production sites to customers are a major consideration.
2. Capacity	These decisions include forecasting, facilities planning, aggregate planning, scheduling, capacity planning, and queuing analysis. Capacity utilization is a major consideration.
3. Inventory	These decisions involve managing the level of raw materials, work-in-process, and finished goods, especially considering what to order, when to order, how much to order, and materials handling.
4. Workforce	These decisions involve managing the skilled, unskilled, clerical, and managerial employees by caring for job design, work measurement, job enrichment, work standards, and motivation techniques.
5. Quality	These decisions are aimed at ensuring that high-quality goods and services are produced by caring for quality control, sampling, testing, quality assurance, and cost control.

Implications of Various Strategies on Production/Operations

TABLE 4-8 Implications of Various Strategies on Production/Operations

Various Strategies	Implications
1. Low-cost provider	Creates high barriers to entry Creates larger market Requires longer production runs and fewer product changes
2. A high-quality provider	Requires more quality-assurance efforts Requires more expensive equipment Requires highly skilled workers and higher wages
3. Provide great customer service	Requires more service people, service parts, and equipment Requires rapid response to customer needs or changes in customer tastes Requires a higher inventory investment
4. Be the first to introduce new products	Has higher research and development costs Has high retraining and tooling costs
5. Become highly automated	Requires high capital investment Reduces flexibility May affect labor relations Makes maintenance more crucial
6. Minimize layoffs	Serves the security needs of employees and may develop employee loyalty Helps to attract and retain highly skilled employees

Production/Operations Audit Checklist

1. Are supplies of raw materials, parts, and subassemblies reliable and reasonable?
2. Are facilities, equipment, machinery, and offices in good condition?
3. Are inventory-control policies and procedures effective?
4. Are quality-control policies and procedures effective?
5. Are facilities, resources, and markets strategically located?
6. Does the firm have technological competencies?

Research and Development Audit

1. Does the firm have R&D facilities? Are they adequate?
2. If outside R&D firms are used, are they cost-effective?
3. Are the organization's R&D personnel well qualified?
4. Are R&D resources allocated effectively?
5. Are management information and computer systems adequate?
6. Is communication between R&D and other organizational units effective?
7. Are present products technologically competitive?

Management Information Systems

- ❖ A **management information system**'s purpose is to improve the performance of an enterprise by improving the quality of managerial decisions
- ❖ An effective **information system** thus collects, codes, stores, synthesizes, and presents information in such a manner that it answers important operating and strategic questions

Management Information Systems Audit

1. Do all managers in the firm use the information system to make decisions?
2. Is there a chief information officer or director of information systems position in the firm?
3. Are data in the information system updated regularly?
4. Do managers from all functional areas of the firm contribute input to the information system?
5. Are there effective passwords for entry into the firm's information system?

Management Information Systems Audit

6. Are strategists of the firm familiar with the information systems of rival firms?
7. Is the information system user-friendly?
8. Do all users of the information system understand the competitive advantages that information can provide firms?
9. Are computer training workshops provided for users of the information system?
10. Is the firm's information system continually being improved in content- and user-friendliness?

Value Chain Analysis (VCA)



Value chain analysis (VCA)

- refers to the process whereby a firm determines the costs associated with organizational activities from purchasing raw materials to manufacturing product(s) to marketing those products
- aims to identify where low-cost advantages or disadvantages exist anywhere along the value chain from raw material to customer service activities

Benchmarking



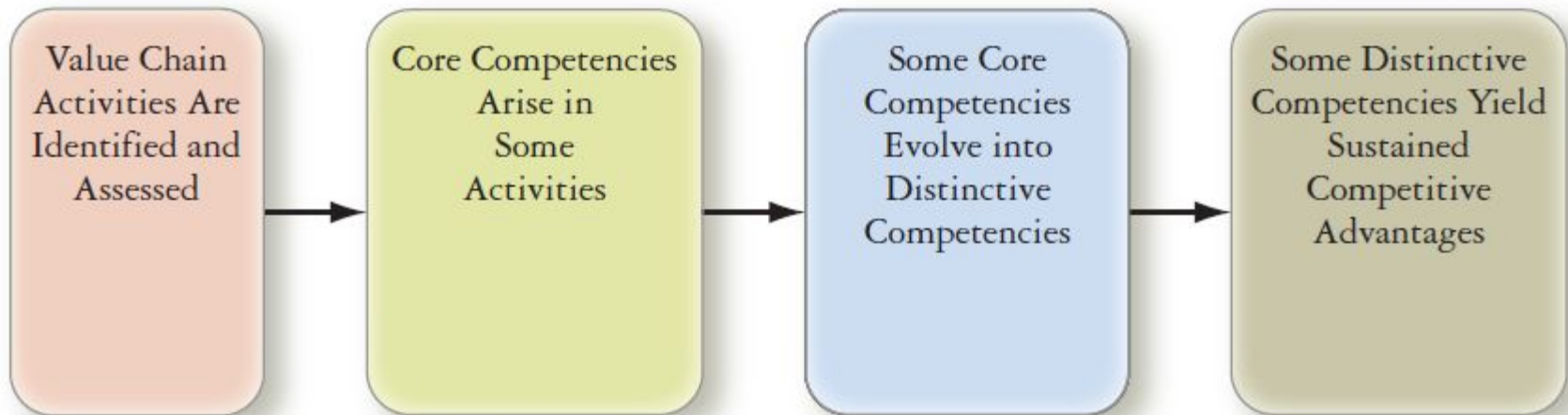
Benchmarking

- an analytical tool used to determine whether a firm's value chain activities are competitive compared to rivals and thus conducive to winning in the marketplace
- entails measuring costs of value chain activities across an industry to determine "best practices"

Transforming Value Chain Activities into Sustained Competitive Advantage

FIGURE 4-8

Transforming Value Chain Activities into Sustained Competitive Advantage



The Internal Factor Evaluation (IFE) Matrix

1. List key internal factors as identified in the internal-audit process
2. Assign a weight that ranges from 0.0 (not important) to 1.0 (all-important) to each factor
3. Assign a 1-to-4 rating to each factor to indicate whether that factor represents a strength or weakness
4. Multiply each factor's weight by its rating to determine a weighted score for each variable
5. Sum the weighted scores for each variable to determine the total weighted score for the organization

A Sample Internal Factor Evaluation Matrix for a Retail Computer Store

TABLE 4-9 A Sample Internal Factor Evaluation Matrix for a Retail Computer Store

Key Internal Factors	Weight	Rating	Weighted Score
Strengths			
1. Inventory turnover increased from 5.8 to 6.7	0.05	3	0.15
2. Average customer purchase increased from \$97 to \$128	0.07	4	0.28
3. Employee morale is excellent	0.10	3	0.30
4. In-store promotions resulted in 20 percent increase in sales	0.05	3	0.15
5. Newspaper advertising expenditures increased 10 percent	0.02	3	0.06
6. Revenues from repair/service segment of store up 16 percent	0.15	3	0.45
7. In-store technical support personnel have MIS college degrees	0.05	4	0.20
8. Store's debt-to-total assets ratio declined to 34 percent	0.03	3	0.09
9. Revenues per employee up 19 percent	0.02	3	0.06
Weaknesses			
1. Revenues from software segment of store down 12 percent	0.10	2	0.20
2. Location of store negatively impacted by new Highway 34	0.15	2	0.30
3. Carpet and paint in store somewhat in disrepair	0.02	1	0.02
4. Bathroom in store needs refurbishing	0.02	1	0.02
5. Revenues from businesses down 8 percent	0.04	1	0.04
6. Store has no website	0.05	2	0.10
7. Supplier on-time delivery increased to 2.4 days	0.03	1	0.03
8. Often customers have to wait to check out	0.05	1	0.05
Total	1.00		2.50

/ END /