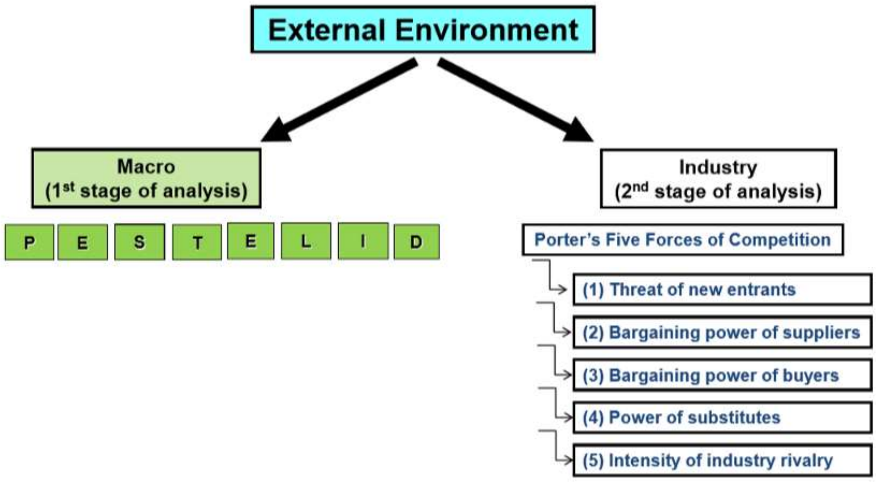
Seminar 1 Analysing the external environment

Objectives

- Understand the purpose of a SWOT analysis and was to conduct this analysis
- Identify opportunities and threats based on an analysis of an organisation's external environment by:
    - Analysing the macro environment using the PESTELID framework
    - Analysing the industry environment using the Porter's Five Forces of Competition framework

Macro and industry environment



Macro-environment: general influences that affect an industry. It tends to affect many industries, but we are concerned with their effect on the growth of the particular industry we are analysing.

Industry environment: consider those factors within the industry that affect both its profitability and the competitive position of organisations within it. Industry – a group of organisations or business units producing close substitutes.

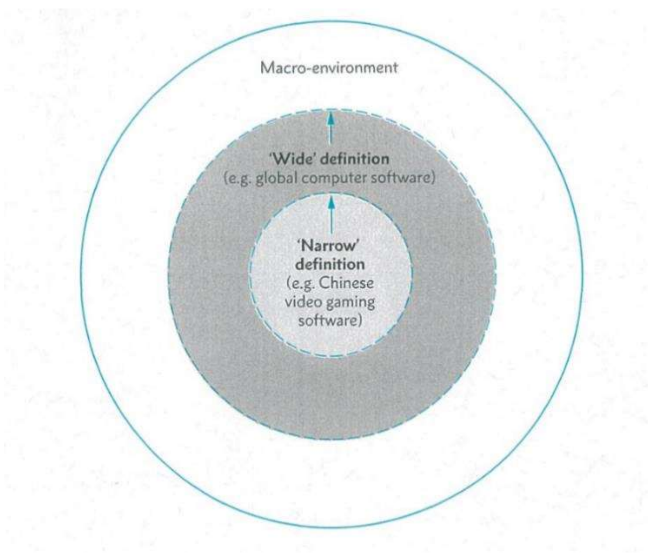


FIGURE 3.1 The external environment

Analysing the macro environment using the PESTELID Framework

Find the major trends affecting the future growth of industry, is it an opportunity or threat?
(*Steps: Identify a trend – explain the trend – conclude*)

- **Political**: changes in specific legislation, government agencies, government administrative regulation. Some issues include: Debt/income level, free trade, pension funding, immigration, health care funding, climate change adoption. RELATES TO THE POLICY.
- **Economic**: relates to Gross National Product, personal disposable income growth rates. Factors also link to the economy in which the firm operates such as: interest, inflation, unemployment and taxation rates. Economies have cycle of growth and recession.
- **Social/cultural**: Changes in the products and services valued and purchased, and also employment expectations. For example, aged care, environmentalism, global issue mobilisation, social networking.
- **Technological**: Any issues relating to technology. May included: online technology changes, growth in internet capabilities, and replacement of manual labour for machine. Technology also impacts upon the internal operations of most organisations and changing the value chain and consequent business model.
- **Environmental**: Any issues that may affect the environment or the sustainability of the environment due to commercial activities.
- **Legal:** Developments in the legal system. WHO RISE THE POLICY.
- **International:** Industries are becoming more international in their orientation. The reductions of trade barriers, different labour rates between countries and increased speed, availability and low cost of international communications are some of the key international trends impacting many organisations
- **Demographic:** Population growth and inflation, also include migration levels, income distribution, ethnicity, average age of the population and genders.

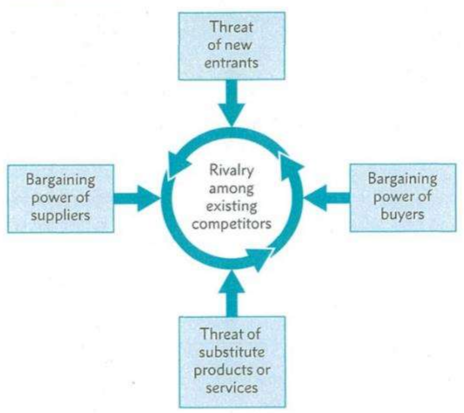
Summarising the analysis

- Assess each issue identified as having a significant positive or negative effect on the growth of the industry, compared with the average growth of industries in general.
- Summarise the +s and -s of all the trends identified, having regard to the relative importance of each factor. (e.g. if all the major factors are +, industry would be expected to grow faster than average.)
- Identify the key opportunities and treats arising.
- Write down the summary, listing the major reasons for your conclusion.

Analysing the industry environment using Porter's Five Force of Competition Framework

What is current and future profitability of the industry.

FIGURE 3.3 The five forces model



Steps:

1. Identify the industry that company belongs to

2. Select one force to discuss

3. Identify all the factors that influence this force and discuss optionally

4. Two conclusion required: High or low threat for this force in the industry? It is an opportunity or threat for this company?

1) **Threats of new entrants**
   a) Economies of scale: large-scale production in order to be cost-efficient
   b) Proprietary product differences
   c) Brand identity
   d) Buyer/customer switching costs
   e) Capital requirements
   f) Access to distribution: have to gain good access to public
   g) Absolute cost advantages: such cost advantages may be built up through production experience, resulting in efficiencies that are difficult to replicate, control over cheap raw materials, and/or low-cost design, operation or distribution.
   h) Government policy
   i) Expected retaliation: retaliation from existing competitors.

2) **Power of substitutes**
   a) Relative price/performance of substitutes
   b) Switching costs
   c) Buyer propensity to substitute

   (SUSBSTITUTES FROM OTHER INDUSTRIES rather than from the industry itself)

3) **Bargaining power of suppliers**
   a) Differentiation of inputs: suppliers have power if their input is crucial to the final product.
   b) Switching costs of supplier and firm in the industry
   c) Supplier concentration relative to industry concentration: a small number of suppliers means that suppliers will have power.
   d) Importance of volume to suppliers: if the volume being sold to the industry is important to suppliers, they will be concerned about it and therefore willing to bargain. Supermarket chains have a great deal of power over suppliers.
   e) Cost relative to total purchases in the industry: if the supplier's cost is a small part of the total cost of supplies, the industry will not be too concerned about it, giving suppliers the power to raise prices and increase margins without experiencing retaliatory action.
   f) Information about supplier's product: if the supplier's product is complex, intangible or unique, the industry may have difficulty understanding exactly what is buying and may be wary of substitutes. (e.g. prescription pharmaceutical products)
   g) Supplier profitability: unprofitable - unable to bargain
   h) Decision maker's incentives : there are incentives for the purchasing decision maker, so it is give power to the supplier over the decision maker, regardless of the relative merits of the individual supplier's product.
   i) Threat of forward integration**:** if the suppliers have the power to enter the industry. The high threat of forward integration increases bargaining power of suppliers.

4) **Bargaining power of buyers (same as suppliers)**

5) **Degree of industry rivalry**
   a) Industry growth rate: if the industry is growing fast, the amount of industry rivalry will be relatively low because there is no room for most or all organisations to prosper.
   b) High fixed cost: high fixed cost will tend to lead to high rivalry, as there are opportunities for marginal cost pricing (pricing below full cost) and these will be marginally profitable. (e.g. hotel)
   c) Intermittent overcapacity: the period of supply exceeding demand and the industry - severe rivalry.
   d) Product differences: rivalry between competitors can be reduced to the extent that their products are differentiated.
   e) Brand identity

f) Switching costs
g) Informational complexity/asymmetry: if products are complex/difficult to ascertain value, buyers will find it difficult to differentiate, thus reducing rivalry.
h) Concentration and balance: each competitor is satisfied with its position in the industry, competition will be low
i) Diversity of competitors
j) Corporate stakes
k) Exit barriers: costly to exist, competitors may decide to stay, even if they are making losses.

Summarising the analysis

- Whether the power of each force is high, average or low. Integrate the factors.
- Current & future profitability
- Organisational profitability will depend on its position within the industry and internal efficiencies. (all organisations in the same industry will not be similar)

Criticisms of the Five Forces Model

- It only explains a relative small amount of profit variance
- It encourages anti-competitive behaviour
- It lacks the necessary dynamism: fail to accurately reflect the true dynamics of an industry and how this industry structure may impact industry profitability.

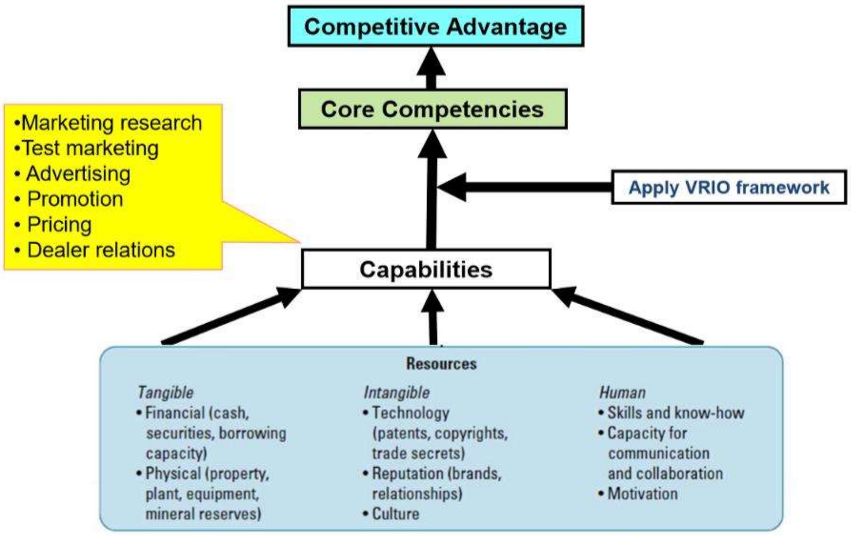
Feedback for seminar 1

1. Have to use both PESTELID and Porter's five forces to identify opportunities and threats by analysing the macro- and industry environment.
2. Using Macro environment (PESTELID) in identifying a trend, ensure that the trend is potentially applicable to more than one industry.
3. **Industry Environment (Porter's Five Forces)** - To discuss the industry environment, firstly, identify explicitly the industry that you wish to analyse. Secondly, choose one of the forces from the Porter's Five Forces framework to discuss. Finally, conclusions must be made at the industry level first (i.e., whether this force is high or low), followed by a conclusion on whether the outcome of this force is an opportunity or threat for Qantas and justify.
4. **Industry Environment (Porter's Five Forces)** - To discuss the industry environment, firstly, identify explicitly the industry that you wish to analyse. Secondly, choose one of the forces from the Porter's Five Forces framework to discuss. Finally, conclusions must be made **at the industry level first** (i.e., whether this force is high or low), followed by a conclusion on whether the outcome of this force is an opportunity or threat for Qantas and justify. Refer to the example in the video again.
5. **Industry Environment (Porter's Five Forces) -** A second use of the Porter's Five Forces framework is to determine whether the airline industry is attractive or unattractive. To do this, the team needs to conclude for each of the five forces, and combine those conclusions to arrive at a judgement. It has implications on whether a company should stay or leave (if it is a current player in this industry) OR enter this industry (if it is a potential entrant).

Seminar 2 Analysing the internal environment

Objectives

- Understand the purpose of a SWOT analysis and ways to conduct this analysis
- Recognise strengths and weaknesses based on an analysis of an organisation's internal environment by:
    - Identifying organisational capabilities using the value chain framework
    - Discussing each capability using the concept of resources; and
    - Determining whether the capability that is a strength is a core competence using the VRIO framework



Capabilities

Capabilities: refers to what company can do with its resources in order to achieve a specific task. Resources themselves do not provide a capability for an entity. Capabilities are usually formed over the life of the entity and are a mix of both tangible and intangible resources.

Capability confers competitive advantage. Only capability will qualify as core competencies.

Classifying capabilities

- A functional analysis: relates to each of the principal functional areas of the company (e.g. corporate, management, R&D, operations, product design etc.)
- A value chain analysis
- Dynamic capabilities: acting as a buffer between firm resources and the fast-changing business environment. The firm's ability to integrate, build, and reconfigure internal and external competencies to address rapidly changing environments.

Competitive advantages

Competitive advantage: a characteristic, feature or opportunity that an organisation possesses that will make it more attractive than its competitors. Must be scarce and relevant.

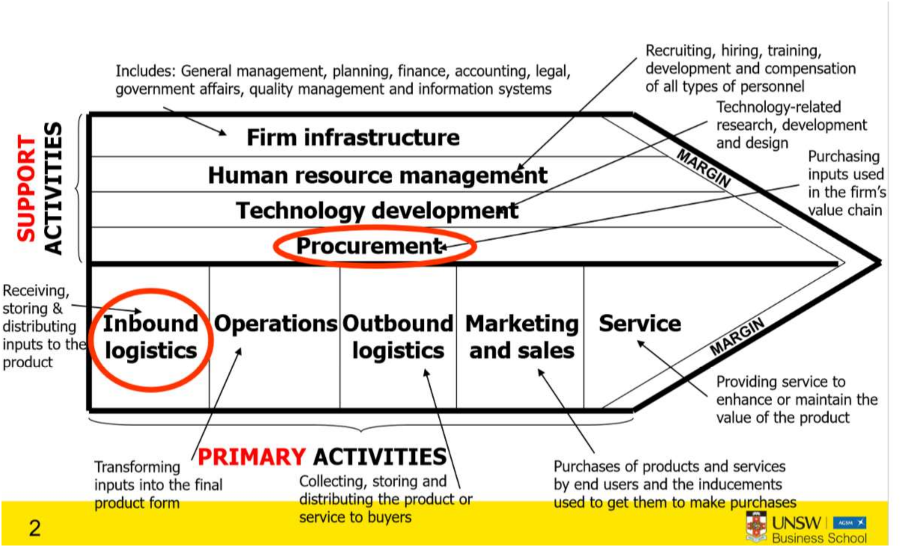
Importance:

- The creation and sustainability of competitive advantage is important for formulating strategies.
- The ability to develop competitive advantage depends on the ability to position their business system in the business environment.
    - Business system: the resources (inputs), activities (throughputs) and product/ service offerings (outputs) intended to create value for customers. These 3 elements should be aligned to create a competitive advantage.

To gain competitive advantage:

- The organisation's product/service should be better fit with the needs of buyers than competitors.
- A competitive organisation should be efficient and effective in performing value-added activities (e.g. logistics, production, R&D, marketing and sales - value chain)
- Has resource base necessary for performing the value-added activities

<u>**Value chain analysis**</u>



Value chain: a template used by an organisation to identify its cost position (capabilities), and the means that might be used to facilitate implementation of a chosen business-level strategy. Competitive advantage can be created if the company's value chain creates additional value without incurring significant extra costs.

Primary activities: directly associated with production, delivery, sales and services.

- <u>Inbound logistics</u>: material handling, warehousing, inventory control
- <u>Operation</u>: packaging, machining, assembly, equipment maintenance.
- <u>Outbound logistics</u>: finished goods warehousing, order processing. These distribute products to customers.
- <u>Marketing and sales:</u> advertising and promotional campaigns.
- <u>Service</u>: enhance and maintain a product's value

Support activities: enable primary activities to take place

- <u>Organisational infrastructure</u>: planning, finance, accounting, legal support, general management, governmental relations.
- <u>Human resource management</u>: recruiting, hiring, training, developing and rewarding company staff. it is responsible for the right mix of skilled staff to perform value chain activities effectively.
- <u>Technology development</u> : process equipment , research and product design and development, and servicing procedures which underpin the company's products and the processes used to manufacture them. Can lead to lower production costs
- <u>Procurement:</u> purchasing items consumed during the production, and fixed assets such as machinery, laboratory equipment, buildings and office equipment.

Value chain and Competitive advantage: Value chain enables company to create customer value. So company need to develop a unique set of activities that reinforce each other in use, and cannot copied by competitors.