Analytical Methods of Business Environment

Analytical Methods of Internal Environment

8. lecture

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Outline of the lecture

1. Value chain analysis
2. VRIO analysis
3. McKinsey 7S model
4. Stakeholders analysis
5. Portfolio analysis
6. SWOT analysis

Introduction

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- Internal business environment is constituted by the organization itself.

- The analysis of internal business environment refers to the analysis of the business internal environment to assist business strategy and performance, the internal strengths and weaknesses of the organization.

- Among the analyses of internal business environment the following methods can be ranked:
    - Porter Model of Value Chain Analysis;
    - McKinsey 7S;
    - VRIO method;
    - Stakeholders analysis;
    - Portfolio analyses – ABC method, BCG matrix, GE matrix.

Value Chain Analysis

- A **value chain is a linked set of value-creating activities** that begin with basic raw materials coming from suppliers, moving on to a series of value-added activities involved in producing and marketing a product or service, and ending with distributors getting the final goods into the hands of the ultimate consumer.

- The focus of value-chain analysis is to examine the corporation in the context of the overall chain of value-creating activities, of which the firm may be only a small part.

Typical Value Chain for a Manufactured Product

Porter´s Model of Value Chain Analysis

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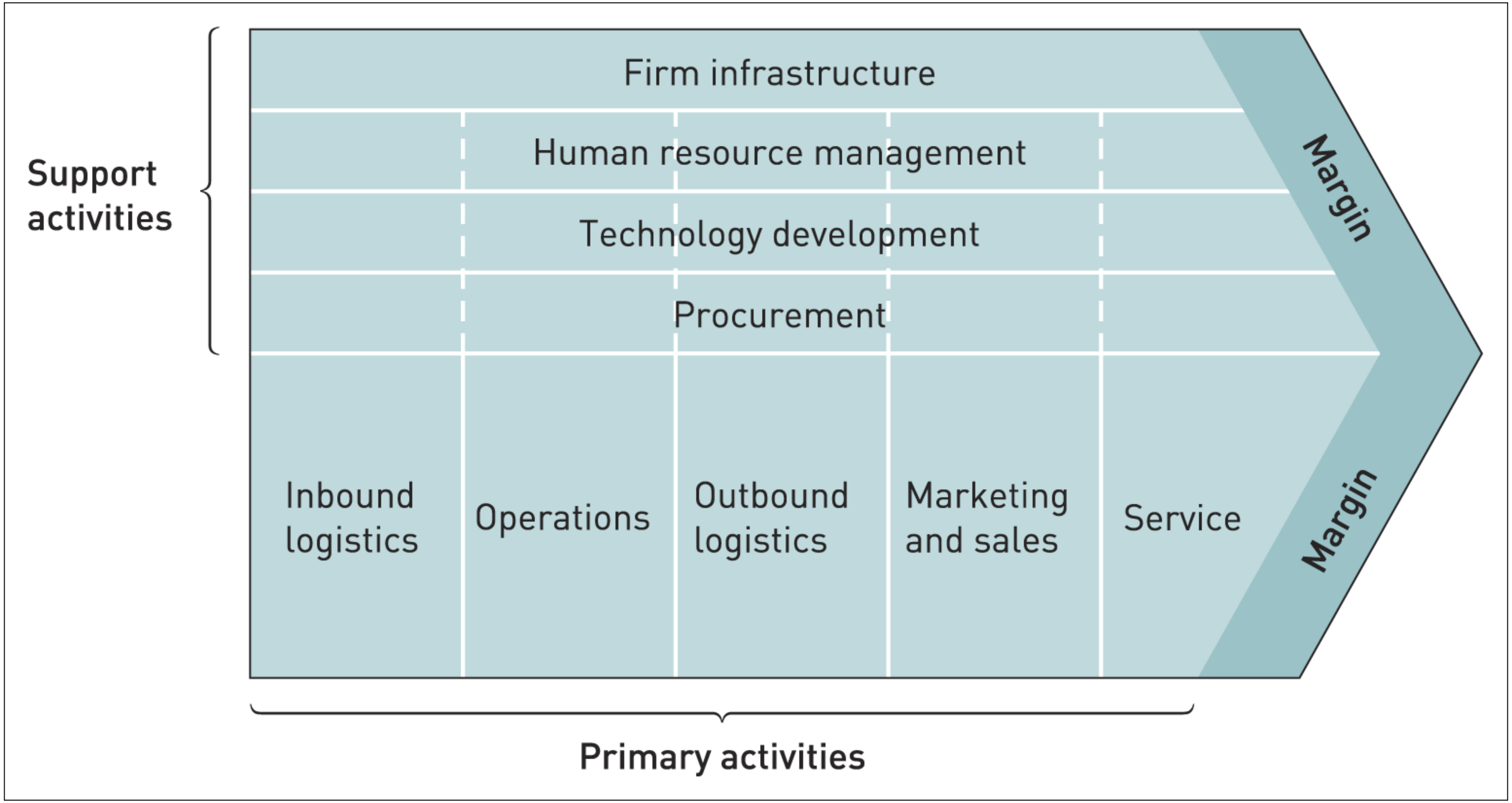
- Value chain analysis proposes a system view of the organization composed of stages in a transformation process with inputs and outputs to each of the distinct stages.

- Value, according to Michael Porter, is the price that a costumer is prepared to pay for an offering. Profit is the difference between this value and total costs to the enterprise of providing that offering.

- Value chain analysis divides an enterprise into a chain of activities and each element in the value chain delivers a part of the total value to the customer and contributes part of the total profit.

- The purpose of value chain analysis is to measure the value delivered and the profit contributed by each link of the chain.

Porter´s Model of Value Chain Analysis



Porter´s Model of Value Chain Analysis

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- Porter s value chain model describes five values that are generating primary activities and support activities.

- ***Primary activities***:
  - Inbound logistics;
  - Operations;
  - Outbound logistics;
  - Marketing and sales;
  - Service.

- ***Support activities:***
  - Procurement;
  - Technology development;
  - Human resource management;
  - Firm infrastructure.

Porter´s Model of Value Chain Analysis

- **Value chain analysis** involves the following three steps:
    1. **Examine each product line's value chain in terms of the various activities** involved in producing that product or service.
    2. **Examine the "linkages" within each product line's value chain**: Linkages are the connections between the way one value activity (for example, marketing) is performed and the cost of performance of another activity (for example, quality control).
    3. **Examine the potential synergies among the value chains of different product lines or business units**: Each value element, such as advertising or manufacturing, has an inherent economy of scale in which activities are conducted at their lowest possible cost per unit of output. If a particular product is not being produced at a high enough level to reach economies of scale in distribution, another product could be used to share the same distribution channel.

VRIO Analysis

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- VRIO analysis was developed by Barney (1995) to identify strategically valuable resources. The analysis builds on the basic ideas of the resource-based view RBV.

- Resources that are subjects of VRIO analysis are:
    - Tangible (physical) and intangible;
    - Human;
    - Financial.

- The term VRIO stands for the initials of four questions that can be asked whether the resource is:
    - Valuable?
    - Rare?
    - Imitable?
    - Organised for usage?

Applying the VRIO

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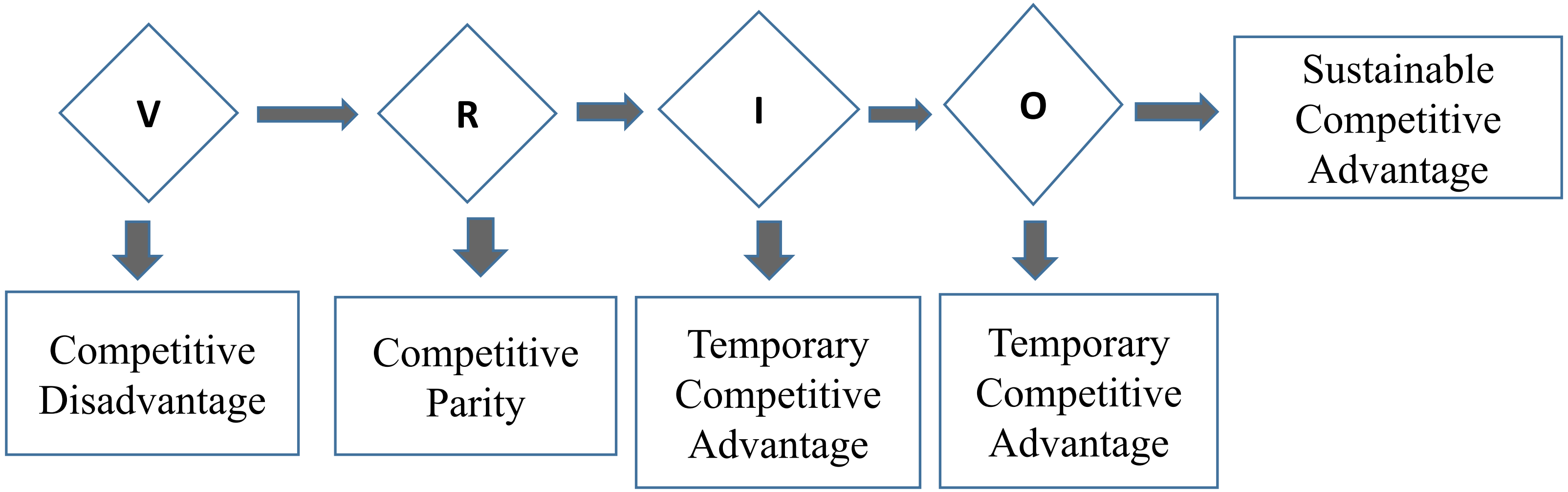

Prostor pro doplňující informace, poznámky

McKinsey 7S Model

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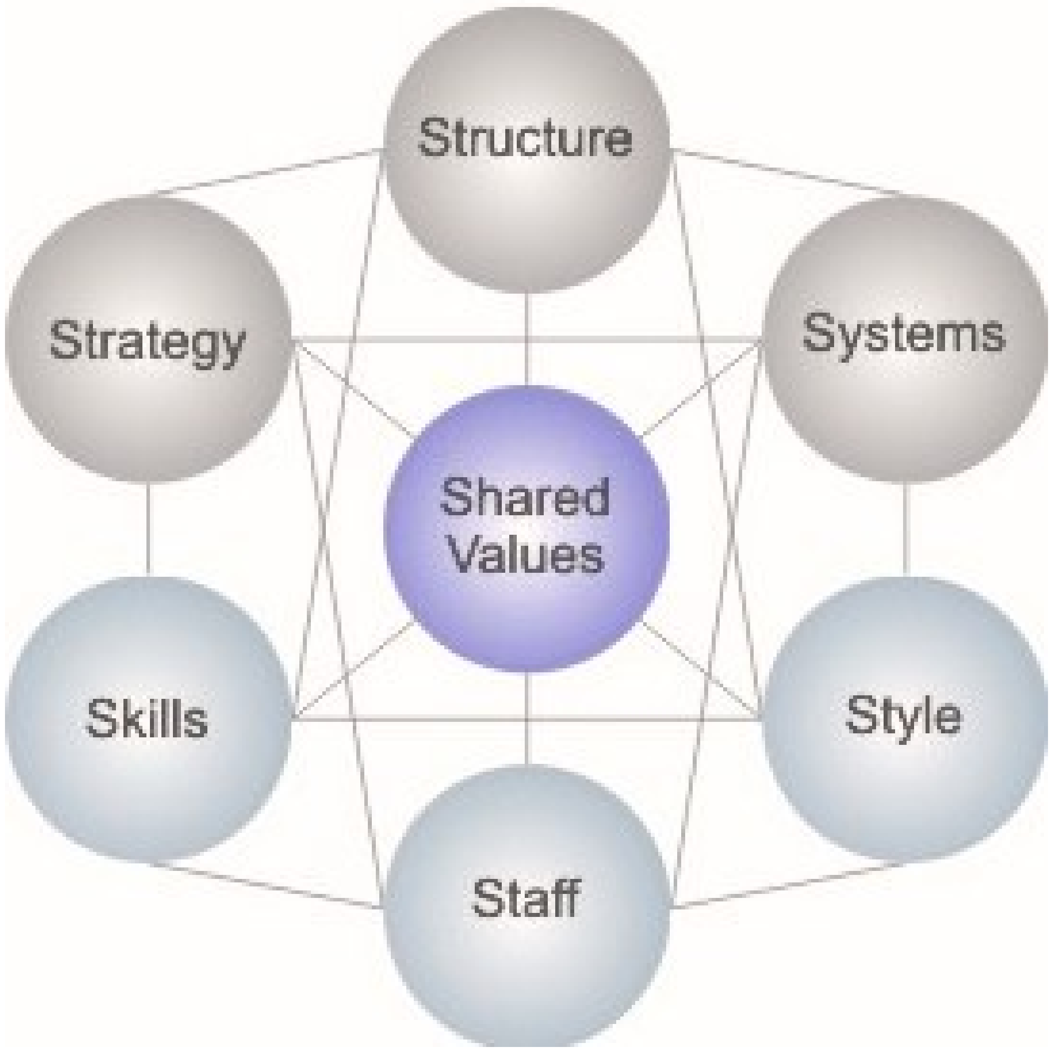
- The McKinsey 7S framework was first published by Waterman and others in 1980. The McKinsey consultants argue that in looking at an organization as a whole, seven variables are important, but the essential thing about them is that they are inter-linked.

- The model can be used in a wide variety of situations where an alignment perspective is useful to help organizations:
    - Improve the performance of a organization;
    - Examine the likely effects of future changes within a organization;
    - Align departments and processes during a merger or acquisition;
    - Determine how best to implement a proposed strategy.

McKinsey 7S Model



McKinsey 7S Model

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- The McKinsey 7S model involves seven interdependent factors which are categorized as either hard or soft elements.

- ***Hard elements*** – are easier to define or identify and management can directly influence them. These are:
  - Strategy;
  - Structure;
  - Systems.

- ***Soft elements*** – can be more difficult to describe and are less tangible and more influenced by culture. These are:
  - Shared values;
  - Skills;
  - Style;
  - Staff.

Stakeholders Analysis

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- Stakeholder is any individual or group that is affected by business decision. Stakeholders have the capacity to affect business performance through their decisions and behavior.

- ***Internal stakeholders*** are all internal members of a organization:
    - Employees;
    - Directors;
    - Shareholders.

- ***External stakeholders*** include:
    - Customers;
    - Suppliers;
    - Competitors;
    - Politicians;
    - Policy-makers;
    - Community;
    - General public

Stakeholders Analysis

- In terms of environmental analysis, organizations need to have an understanding of steps in analysis:
  - Who are stakeholders of the organization;
  - Identification nature of interests of stakeholders;
  - Nature and level of their interest in the organization;
  - Consider whether there are any conflicts between the interests of different stakeholders;
  - Power of stakeholders to exert influence – consider in what way and to what extent, each stakeholder exercises power of influence.

Portfolio Analysis

- Portfolio analysis could be defined as a set of techniques that help strategists in taking strategic decisions with regard to individual products or business in a organization s portfolio.

- The objective of the analysis is to determine how to allocate resources to each of the product or business in the organization s portfolio.

- It is primarily used for competitive analysis and corporate strategic planning in multiproduct and multi-business organizations.

- The analysis of products or business can be performed by using these methods:
    - Boston Consulting Group Matrix BCG matrix;
    - General Electric Matrix GE matrix.

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BCG matrix

- Boston Consulting Group matrix BCG matrix provides a graphic representation for a organization to examine the different businesses in a organization s portfolio on the basis of their relative market shares and industry growth rates.

- Vertical axis denotes the rate of growth in sales, in percentage, for a particular industry.

- Horizontal axis represents the relative market share, which is the ratio of organization s sales to the sales of the industry s largest competitor or market leader.

- The result of combining the industry growth rate and the relative market share in a four-cell matrix.

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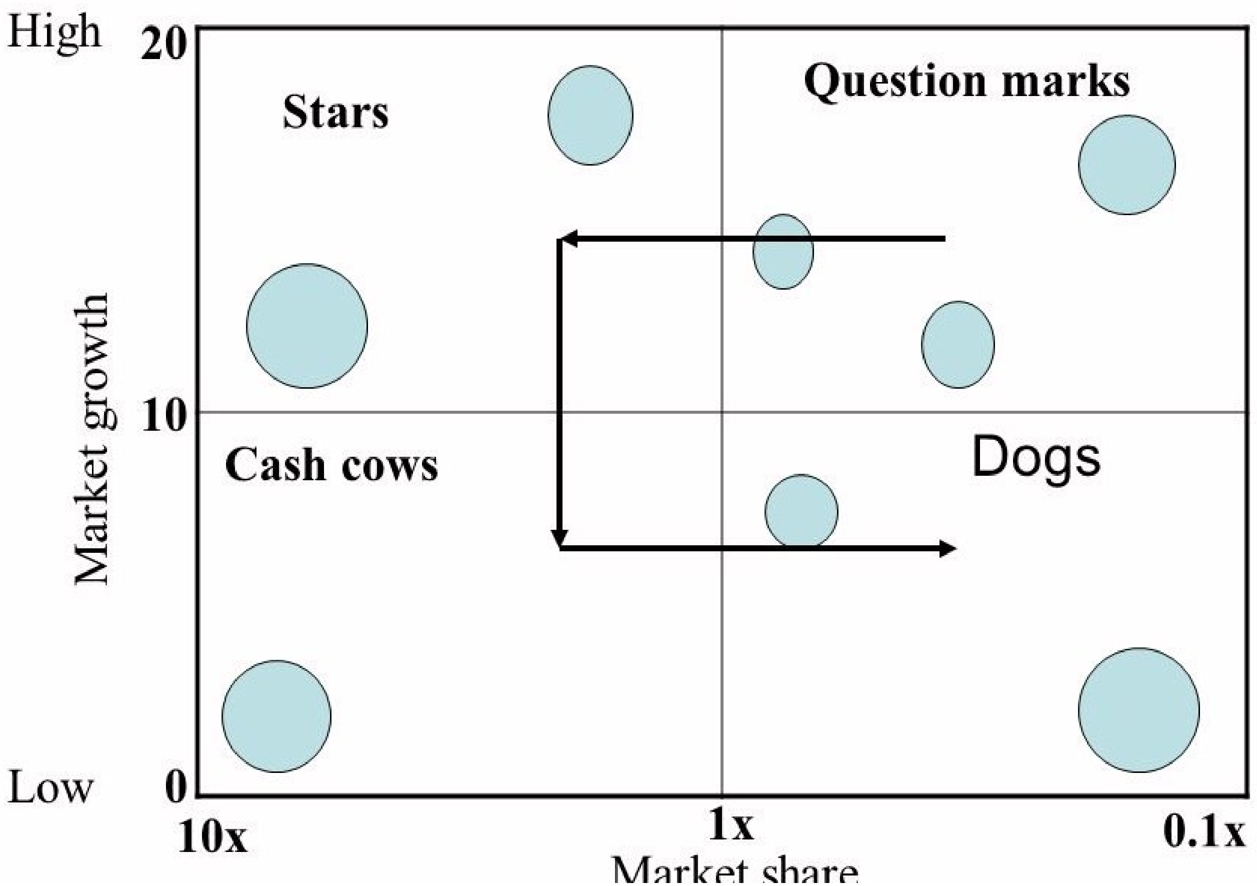
BCG matrix



Market growth is expressed in percentage terms.

BCG matrix

- ***Question marks*** (problem children) – businesses with high industry growth but low market share for a organization. They are usually new products which have a good commercial potential.

- ***Stars*** – are businesses with high industry growth and high market share for a organization. A organization generally pursues an expansion strategy to establish a strong competitive position with regard to a star business.

- ***Cash cows*** – are businesses which generate high market share but their rate of market growth is slow as cash cow businesses lose their attractiveness and tend towards a decline.

- ***Dogs*** – are businesses with related slow industry growth and have a low relative market share. They neither generate nor require large amount of cash.

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GE McKinsey matrix

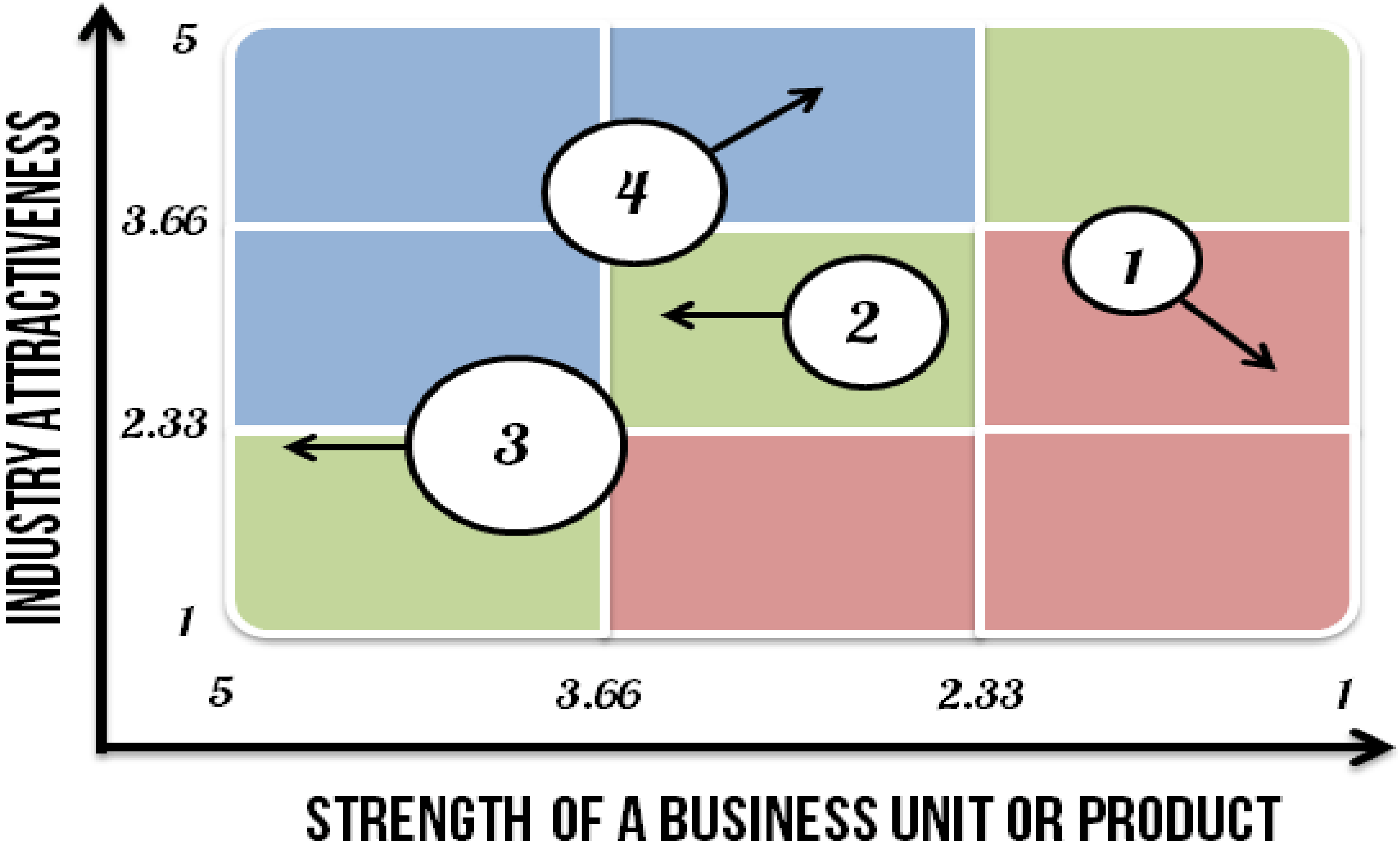
- General Electric McKinsey matrix is very similar to BCG matrix. GE matrix is used to analyze organization s product or business unit portfolio and facilitate the investment decisions.

- GE matrix is a nine cell matrix. It is a more sophisticated business portfolio framework than the BCG matrix – the matrix has multicriterial character.

- The organization s products or business units are evaluated on two axes:
    - Industry attractiveness;
    - Competitive strength.

- There are three groups of boxes (three fields) in GE matrix:
    - Investment/growth;
    - Selectivity/earnings;
    - Harvest/divest boxes.

GE McKinsey matrix



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GE McKinsey matrix

- **Industry attractiveness** indicates how hard or easy it will be for a organization to compete in the market and earn profit.
- Industry attractiveness consists of many factors that collectively determine the competition level in it. There s no definite list of which factors should be included to determine industry attractiveness, but the following are the most common:
    - Long run growth rate;
    - Industry size;
    - Industry profitability (entry barriers, exit barriers etc.);
    - Industry structure;
    - Product life cycle changes;
    - Changes in demand;
    - Trend of prices;
    - Macro environment factors;
    - Seasonality;
    - Availability of labor;
    - Market segmentation.

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GE McKinsey matrix

- **Competitive strength** measures how strong, in terms of competition, a particular business unit (or product) is against its rivals. Managers try to determine whether a business unit has a sustainable competitive advantage.

- The following factors determine the competitive strength of a business unit:
    - Total market share;
    - Market share growth compared to rivals;
    - Brand strength;
    - Profitability of the organization;
    - Customer loyalty;
    - Resources or capabilities;
    - Business unit strength in meeting industry s critical success factors;
    - Strength of a value chain;
    - Level of product differentiation;
    - Production flexibility.

GE McKinsey matrix: Steps for performing of GE matrix

- Determine industry attractiveness of each business unit
    - Make a list of factors, assign weights, rate the factors, calculate the total scores.
- Determine the competitive strength of each business unit
    - Make a list of factors, assign weights, rate the factors, calculate the total scores.
- Plot the business units on a matrix
- Analyze the information
    - Invest/grow box – organizations should invest into the business units that fall into these boxes.
    - Selectivity/earning box – manager should invest into these business units only if manager has the money left over the investments in invest/grow business units group.
    - Harvest/divest box – business unit that are operating in unattractive industries.
- Identify the future direction of each business unit
- Prioritize investments

GE McKinsey matrix: Advantages and diasadvantages of GE matrix

- Advantages
  - Helps to prioritize the limited resources in order to achieve the best returns.
  - Managers become more aware of how their products or business units perform.
  - Identifies the strategic steps the organization needs to make to improve the performance of its business portfolio.

- Disadvantages
  - Requires a consultant or a highly experienced person to determine industry s attractiveness and business unit strength as accurately as possible.
  - It is costly to conduct.
  - It doesn t take into account the synergies that could exist between two or more business units.

SWOT Analysis

- SWOT analysis combines internal and external analyses – the Strengths and Weaknesses of the organizations coupled with the Opportunities and Threats in the external business environment.

- Benefits of SWOT analysis
    - Simplicity;
    - Lower costs;
    - Flexibility;
    - Integration and synthesis;
    - Collaboration.

- Criticisms against SWOT analysis:
    - It allows companies to create lists without serious consideration of the issues;
    - It often becomes a sterile academic exercise of classifying data and information.

SWOT Analysis

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	Strengths	Weaknesses
Opportunities	S-O strategy maxi – maxi Aggressive strategy	W-O strategy mini – maxi Turnaround strategy
Threates	S-T strategy maxi – mini Diversification strategy	W-T strategy mini – mini Defensive strategy