

CHAPTER 3

STRATEGIC ANALYSIS: INTERNAL ENVIRONMENT

1. INTRODUCTION

- Strategic Analysis is equally important when it comes to internal environment assessment.
- Internal environment refers to the sum total of
 - People - individuals and groups, stakeholders,
 - Processes - input-throughput-output,
 - Physical infrastructure - space, equipment and
 - Physical conditions of work - lines of authority & power, responsibility, accountability and
 - organizational culture - intangible aspects of working-relationships, philosophy, values, ethics that shape an organization’s identity.
- Internal environment is specific to each organization and is very important to understand for strategic analysis.

2. UNDERSTANDING KEY STAKEHOLDERS

Stakeholders refer to any person/group of individuals, internal or external, that has an

- interest in the business or corporate strategy of the organization or can impact it.

They may be the management, employees, shareholders, investors, suppliers, customers, regulators and so on. A firm may be viewed as a coalition of stakeholders.

Identification of Key Stakeholder: It is important to identify key stakeholders as each stakeholder exerts a different level of influence and can have differing levels of interest in the organisation.

For example, an organisation involved in healthcare innovation needs to have a long-term perspective about its return on investment (ROI) as there may be a long time between investment into research timelines and a commercial outcome.

Example of Key Stakeholders and their requirements for an OTT Platform

| Shareholders | CEO & Board of Directors | Major Vendors (Production House) | Consumers (Viewers) | Employees |
|------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------|---------------------------------------------------------------------------------------------------------------------------------|
| <ul style="list-style-type: none"> ▪ Innovation & continuous creative content ▪ Total shareholder return (ROI) ▪ Corporate social | <ul style="list-style-type: none"> ▪ Prestige ▪ Market share ▪ Revenue & profit growth | <ul style="list-style-type: none"> ▪ Growth ▪ Stability of ordering ▪ Stable margins | <ul style="list-style-type: none"> ▪ New content - Innovation ▪ Better deals - Pricing ▪ Value for | <ul style="list-style-type: none"> ▪ Wages & benefits ▪ Stability of employment ▪ Pride of |

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| responsibility ▪ Highest market share | ▪ Market rankings | | money ▪ Continuous supply | working for a reputed organisation |
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2.1. MENDELLOW'S MATRIX

The Mendelow Stakeholder matrix (also known as the Stakeholder Analysis matrix and the Power-Interest matrix) is a simple grid-based framework to help manage key stakeholders.

In order to manage a project, it is very critical to manage the competing interests of various stakeholders.

Mendelow suggests that one should analyse stakeholder groups based on

- a) Power i.e. the ability to influence organisation strategy or resources. Power can be assessed based on factors such as authority, resources, and expertise; and
- b) Interest i.e. how interested they are in the organisation succeeding. Interest can be gauged by their level of involvement, expectations, and potential benefits or risks.

Some stakeholders will hold more Power than others, & some stakeholders will have more Interest than others.

Management needs to

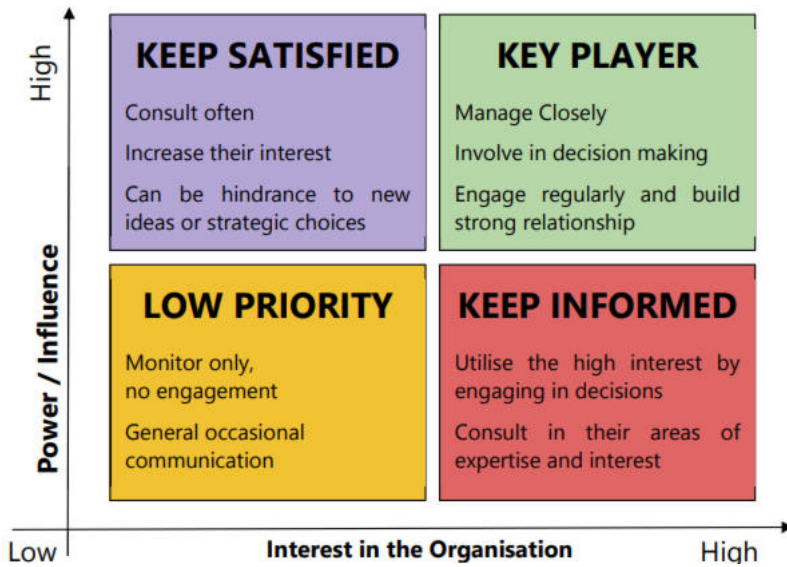
- closely manage those stakeholders who have High Power and High Interest and need to invest lot of time and effort in them while
- rarely monitor those stakeholders with low power and low interest like research institutes seeking an organisation data and minimum effort expended on them in terms of time and money.

Examples

- i) A big shareholder is likely to have high power & high interest in the organisation, whereas a big competitor would have high power to impact strategy, but potentially less Interest in success of rival organisation.
- ii) CEO is likely to have more Power to influence the work and also high interest in it being successful. Keeping them informed almost daily should be a priority.

Developing a Grid of Stakeholders/ Steps to analyze and manage the stakeholders effectively?

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| i) Identify Stakeholders: | Begin by identifying all relevant stakeholders for the organization. This includes individuals, groups, or organizations that may be impacted by or have an impact on the activities. |
| ii) Assess Power and Interest: | For each stakeholder, assess their power to influence the organization and their level of interest in its success. |
| iii) Plot Stakeholders on the Grid: | Create a grid with Power on one axis and Interest on the other. Plot each stakeholder on the grid based on the assessment. Stakeholders with high power and high interest are placed in the "Key Players" quadrant, those with high power but low interest are in the "Keep Satisfied" quadrant, those with low power but high interest are in the "Keep Informed" quadrant, and those with low power and low interest are in the "Low Priority" quadrant. |
| iv) Develop Strategies for each Quadrant: | Refer table below. |
| v) Monitor and Adapt: | Continuously monitor the power and interest of stakeholders and adjust your strategies accordingly. Stakeholders may move between quadrants based on changing circumstances, so it's important to remain flexible and responsive. |



Categorization of stakeholders into four groups by Mendelow's & strategy for each category:

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| 1. KEEP SATISFIED Stakeholders: | High power, less interested people – Organisation should put in enough work with these people to keep them satisfied by providing them their intended information on a regular basis. For example, banks, government, customers, etc. |
| 2. KEY PLAYERS Stakeholders: | High power, highly interested people – Organisation's aim should be to fully engage this group of stakeholders, making the greatest efforts to satisfy them, take their advice, build actions and keep them informed with all information on a regular basis. For example, Shareholders, CEO, Board of Directors, etc. |
| 3. LOW PRIORITY Stakeholders: | Low power, less interested people – Organisation should only monitor them with no actions to satisfy their expectations. Strategically, minimal efforts should be spent on this group of stakeholders while keeping an eye to check if their levels of interest or power change. For example, business magazines, media houses, etc. |
| 4. KEEP INFORMED Stakeholders: | Low power, highly interested people – Organisation should adequately inform this group of people and communicate with them to ensure that no major issues arise. This audiences can also help with real time feedbacks and areas of improvement for an organisation. For example, employees, vendors, suppliers, legal experts, etc. |

Since environment is highly dynamic and uncertain, things might happen that can cause stakeholders to suddenly move between quadrants.

For example, an organisation might inadvertently contravene a regulation, say GST compliance which would cause the regulatory body i.e. the Indirect Taxes Department to move from High Power, Low Interest to High Power, High Interest.

This would then require a different way of managing and communicating with this stakeholder.

Equally, the media houses would also move from Low Power, Low interest, to Low Power, High Interest.

So, it's always worth re-analysing the Mendelow's grid for one's organisation in the event of a change in the environment.

Activity: Identify and group the below stakeholders in the 4 groups as suggested by Mendelow for an Ecommerce startup.

Ms. Suhasini (CEO), Mango Partners & TRIK Group (Investors), MSME Ministry, Customers from North-East India, Sellers from Rajasthan, Jandhan Bank (Lender), & Kumar S and Sharma T (Sr. Managers in the Co.)

3. STRATEGIC DRIVERS

Strategic Drivers involves analysis of the

- key markets in which the organisation operates, as well as its key customers,
- the products and services it provides,
- the channels in which the products or services are delivered, and
- the organisation's competitive advantage.

Strategic drivers consider what differentiates an organisation from its competitors.

Key strategic drivers of an organisation include:

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| a) Industry and markets | b) Customers | c) Products/services | d) Channels |
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3.1. INDUSTRY AND MARKETS

In terms of the internal environment, it is very important for an organisation to understand its relative position in the industry and in the market in which it operates.

Similar companies are grouped together into industries. Basically, industry grouping is based on the primary product that a company makes or sells.

For example, Maruti, Mahindra, Tata Motors, TVS, Bajaj Auto, are all selling automobiles as their primary product and thus categorised into Automotive Industry.

Similarly, Zara, H&M, Marks & Spencer, Pantaloons, Westside, Uniqlo, are all selling apparels and accessories for the youth, and thus categorised under apparels industry.

A market is defined as the sum total of all the buyers and sellers in the area or region under consideration. The market may be a physical entity or may be virtual like e-commerce websites and applications. It may further be local or global, depending on which all countries the business sells its products in. The value, cost and price of items traded are as per forces of supply and demand in a market.

Is market the same for all businesses?

No. Each business has its own set of customers i.e. market and more so, each product within a business has its own market.

For example, for a FMCG brand selling Shampoos, Dairy Products, Flours, Washing Powder, etc. - each product line will have a separate market to cater to and therefore build strategies specific to the market of concern.

3.1.1. ANALYSING INDUSTRY AND MARKETS

Industry and market analysis is extremely important to identify one's position as compared to the competitors, who can be of equal size and value, or bigger in size and value or even smaller and newer.

Further, identifying the strongest & weakest companies help understand what techniques can be implemented and which ones are to be avoided.

However, when an industry has so many competitors, it is not practical to examine each one in-depth. Hence, grouping them into categories based on various parameters can be really insightful and time saving.

For example, Smart Phone industry has numerous options to select from.

A tool to study the market positions of rival companies by grouping them into like positions is **strategic group mapping**.

Strategic group consists of those rivals who have similar competitive approach and position in market (comparable product, price, quality etc.)

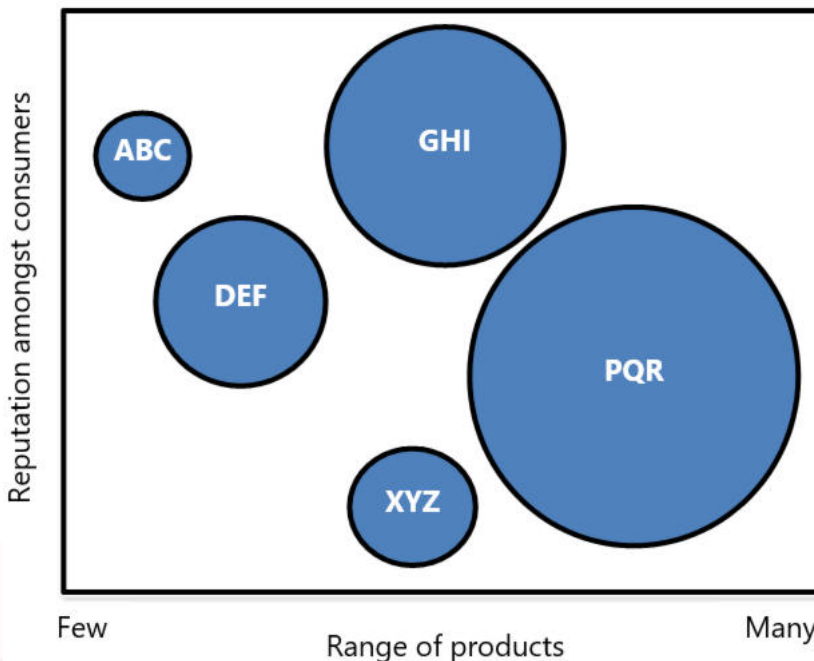
It reveals the competitive positions of industry participants.

An industry contains only one strategic group when all sellers pursue essentially identical strategies and have comparable market positions.

At the other extreme, there are as many strategic groups as there are competitors when each rival pursues a distinctively different competitive approach and occupies a substantially different competitive position in the marketplace.

Procedure for constructing strategic group map:

- a) Identify competitive characteristics that differentiate Firms in the industry.
 - Price/ Quality (High, Medium, Low)
 - Geographic coverage (Local, National, Global)
 - Degree of services offered (No-frills, Limited, full)
- b) Plot Firms on 2 variable map using pairs of differentiating characteristics.
- c) Assign firms that fall in about same strategy space to same strategic group
- d) Draw circle around each group where each group represents their relative market share.



A simple glance of the mapping chart shows us that even though ABC has few models, but it has great reputation in the market.

Similarly, GHI has a good range of products and is the most reputed company in laptops.

Another view is that XYZ and GHI have the same number of models as both are on the same place on X-Axis, but GHI has much greater reputation than XYZ, as it has a bigger bubble and is higher on the Y-Axis.

3.1.2. CUSTOMERS

Understanding the different types of customers to whom the Organisation’s products/services are sold is not only important but also the first step in deciding the product/services.

Different customers may have different needs and require different sales models or distribution channels.

Example: In case of a headphones brand - the customers can be grouped under high value buyers, medium value buyers and low value buyers based on the amount they are willing to spend on a product, thus helping the business understand their key customers and focus areas of improvement.

Customer versus Consumer

Consumers are the ones who finally use a product/service, while customers are the buyers of that product. A customer can be a consumer and vice versa.

Note: From a pricing perspective, customer is of more importance and from value creation and design/ usability, consumer needs to be the kept at the center of decision making.

For example, baby diapers are bought by parents (customers) who are willing to pay higher price for higher quality, while the real consumers are the babies, who are more concerned about the comfort and easiness of the diaper. If babies do not accept the product i.e. if consumers aren’t satisfied, it is difficult to retain the buyer i.e. customers as well.

3.1.3. PRODUCT/ SERVICES

Products and services are closely linked and inter-related with the markets that the Organisation wants to serve. As part of analysis of strategic driver, business needs to identify key product/services that the Organisation offers and how these are performing.

Product stands for the combination of “goods-and-services” that the company offers to the target market. Strategies are needed for managing existing product over time, adding new ones and dropping failed products.

The products can also be classified on the basis of industrial or consumer products, essentials or luxury products, durables or perishables.

Products can also be differentiated on the basis of size, shape, colour, packaging, brand names, after-sales service and so on.

Quite often the differentiation is psychological rather than physical. It is enough if customers are persuaded to believe that the marketer’s product is different from others.

For example, Shampoos with different branding namely Head & Shoulders, Olay, Old Spice, Pantene are all produced by the same company P&G.

It answer the general question: What business are we in and what should be done to win over competition in each product/service we serve.

Pricing strategies for entering a market

For new product, pricing objective should be

- a) to have a customer centric approach i.e. to make product acceptable to customer i.e.,
- b) produce sufficient returns through a reasonable margin over cost; and
- c) increase market share.

Two common pricing strategies are:

| Price skimming | Price penetration |
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| Prices are set at very high level initially for new product. | Prices are kept quite low for new product which itself is it’s selling point. |

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| <p>Product is directed towards customers who are</p> <ul style="list-style-type: none"> ➤ insensitive to price and ➤ sensitive to brand and loyalty. | <p>This enables a large no of potential customers to afford and buy new product.</p> |
| <p>Examples: Call rates of mobile telephones were set very high initially. Apple launching air pods</p> | <p>Examples: Jio launching cheap data plans and set top box</p> |

| Products and services need heavy investment in reaching out to customers. Types of Marketing Strategies: | |
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| 1) Social marketing | It refers to design, implementation and control of programs which aims to increase acceptability of a social idea, cause or practice among target market/society. E.g. Campaign for No smoking, No dowry, No tax evasion. |
| 2) Augmented marketing | It means providing additional benefits to a customer along with the core product. E.g: Extra warranty, 24x7 online tech support, movies on demand etc. |
| 3) Direct marketing | It involves using advertisement medium that interacts directly with customers. E.g. Email, SMS, catalogue marketing, electronic marketing, Tele calling etc. |
| 4) Person marketing | People are also marketed. It involves activities to create, maintain or change attitude and behavior of target audience towards a particular person. E.g. Politicians, sports stars, film stars, etc. market themselves to get votes, or to promote their careers. |
| 5) Organization marketing | It involves activities to create, maintain or change attitude and behavior towards a particular Organization. Both profit and non-profit organizations practice Organization marketing. |
| 6) Place marketing | It involves activities to create, maintain or change attitude or behavior towards a particular place. E.g. Tourism marketing |
| 7) Relationship marketing | It involves creating, maintaining and enhancing strong relationship with customers and other stakeholders. E.g: Airlines Loyalty programs or Airlines offering special lounges at major airports for frequent flyers. |
| 8) Service marketing | It involves applying concepts of marketing to service sector. |
| 9) Differential marketing | It is a market-coverage strategy and involves activities to target several market segments and design separate offer for each segment. E.g: HUL has Lux in popular segment and Pears in premium segment. |
| 10) Concentrated Marketing | In this, Firm goes after large share of a target market. It can also take the form of Niche marketing. |
| 11) Synchro marketing | When demand for a product is irregular due to season or during certain part of day, it causes overworked capacity or idle capacity. Synchro marketing is used to find ways to alter the demand pattern through flexible pricing and other incentives. E.g: Movie tickets sold at lower rate during weekdays, Happy Hours in Restaurants. |
| 12) Demarketing | It involves activities to reduce demand temporarily or permanently. It does not aim to destroy demand but only reduce it or shift it. It is pursued when there is overflow of demand. |

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| | For example, buses are overloaded in the morning and evening, roads are busy for most of times, zoological parks are over-crowded on Saturdays, Sundays and holidays. Here demarketing can be applied to regulate demand. |
| 13) Enlightened marketing | It is a marketing philosophy that Company's marketing should support long term performance of an Organization and marketing. Five principles are : a) Value marketing b) Innovative marketing c) Customer oriented marketing d) Societal marketing e) Sense of mission marketing |

3.1.4. CHANNELS

Channels are the distribution system by which an organisation distributes its product or provides its service.

Wider and stronger channel helps the business

- a) to fight and win over competition; and
- b) help keep new players away from entering the industry, thus acting as barriers to entry.

Few examples of how the following companies distribute their products and services:

- i) Lakme - sells its products via retail stores, intermediary stores (like Nykaa, Westside, Reliance Trends), as well as online mode like Amazon, Flipkart, Nykaa online and its own website.
- ii) Boat Headphones - only online via e-commerce platforms like Flipkart and Amazon and its own website.
- iii) Coca Cola - retail shops across the nation, in each district, each town as well as online mode via Dunzo, Blinkit, etc.

Types of channels:

| i) The sales channel | ii) The product channel | iii) The service channel |
|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <p>These are the intermediaries involved in selling the product through each channel and ultimately to the end user.</p> <p>The key question is: Who needs to sell to whom for your product to be sold to your end user?</p> <p>For example, many fashion designers use agencies to sell their products to retail organisations, so that consumers can access them.</p> | <p>The product channel focuses on the series of intermediaries who physically handle the product on its path from its producer to the end user.</p> <p>For example, Australia Post, who delivers and distributes many online purchases between the seller and purchaser when using eBay and other online stores.</p> | <p>The service channel refers to the entities that provide necessary services to support the product, as it moves through the sales channel and after purchase by the end user.</p> <p>The service channel is an important consideration for products that are complex in terms of installation or customer assistance.</p> <p>For example, a Bosch dishwasher may be sold in a Bosch showroom, and then once sold it is installed by a Bosch contracted plumber.</p> |

Importance of Channel Analysis:

- i) It helps business to scale up and expand beyond the current geographies and markets.
- ii) When a business plans to grow to newer markets, they need to develop or leverage existing channels to

get to new customers.

Examples:

- a) If a healthcare brand wants to reach out to elderly customers, they need to be more focused on offline mode of business where agents reach out physically to the elderly as most of their potential customers (i.e. the old aged) are not active on smartphones.
- b) If a new drink brand wants to acquire customers, they need to place their products via every channel possible to get more attraction from customers like placing their drinks in stores, and shops alike, offering competitive campaigns to create awareness via online modes (social media).
- c) Bottled water and cold drinks are available at hill stations. This is possible because of strong channels of distribution.

Some of the most renowned brands who have created competitive advantage in channels are Coca Cola, HUL, Patanjali, Asian Paints, Ola, to name a few.

4. ROLE OF RESOURCES AND CAPABILITIES: BUILDING CORE COMPETENCY

- C.K. Prahalad & Gary Hamel advocated concept of core competency & is widely used in management.
- Core competencies are the unique strength of an organization which may not be shared by others. It is created by superior integration of technological, physical and human resources.
- It is a source of competitive advantage. It simply means whatever a Firm does best.
Example: Marketing and Sales is a core competence of Hindustan Unilever Limited while low operating costs is core competence of Wal-Mart.
- Core competency involves utilization of several individual skills and techniques like technological and managerial know-how, human resource, wisdom and experience.
- Therefore, core competencies can't be built on one capability or single know-how technique. Instead, it has to be integration of many resources.
- Optimal way to define core competence is to consider it as sum of 5 to 15 developed expertise.

4.1. 3 AREAS WHERE MAJOR CORE COMPETENCIES ARE IDENTIFIED – AS PER CK PRAHLAD & GARY HAMEL

| i) Competitor Differentiation | ii) Customer Value | iii) Application to other markets |
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| <p>A company is said to have core competency if its's competency is unique & difficult for others to copy.</p> <p>Company should keep on improving those skills to sustain competitive position.</p> <p>Unique skills & resources doesn't mean that it has to be possessed by one company only.</p> <p>If many companies have similar skills and one company is able to perform it significantly better, that Company has core competency.</p> <p>For example, it is quite difficult to imitate patented innovation, like Tesla has been winning over competition in electric vehicles.</p> | <p>It includes all the skills needed to provide fundamental benefits to the end customer.</p> <p>In order to be core competency, the Service or product has to have real impact on customers as the reason to purchase them.</p> <p>If the customer chooses the product without this, the competence is not core competency.</p> | <p>Core competency must be applicable to whole organization and not only to a particular area.</p> <p>A skill is considered core competency only if it is fundamental to whole organization.</p> <p>Core competency should be used throughout organization to open up potential new markets.</p> |

If above three conditions are met, the Company can regard a competence as core competence.

4.2. WHY TO IDENTIFY AND DEVELOP CORE COMPETENCY

Core competencies distinguish a company competitively and reflect its personality.

It is important to identify core competencies because it is difficult to retain those competencies in a price war and cost-cutting environment.

Failing to identify core competencies is a kind of opportunity loss for a company.

Examples

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| Small retail shops have CC in the areas of | a) Personal service to customers | b) Extended working hours |
| | c) Easy credit | d) Free home deliveries |
| | e) Amicable style of the owner | f) Proximity |
| Big retail stores & super markets have CC in areas of | a) Merchandising | b) Securing supplies at lower cost |
| | c) In-house management | d) Computerized stock ordering |
| | e) Billing systems | f) own brand labels |
| Supermarkets compete with one another with CC as to | a) Locational advantage | b) Quality assurance |
| | c) Customer convenience in shopping | |

4.3. CRITERIA FOR BUILDING CORE COMPETENCIES?

Four specific criteria of sustainable competitive advantage that firms can use to determine those capabilities that are core competencies.

| Valuable | Rare | Costly to Imitate | Non-substitutable |
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| Valuable capabilities are those which allow Firms to exploit opportunities or tackle threats. | Core competencies are rare capabilities possessed by very few competitors. | It means such capabilities which is not easy to copy or develop. | It means there must not be strategic equivalent which is easily available or imitable. |

When a capability is 'valuable NCR', it is core competency & a source of sustainable competitive advantage.

Example: Airtel has its marketing campaign that talks about Zero Customer Complaints. This is about creating a core competency of great customer service.

5. COMBINING EXTERNAL AND INTERNAL ANALYSIS (SWOT ANALYSIS)

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| | Helpful to achieving the objective | Harmful to achieving the objective |
| Internal origin (attributes to the organization) | S Strengths | W Weaknesses |
| External origin (attributes to the environment) | O Opportunities | T Threats |

SWOT Analysis Example

SWOT analysis is the analysis of a business's strengths, weaknesses, opportunities and threats.

It is implemented before all company actions, whether it is exploring new initiatives, revamping internal policies, considering opportunities to grow or alter a plan midway.

It is a tool which is used for both Internal and External Analysis and helps in growth.

| Strength (+) | Weakness (-) | Opportunity (+) | Threat (-) |
|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Inherent capabilities of an Organization used to gain strategic advantage. | Inherent limitations/ constraints which creates strategic disadvantage. | Favourable condition in organization's environment to strengthen its position. | Unfavourable condition in organization's environment which causes risk or damage to organization's position. |
| <ul style="list-style-type: none"> ▪ Financial condition ▪ Superior skills/ cost or tech. advantages ▪ Better product quality ▪ Strong Distribution N/w ▪ Multiple Partners with varied expertise ▪ Long Term contractual service agreements ▪ 70 years of brand value ▪ Services spread across India ▪ Large employee strength to deliver work ▪ Well diversified business | <ul style="list-style-type: none"> ▪ Obsolete/ outdated products or facilities ▪ High inventory/ debtors ▪ No strategy ▪ Underutilized capacity ▪ No automation of work and documentation ▪ Low employee morale | <ul style="list-style-type: none"> ▪ New product/ market launch ▪ New tender/ contracts ▪ Opening of market/ Lower trade barrier ▪ Internet & e-commerce ▪ Automation driven advancement ▪ Startups can be supported with experienced partners ▪ Investment in technology can multiply returns. | <ul style="list-style-type: none"> ▪ Large New entrant ▪ substitute products ▪ Increasing competition ▪ Market slowdown ▪ Scandals & New Laws ▪ Online players entering market ▪ AI based solutions and applications. ▪ Price point of online being very competitive ▪ Speed of work becoming faster by the day. |

5.1. PURPOSE/ OBJECTIVE OF SWOT ANALYSIS

It enables management to

- create a firm's specific business model which
- best aligns/ fits/ matches an organization's capabilities
- with demand of market/ environment.

It shows areas where an organization is performing well, as well as areas that need improvement.

SWOT Analysis provides competitive advantage to an organization.

Key Reasons/Significance of SWOT Analysis:

| i) Logical Framework of Analysis | ii) Comparative Account | iii) Guide Strategists in strategy identification |
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| It provides ~ to management to identify all issues which may impact Org. in long or short term. | It provides ~ of internal & external environment to managers to compare O&T with S&W of an Org. | It ~ in case there is any difficulty in selection of appropriate strategy. |

Criticism of SWOT Analysis:

It does not generally provide for evaluation of strengths, weaknesses, opportunities and threats in the competitive context.

6. COMPETITIVE ADVANTAGE: USING MICHAEL PORTER'S GENERIC STRATEGIES

- Competitive advantage is the position of a firm to maintain and sustain a favourable market position when compared to the competitors.
- It is a set of unique features of a Company and its products
 - that are perceived by target market and customers
 - as significant and superior to competition.
- Competitive advantage provides edge over rivals.
- An organization is said to have competitive advantage if its profitability is higher than average profitability of Industry.
- “If you don’t have a competitive advantage, don’t compete”- Jack Welch
- Competitive advantage is said to be achieved if other Firm’s efforts to imitate it has failed.

| Resources | Capabilities |
|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| It includes a. Tangible resources that can be seen and quantified. E.g. plant & machinery, factory b. Intangible resources like goodwill, capacity for innovation, HR skills, Knowledge, trust between managers and employees, patents, copyrights etc. It is developed over a period of time & difficult to imitate. | It exists when resources are purposefully integrated / used to achieve a specific task or set of tasks. Examples: a) Effective customer service, b) Effective and efficient control of inventories, c) Product & design quality, d) Digital technology. |

If a firm possesses resources and capabilities which are superior to those of competitors, then as long as the firm adopts a strategy that utilizes these resources and capabilities effectively, it should be possible for it to establish a competitive advantage.

6.1. SUSTAINABILITY OF COMPETITIVE ADVANTAGE

All competitive advantages have a limited life. The question of duplication is not if it will happen, but when. Sustainability of competitive advantage depends on 4 major characteristics of resource and capability:

| Durability | Transferability | Imitability | Appropriability |
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| Period over which competitive adv. is sustained depends on the rate a Firm’s resources & capabilities deteriorate. If rate of product innovation is fast, patents/ tech. are more likely to get obsolete. On the other hand, consumer brand names have a highly durable appeal. | Competitive advantage also depends on ability of rivals to gain access to necessary resources and capabilities. easier it is to transfer resources and capabilities between companies, the less sustainable will be the competitive advantage | If resources and capabilities can’t be purchased, rivals need to build it from scratch. If competitor is able to build resource and capabilities easily, competitive advantage is not sustainable. For example, In financial services, innovations lack legal protection and are easily copied. | Refers to ability of Firm’s owner to appropriate the return on its resource base. If resources and capabilities provide competitive advantage, there is issue of who is receiving return on such resource & capabilities. |

7. MICHAEL PORTER'S GENERIC STRATEGIES

According to Porter, strategies allow organizations to gain competitive advantage from three different bases: cost leadership, differentiation, and focus. Porter called these base generic strategies.

These strategies have been termed generic, because they can be pursued by any type or size of business firm and even by not-for-profit organizations.

| Cost leadership strategies | Differentiation strategies | Focus strategies |
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| <p>This strategy emphasizes on producing</p> <ul style="list-style-type: none"> ➤ standardized products at a ➤ very low per-unit cost for ➤ consumers who are price-sensitive. | <p>This strategy aimed at producing products and services considered</p> <ul style="list-style-type: none"> ➤ unique industry-wide ➤ for consumers who are relatively price-insensitive. | <p>This strategy is aimed at producing products and services that</p> <ul style="list-style-type: none"> ➤ fulfil the needs of small groups of consumers with ➤ very specific taste. |

Larger firms with greater access to resources typically compete on a cost leadership and/or differentiation basis, whereas smaller firms often compete on a focus basis.

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| COMPETITIVE SCOPE | Broad Target | Cost Leadership | Differentiation |
| | Narrow Target | Focussed Cost Leadership | Focussed Differentiation |
| | | Low-Cost products/services | Differentiated products/services |

7.1. COST LEADERSHIP STRATEGY

Cost leadership strategy is low-cost competitive strategy that aims at broad mass market.

It involves producing

- standard products
- at very low cost per unit
- for price sensitive market.

It involves vigorous efforts to reduce cost in area of Procurement; Production; Storage & Distribution of goods.

Also, economies of scale and reduction in overhead is done due to large volume of sale.

Because of lower cost, cost leader is able to charge lower price than its competitors and still make satisfactory profit.

A primary reason for pursuing forward, backward, and horizontal integration strategies is to gain cost leadership benefits.

But cost leadership strategy must be pursued along with differentiation.

Examples:

- McDonald's fast-food restaurants have successfully followed low-cost leadership strategy.
- Walmart has also successfully followed low-cost leadership strategy.

- c) Decathlon Group’s mega sports stores have been following low-cost leadership strategy to gain international recognition and also beat competition.

| When is cost leadership strategy effective? | How to achieve cost leadership? |
|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <p>a) Market has many price sensitive customers.</p> <p>b) Buyers do not care much about differentiation or brand.</p> <p>c) There is little scope of differentiation.</p> <p>d) There are large no. of buyers with bargaining power.</p> | <p>a) Prompt forecasting of demand of product/ service</p> <p>b) Optimum utilization of resources</p> <p>c) Achieving economies of scale to reduce cost per unit</p> <p>d) Standardization of product for mass production</p> <p>e) Invest in cost saving techniques for smart working</p> <p>f) Resistance to differentiation till it becomes essential</p> |

ADVANTAGES OF COST LEADERSHIP STRATEGY

Cost leadership strategy enables a Firm to be profitable even with 5 forces of Porter’s Five Forces Model:

| Rivalry | Buyer | Supplier | New Entrants | Substitute |
|------------------------------------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------|
| Competitors try to avoid price wars, since low-cost Firm will continue to earn profit even if they reduce their price. | Powerful buyers will not be able to exploit cost leader as its cost is already lowest. Hence, buyer will continue to buy from it. | Since cost leader has lowest cost in industry, it is able to absorb greater price increase by its suppliers before it is compelled to increase the price. | Cost leader creates entry barriers for new entrants due to low cost. | Cost leader is able to lower cost to ensure that buyer continues with their product. They can also invest to develop substitutes. |

DISADVANTAGES OF COST LEADERSHIP STRATEGY

- a) Cost advantage may not be for long period as competitors may follow cost reduction techniques as well.
- b) This strategy can be successful only if Firm can achieve higher sales volume.
- c) In this strategy, expenses on advertisement, marketing, research & development etc. is minimal which may be counter-productive in long run.
- d) Technological changes are great threat to cost leader.

7.2. DIFFERENTIATION STRATEGY

This strategy is aimed at broad mass market and involves creating and producing

- unique products and service
- directed at customers who are relatively price insensitive.

Differentiation/ uniqueness can be in

- Product design; Brand; Features; Quality; Customer service etc.

It should be pursued only after a careful study of buyers’ needs and preferences to determine the feasibility of incorporating one or more differentiating features into a unique product.

A successful differentiation strategy allows a firm to charge a higher price for its product and to gain customer loyalty, because consumers may become strongly attached to the differentiated features.

Note: All Firms essentially follow differentiation strategy because only one Firm can be cost leader.

For example, Domino’s Pizza has been offering home delivery within 30 minutes or the order is free, is a unique

selling point that differentiates it from its rivals.

Basis/ Forms/ Types of Differentiation

| Product Differentiation | Price Differentiation | Organizational Differentiation |
|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|----------------------------------------------------------------------------------------------------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| It means innovative products which give Org. an edge over competitors New product involves higher cost due to R&D, marketing but return may be higher if it is valued by customers. | It means company can either offer lowest price or can charge highest price in the industry. It fluctuates based on its supply and demand. | It involves maximizing power of a brand or using specific advantage of Organization to differentiate its products. E.g.: Brand image, customer loyalty, locational advantage, R&D capability. |
| For example, Apple iPhone, has invested huge amounts of money in R&D, and the customers' value that. They want to be among the first ones to try the new offerings from the company. | For example, Apple iPhone dominates the smart phone segment by charging higher prices for its products. | For example, Apple has been building customer loyalty since years and has a fanbase of consumers that are called "Apple Fanboys/Fangirls" |

Achieving Differentiation Strategy

- a) Offer utility to customers and match the product with their taste and preference.
 - b) Improve/Elevate performance of product
 - c) Offer high-quality product/service for buyer satisfaction.
 - d) Rapid product innovation by investing in R&D.
 - e) Take steps for enhancing the brand image and brand value.
 - f) Fixing product prices based on the unique features of product & buying capacity of customer.
- Differentiate → Customer loyalty → Charge premium

ADVANTAGES OF DIFFERENTIATION STRATEGY

Differentiation strategy enables a Firm to be profitable even with 5 forces of Porter's Five Forces Model:

| Rivalry | Buyer | Supplier | Entrants | Substitute |
|--------------------------------------------------------------------------------------------------------------------------------|-------------------------------------------------------------------------------------------------------|--------------------------------------------------------------------------------------------------------------|--------------------------------------------------------------------------------------------------|----------------------------------------------------------------------------------------------|
| Brand loyalty gives an Organization competitive advantage over rivals as customers will be less sensitive to changes in price. | They do not negotiate for price as they get special features & they have fewer options in the market. | Since differentiation allows Org. to charge higher price, they can absorb increase in price of raw material. | Since, innovative products are expensive to make & offer, it acts as a barrier for new entrants. | Substitutes can't replace differentiated product due to high brand value & customer loyalty. |

DISADVANTAGES OF DIFFERENTIATION STRATEGY

- a) It does not guarantee competitive advantage if standard product sufficiently meets customer needs.
- b) If differentiation is not valued by customer, this strategy fails. In such cases, C.L. strategy is preferred.
E.g. Home delivery of packed snacks in 30 minutes would not even be a differentiator as the consumer wouldn't value such an offer.
- c) In long run, uniqueness is difficult to sustain as competitors may copy differentiating uniqueness.
Firms must find durable sources of uniqueness that cannot be imitated quickly or cheaply by rival firms.

E.g. Amazon Prime offers deliver within two hours. This is quite difficult to imitate by its rivals, and thus this differentiating factor helps it to lead the market.

- d) Charging too high price for differentiated product may cause customers to switch to different product.
E.g. As we see a shift of iPhone users to other android flagship smart phones.

7.3. FOCUS STRATEGY

Focus strategy means an organization concentrates on

- particular group of customers, geographic market or product line
- in order to serve well defined but narrow market
- better than competitors who serve broader market.

Focus strategy is successful when

- a) Consumers have distinctive preferences or requirements,
- b) Industry segment is of sufficient size,
- c) Has good growth potential, and
- d) Not crucial to success of other major competitors.

For example, Ferrari sports cars.

Strategies such as market penetration and market development offer substantial focusing advantages.

Focus strategies are most effective when consumers have distinctive preferences or requirements, and when the rival firms are not attempting to specialize in the same target segment.

Focus strategy can be pursued along with cost leadership strategy or differentiation strategy.

| Focused C.L. strategy | Focused Differentiation strategy |
|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <p>In this, Firm competes with its competitors on price to charge in target narrow market. It does not mean that the Firm charges lowest price in industry. Rather, it charges low price as compared to its competitors in target market.</p> | <p>In this, Firm competes with its competitors based on unique features that fulfills the demand of a narrow market. Here, narrow markets are defined in different ways in different settings. Some Firms using F.D. strategy concentrate their efforts on</p> <ul style="list-style-type: none"> ➤ Particular sale channel likes selling over Internet, or ➤ A particular demographic group. <p>For example, Rolls-Royce sells limited number of high-end, custom-built cars.</p> |

| Achieving Focus Strategy | Advantage | Disadvantage |
|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <ul style="list-style-type: none"> a) Selecting specific niches not covered by CL or differentiator. b) Creating superior skills for catering to such niche market. c) Generating higher efficiency for catering to such niche market. d) Developing Innovative ways for catering to such niche market. | <ul style="list-style-type: none"> a) Premium price can be charged for such specialised product/ service. b) Rivals & new entrants find it difficult to compete due to enhanced expertise in target market. | <ul style="list-style-type: none"> a) Due to limited demand of product, sales may be limited & cost may not be recovered. b) Niche could disappear or be taken over by competitors by acquiring same competencies. c) Firms lacking distinctive competencies may not pursue this strategy. |

Advantages & Disadvantages of Focused Differentiation: To be discussed in Divyastra

7.4. BEST COST PROVIDER STRATEGY

It is further development of 3 generic strategies.

It aims to provide more value to customer by emphasizing on both, lower cost & better-quality upscale differentiated products.

It can be done in following two ways: [Sub strategies]

- a) By offering products at a lower price than what is being offered by rivals for same / similar quality; or
- b) Charging similar price as rivals for better quality product as compared to rivals.

For example, android flagship phones from OnePlus, Xiaomi, Oppo, Vivo, etc., are all rooting for giving better quality at lowest prices to the customers. They are following the best-cost provider strategy to penetrate market.

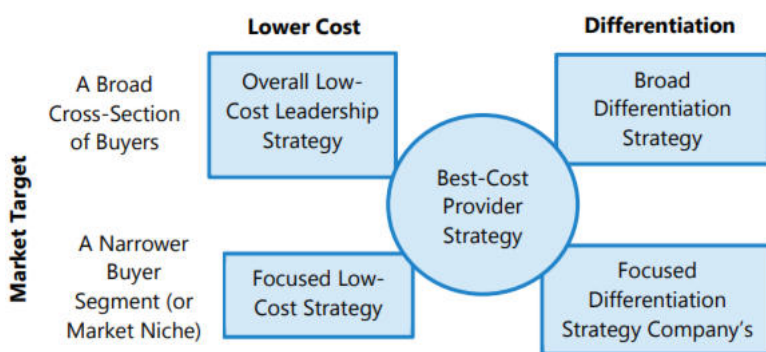


Figure: The Five Generic Competitive Strategies

ACTIVITY FOR MICHAEL PORTER'S GENERIC STRATEGIES

| Business Idea | Michael Porter's Generic Strategy |
|----------------------------------------------------------------------------------------------------------------------------------------|-----------------------------------|
| Building the best-in-class headphones with noise cancellation and premium quality ear cushions | |
| Providing maximum value features in a phone which is within the spendable limits of the middle class of India | |
| Being in a position to dominate the glass manufacturing units across the country and thus using economies of scale to beat competition | |
| Targeting the below poverty line individuals and providing them nutritious meals | |