

Agenda for today

Internal analysis of a firm

- How to identify the firms' strengths and weaknesses?
- How do they compare with that of competitors?
- How can a firm obtain sustainable competitive advantage?
- How can we amalgamate the internal and external analysis of the firm?

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Sustainable competitive advantage

Du Pont Analysis

Measures	Wal-Mart	Target	Kmart
Profitability: Net Income/Sales	0.03	0.04	-0.07
Operating Efficiency: Sales / Assets	2.69	1.54	2.74
Leverage: Assets/Equity	2.41	3.03	32.57
Return on Equity	0.20	0.18	-4.25

Measures
1 Profitability (Net income / Sales)
2 Operating Efficiency (Sales / Assets)
3 Leverage (Asset / Equity)
ROE

Rate at which sales is converted into profits.

Rate at which assets are used to generate sales.

Extent to which the firm relies on debt.

Debt - Interest - Wasteful + tax benefits + ownership. EBITA

Equity

$$\frac{\text{Net Income}}{\text{Sales}} \times \frac{\text{Sales}}{\text{Assets}} \times \frac{\text{Assets}}{\text{Equity}} = \frac{\text{Net Income}}{\text{Equity}}$$

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Theoretical Underpinnings

Resource Based View *Jay Barney. RBV*

- Assumes that a firm's resources and capabilities are the primary drivers of competitive advantage and economic performance
- **Resources** can be either tangible and intangible assets of a firm
 - **tangible:** factories, products
 - **intangible:** reputation
- **Capabilities** are a subset of resources that enable a firm to take full advantage of other resources
 - marketing skill, cooperative relationships

Activities x Resource = Capability.

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Resource Based View

Identifying resources and capabilities *Michael Porter*

The diagram illustrates the flow from resources to margins. It is structured as a funnel pointing to the right, labeled 'MARGIN' at the top and 'MARGIN' at the bottom. The funnel is divided into two main sections: 'Secondary' (top) and 'Primary' (bottom). The 'Secondary' section includes Firm Infrastructure, Human Resource Management, and Technology Development. The 'Primary' section includes Procurement, Inbound Logistics, Operations, Outbound Logistics, Marketing and Sales, and Service. Red checkmarks (✓) are placed under Inbound Logistics, Operations, and Service. Red crosses (✗) are placed under Marketing and Sales. Red arrows point from the 'Secondary' section down to the 'Primary' section, and from the 'Primary' section towards the 'MARGIN' tip of the funnel.

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Resource Based View

Identifying resources and capabilities

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Porters Five Forces

Industry Analysis for Franchise Owners

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Porter's Value Chain

Identifying resources and capabilities

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IT as a resource and capability

The productivity paradox

- Erik Brynjolfsson (1991) CACM, "The Productivity Paradox"
 - Studies on investment in IT and productivity showed that gains in productivity were not realized.
- Why?
 - Mismeasurement of outputs and inputs
 - Lags due to learning and adjustment
 - Redistribution and dissipation of profits
 - Mismanagement of information and technology

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IT as a resource and capability

IT doesn't matter

- Nicholas Carr (2003), "IT Doesn't Matter", *Harvard Business Review*.
 - As IT becomes more ubiquitous, it also becomes less of a differentiator.
 - Technology is so readily available, and software is so easily copied, that new tools will not give companies sustained competitive advantage.
- Carr suggests:
 - Technology is a commodity and should be managed like one.
 - Low cost: Wait until it is cost effective to adopt.
 - Low risk: Adopt slowly so other companies can take the risks associated with new technologies.
 - IT should operate as a utility in a company. Good service with minimal downtime.

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Resource Based View

Four category of resources

- Financial (cash, retained earnings)
- Physical (plant and equipment, geographic location)
- Human (skills and abilities of individuals)
- Organizational (reporting structures, relationships)

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Resource Based View

Two Critical Assumptions

- Resource Heterogeneity
 - Different firms may have different resources.
 - Heterogeneity of resources typically occurs as the result of "bundling" the resources and capabilities of a firm.
- Resource Immobility
 - It may be costly for firms without certain resources to acquire or develop them.
 - Some resources may not spread from firm to firm easily.

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Resource Based View

VRIO Framework

- A resource is judged based on its:
 - Physical
 - Path Dependency
 - Causal Ambiguity
 - Economic
- **Value:** Does the resource enable the firm to exploit an opportunity or neutralize a threat? Does it lead to increase in revenues or decrease in costs?
- **Rarity:** The resource must be scarce enough to avoid perfect competition dynamics and allow the firm to obtain above normal profits
- **Imitability:** Competitors must face a cost disadvantage in imitating the resource. The firm should get sufficient lead time before a duplicate or substitute emerges.
- **Organization:** The structure and control systems of the firm must be aligned to take advantage of the resource.
- If a firm has resources meeting all the above criterion, then it can expect to enjoy **sustained competitive advantage**

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Resource Based View

VRIO Framework

	V VALUABLE	R RARE	I INIMITABLE	O ORGANIZED	
NO					COMPETITIVE DISADVANTAGE
YES		NO			COMPETITIVE PARITY
YES	YES	YES	NO		TEMPORARY COMPETITIVE ADVANTAGE
YES	YES	YES	NO		UNUSED COMPETITIVE ADVANTAGE
YES	YES	YES	YES		SUSTAINABLE COMPETITIVE ADVANTAGE

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SWOT

Combining internal and external analysis of firm

Supplier *Substitutes (online)*
Rivalry

	Opportunities (external, positive)	Threats (external, negative)
Strengths (internal, positive)	Strength-Opportunity strategies <i>New Category</i> Which of the company's strengths can be used to maximize the opportunities you identified? 1 <i>Online/Retail mkt</i>	Strength-Threats strategies How can you use the company's strengths to minimize the threats you identified? 2 <i>Pricing, M&A</i>
Weaknesses (internal, negative)	Weakness-Opportunity strategies What action(s) can you take to minimize the company's weaknesses using the opportunities you identified? 3	Weakness-Threats strategies How can you minimize the company's weaknesses to avoid the threats you identified? 4

Supply Chain info.
Customer Relationship

- Automation
- Segmentation - multi format retail *- Survey*
- Hand delivery

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Summary

- Resource Based View
- Difference between resources and capabilities
- Porters Value Chain
- Four categories of resources
- Assumptions of RBV
- VRIO framework
- SWOT based Strategies

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