Lecture 3

Environmental Scanning and Industry Analysis
Environments

Environmental uncertainty:

*The degree of complexity plus the degree of change existing in an organization’s external environment.*
Environments

Environmental scanning:

The monitoring, evaluating, and disseminating of information from the external and internal environments to key people within the corporation to avoid strategic surprise and ensure the long-term health of the firm.
External Environment

External Environmental Variables:

Societal/community environment:

*General forces that do not directly touch on the short-run activities but often influence its long-run decisions.*
External Environment

External Environmental Variables:

Task environment:
Those elements or groups that directly affect the corporation and, in turn, are affected by it. The task environment is the industry within which that firm operates.
External Environment

External Environmental Variables:

Industry analysis:

An in-depth examination of key factors within a corporation’s task environment.
External Environment

Analysis of Societal Environment
Economic, Sociocultural, Technological, Political–Legal Factors

- Market Analysis
- Community Analysis
- Competitor Analysis
- Supplier Analysis
- Interest Group Analysis

Selection of Strategic Factors
- Opportunities
- Threats

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External Environment

Societal environment forces:

• Economic forces
  – Regulate the exchange of materials, money, energy, and information

• Technological forces
  – Generate problem-solving inventions
External Environment

Societal environment forces:

• Political-legal forces
  – Allocate power, provide laws and regulations

• Socio-cultural forces
  – Regulate values, mores\traditions, and customs
# Societal Environment

## Important Variables

<table>
<thead>
<tr>
<th>Economic</th>
<th>Technological</th>
<th>Political-Legal</th>
<th>Sociocultural</th>
</tr>
</thead>
<tbody>
<tr>
<td>GDP trends</td>
<td>Total government spending for R&amp;D</td>
<td>Antitrust regulations</td>
<td>Lifestyle changes</td>
</tr>
<tr>
<td>Interest rates</td>
<td>Total industry spending for R&amp;D</td>
<td>Environmental protection laws</td>
<td>Career expectations</td>
</tr>
<tr>
<td>Money supply</td>
<td>Focus of technological efforts</td>
<td>Tax laws</td>
<td>Consumer activism</td>
</tr>
<tr>
<td>Inflation rates</td>
<td>Patent protection</td>
<td>Special incentives</td>
<td>Rate of family formation</td>
</tr>
<tr>
<td>Unemployment levels</td>
<td>New products</td>
<td>Foreign trade regulations</td>
<td>Growth rate of population</td>
</tr>
<tr>
<td>Wage/price controls</td>
<td>New developments in technology transfer from</td>
<td>Attitudes toward foreign companies</td>
<td>Age distribution of population</td>
</tr>
<tr>
<td>Devaluation/revaluation</td>
<td>lab to marketplace</td>
<td>Laws on hiring and promotion</td>
<td>Regional shifts in population</td>
</tr>
<tr>
<td>Energy availability and</td>
<td>Productivity improvements through automation</td>
<td>Stability of government</td>
<td>Life expectancies</td>
</tr>
<tr>
<td>cost</td>
<td></td>
<td></td>
<td>Birth rates</td>
</tr>
<tr>
<td>Disposable and</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>discretionary income</td>
<td></td>
<td></td>
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</tr>
</tbody>
</table>

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External Environment

Socio-cultural Trends

- Increasing environmental awareness
- Growth of the seniors market
- Decline of the mass market
- Changing pace and location of life
- Changing household composition
- Increasing diversity of workforce and markets
Workforce Diversity

• Heterogeneous workforce in terms of gender, race, ethnicity, and age.
  • workforce is getting older
  • In US Asians and Hispanics are an increasingly large percentage of workforce
    – “melting pot” approach versus celebration of differences
External Environment

External Strategic Factors

Factors influencing the choice of the strategic factors:

– Personal values of managers
– Functional experience of managers
– Success of current strategies
– Strategic myopia/ shortsightedness
  • Willingness to reject unfamiliar as well as negative information
External Environment

Issues Priority Matrix

• Identify likely trends:
  – Societal and task environments
    • Strategic environmental issues

• Assess probability of trends occurring
  – Low to High

• Ascertain\find likely impact of trends on the corporation
  – Low to High
Issues Priority Matrix

![Issues Priority Matrix Diagram](image-url)

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External Strategic Factors

Defined:

*Key environmental trends that are judged to have both a medium to high probability of occurrence and a medium to high probability of impact on the corporation.*

• *Those environmental trends judged to be a corporation’s strategic factors are then categorized as opportunities and threats and are included in strategy formulation.*
Industry Analysis

Industry

A group of firms producing a similar product or service, such as soft drinks, health services or financial services.
Industry Analysis

Potential Entrants

Relative Power of Unions, Governments, etc.

Threat of New Entrants

Other Stakeholders

Industry Competitors

Rivalry Among Existing Firms

Threat of Substitute Products or Services

Suppliers

Bargaining Power of Suppliers

Bargaining Power of Buyers

Substitutes

Buyers

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Industry Analysis

Porter’s approach:

Assess the six forces --

• Threat of new entrants
• Rivalry among existing firms
• Threat of substitute products
• Bargaining power of buyers
• Bargaining power of suppliers
• Relative power of other stakeholders
Industry Analysis

Threat of New Entrants --

Barriers to entry:

- Economies of Scale
- Product Differentiation
- Capital Requirements
- Switching Costs
- Access to Distribution Channels
- Cost Disadvantages Independent of Size
- Government Policy
Industry Analysis

Rivalry Among Existing Firms --

Intense rivalry related to:

- Number of competitors
- Rate of Industry Growth
- Produce or Service Characteristics
- Amount of Fixed Costs
- Capacity
- Height of Exit Barriers
- Diversity of Rivals
Industry Analysis

Threat of Substitute Products/Services

Substitute Products:

Those products that appear to be different but can satisfy the same need as another product. To the extent that switching costs are low, substitutes can have a strong effect on an industry.
Industry Analysis

Bargaining Power of Buyers --

Buyer is powerful when:

- Buyer purchases large proportion of seller’s products
- Buyer has the potential to integrate backward
- Alternative suppliers are plentiful
- Changing suppliers costs very little
- Purchased product represents a high percentage of a buyer’s costs
- Buyer earns low profits
- Purchased product is unimportant to the final quality or price of a buyer’s products
Industry Analysis

Bargaining Power of Suppliers --

Supplier is powerful when:
• Supplier industry is dominated by a few companies but sells to many
• Its product is unique and/or has high switching costs
• Substitutes are not readily available
• Suppliers are able to integrate forward and compete directly with present customers
• Purchasing industry buys only a small portion of the supplier’s goods.

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Industry Analysis

Industry Evolution

most industries evolve through a series of stages from growth to decline.

Fragmented Industry –

*No firm has large market share and each firm serves only a small piece of the total market in competition with others.*

Consolidated Industry –

*Dominated by a few large firms, each of which struggles to differentiate its products from the competition.*

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Continuum\range of International Industries

**Multidomestic**

Industry in which companies tailor their products to the specific needs of consumers in a particular country.

- Retailing
- Insurance
- Banking

**Global**

Industry in which companies manufacture and sell the same products, with only minor adjustments made for individual countries around the world.

- Automobiles
  - Tires
  - Television sets
Industry Analysis

Global Industries

Classifying Industry primarily multidomestic or primarily global based on:

Pressure for coordination
  – Within the multinationals in that industry
  – Pressure for local responsiveness
    – On the part of Individual country market.

If the pressure for coordination with multinationals is strong and the pressure for local responsiveness is weak within a particular industry, the industry is global.

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Industry Analysis

Strategic Groups

Defined:

A set of business units or firms that pursue similar strategies with similar resources.
Strategic group analysis

• “Aims to identify organizations with similar strategic characteristics, following similar strategies or competing on similar bases”.

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Some characteristics for identifying strategic groups

To measure how org. are differ based on the following characteristics:
1- The extent of product diversity.
2- Extent of geographical coverage.
3- Number of market segment served.
4- Distribution channels used.
5- Number of branding.
6- Product quality.
7- Technological leadership.
8- R&D capability.
9- Cost position.
10- Utilization of capacity.
11- Separate company, or relationship with parent.
12- Relationship to influence groups, e.g., government.
13- Size of organization.
Why strategic group analysis is important?

• Identify who most direct competitor.
• On what basis the competitors are competing on.
• It raises the question of how possible to move from one group to another.
Industry Analysis

**Strategic Types**

it is used to analyze the level of competitive intensity within a particular industry.

Defined:

*Category of firms based on a common strategic orientation and a combination of structure, culture, and processes consistent with that strategy.*
Industry Analysis

Strategic Types –

Categorized by one of four general strategic orientations:

• Defenders
  – Companies with a limited product line; focus on improving efficiency of current operations
Industry Analysis

Strategic Types (continued)–

• Prospectors:
  – Companies with fairly broad product lines; focus on product innovation and market opportunities.
Industry Analysis

Strategic Types (continued)

• Analyzers:
  – Corporations that operate in at least two different product-market areas – one stable and one variable.
Industry Analysis

Strategic Types (concluded)–

• Reactors:
  – Corporations that lack a consistent strategy-structure-culture relationship.
## Industry Matrix

<table>
<thead>
<tr>
<th>Key Success Factors</th>
<th>Weight</th>
<th>Company A Rating</th>
<th>Company A Weighted Score</th>
<th>Company B Rating</th>
<th>Company B Weighted Score</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>1</td>
<td>2</td>
<td>3</td>
<td>4</td>
<td>5</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>1.00</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Industry Analysis

Forecasting Techniques:

Extrapolation: the extension of present trends into the future. It rests on the assumption that the world change slowly. Time-series methods are used.

- Brainstorming
- Expert opinion
- Statistical modeling
- Scenario writing: upon a series of historical data plus informed hunches from key people
## External Factor Analysis Summary (EFAS)

<table>
<thead>
<tr>
<th>External Factors</th>
<th>Impact on company</th>
<th>company Response rate</th>
<th>Response Rate</th>
<th>Comments</th>
</tr>
</thead>
<tbody>
<tr>
<td>Opportunities</td>
<td>1</td>
<td>2</td>
<td>3</td>
<td>4</td>
</tr>
<tr>
<td>Threats</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total Weighted Score</td>
<td>1.00</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

### Notes:
1. List opportunities and threats (5–10) in column 1.
2. Weight each factor from 1.0 (Most Important) to 0.0 (Not Important) in Column 2 based on that factor’s probable impact on the company’s strategic position. The total weights must sum to 1.00.
3. Rate each factor from 5 (Outstanding) to 1 (Poor) in Column 3 based on the company’s response to that factor.
4. Multiply each factor’s weight times its rating to obtain each factor’s weighted score in Column 4.
5. Use Column 5 (comments) for rationale used for each factor.
6. Add the weighted scores to obtain the total weighted score for the company in Column 4. This tells how well the company is responding to the strategic factors in its external environment.

**Source:** T. L. Wheelen and J. D. Hunger, “External Strategic Factors Analysis Summary (EFAS).” Copyright © 1991 by Wheelen and Hunger Associates. Reprinted by permission.
## External Factor Analysis Summary (EFAS) - Maytag Example

<table>
<thead>
<tr>
<th>External Factors</th>
<th>Weight</th>
<th>Rating</th>
<th>Weighted Score</th>
<th>Comments</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Opportunities</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>• Economic integration of</td>
<td>.20</td>
<td>4</td>
<td>.80</td>
<td>Acquisition of Hoover</td>
</tr>
<tr>
<td>European Community</td>
<td></td>
<td></td>
<td></td>
<td>Maytag quality</td>
</tr>
<tr>
<td>• Demographics favor quality</td>
<td>.10</td>
<td>5</td>
<td>.50</td>
<td>Low Maytag presence</td>
</tr>
<tr>
<td>appliances</td>
<td></td>
<td></td>
<td></td>
<td>Will take time</td>
</tr>
<tr>
<td>• Economic development of</td>
<td>.05</td>
<td>1</td>
<td>.05</td>
<td>Maytag weak in this channel</td>
</tr>
<tr>
<td>Asia</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>• Opening of Eastern Europe</td>
<td>.05</td>
<td>2</td>
<td>.10</td>
<td></td>
</tr>
<tr>
<td>• Trend to “Super Stores”</td>
<td>.10</td>
<td>2</td>
<td>.20</td>
<td></td>
</tr>
<tr>
<td><strong>Threats</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>• Increasing government regulations</td>
<td>.10</td>
<td>4</td>
<td>.40</td>
<td>Well positioned</td>
</tr>
<tr>
<td>• Strong U.S. competition</td>
<td>.10</td>
<td>4</td>
<td>.40</td>
<td>Well positioned</td>
</tr>
<tr>
<td>• Whirlpool and Electrolux strong globally</td>
<td>.15</td>
<td>3</td>
<td>.45</td>
<td>Hoover weak globally</td>
</tr>
<tr>
<td>• New product advances</td>
<td>.05</td>
<td>1</td>
<td>.05</td>
<td>Questionable</td>
</tr>
<tr>
<td>• Japanese appliance companies</td>
<td>.10</td>
<td>2</td>
<td>.20</td>
<td>Only Asian presence is Australia</td>
</tr>
<tr>
<td><strong>Total Scores</strong></td>
<td>1.00</td>
<td></td>
<td>3.15</td>
<td></td>
</tr>
</tbody>
</table>
Review

• How can a decision maker identify external strategic factors in a corporation's external international environment?

• What can a corporation do to ensure that information about strategic environmental factors gets to the attention of strategy makers?
Group discussion

• What are the forces driving industry competition in the airline industry?
• The first part of the exercise evaluate each of the current forces driving industry competition.
• indicate whether they marked high, medium, or low for each force.
• which of these forces are changing and why.
• evaluate the future level of competitive intensity in the airline industry. Would they invest or look for a job in this industry?