# 25 NEED TO KNOW

# STRATEGY TOOLS

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## Praise for **25 need-to-know strategy tools**

"This is a highly practical, punchy and brilliantly written guide to strategy development. It is perfect for managers of large and small businesses who need to make big decisions, but have limited time for long tomes on business theory. An excellent read."

Charles Ind, Managing Partner, Bowmark Capital LLP

"I wish I had written this book: extremely practical and clear, but full of rich content. It is a terrific compendium of all the major strategy tools, brought to life with great examples. Definitely the best strategy book around for people who think they can't read strategy books."

Marcus Alexander, Strategy Professor, London Business School

"This book does a superb job demystifying strategy and bringing it within the reach of anyone who takes the time to read it and apply the tools. Strategy made simple."

Jeff van der Eems, Chief Executive Officer, United Biscuits International

"An excellent guide to setting strategy for businesses large and small. I particularly liked the focus on really understanding the sources of sustainable competitive advantage in the key areas of a business. The techniques described for achieving this, combined with the recommended emphasis on detailed quantitative analysis, will be of great benefit to any enterprise."

Adrian Beecroft, Chairman, Dawn Capital and former Chief Investment Officer, Apax Partners your competitors getting an average operating margin of a certain per cent.

But will competitive forces conspire to threaten that margin over the next few years? Or has the industry competition of the last few years been unsustainable and likely to ease off in the future?

In short, what will be the effect of competitive dynamics on pricing in your industry over the next few years?

Will competition intensify and put pressure on prices? Will it stay more or less as is and pricing move as it has been doing in recent times? Or will competition ease off, enabling players to nudge up pricing over the next few years?

## When to use it – or be wary

I cannot recall a strategy assignment when I did not deploy this tool. It is an essential arrow in the strategist's quiver.

But it has had its critics over the years. Some believe that boundary definition – this activity is part of the industry you operate in, that activity is not – can, in itself, place strategy development in a straitjacket. Pioneering companies succeed by redefining industry boundaries – see, for example, blue ocean strategy, Tool 15.

This critique can often be addressed by further segmentation – by returning to Tool 1 and redefining key product/market segments to allow for shifting boundaries.

Other critics have promoted the corporate environment (government, the regulatory framework, pressure groups, etc.) as a sixth force, while still others believe that complements, as distinct from substitutes, should be a separate and sixth force.

These are valid points, but to an extent industry-specific, with some industries more affected by such forces than others. Porter himself recognises the influence of these forces, but incorporates them effectively as sub-forces to his five main forces.

Kevin Coyne and Somu Subramaniam challenged Porter's model in 2001 on three grounds. They questioned these assumptions:

- An industry consists of a set of unrelated buyers, sellers, substitutes and competitors that interact at arm's length – with little allowance made for codependent systems, such as strategic alliances, networks and webs, or privileged relationships, whether based on financial interest, friendship, trust or ethnic loyalty.
- Wealth will accrue to companies that erect barriers against competitors and potential entrants, in other words the source of value is structural advantage – with little allowance made for management, whether through frontline execution or insight/foresight.
- Uncertainty is low, allowing the prediction of competitive response and contingency planning – with little allowance made for differing degrees of uncertainty, ranging from the structural, where the model may be valid, through alternative scenarios and continuous uncertainty to complete ambiguity, where the model is invalid.

The authors make valid points, and the first bullet, especially, needs to be borne in mind in industry analysis. But they offer a revised industry model, reinforced by a risk-adjusted situation analysis, which is so complex that they fail to spot the true genius of Porter's model. It is a starting point for industry analysis and strategy development, not the end point. Its simplicity is its overriding virtue.

Finally, Porter's model has taken some hits from those who point out, conclusively, as in the second bullet above, that industry structure alone tends to be insufficient to explain differences in profitability. Richard Rumelt, for example, in a 1991 study, found that differences in firms' profitability can be attributed much more to specific 'firm effects' (44 per cent) than to 'industry effects' (4 per cent). (Incidentally, the unexplained variance was 45 per cent.) Other studies have shown likewise.

But this does not invalidate the model. Industry analysis is part of the strategy story and Porter's Five Forces model a very large part of industry analysis. It is not the final word, but arguably the most critical tool in a strategy development toolkit.

**case study**

## Using it: Blockbuster

There are times when all of Porter's five forces seem to conspire against an industry sector. Just ask Blockbuster.

At its peak in the mid-2000s, Blockbuster had over 4,000 video/DVD/game rental shops throughout the USA, employing over 60,000 people. It was also the largest such chain in Canada and the UK and had operations in 17 countries. By the time it filed for Chapter 11 bankruptcy in September 2010, only 700 stores were still trading in the USA. What had gone wrong?

The industry had moved on. As for its main competitor, Movie Gallery Inc. (with Hollywood Video and Game Crazy), which preceded Blockbuster by three years into bankruptcy, the five forces were arraigned against them:

- Industry rivalry (1) had intensified due to dampened demand, caused by:
  - new entrants (2) that focused on alternative, consumer-friendly distribution methods, in particular by post (Netflix, with less demanding return requirements) and pick-up kiosks (Redbox)
  - substitute products, (3) especially video on-demand services from streaming over the Internet (Netflix again, far ahead of Blockbuster's own streaming product).
- Meanwhile consumers (4) have become savvier and able to select from a wider variety of competing offerings for movies, television and games, thereby putting pressure on pricing.
- Suppliers (5) were becoming more demanding, as the bargaining power of the bricks and mortar movie and game rental chains waned.

Blockbuster was bought at auction by Dish Network, the satellite television service provider. Dish resolved to deploy the Blockbuster brand to compete directly with Netflix and to keep 90 per cent of stores open. These plans seemed highly optimistic and, indeed, were soon scaled back to retaining only the most profitable branches. Two years later, however, it was with a sense of inevitability, given the mal-alignment of the five forces against it, that Dish announced the closure of all remaining Blockbuster stores.

Progress was blocked, the chain busted.

# 7

# Rating competitive position

## This tool will help you:

- Rate your firm's performance against the key success factors in each main segment
- Assess how well positioned your firm is in each segment
- Target the strategic gap between where you are today and where you should aim to be in the future

## About this tool

'A man can't be too careful in the choice of his enemies', said Oscar Wilde. So, too, perhaps, with firms and their choice of where and with whom to compete.

With whom have you chosen to compete? And how do you rate against them?

How is your overall competitive position? And theirs? How do your relative positions differ by product/market segment?

In this tool you will rate your competitive position against each key competitor, over time and for each main segment.

You could do this right now, at your desk, based on feedback you and your sales and purchasing teams have received from customers and suppliers over the years. Or you could do it more methodically, via a structured interviewing programme, primarily of customers.

In this analysis you will assess your strengths and weaknesses and those of your peers. It will pinpoint your source of competitive advantage – as well as that of your most formidable competitor.

## How to use it

There are three stages in rating competitive position and you should follow these for each of your firm's main product/market segments:

1. Identify and weight customer purchasing criteria (CPCs) – what customers need from their suppliers in each segment, that is you and your competitors
2. Derive and weight key success factors (KSFs) – what you and your competitors need to do to satisfy these customer needs and run a successful business
3. Rate your competitive position – how you rate against those key success factors relative to your competitors.

We'll assume, for the purposes of this book, that you have already undertaken the first two stages and have derived and weighted KSFs for each of your main product/market segments – either methodically or using your business judgement. As a check, you might choose to take a quick look at Tools 23 and 24 in this book's more comprehensive partner, *Key Strategy Tools*, where the processes for identifying CPCs and deriving KSFs are set out in detail.

The process of rating competitive position is straightforward. Use a 0–5 rating system. If you perform about the same as your peers against a KSF, give yourself a score in the middle, a 3 (good, favourable). If you perform very strongly, even dominantly, a 5 (very strong). Poorly, a 1 (weak). If you perform not quite as well as most others, give yourself a 2 (tenable). Better than most, a 4 (strong).

Now do the same for each of your competitors against that KSF. Who's the best performer against this KSF? Do they merit a 5, or are they better but not **that** much better than others, for a 4?

And so on against each KSF.

If you've used Excel, your competitive position literally falls out at the bottom of the spreadsheet. Your overall rating is the sum of each rating (r) against each KSF, multiplied by the percentage weighting (w) of the KSF. If there are n KSFs, your overall rating will be **(r1 * w1) + (r2 * w2) + (r3 * w3) + .... + (rn * wn)**. As long as the percentage weightings add up to 100 per cent, you should get the right answer.

Figure 7.1 gives an example, one adapted from a recent strategy assignment. It shows that the company was the leading player in its niche UK engineering market, but there was no room for complacency. The company had the largest presence in the market,

| Key success factors in UK engineering niche market | Weighting | The company | Competitor A | Competitor B |
|---|---|---|---|---|
| **Market share** | 15% | 5 | 3.3 | 2 |
| **Cost factors** | 35% | 4 | 3.5 | 2.5 |
| **Differentiation factors:** Product capability and range | 15% | 4 | 4.5 | 3 |
| Product reliability | 15% | 4 | 4 | 2.5 |
| Engineering service network | 10% | 5 | 3.5 | 2.5 |
| Customer service | 10% | 3 | 3 | 2 |
| **Competitive position** | **100%** | **4.2** | **3.6** | **2.5** |

Key: 1 = Weak, 2 = Tenable, 3 = Favourable, 4 = Strong, 5 = Dominant

**Figure 7.1** **Competitive position: an example**