[Academic Script]
[Internal Environment Analysis]

Subject:	Business Economics
Course:	B.A., 6th Semester, Undergraduate
Paper No. & Title:	Paper – 602 Business Strategy & Ethics
Unit No. & Title:	Unit - 2 Environmental Analysis
Lecture No. & Title:	3: Internal Environment Analysis

Internal environment

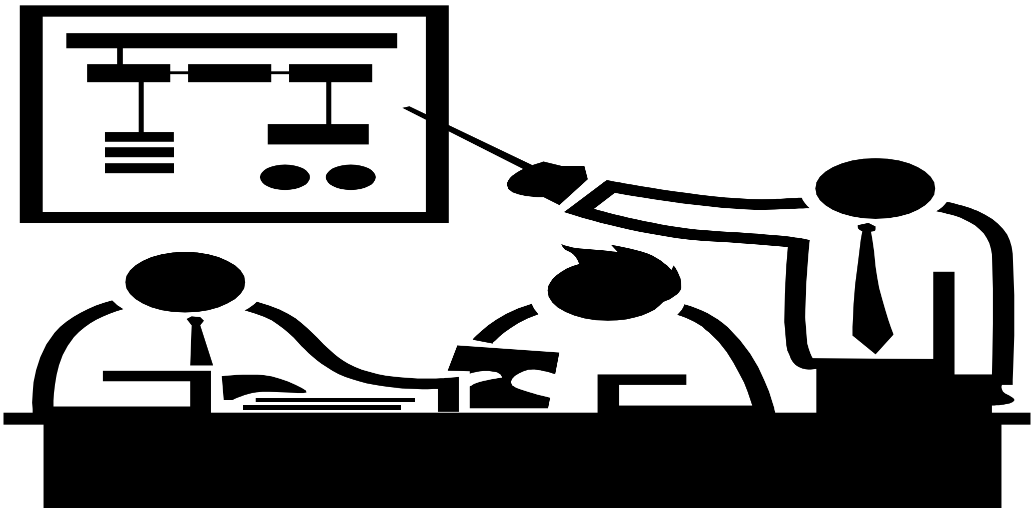
Introduction:

Studying this chapter should provide students with the strategic management knowledge needed to:

1. Explain the need for firms to study and understand their internal environment.
2. Define value and discuss its importance.
3. Describe the differences between tangible and intangible resources.
4. Define capabilities and discuss how they are developed.
5. Describe four criteria used to determine whether resources and capabilities are core competencies.
6. Explain how value chain analysis is used to identify and evaluate resources and capabilities.
7. Define outsourcing and discuss the reasons for its use
8. To understand the importance of company profile.
9. Define company’s strength and weakness.

- **Value of Systematic Internal Assessment**

Internal Analyses' Outcomes



Unique resources, capabilities, and competencies (*required for sustainable competitive advantage*). By studying the internal environment, firms identify what they *can do*

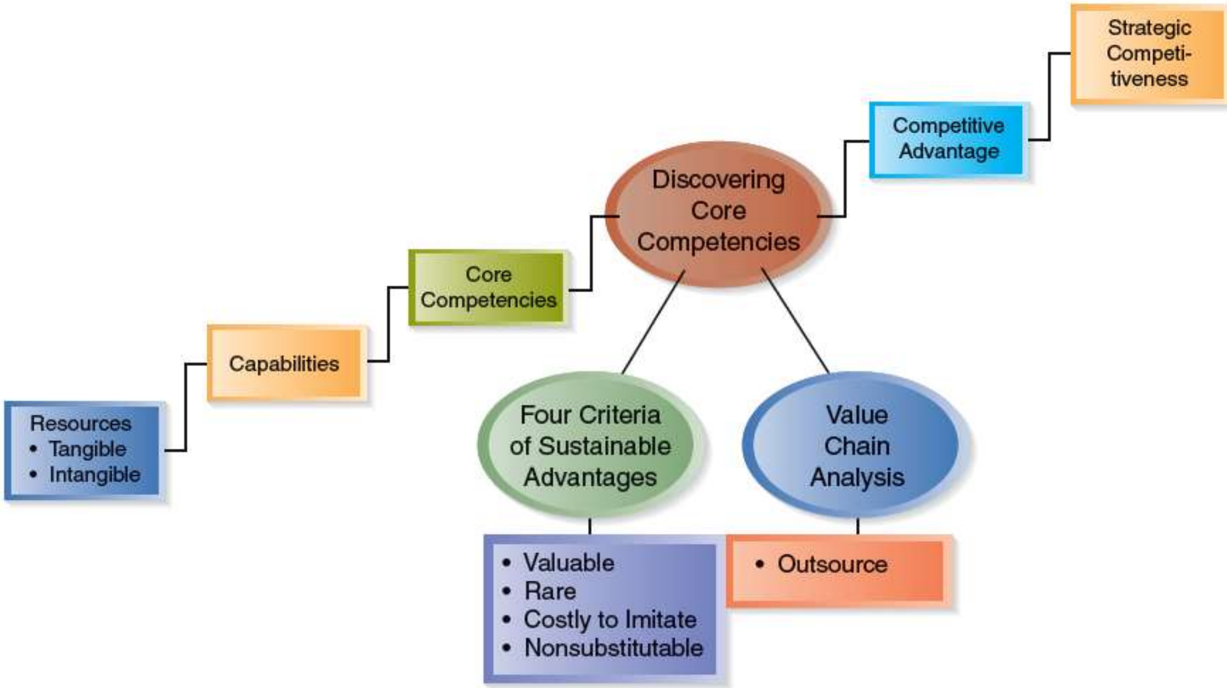
The Context of Internal Analysis

- **Global Economy**

  - Traditional sources of advantages can be overcome by competitors' international strategies and by the flow of resources throughout the global economy.

- **Global Mind-Set**
    - The ability to study an internal environment in ways that are not dependent on the assumptions of a single country, culture, or context.
- **Analysis Outcome**
    - Understanding how to leverage the firm's bundle of heterogeneous resources and capabilities.

Components of Internal Analysis Leading to Competitive Advantage and Strategic Competitiveness



Creating Value

- By exploiting their core competencies or competitive advantages, firms create value.
- **Value is measured by:**
  - Product performance characteristics
  - Product attributes for which customers are willing to pay

- **Firms create value by innovatively bundling and leveraging their resources and capabilities.**
- **Superior value → Above-average returns**

Creating Competitive Advantage

- Core competencies, in combination with product-market positions, are the firm's most important sources of competitive advantage.
- Core competencies of a firm, in addition to its analysis of its general, industry, and competitor environments, should drive its selection of strategies.

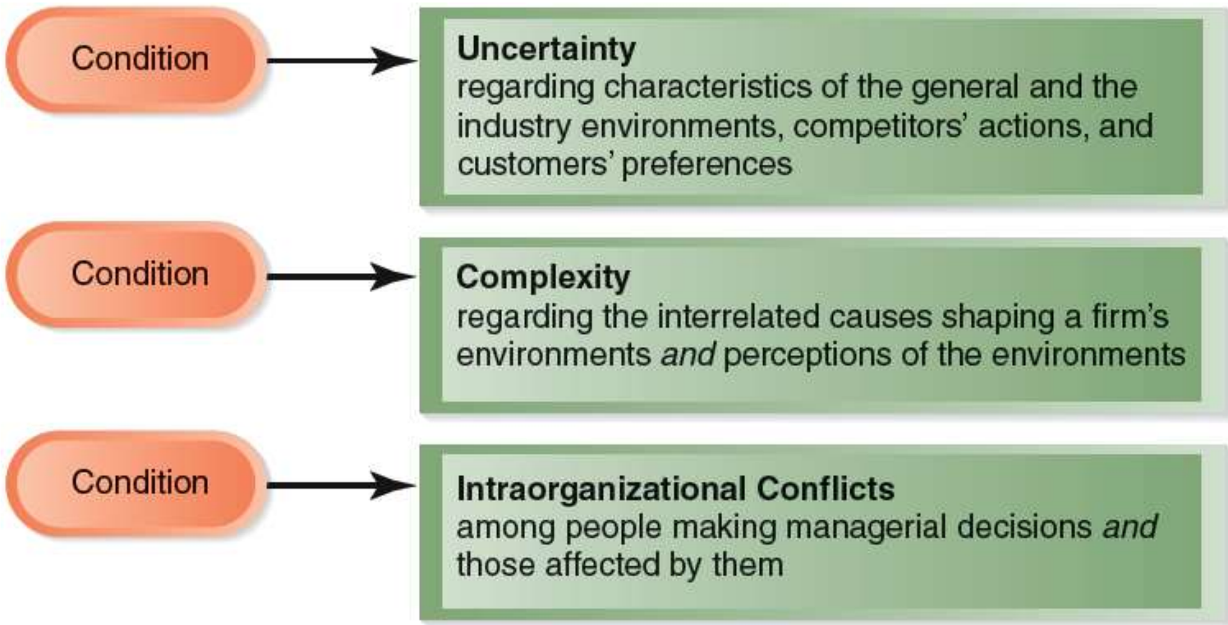
The Challenge of Internal Analysis

- **Strategic decisions in terms of the firm's resources, capabilities, and core competencies:**
  - Are non-routine.
  - Have ethical implications.
  - Significantly influence the firm's ability to earn above-average returns.

- **To develop and use core competencies, managers must have:**
  - Courage
  - Self-confidence
  - Integrity

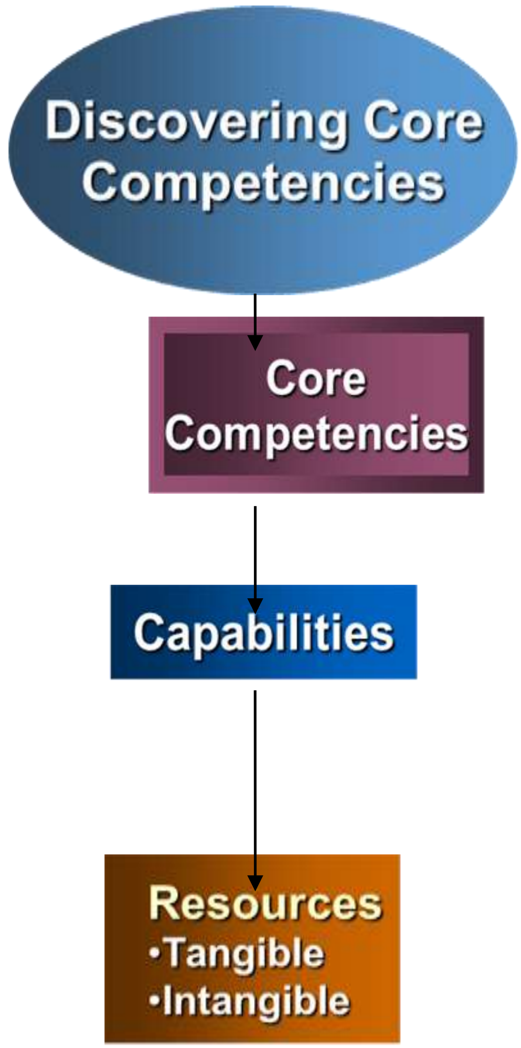
- ➢ The capacity to deal with uncertainty and complexity
- ➢ A willingness to hold people (and themselves) accountable for their work

Conditions Affecting Managerial Decisions about Resources, Capabilities, and Core Competencies



- **Resources**
  - ➢ Are the sources of a firm's capabilities?
  - ➢ Are broad in scope.
  - ➢ Cover a spectrum of individual, social and organizational phenomena.

➢ Alone, do not yield a competitive advantage.



➢ Are a firm's assets, including people and the value of its brand name.

➢ Represent inputs into a firm's production process, such as:

- Capital equipment
- Skills of employees
- Brand names
- Financial resources

- Talented managers

- **Types of Resources**
  - **Tangible resources**
    - Financial resources
    - Physical resources
    - Technological resources
    - Organizational resources
  - **Intangible resources**
    - Human resources
    - Innovation resources
    - Reputation resources

- **Human Resources**
  - Knowledge
  - Trust
  - Managerial capabilities
  - Organizational routines

Innovation Resource:

Ideas

Scientific capabilities

Capacity to innovate

- **Reputational Resources:**
  - Reputation with Brand name
  - Perceptions of product
  - Reputation with suppliers
  - For efficient, effective, supportive, and mutually beneficial interactions and relationships
  - quality, durability, and reliability
- **Capabilities**
  - Represent the capacity to deploy resources that have been purposely integrated to achieve a desired end state
  - Emerge over time through complex interactions among tangible and intangible resources
  - Often are based on developing, carrying and exchanging information and knowledge through the firm's human capital
  - The foundation of many capabilities lies in:
    - The unique skills and knowledge of a firm's employees
    - The functional expertise of those employees
  - Capabilities are often developed in specific functional areas or as part of a functional area.

- **Four criteria for determining strategic capabilities:**
    - Value
    - Rarity
    - Costly-to-imitate
    - Non substitutability

- **Core Competencies**
    - Resources and capabilities that are the sources of a firm's competitive advantage:
        - Distinguish a company competitively and reflect its personality.
        - Emerge over time through an organizational process of accumulating and learning how to deploy different resources and capabilities.
        - Activities that a firm performs especially well compared to competitors.
        - Activities through which the firm adds unique value to its goods or services over a long period of time.

Building Core Competencies

Four Criteria of Sustainable Competitive Advantage

- Valuable capabilities
- Rare capabilities
- Costly to imitate
- Non substitutable

- **Valuable Capabilities** •
- Help a firm neutralizes threats or exploit opportunities.
- **Rare Capabilities** •

Are not possessed by many others

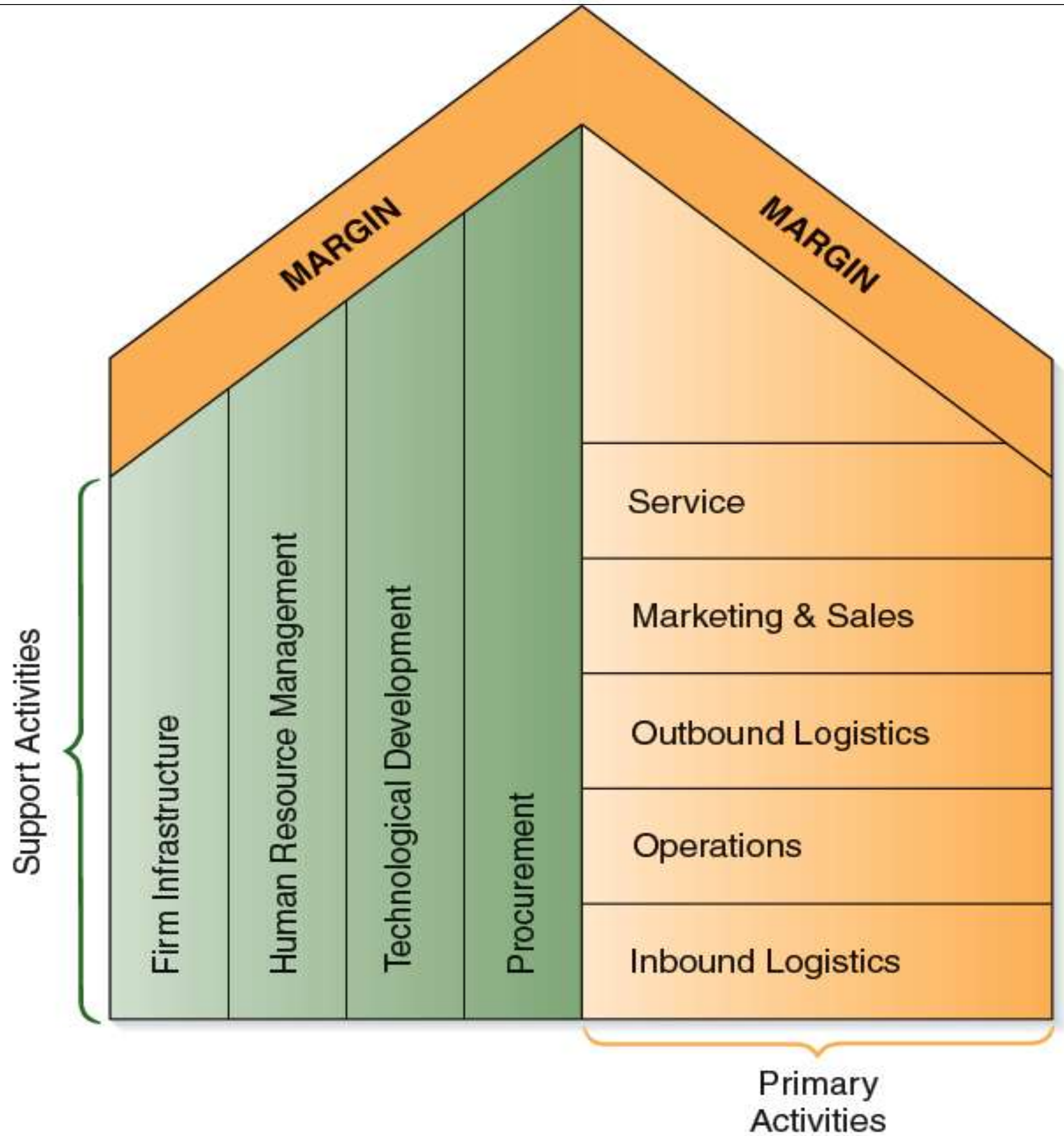
- **Costly-to-Imitate Capabilities**
- Historical: A unique and a valuable organizational culture or brand name
- Ambiguous cause: The causes and uses of a competence are unclear
- Social complexity: Interpersonal relationships, trust, and friendship among managers, suppliers, and customers
- **Non substitutable Capabilities**
  - No strategic equivalent
    - Firm-specific knowledge
    - Organizational culture

- Superior execution of the chosen business model

Value Chain Analysis

- Allows the firm to understand the parts of its operations that create value and those that do not.
- **A template that firms use to:**
  - Understand their cost position.
  - Identify multiple means that might be used to facilitate implementation of a chosen business-level strategy.
- **Primary activities involved with:**
  - A product's physical creation
  - A product's sale and distribution to buyers
  - The product's service after the sale
- **Support Activities**
  - Provide the assistance necessary for the primary activities to take place.

- **Value Chain**
  - Shows how a product moves from the raw-material stage to the final customer.
  - To be a source of competitive advantage, a resource or capability must allow the firm:
  - To perform an activity in a manner that is superior to the way competitors perform it, or
  - To perform a value-creating activity that competitors cannot complete



Examining the Value-Creating Potential of Primary Activities

Inbound Logistics

Activities, such as materials handling, warehousing, and inventory control, used to receive, store, and disseminate inputs to a product.

Operations

Activities necessary to convert the inputs provided by inbound logistics into final product form. Machining, packaging, assembly, and equipment maintenance are examples of operations activities.

Outbound Logistics

Activities involved with collecting, storing, and physically distributing the final product to customers. Examples of these activities include finished goods warehousing, materials handling, and order processing.

Marketing and Sales

Activities completed to provide means through which customers can purchase products and to induce them to do so. To effectively market and sell products, firms develop advertising and promotional campaigns, select appropriate distribution channels, and select, develop, and support their sales force.

Service

Activities designed to enhance or maintain a product's value. Firms engage in a range of service-related activities, including installation, repair, training, and adjustment.

Each activity should be examined relative to competitors' abilities. Accordingly, firms rate each activity as superior, equivalent, or inferior.

Examining the Value-Creating Potential of Support Activities

Procurement

Activities completed to purchase the inputs needed to produce a firm's products. Purchased inputs include items fully consumed during the manufacture of products (e.g., raw materials and supplies, as well as fixed assets—machinery, laboratory equipment, office equipment, and buildings).

Technological Development

Activities completed to improve a firm's product and the processes used to manufacture it. Technological development takes many forms, such as process equipment, basic research and product design, and servicing procedures.

Human Resource Management

Activities involved with recruiting, hiring, training, developing, and compensating all personnel.

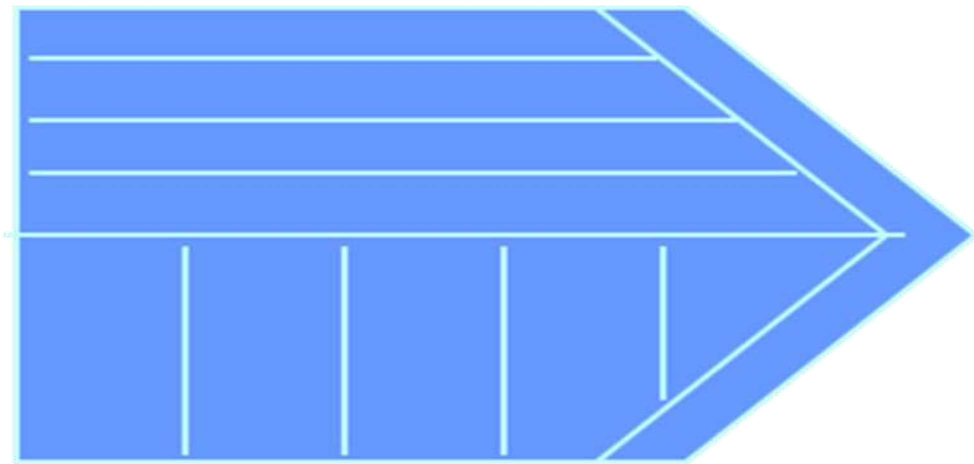
Firm Infrastructure

Firm infrastructure includes activities such as general management, planning, finance, accounting, legal support, and governmental relations that are required to support the work of the entire value chain. Through its infrastructure, the firm strives to effectively and consistently identify external opportunities and threats, identify resources and capabilities, and support core competencies.

(Remain)

Each activity should be examined relative to competitors' abilities. Accordingly, firms rate each activity as *superior, equivalent,* or *inferior.*

Value Chains are part of a *Total Value System*



Supplier Value Chain

It is an Upstream Value

It performs valuable activities that complement the firm's activities

Channel Value Chain

Each firm must eventually find a way to become a part of *some* buyer's value chain

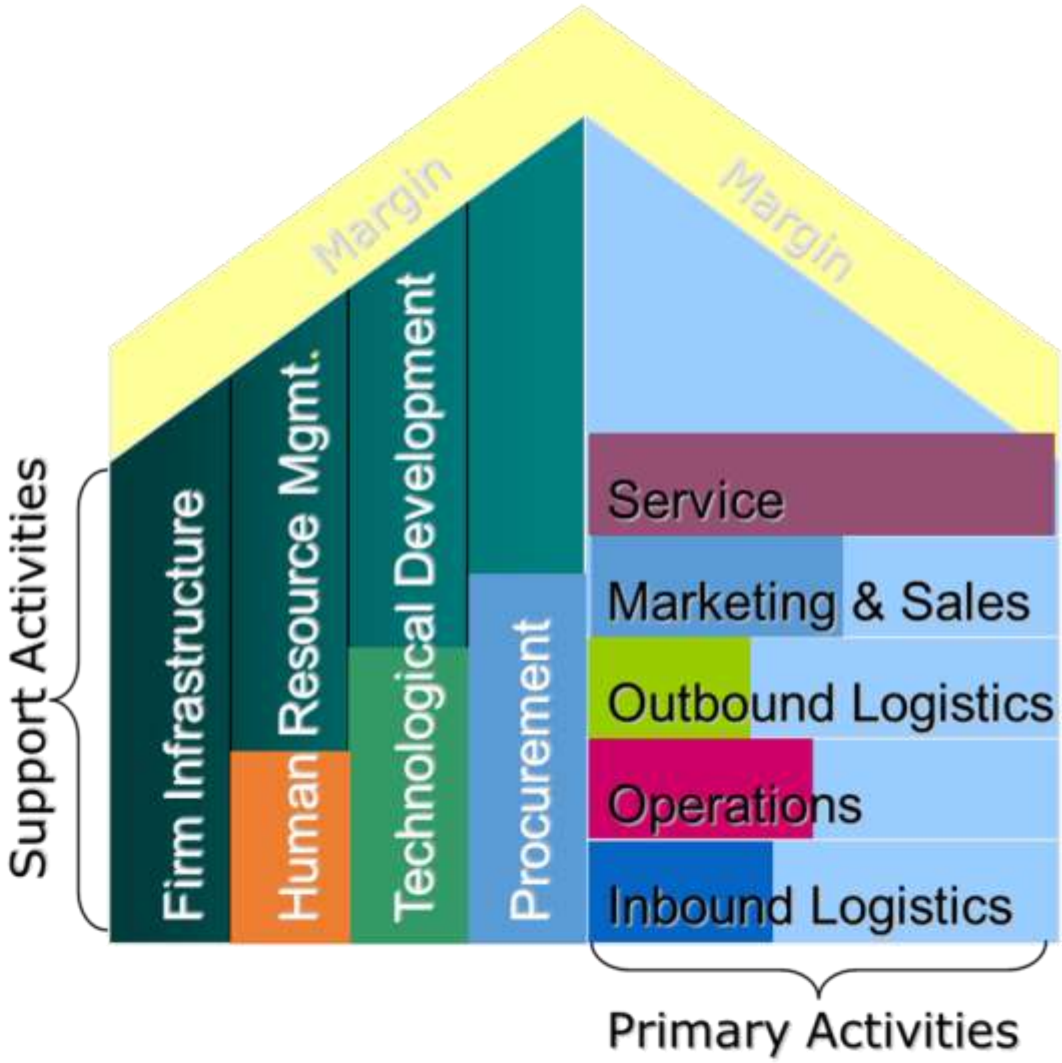
Buyer Value Chain

Ultimate basis for differentiation is the ability to play a role in a buyer's value chai

Outsourcing

Outsourcing is the purchase of some or all of a value-creating activity from an external supplier

Usually this is because the specialty supplier can provide these functions more efficiently



Strategic Rationales for Outsourcing

- **Improve Business Focus**
  - lets company focus on broader business issues by having outside experts handle various operational details
- **Provide Access to World-Class Capabilities**
  - the specialized resources of outsourcing providers makes world-class capabilities available to firms in a wide range of applications
- **Accelerate Business Re-Engineering Benefits**
  - achieves re-engineering benefits more quickly by having outsiders--who have already achieved world-class standards--take over process
- **Share Risks**
  - reduces investment requirements and makes firm more flexible, dynamic and better able to adapt to changing opportunities
- **Free Resources for Other Purposes**
  - permits firm to redirect efforts from non-core activities toward those that serve customers more effectively

<u>Outsourcing Issues</u>

- **Greatest Value**
  - outsource only to firms possessing a core competence in terms of performing the primary or support activity being outsourced
- **Evaluating Resources and Capabilities**
  - don’t outsource activities in which the firm itself can create and capture value
- **Environmental Threats and Ongoing Tasks**
  - do not outsource primary and support activities that are used to neutralize environmental threats or complete necessary ongoing organizational tasks
- **Nonstrategic Team of Resources**
  - do not outsource capabilities that are critical to their success, even though the capabilities are not actual sources of competitive advantage
- **Firm’s Knowledge Base**
  - do not outsource activities that stimulate the development of new capabilities and competencies

- **Developing the company profile**

A company profile is essentially a resume for company that company use to establish its credibility with the market it serves. Company profile helps potential customers to understand company's business as well as to understand company's approach, unique strength and relevant experience.

Company profile demonstrates its ability to effectively meet customer needs. It also helps others who are in contact with you such as lenders, the media, and job candidates to better understand its business.

What should be included in company profile?

1. Briefly write down company's background information.
2. Provide more detail on company's products or services.
3. Highlight company's strengths and successes.
4. Include qualifications of company and its staff.
5. Summarize company's selling statement.
6. Close with company contact information.

Benefits of company profile:

A company profile would benefit any company wanting to establish its credibility including:

1. A consulting firm where its critical for the company to establish the bases for its expertise.
2. A service provider with a service that can't be evaluated before the sale where the prospects assess the company's ability to

provide the service based on its assessment of the company itself.

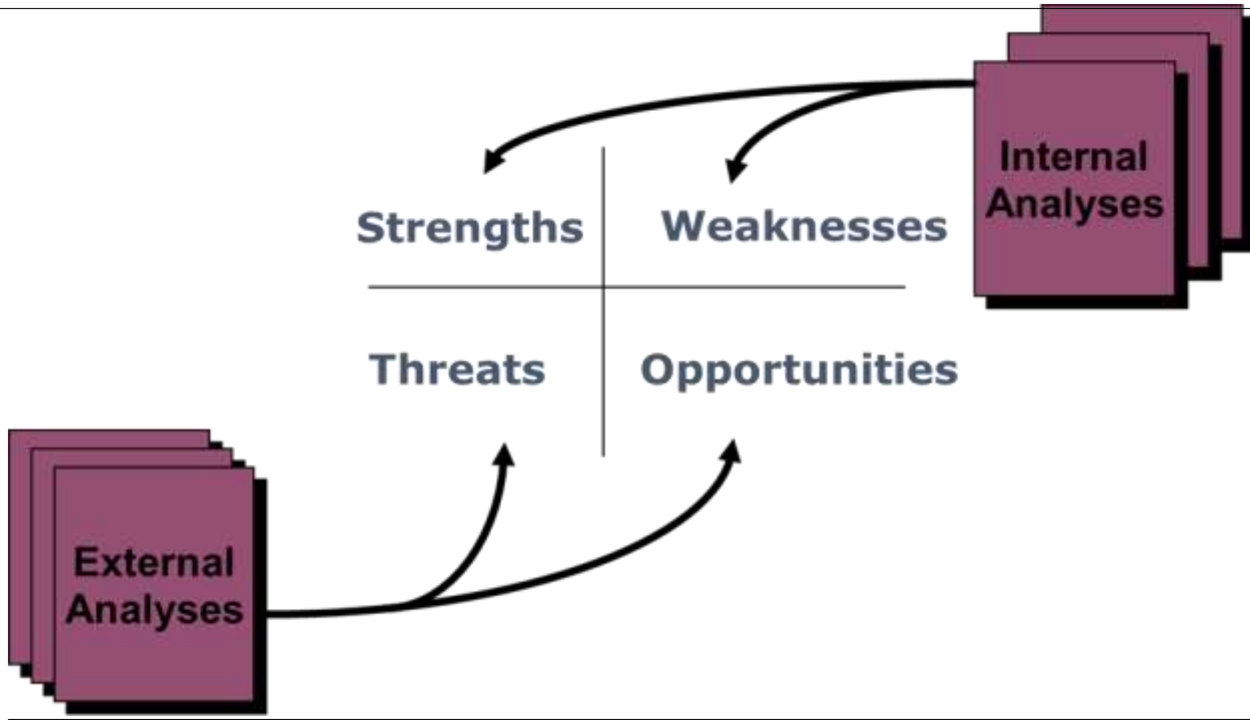
3. A company that lacks a recognized name in the market it serves.

The use of company profile:

There are many ways to use a company profile such as :

1. To use company's website as a means of establishing company's credibility.
2. Using a print version as a sales tool at trade shows or in mailings to prospects.
3. Providing it to lenders to help in secure financing.
4. Adding it to media kit and including it with press releases to give the media background information about company.
5. Using it as recruiting tool to promote company to job candidates

- **Profile of company's strength and weaknesses**



SWOT analysis is a simple but powerful tool for sizing up a company's resource capabilities and deficiencies, its market opportunities, and the external threats to its future well-being.

A first-rate SWOT analysis provides the basis for crafting a strategy that capitalizes on the company's resources, aims squarely at a capturing the company's best opportunities, and defends against the threats to its well being.

Strength

A company's resource strengths represent competitive assets and are big determinants of its competitiveness and ability to succeed in the market place. A competence is an activity that a company has learned to perform well. A core competence is a competitively important activity that a company performs better than other internal activities.

A distinctive competence is a competitively important activity that a company performs better than its rivals—it thus represents competitively superior resource strength.

A. **Identifying Company Resource Strengths and Competitive Capabilities**

1. A resource strength is something a company is good at doing or an attribute that enhances its competitiveness. Strength can take any of several forms:

a. A skill, specialized expertise, or competitively important capability

b. Valuable physical assets

c. Valuable human assets and intellectual capital

d. Valuable organizational assets

e. Valuable intangible assets

f. An achievement or attribute that puts the company in a position of market advantage

g. Competitively valuable alliances or cooperative ventures

2. A company's resource strengths represent competitive assets.

3. The caliber of a firm's resource strengths and competitive capabilities, along with its ability to mobilize them in the pursuit of competitive advantage, are big determinants of how well a company will perform in the marketplace.

4. Assessing a Company's Competencies and Capabilities—What Activities Does it Perform Well?: One of the most important aspects of appraising a company's resource strengths has to do with its competence level in performing key pieces of it's business.

5. Company competencies can range from merely a competence in performing an activity to a core competence to a distinctive competence.

a. A competence is something an organization is good at doing. It is nearly always the product of experience, representing an accumulation of learning and the buildup of proficiency in performing an internal activity.

b. A core competence is a proficiently performed internal activity that is central to a company's strategy and competitiveness. A core competence is more valuable resource strength than a competence because of the well-performed activity's core role in the company's strategy and the contributions it makes to the company's success in the marketplace.

c. A distinctive competence is a competitively valuable activity that a company performs better than its rivals. A distinctive competence signifies even greater proficiency than a core competence.

6. The conceptual differences between a competence, a core competence, and a distinctive competence draw attention to the fact that competitive capabilities are not all equal.

7. Core competencies are competitively more important than simple competencies because they add power to the company's strategy and have a bigger positive impact on its market position and profitability.

8. The importance of a distinctive competence to strategy-making rests with:

a. The competitively valuable capability it gives a company

b. Its potential for being the cornerstone of strategy

c. The competitive edge it can produce in the marketplace

9. What is the Competitive Power of Resource Strength? What is most telling about a company's strengths is how competitively powerful they are in the marketplace.

10. The competitive power of a company strength is measured by how many of the following four tests it can pass:

a. Is the resource strength hard to copy?

b. Is the resource strength durable – does it have staying power?

c. Is the resource really competitively superior?

d. Can the resource strength be trumped by different resource strengths and competitive capabilities of rivals?

11. The vast majority of companies are not well endowed with competitively valuable resources, much less with competitively superior resources capable of passing all four tests with high marks. Most firms have a mixed bag of resources.

12. Only a few companies, usually the strongest industry leaders or up-and-coming challengers, possess a distinctive competence or competitively superior resource.

13. Sometimes a company derives significant competitive vitality, maybe even a competitive advantage, from a collection of good-adequate resources that collectively have competitive power in the marketplace.

Weakness

A company's resource strengths represent competitive assets; its resource weaknesses represent competitive liabilities.

B. Identifying Company Resource Weaknesses and Competitive Deficiencies

1. A weakness or competitive deficiency is something a company lacks or does poorly in comparison to others or a condition that puts it at disadvantage in the marketplace.

2. A company's weaknesses can relate to:

a. Inferior or unproven skills or expertise or intellectual capital in competitively important areas of the business

b. Deficiencies in competitively important physical, organizational, or intangible assets

c. Missing or competitively inferior capabilities in key areas

3. Internal weaknesses are shortcomings in a company's complement of resources and represent competitive liabilities.

Summary:

In this chapter we discuss the technique of evaluating company's resources capabilities and competences. Managers often start their internal analysis with questions like, how well is the current strategy working? What is our current situation? What are our strengths and weaknesses? SWOT analysis is a traditional approach that has been in use for decades to help structure managers' pursuit of answers to these questions.

Value chain analysis has managers look at and disaggregate their business as a chain of activities that occur in a sequential manner to create a products or services they sale. The value chain approach breaks down the firms activities into primary and support categories of activities, then breaks these down further into specific types of activities with the objective to disaggregate activity into as many meaningful subdivisions as possible. once down, managers attempt to attribute costs to each. Doing this gives managers very distinct ways of isolating the things they do well and not so well, and it isolates activities that are truly key in meeting customers' needs- true potential sources of competitive advantage.