
Tools For Strategic Analysis

Strategic analysis is a theoretically informed understanding of the environment in which an organisation is operating, together with an understanding of the organisation's interaction with its environment in order to improve organisational efficiency and effectiveness by increasing the organisation's capacity to deploy and redeploy its resources intelligently (Chartered Institute of Management Accountants 2007).

Business analysis models are useful tools and techniques that can help a business understand their organisational environment and think more strategically about the business. There are a number of tools available but three will be explored in more detail:

- SWOT (strengths, weaknesses, opportunities, threats) analysis
- PESTLE (political, economic, social, technological, legal and environmental) analysis
- Porter's Five Forces framework

SWOT analysis

A SWOT analysis is a simple but widely used tool that helps in understanding the strengths, weaknesses, opportunities and threats involved in a project or business activity. Once you identify these you can capitalise on your strengths, minimise the effects of your weaknesses, make the most of any opportunities and reduce the impact of any threats. A SWOT analysis gives you a better insight into your internal and external business environment. However, it does not always prioritise the results, which can lead to an improper strategic action. One way to make better use of the SWOT framework is to consider the customer's perspective when making strategic plans and decisions. A SWOT should start by defining the objective of the project or business activity and identify the internal and external factors that are important to achieving that objective. Strengths and weaknesses are usually internal to the organisation, while opportunities and threats are usually external. Often these are plotted on a simple 2x2 matrix.

The main advantages of conducting a SWOT analysis is that it has little or no cost and can be conducted by anyone that knows your business. You can also use a SWOT analysis when you don't have much time to address a complex situation. For complex issues, you will usually need to conduct more in-depth research and analysis to make decisions.

A SWOT analysis only covers issues that can definitely be considered a strength, weakness, opportunity or threat. Because of this, it's difficult to address uncertain or two-sided factors, such as factors that could either be a strength or a weakness or both, with a SWOT analysis (e.g. you might have a prominent location, but the lease may be expensive).

A SWOT analysis may be limited because it:

- doesn't prioritise issues
- doesn't provide solutions or offer alternative decisions
- can generate too many ideas but not help you choose which one is best

-
- can produce a lot of information, but not all of it is useful.

PEST analysis

PEST analysis is a scan of the external macro-environment in which an organisation exists. It is a useful tool for understanding the political, economic, socio-cultural and technological environment that an organisation operates in. It can be used for evaluating market growth or decline, and as such the position, potential and direction for a business.

Political factors. These include government regulations such as employment laws, environmental regulations and tax policy. Other political factors are trade restrictions and political stability.

Economic factors. These affect the cost of capital and purchasing power of an organisation. Economic factors include economic growth, interest rates, inflation and currency exchange rates.

Social factors. These impact on the consumer's need and the potential market size for an organisation's goods and services. Social factors include population growth, age demographics and attitudes towards health.

Technological factors. These influence barriers to entry, make or buy decisions and investment in innovation, such as automation, investment incentives and the rate of technological change.

PEST factors can be classified as opportunities or threats in a SWOT analysis. It is often useful to complete a PEST analysis before completing a SWOT analysis.

It is also worth noting that the four paradigms of PEST vary in significance depending on the type of business. For example, social factors are more obviously relevant to consumer businesses. Conversely, political factors are more obviously relevant to a defence contractor or aerospace manufacturer.

Limitations of PEST Analysis

The external factors considered during PEST analysis change and sometimes at a very fast pace, therefore making it difficult to predict why and how these factors may affect the present or future of the project. Its simple presentation can also be considered a limitation. It is common to present a simple list of the environmental factors that can affect the project. Unless the attributing factors are examined in more detail to consider the degree of impact, the findings of the analysis don't seem to be of much value. Collecting large amounts of relevant data from the correct sources may also be an issue, especially since most of the pertinent data must be collected from external agencies. This makes a PEST analysis not only time consuming but costly as well. The lack of easily available updated information can mean that too many assumptions are made. Often the factors mentioned in the analysis are based more on assumptions and less on actual facts. An analysis based on unfounded assumptions can lead to planning disasters. A proper PEST analysis requires a lot of information to be collected. But when handling too much information, the users tend to get confused and lose sight of what factors are more critical. This ambiguity in prioritising the affecting factors can put the entire

planning on the wrong track. PEST analysis alone is insufficient for the purpose of strategic planning, since it scans only the external environment while completely ignoring the internal environment and the competitive scenario. For PEST analysis to make some worthwhile contributions towards strategic planning it must be in conjunction with other tools like SWOT analysis to get a more realistic overall picture.

PEST does offer a viable technique for carrying out an environmental scan for a project, however, its effectiveness depends on the accuracy of the data collected, timely updates to accommodate changes and the use of additional tools that can trim down the limitations of a PEST analysis to some extent.

Porter's Five Forces

Porter's five forces of competitive position analysis was developed in 1979 by Michael E. Porter of Harvard Business School. It helps a business understand both the strength of the current competitive position, and the strength of the position they may be considering moving into.

This theory is based on the concept that there are five forces which determine the competitive intensity and attractiveness of a market. Porter's five forces helps to identify where power lies in a business situation. Strategic analysts often use Porter's five forces to understand whether new products or services are potentially profitable. By understanding where power lies, the theory can also be used to identify areas of strength, to improve weaknesses and to avoid mistakes.

The five forces are:

1. Supplier power. An assessment of how easy it is for suppliers to drive up prices. This is driven by:
 - the number of suppliers of each essential input
 - the uniqueness of their product or service
 - the relative size and strength of the supplier
 - the cost of switching from one supplier to another.
2. Buyer power. An assessment of how easy it is for buyers to drive prices down. This is driven by:
 - the number of buyers in the market
 - the importance of each individual buyer to the organisation
 - the cost to the buyer of switching from one supplier to another.
 - If a business has just a few powerful buyers, they are often able to dictate terms.
3. Competitive rivalry. The key driver is the number and capability of competitors in the market. Many competitors, offering undifferentiated products and services, will reduce market attractiveness.
4. Threat of substitution. Where close substitute products exist in a market, it increases the likelihood of customers switching to alternatives in response to price increases. This reduces both the power of suppliers and the attractiveness of the market.
5. Threat of new entry. Profitable markets attract new entrants, which erodes profitability. Unless incumbents have strong and durable barriers to entry, for example, patents, economies of scale, capital requirements or government policies, then profitability will decline to a competitive rate.

Porter's Five Forces model can be used to good analytical effect alongside other models such as the SWOT and PEST analysis tools. Porter's Five Forces model provides suggested points under each main heading, by which you can develop a broad and sophisticated analysis of competitive position, as might be used when creating strategy, plans, or making investment decisions about a business or organisation. The most useful thing about Porter's five forces is that it encourages companies to look beyond their immediate business ventures to their industry as a whole when making long-term plans. Porter's still plays a vital role in that, but it can't be the sole tool in the toolbox when it comes to building a business strategy.

Porter's five forces have several weaknesses. The first is in its composition, as a static model, it provides a snapshot of the wider industry at some point in the past. This can be useful for informing short-term strategy, but the window of applicability for the information coming out of Porter's five forces has also been narrowed by rapidly evolving external factors. These are trends like globalisation and rapid technological advances that weren't as prominent when Porter devised his framework. The other weakness is that a lot of people use Porter's five forces in ways it was never intended. Trying to apply Porter's five forces to a specific company rather than an industry as a whole is the most common mistake. Porter's five forces can provide information to enlighten strategic discussions, but it isn't an individual-company analysis tool. In addition equal attention should not be paid to all five forces, for most industries there will be one or two forces that outweigh all the others.

In conclusion there are a number of tools available to support businesses with strategic analysis and planning. Three have been explored in more detail, a SWOT analysis is a simple commonly used tool however it does not prioritise actions. The PEST is another tool that is useful for understanding the political, economic, socio-cultural and technological environment that an organisation operates in. However, each paradigm will have different levels of importance according to the type of business and it is sometimes useful to complete this along with a SWOT. A PEST analysis most commonly measures a market, a SWOT analysis measures a business unit, a proposition or idea. The Porters five forces model is the last one that has been explored, this is useful for assessing the potential for profitability in an industry. With a little adaptation, it is also useful as a way of assessing the balance of power in more general situations. It enables the business to look at how each of the five forces can be affected to move the balance of power more in the business's favour. It may be useful for businesses to use more than one of the tools to ensure they have a comprehensive analysis of their business.