

THE LIMITATIONS OF SWOT ANALYSIS

SWOT analysis is a tried-and-true tool of strategic analysis. SWOT (strengths, weaknesses, opportunities, threats) analysis is used regularly in business to initially evaluate the opportunities and threats in the business environment as well as the strengths and weaknesses of a firm's internal environment. Top managers rely on SWOT to stimulate self-reflection and group discussions about how to improve their firm and position it for success.

But SWOT has its limitations. It is just a starting point for discussion. By listing the firm's attributes, managers have the raw material needed to perform more in-depth strategic analysis. However, SWOT cannot show them how to achieve a competitive advantage. They must not make SWOT analysis an end in itself, temporarily raising awareness about important issues but failing to lead to the kind of action steps necessary to enact strategic change.

Let's look at some of the limitations of SWOT analysis.

Strengths May Not Lead to an Advantage

A firm's strengths and capabilities, no matter how unique or impressive, may not enable it to achieve a competitive advantage in the marketplace. It is akin to recruiting a concert pianist to join a gang of thugs—even though such an ability is rare and valuable, it hardly helps the organization attain its goals and objectives! Similarly, the skills of a highly creative product designer would offer little competitive advantage to a firm that produces low-cost commodity products. Indeed, the additional expense of hiring such an individual could erode the firm's cost advantages. If a firm builds its strategy on a capability that cannot, by itself, create or sustain competitive advantage, it is essentially a wasted use of resources.

SWOT's Focus on the External Environment Is Too Narrow

Strategists who rely on traditional definitions of their industry and competitive environment often focus their sights too narrowly on

current customers, technologies, and competitors. Hence they fail to notice important changes on the periphery of their environment that may trigger the need to redefine industry boundaries and identify a whole new set of competitive relationships. Consider *Encyclopaedia Britannica*, whose competitive position was severely eroded by a "nontraditional" competitor—CD-based encyclopedias (e.g., Microsoft *Encarta*) that could be used on home computers—and later by online encyclopedias (e.g., Wikipedia).

SWOT Gives a One-Shot View of a Moving Target

A key weakness of SWOT is that it is primarily a static assessment. It focuses too much of a firm's attention on one moment in time. Essentially, this is like studying a single frame of a motion picture. You may be able to identify the principal actors and learn something about the setting, but it doesn't tell you much about the plot. Competition among organizations is played out over time. As circumstances, capabilities, and strategies change, static analysis techniques do not reveal the dynamics of the competitive environment.

SWOT Overemphasizes a Single Dimension of Strategy

Sometimes firms become preoccupied with a single strength or a key feature of the product or service they are offering and ignore other factors needed for competitive success. For example, Toyota, the giant automaker, paid a heavy price for its excessive emphasis on cost control. The resulting problems with quality and the negative publicity led to severe financial losses and an erosion of its reputation in many markets.

SWOT analysis has much to offer, but only as a starting point. By itself, it rarely helps a firm develop competitive advantages that it can sustain over time.

Sources: Shapiro, C. & Varian, H. R. 2000. Versioning: The smart way to sell information. *Harvard Business Review*, 78(1): 99–106; and Picken, J. C. & Dess, G. G. 1997. *Mission critical*. Burr Ridge, IL: Irwin Professional.

Before moving to value-chain analysis, let's briefly revisit the benefits and limitations of SWOT analysis. As discussed in Chapter 2, a SWOT analysis consists of a careful listing of a firm's strengths, weaknesses, opportunities, and threats. While we believe SWOT analysis is very helpful as a starting point, it should not form the primary basis for evaluating a firm's internal strengths and weaknesses or the opportunities and threats in the environment. Strategy Spotlight 3.1 elaborates on the limitations of the traditional SWOT approach.

We will now turn to value-chain analysis. As you will see, it provides greater insights into analyzing a firm's competitive position than SWOT analysis does by itself.

Value-Chain Analysis

value-chain analysis
a strategic analysis of an
organization that uses
value-creating activities.

Value-chain analysis views the organization as a sequential process of value-creating activities. The approach is useful for understanding the building blocks of competitive advantage and was described in Michael Porter's seminal book *Competitive Advantage*.

Value is the amount that buyers are willing to pay for what a firm provides them and is measured by total revenue, a reflection of the price a firm's product commands and the quantity it can sell. A firm is profitable when the value it receives exceeds the total costs involved in creating its product or service. Creating value for buyers that exceeds the costs of production (i.e., margin) is a key concept used in analyzing a firm's competitive position.

Porter described two different categories of activities. First, five **primary activities**—inbound logistics, operations, outbound logistics, marketing and sales, and service—contribute to the physical creation of the product or service, its sale and transfer to the buyer, and its service after the sale. Second, **support activities**—procurement, technology development, human resource management, and general administration—either add value by themselves or add value through important relationships with both primary activities and other support activities. Exhibit 3.1 illustrates Porter's value chain.

To get the most out of value-chain analysis, view the concept in its broadest context, without regard to the boundaries of your own organization. That is, place your organization within a more encompassing value chain that includes your firm's suppliers, customers, and alliance partners. Thus, in addition to thoroughly understanding how value is created within the organization, be aware of how value is created for other organizations in the overall supply chain or distribution channel.³

Next, we'll describe and provide examples of each of the primary and support activities. Then we'll provide examples of how companies add value by means of relationships among activities within the organization as well as activities outside the organization, such as those activities associated with customers and suppliers.⁴

Primary Activities

Five generic categories of primary activities are involved in competing in any industry, as shown in Exhibit 3.2. Each category is divisible into a number of distinct activities that depend on the particular industry and the firm's strategy.⁵

Inbound Logistics Inbound logistics is primarily associated with receiving, storing, and distributing inputs to the product. It includes material handling, warehousing, inventory control, vehicle scheduling, and returns to suppliers.

Just-in-time (JIT) inventory systems, for example, were designed to achieve efficient inbound logistics. In essence, Toyota epitomizes JIT inventory systems, in which parts

primary activities sequential activities of the value chain that refer to the physical creation of the product or service, its sale and transfer to the buyer, and its service after sale, including inbound logistics, operations, outbound logistics, marketing and sales, and service.

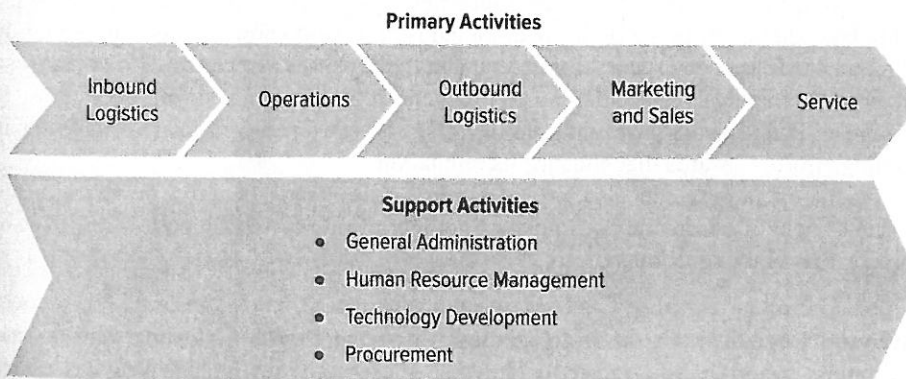
support activities activities of the value chain that either add value by themselves or add value through important relationships with both primary activities and other support activities, including procurement, technology development, human resource management, and general administration.

LO3.2

The primary and support activities of a firm's value chain.

inbound logistics receiving, storing, and distributing inputs of a product.

EXHIBIT 3.1 The Value Chain: Primary and Support Activities



Adapted from *Competitive Advantage: Creating and Sustaining Superior Performance* by Michael E. Porter, 1985, 1998, Free Press.

SCHMITZ CARGOBULL: ADDING VALUE TO CUSTOMERS VIA IT

Germany's truck and trailer manufacturer, Schmitz Cargobull, mainly serves customers that are operators of truck or trailer fleets. Like its rivals, the company derives a growing share of revenue from support services such as financing, full-service contracts for breakdowns and regular maintenance, and spare-parts supplies.

What sets the company apart is its expertise in telematics (the integrated application of telecommunications data) to monitor the current state of any Schmitz Cargobull-produced trailer. Through telematics, key information is continually available to the driver, the freight agent, and the customer. They can track, for instance, when maintenance is done, how much weight has been loaded, the current cargo temperature, and where the vehicle is on its route. Therefore, Schmitz Cargobull customers can better manage their trailer use and minimize the risk of breakdowns. The decision to introduce telematics, not surprisingly, derived from

management's belief that real-time sharing of data would bind the company more closely to customers.

In applying its telematic tools in its products, Schmitz Cargobull is providing clear, tangible benefits. It uses information technology only where it makes sense. On the production line, for example, workers implement statistical quality controls manually, rather than rely on an automated system, because the company found manual control improves engagement and job performance.

That strategy has helped Schmitz Cargobull become an industry leader. In 2013, the company controlled 82 percent of the sales of semitrailer reefers (refrigerated trailers) in Germany, and its market share in Europe was about 50 percent. Further, its results for the fiscal year ending March 2014 are most impressive: sales increased by 7.5 percent and pretax profit soared 66 percent.

Sources: Anonymous. 2014. Schmitz Cargobull AG announces earnings and production results for the year ending March 2014. www.investing.businessweek.com, July 31: np; Anonymous. 2014. Premiere at the IAA Show 2014: Increased I-beam stability and payload. www.cargobull.com, September: np; and Chick, S. E., Huchzermeier, A., & Netessine, S. 2014. Europe's solution factories. *Harvard Business Review*, 92(4): 11–115.

Interrelationships among Value-Chain Activities within and across Organizations

We have defined each of the value-chain activities separately for clarity of presentation. Managers must not ignore, however, the importance of relationships among value-chain activities.²⁶ There are two levels: (1) **interrelationships** among activities within the firm and (2) relationships among activities within the firm and with other stakeholders (e.g., customers and suppliers) that are part of the firm's expanded value chain.²⁷

With regard to the first level, consider Lise Saari's interview (pages 83–84) on the strategic importance of effective human resource management practices. As she notes: "HR [must be] a true partner of the business, with a deep and up-to-date understanding of business realities and objectives, and, in turn, [must ensure] HR initiatives fully support them at all points of the value chain."

With regard to the second level, Campbell Soup's use of electronic networks enabled it to improve the efficiency of outbound logistics.²⁸ However, it also helped Campbell manage the ordering of raw materials more effectively, improve its production scheduling, and help its customers better manage their inbound logistics operations.

interrelationships collaborative and strategic exchange relationships between value-chain activities either (a) within firms or (b) between firms. Strategic exchange relationships involve exchange of resources such as information, people, technology, or money that contribute to the success of the firm.

Integrating Customers into the Value Chain

When addressing the value-chain concept, it is important to focus on the interrelationship between the organization and its most important stakeholder—its customers. Some firms find great value by directly incorporating their customers into the value creation process. Firms can do this in one of two ways.

First, they can employ the "prosumer" concept and directly team up with customers to design and build products to satisfy their particular needs. Working directly with customers in this process provides multiple potential benefits for the firm. As the firm develops individualized products and relationship marketing, it can benefit from greater customer satisfaction and loyalty. Additionally, the interactions with customers can generate insights that