

Value from Competitive Intelligence

Best Practice in Competitor Analysis

Table of Contents

| | | |
|-----------|--|----------|
| 1. | Competitive Strategy | 2 |
| 2. | The Purpose of Competitor Analysis..... | 3 |
| 3. | Collecting Information | 3 |
| 3.1. | Individuals..... | 4 |
| 3.2. | Facilities..... | 5 |
| 3.3. | Culture..... | 5 |
| 3.4. | Environment..... | 6 |
| 4. | Drawing Conclusions..... | 6 |
| 4.1. | Formal Modeling..... | 7 |
| 4.2. | Intuitive Decision Making..... | 7 |
| 5. | Presenting Results | 7 |
| 6. | Implementing Actions | 9 |
| 6.1. | Competitive Radar | 9 |
| 6.2. | Competitive Signaling | 10 |

1. Competitive Strategy

Dealing with strategy from a management perspective is often perceived to be of rather theoretical value. This notion is caused by the static and numbers-driven methodology which strategy professionals usually apply to this very complex and dynamic set of problems. The difficulty of getting strategic recommendations implemented further reduces a manager's readiness to undertake regular and extensive strategy work.

This view, however, creates an enormous risk for an organization in a highly competitive environment. In phases of constant and satisfactory growth, as well as during times of consolidation, being caught by surprise can have serious consequences for a company (Exhibit 1).

Real threats from competition - examples

| | | |
|---|--|---|
| | <p><i>Customer Base Erosion</i></p> <ul style="list-style-type: none"> ▪ Marks & Spencer general retail ▪ Triumph motorcycles ▪ Eddie Bauer mail order | <p><i>Product Innovation</i></p> <ul style="list-style-type: none"> ▪ Agfa Gevaert still photography ▪ Royal Mail mail service ▪ Palm hand-held devices |
| <p>Long-term</p> <p>Time Horizon</p> | <p><i>Marketing Mix</i></p> <ul style="list-style-type: none"> ▪ Opel passenger vehicles ▪ E.ON UK electricity retail ▪ CREST toothpaste | <p><i>Competitive Take-Over</i></p> <ul style="list-style-type: none"> ▪ Mannesmann mobile telecom ▪ Compaq computers ▪ TWA airline |
| | <p>Organic</p> <p>Type of Threat</p> | <p>Disruptive</p> |

Exhibit 1

Neglecting competition can result in two types of threats. Either a company enters into a phase of a long and painful decline, or a sudden loss of market share, profitability, threaten the company's independence or even its very survival. From hindsight, both instances can often be traced back to a single event in the company's past. Research has shown that in most cases these events are marked by management's failure to deal with competitive threats. We have coined the term "Competitive Signal Ignorance" (CSI) for this event.

2. The Purpose of Competitor Analysis

The main purpose of systematic competitor analysis is to avoid the CSI trap. The analysis will create the basis to decide on competitive actions and reactions. In this respect, it plays an important role in the process of regular, ongoing strategy development as well as in very critical situations, when an immediate response to a competitor's action will be required.

Competitive strategy is a highly dynamic process, like a game of chess. The next move depends as much on the expected next move of competitors as on a company's own market position, goals, ambitions, strengths, and weaknesses. Therefore, the analysis should not be limited to understanding relative strengths and weaknesses – a rather static view of the competitive arena – but at forecasting the most relevant competitors' goals, plans, and moves. The cost of failing to recognize the dynamic nature of strategy can be expressed in missed opportunities and strategic errors.¹ For example, the failure to anticipate a changing market structure cost Okidata its comfortable lead over Hewlett Packard in the printer market. The failure to consider potential interactions over time, the second example of a strategic error, can lead to mutually destructive behavior for an entire class of competitors, as can be observed in the German market for mobile telephony for the last decade.

In order to make competitive intelligence “workable” and generate measurable value in an organization, a very pragmatic and concrete approach must be selected for all four steps of competitor analysis: (1) collecting information, (2) drawing conclusions, (3) presenting results, and (4) implementing actions.

3. Collecting Information

The first step is to define the competitive arena. What is the relevant set of competitors? Usually, management is very good at pointing to the existing competition that is of major relevance in the current situation of the business, the market, and the environment. Ignoring potential new competitors, however, is a much bigger threat. There are numerous cases where the most serious threat came from “industry outsiders” and new entrants. Famous is the case of the US railroad industry, which has almost been wiped out by the rapid growth of air transportation.

¹ George S. Day, David Reibstein, *Introduction: The Dynamic Challenges for Theory and Practice*, in: Wharton on Dynamic Competitive Strategy, John Wiles & Sons, Inc., New York, 1997

The best way to define the competitive arena is to take the customer’s perspective². The most important questions to answer are: What is the purpose of our product or service? Which offers can be seen as supplementary or complementary, regardless of current marketing mix specifics as, for example, price or placement?

Once the arena has been defined, relevant information on competitors must be collected. There are numerous sources where relevant information on competitors can be found. First, it is important to understand which type of information to look for. The information type is determined by the forces at work in the competitive arena (Exhibit 2).

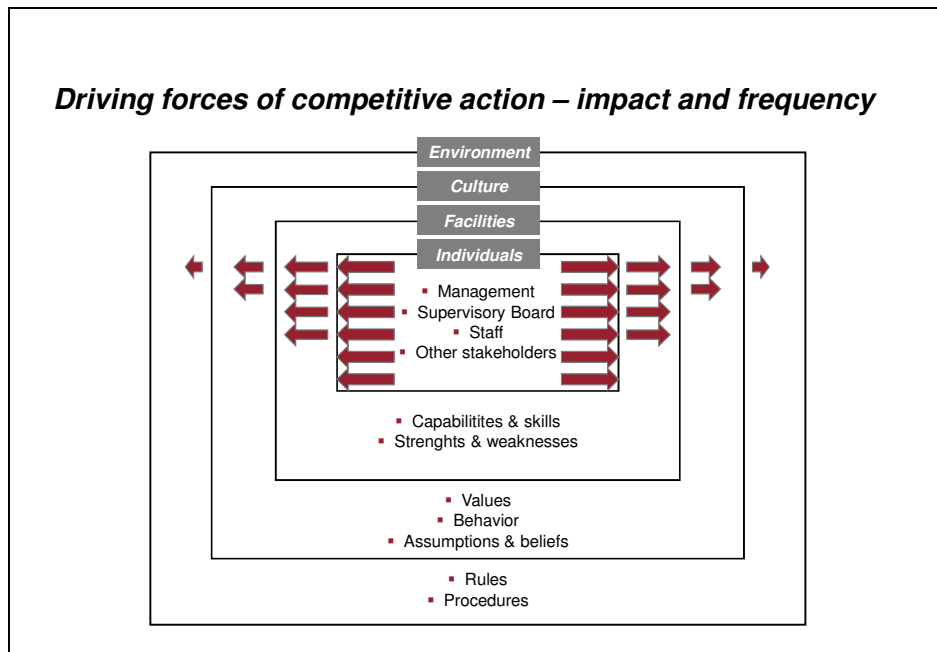


Exhibit 2

These forces are “Individuals”, “Facilities”, “Culture”, and “Environment”³

3.1. Individuals

All key members of management and other important stakeholders of the competitor organization should be in scope. Key decision makers and other individuals that

² A great many organizations have difficulties to adapt a true customer point of view because they are constantly blinded by their own assumptions about customer value and product purpose. An outside perspective can add enormous value in these situations.

³ The sequence describes the order of relevance of forces from a dynamic perspective. Individuals react far more frequent and effective than the environment to competitive actions. A cultural change on average requires greater resources and time than building new capabilities or skills.

they must report or refer to, will act based on past experience and future expectations. Therefore, the most important information regarding competitive intelligence will help to draw as accurately as possible a picture of the individuals in charge. Some of the relevant questions are: What has led their career path them to believe? Which significant events have taught them specific cause-effect relationship patterns? Have they demonstrated aggressive or rather moderate reactions in the past? Does a specific team constellation favor or hinder certain types of decisions and actions? The media of the internet area offer a bounty of publicly available information, which a “competitive profiler” can draw on.

3.2. Facilities

The term “facilities” describes all core capabilities, skills, strengths, weaknesses, and limitations of an organization’s action space. Starting from a competitor’s current strategic position, goals, and ambitions, a description of the company’s situation can be drawn. A highly effective framework, which can be applied to compile a complete view on all relevant elements of an organization, is the “7 S” model⁴. For each of the elements, key data should be collected and combined in order to assemble an integrated picture of the organization’s capabilities and skills. It is important to look at the present as well as the future. What is management likely to expect regarding financial resources, market share, product portfolio, staff development etc.? Most of these questions can be answered by compiling a comprehensive set of publicly available information on the company under scrutiny. However, there is one major pitfall of an outside-in analysis: Decisions are often made with a forward view, which incorporates wishes and aspirations rather than reality and facts. This, again, means that decisions will often be biased with the individual’s *representativeness heuristics*.⁵ These biases have to be taken into account when estimating competitor management’s judgment of the organization’s facilities.

3.3. Culture

An organization’s culture includes values, behavioral patterns, assumptions and beliefs guide decisions and actions of an organization. Culture counts in competitive analysis because managers both impact and regard corporate culture when making competitive decisions – explicitly as well as implicitly. Firstly, cultural assumptions will change with the change of the carriers of these assumptions.⁶ So, it

⁴ See „*In Search of Excellence*“, Thomas J. Peter, Robert H. Waterman, Jr., Warner Books, New York, 1982

⁵ Daniel Kahneman und Amos Tversky have coined the term ‘representative heuristic’ to describe decision makers, who tend to focus on a small set of intuitively plausible variables, ignoring other issues critical to a decisions outcome.

⁶ „*The Corporate Culture Survival Guide*“, Edgar H. Schein, New York, 1999

is important to understand which cultural assumptions management brings to the table. Secondly, management is fully attentive to the fact that decisions, which are made without awareness of the operative cultural forces, may have unanticipated and undesirable consequences. As culture is difficult to change in the short run, management will place its decisions inside the cultural boundaries of an organization. Reading culture from the outside is a highly delicate task, though. First, it requires a clear model of what constitutes corporate culture and how the various elements of culture will impact decisions. Second, a deep experience in observing and interpreting cultural elements is essential in order to avoid costly misreading. This is even more important as the most critical cultural elements are deeply enshrined and hidden in the organization rather than obvious and easy to spot.

3.4. Environment

The environment comprises of all formal and informal rules and procedures, which define externally set boundaries and degrees of freedom to act. Industry-specific environmental boundaries are usually transparent and well understood as long as they are formal and public., There often exist, however, hidden mechanisms which often have an even greater impact on competitive decisions than formal rules and regulations. For example, large-scale power suppliers operate in most cases on an unspoken “license”. Their image with the public has a considerable impact on politicians’ and regulatory authorities’ willingness to consent to their requests. Similar effects can be observed in the banking industry, in the insurance sector, and in a number of other industries. Of more relevance, however, are company-specific environmental considerations. An overarching corporate strategy, for example, is a definite border that management will not cross. The same can be true for shareholders’ demands or other stakeholders’ requests. The most important of all environmental factors, though, is a competitor’s expectation about the market’s development and the industry structure – including the strategy of its most relevant competitors! Exactly at this stage, the highly dynamic character of competitive analysis becomes obvious. Assumptions about competitors’ assumptions on its competitors cannot be developed and utilized in a static manner. One must apply methods from game theory and dynamic modeling in order to draw sensible conclusions that lead in to targeted actions.

4. Drawing Conclusions

The task of drawing correct conclusions from a the vast amount of data which can be compiled, is best approached with a combination of formal modeling on one hand and intuitive decision making on the other.

4.1. Formal Modeling

The purpose of building a model of dynamic competitive action is to shed light on the options management has to consider when making a decision. Models, mainly from the arena of game theory⁷, will never be able to generate automatic answers. However, they will create a much clearer understanding of the various options for all stakeholders concerned. The best results both from a theoretical as well as a pragmatic point of view will be achieved when model-type descriptions of competitive behavior are fed into collective exercises like role plays and desktop war games.

4.2. Intuitive Decision Making

Intuition is a powerful means of estimating the probability and outcome of specific competitive actions. Management's Intuition can draw on a vast spectrum of management experience, stored in a subconsciously functioning decision machine. If a conclusion drawn from formal modeling "just does not feel right" then this is the best indicator that there is substantial room for improvement – either in data collecting or in modeling.

A dossier of five to ten text pages should be compiled on each relevant competitor in order to ensure appropriate precision and depth. Expected actions and reactions for all types of threats in the short as well as in the long run (compare Exhibit 1) should either be listed or explicitly excluded in case of low forecast probability. In addition, for all of the statements a specific set of observable early-warning signals should be determined. These signals are of substantial value when it comes to constantly screening the competitive landscape for opportunities and threats.

5. Presenting Results

The most effective way to present the results concerning an individual competitor is in the form of a "Strategic Response Profile". The focus of this presentation is on describing a competitor's expected action and reaction. It evaluates the probability and the forecast strength based on a condensed and structured report (Exhibit 3).

⁷ For example: Analytic Hierarchy Process, Evaluation of Preemption Options, Probability Trees, Behavioral Frame. For details, see ⁷ George S. Day, David Reibstein, Wharton on Dynamic Competitive Strategy, John Wiles & Sons, Inc., New York, 1997

Strategic Response Profile - Example

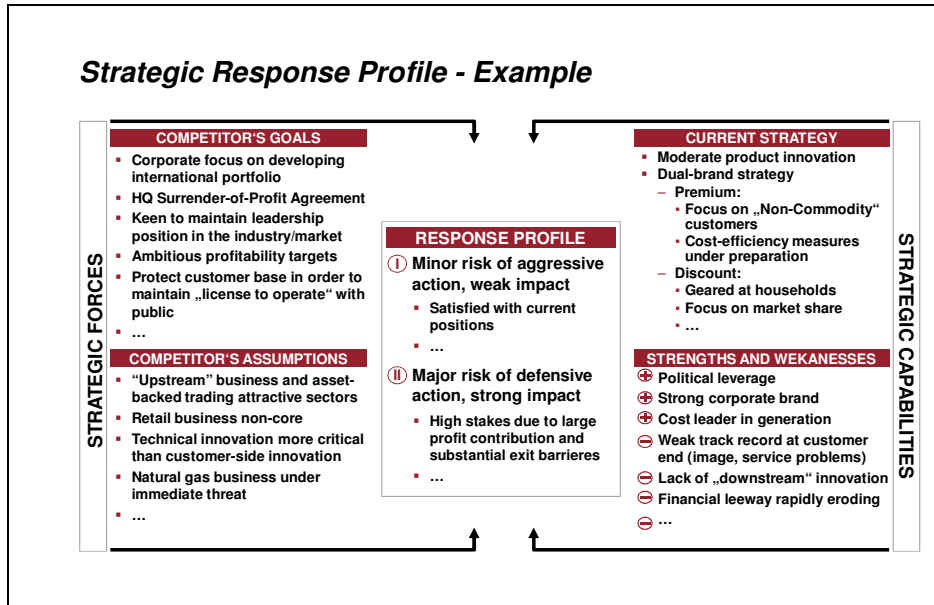


Exhibit 3

In order to give an overview of the competitive situation of a sector or the market, a “Competitor Response Field” can be drawn (Exhibit 4).

Competitor Response Field – Example

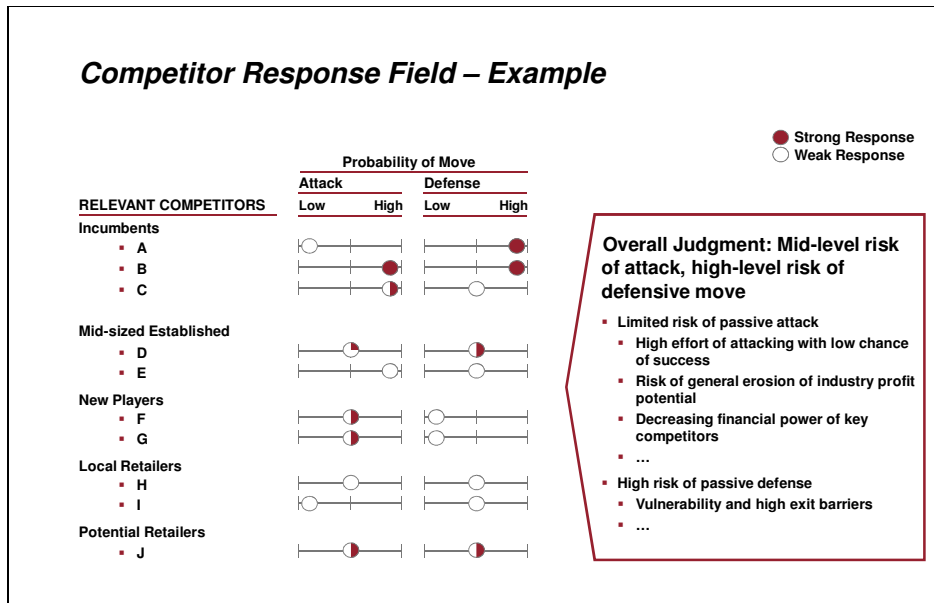


Exhibit 4

The Competitor Response Field offers a quick and precise view of the imminent risks from the industry’s current competitive landscape. Comparing Response Fields over a longer period of time gives a motion-like picture of how the industry structure and the competitive positions change. Such a picture offers valuable insights

into competitors’ internal struggles and developments and, at the same time, delivers a future outlook on the relevance of individual players.

6. Implementing Actions

Implementing strategic actions is a full-fledged management topic on its own. Two fundamental dimensions define the space of actions on which a strategy can be built (Exhibit 5).

Competitive action space - examples

| | | | |
|------------|---------------------|---|---|
| | | Strategic Asset Development <ul style="list-style-type: none"> ▪ Brand recognition & reputation ▪ Capabilities & skill building ▪ Gaining customer access | Leverage Improvement <ul style="list-style-type: none"> ▪ Changing regulatory boundaries ▪ Improving financial leeway ▪ Strategic alliances, mergers & acquisitions |
| Long-term | Time Horizon | | |
| | | Competitive Positioning <ul style="list-style-type: none"> ▪ Preemption & following ▪ Teasing & challenging ▪ Competitive signaling | Protective Actions <ul style="list-style-type: none"> ▪ Partnering & cooperation ▪ Legal & litigation ▪ PR & communication |
| Short-term | | | |
| | | Customer | Competitor |
| | | Focus | |

Exhibit 5

The decision on which actions to take depends as much on the reading of competitive signals in a company’s arena as on its own ambitions, targets, strengths, weaknesses etc. There are two specific topics dealing with implementation, however, which mainly concern the field of competitive intelligence. The first is establishing a regular competitive intelligence function, an organizational capability, which is called “Competitive Radar”. The second regards a specific action type, the so called “Competitive Signaling”.

6.1. Competitive Radar

The value from competitive intelligence will be drastically reduced if it is done in a non-regular or incomprehensive manner. The most dangerous threats usually come from marginal players. The most surprising moves typically occur in times of calm. Therefore, a function with formal responsibility for competitive analysis should be established as the most important, as well as the most urgent, competitive action.

6.2. Competitive Signaling

Sending and receiving signals between competitors is the key function transmitting the dynamics of competitive strategy. Sending signals can become a highly cost-efficient way of “steering” competitors in a certain direction. Signals can discourage attacks, block a planned market entry, help to discipline an errant competitor, influence an industry’s code of conduct, divide the market among a limited number of competitors, send trial balloons, and even bluff the competition.⁸ In order to maximize a signal’s effect, however, a company must make explicit assumptions about the readability and credibility of a signal from its competitors’ point of view, and at the same time, on the probable reactions. Developing a reliable forecast of competitive reactions to signals is probably the most difficult but also the most valuable piece of art in the arena of competitive intelligence.

Berlin, September 2010

Theron Advisory Group

⁸ See also Day, George S. et al.