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FUNDAMENTALS OF STRATEGIC MANAGEMENT

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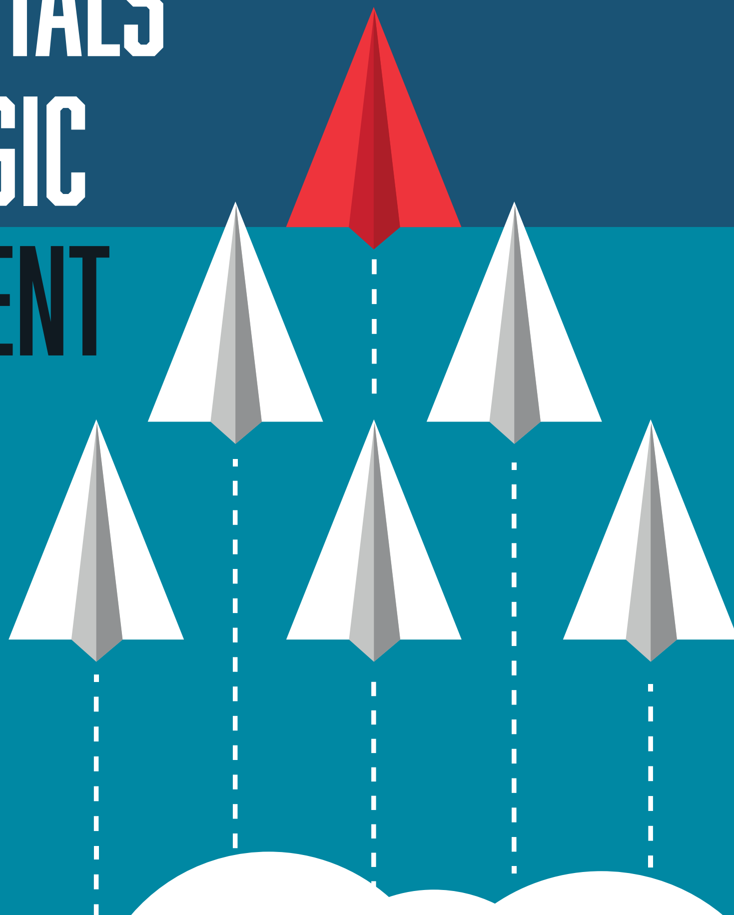

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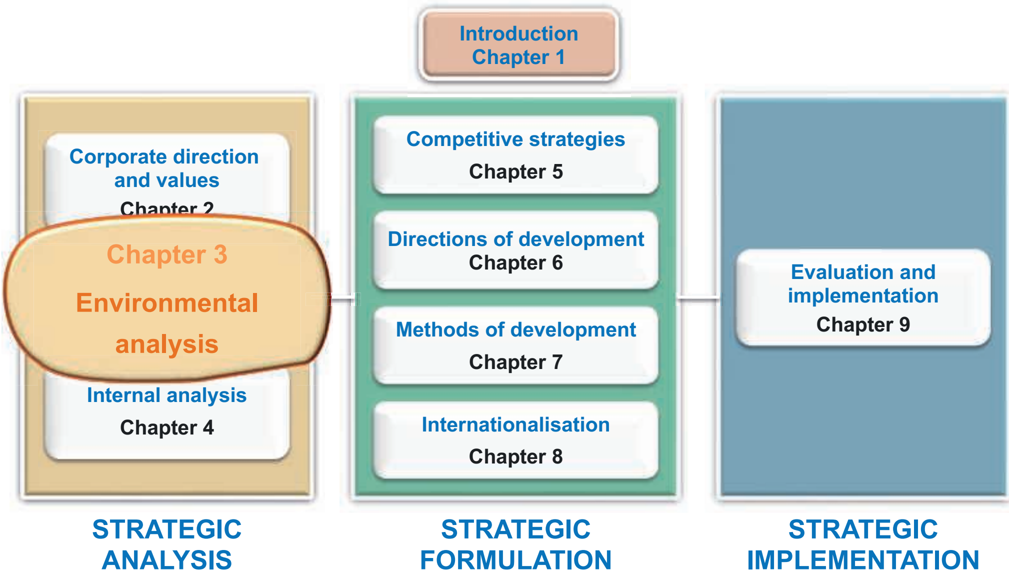


LEARNING GOALS

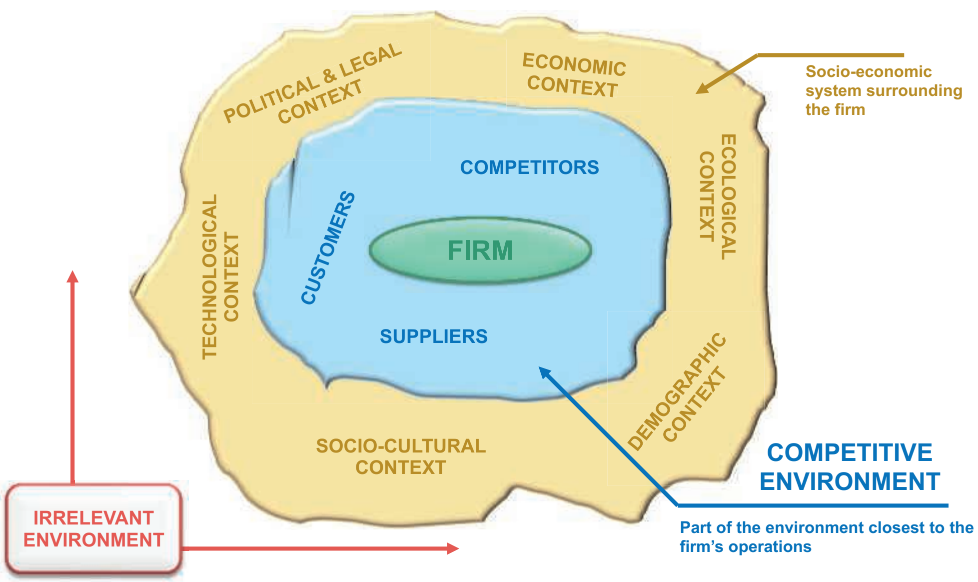
- Know what the company's environment is and its types: general and competitive.
- Study techniques for analysing both the general and the competitive environments.
- Identify segments within an industry, especially from a supply-side perspective.

3.1. THE BUSINESS ENVIRONMENT

The concept of environment refers to everything over which a firm has no control (Mintzberg, 1979). According to this definition, the environment is extremely far-reaching, so it would be almost impossible to analyse from an operational point of view. Therefore, we need to delimit the **relevant environment** for analysis that is made up of all those external factors that influence a firm's decisions and performance (Grant, 2019:60). As they are external factors, a firm cannot control them, but they may, however, have a significant impact on the success of its strategy. Their analysis allows identification of the influence, which may be positive or negative, and therefore the most appropriate way to respond to it.

When analysing the environment, a distinction is often drawn between two levels, namely, general and competitive, with this differentiation explained by both the methodology used and the objectives pursued (Figure 3.1). The **general environment** refers to the external medium surrounding the firm from an overall perspective, namely, the socio-economic system within which it operates. The **competitive environment**, by contrast, refers to that part of the environment closest to the firm's everyday operations, that is, the industry to which the firm belongs.

Figure 3.1. General environment and competitive environment



The great challenge the environment poses to management stems from the uncertainty it entails, as there are factors a firm cannot control. In general, the more dynamic, complex, diverse, and hostile an environment is, the greater the uncertainty the firm faces. The current environment is characterised by high uncertainty due to multiple factors in the recent evolution of the economic, political, and social system, which include the globalisation of the economy, the acceleration of technological change, the progressive removal of international trade barriers, and changes in society's cultural, environmental, and ethical values, amongst others.

A firm's management needs to obtain the best possible information on the nature and extent of the environmental factors affecting it. Factors that favour its operations are known as **opportunities**, whereas those that constitute a hindrance are referred to as **threats**. To identify and evaluate both, a presentation is provided here of several techniques for analysing the general and competitive environments.

See the digital edition

Strategic Tale 4.1: In a pickle!, by Luis Ángel Guerras Martín.

3.2. ANALYSIS OF THE GENERAL ENVIRONMENT

The purpose of analysing the general environment is to identify different variables that affect the firm's operations from a dual perspective: 1) those related to the general political, economic, and social system surrounding the firm, and 2) those linked to its localisation in a specific country, region or geographical area, as not all economic areas or systems are equally attractive for the pursuit of business activities.

Among the former, some of the more significant would be the country's provision of infrastructures (transport, telecommunications, education, etc.), the market's regulatory framework (goods and services, labour market, etc.), public policies (public expenditure and deficit, fiscal and monetary policy, and welfare costs), business culture or the assessment that society makes of its business fabric, and the conduct of the social partners (business and labour organisations) (Cuervo, 1993:364-366).

As regards those variables related to localisation, the model referred to as **Porter's Diamond** suggests each country or nation has its own idiosyncrasies for explaining why some are more competitive than others and why certain industries within each country are more competitive than others. The aim, therefore, is to explain how belonging to a specific country and to a certain industry in that country influences the way a firm obtains an advantageous position for competing with firms from other countries. This model is based on four factors whose combined effect informs a country's competitiveness (Porter, 1990:7-15): 1) provision of relevant and specialised production factors, 2) conditions of domestic demand, 3) highly competitive, similar and auxiliary sectors, and 4) the strategy, structure and rivalry of existing firms.

It should be noted that, as the implementation of a strategy will extend over a long period of time, it seems expedient to investigate how external factors, both those arising from the general environment and those from the competitive one, will manifest themselves in the future. In a turbulent environment in which changes abound, **prospective methods** are required for defining such factors. These methods are characterised by providing a more global vision of the future, giving special importance to qualitative and subjective aspects, assuming that the relationships between variables are dynamic and evolve over time, accepting that the future depends upon the past and on the decisions made in the present, and therefore adopting an essentially proactive and creative attitude toward the future (Menguzzato and Renau, 1991).

See the digital edition

Application 3.1: Spain's global competitiveness index, by Jorge Cruz González and Application 3.2: España Global ("Global Spain"), by Marta Beatriz García Moreno and Susana Mª García Moreno.

One of the instruments given the greatest importance and exposure in the analysis of highly changing future environments is the **scenarios method**. A scenario is a description of the circumstances, conditions, or events that may depict the environment at a future time. This means that a scenario is more of a teaching and learning instrument that helps better understand how the future may unfold, and that the effort a firm's top managers make to define it is just as important, if not more so, than the outcome that may be achieved. Its design requires considering the relevant variables to incorporate, their interrelations, and the ramifications of strategic decisions, thereby preparing management to better adapt to the environment's contingencies.

See the digital edition

Strategic Tale 4.2: What is to become of me? by Irene Campos García and Application 3.3: Scenarios on the influence of the Omicron variant of COVID-19 on the world economy, by Javier Amores Salvadó.

The purpose of analysing the general environment is to assess the wealth and prosperity of the firm's external context, which may affect its performance potential. We shall therefore study two approaches, namely, the environment's strategic profile and industrial districts.

3.2.1. The environment's strategic profile

The **environment's strategic profile** is used to conduct a diagnosis of the general setting. This profile is created in two stages. The first involves drafting a list of the key factors in the environment, i.e., the significant variables that should be analysed. These key factors tend to be grouped according to different dimensions. The second one is designed to assess the impact of those variables on the firm's business to identify the main opportunities and threats.

Given the broad diversity of variables and the complexity posed by the general environment, there is a prior need to define the boundaries of the analysis, both from a territorial perspective (world, country, region, etc.), and according to the relevance of the variables themselves. Lederman (1984) suggests that this selection involves considering two aspects: the possibility of its occurrence and the size of the impact on the firm if and when it does.

With a view to improving the analysis, the variables are organised into several dimensions, which, for our purposes here, are as follows[1]: political-legal, economic, demographic, socio-cultural, technological, and ecological (Figure 3.2).

The **political and legal dimension** concerns government stability and the general policies that public administrations follow in areas such as taxation, labour legislation, foreign trade, or social welfare. The **economic dimension** affects the nature and direction of the economic system in which the firm operates, as reflected in its main economic indicators. The **demographic dimension** covers the main changes in the population's structure, such as the population pyramid, life expectancy, birth rate, ethnic diversity, and migration.

The **socio-cultural dimension** includes both the beliefs, values, attitudes, and lifestyles of the people who make up society and the cultural, ecological, demographic, religious, educational, and ethnic conditions of the social system as a whole. The scientific and technological framework that defines the state of a system is contained in the **technological dimension**. Finally, the **ecological dimension** encompasses aspects such as the availability of natural resources, renewable energy, climate change, recycling and waste management, and, in general, everything that affects sustainability.

The second stage involves rating the behaviour of each of the key factors on a Likert scale from one (1) to five (5) or, to put it another way: very negative (VN), negative (N), neutral or indifferent (I), positive (P) and very positive (VP) (Likert, 1967). Figure 3.2 illustrates a strategic profile. It can be used to observe and readily identify opportunities (scores toward the right) and threats (scores toward the left).

The environment's strategic profile is a very simple and easy-to-interpret tool that involves two major issues: a) identifying the key variables in the general environment, and b) assessing the impact this has on the firm's business. This rating is provided subjectively by the firm's management, reflecting how it perceives the various variables in the environment. Different managers or analysts might therefore reach different conclusions, which means that involving several people in the process might reinforce this perception if there is convergence, or generate a different positioning regarding the same situation if there is divergence. What's more, the correct use of this tool requires considering three important aspects:

1. This analysis has some variants and denominations depending on the authors. Among the best-known is the PESTEL Analysis, or PESTLE, which refers to the acronym for the dimensions analysed: political, economic, socio-cultural, technological, ecological, and legal (Whittington *et al.*, 2020).

Figure 3.2. The environment's strategic profile

KEY FACTORS IN THE ENVIRONMENT

POLITICAL-LEGAL DIMENSION
- Government stability
- Fiscal and monetary policies
- Anti-trust legislation
- Labour legislation
- …

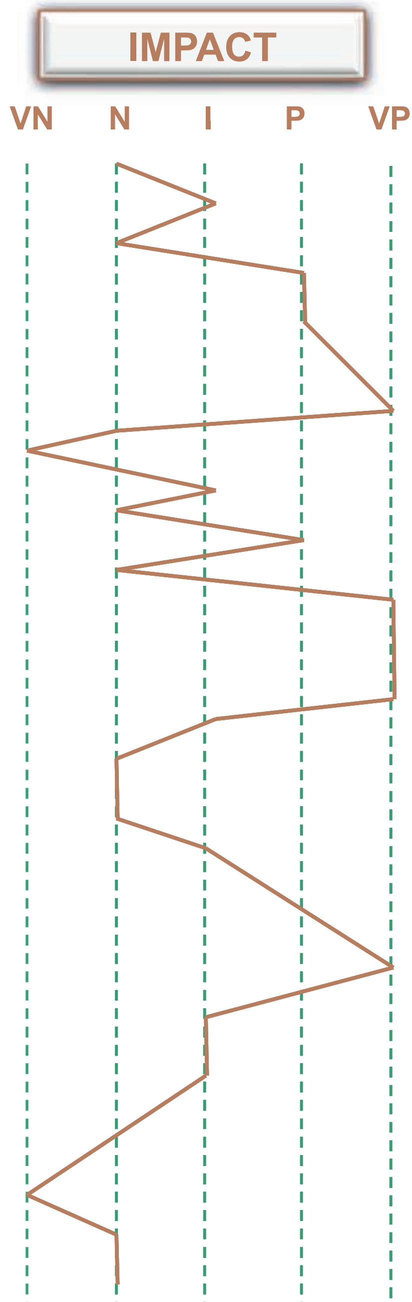
ECONOMIC DIMENSION
- Trends in GDP
- Interest rates
- Rate of inflation
- Unemployment
- Emergent countries
- …

DEMOGRAPHIC DIMENSION
- Population pyramid
- Life expectancy
- Birth rate
- Ethnic diversity
- …

SOCIO-CULTURAL DIMENSION
- Social unrest
- Changes in life-style
- Social values and attitudes
- Level of education
- …

TECHNOLOGICAL DIMENSION
- R&D policy
- Information technologies
- Technological changes
- Technology transfer
- Knowledge protection
- …

ECOLOGICAL DIMENSION
- Natural resources
- Climate change
- Renewable energies
- Waste management
- Energy consumption
- …



– Not all the variables in the general environment have a significant impact on a specific industry or firm, so the relevant factors have to be identified in each case.
– Similar characteristics of the general environment may have different effects in different industries (Dess *et al.*, 2019:47).
– The impact the general environment has may vary significantly even among firms in the same industry.

See the digital edition

Application 3.4: Strategic profile of the general environment for the audiovisual sector in Spain: a view from Atresmedia, by Eva Pelechano Barahona and Fernando E. García Muiña and Brief Case 50: Covid-19 and its impact on the general environment, by Diego Corrales Garay and Antonio Montero Navarro.

Application 3.5

Pets replace children

by Jorge Cruz González

Spanish homes today have more pets than children, with the last decade recording a sharp drop in the birth rate, which is now at its lowest level in 80 years. In fact, since 2015, there have been more deaths than births in Spain. In turn, the number of pets has increased significantly, with more than 13 million officially registered, although some estimates raise the figure to 29 million. When we consider young people's life projects, everything indicates that this trend will grow, with a recent study revealing that one in five millennials have decided to choose pets over children.

Yet it is not just about the growing number of pets in homes; they have also become another member of the family. This change in mentality has had an impact on the costs involved in having a pet, such as food, hygiene products, toys, veterinary care, grooming services, dog walkers, and trainers, whose combined annual turnover now exceeds two billion euros. By contrast, the ever-greater presence of pets has clearly had adverse effects on sectors linked to childcare and education, including nurseries, schools, buggies, booster seats, textbooks, and school supplies.

In several cases, however, the effects are not uniform even within the same activity sector. For example, the outlook within the hospitality sector is pessimistic for the family hotel segment, while "dog-friendly" accommodation is expanding exponentially. The pharmaceutical industry is a similar case, but is expected to increase for pets. Finally, in the textile and footwear industries, the segments aimed at infants and children will see their target audience shrink, while the industry as a whole should not, in theory, be affected.

Sources:
– ANFAAC: *2021 Census Study*.
– INE: *Statistics on births and deaths 2020*.
– El País (19/05/2019): *More dogs than children under 15 years of age*.

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This book is designed as basic support for the higher education of undergraduates in Business Administration and Management and similar degree courses who are interested in subjects related to Management and Strategy and are studying the syllabus in English. The text is especially recommended for short courses and has been adapted to the teaching methods proposed by the European Higher Education Area (Bologna Process).

It may also be of great use as an introduction to the subject for post-graduate students on courses at universities, business schools and similar institutions, in subjects related to Strategy, as well as a required reference tool for all those professionals and business executives who, from a practical perspective, assume a predominantly applied view of business and are responsible for managing and advising firms.

Through this three-pronged approach, the book serves as an introductory handbook that covers the more salient issues and problems that comprise the theoretical corpus of the management model known as Strategic Management. Accordingly, it incorporates a raft of teaching resources –examples, applications, assessment questions, recommended readings, summary tables, case discussions, videos, strategic tales, and more– to provide the reader with a better understanding of the theoretical content developed.

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