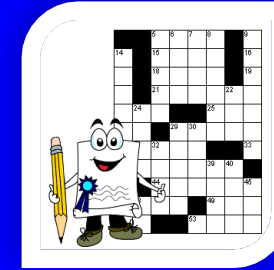


# Eleonora Escalante, MBA - MEng

Strategic Corporate Advisory Services

Creating Corporate Integral Value (CIV)



## Leg 6. Value Chain Analysis Advantages and Disadvantages Value Chain Analysis.

**BIG BUSINESS WORD SEARCH PUZZLE**

T	C	O	R	P	O	R	A	T	I	O	N	A	C	I	Y	M
R	T	I	W	M	O	N	O	P	O	L	Y	D	U	W	N	L
A	X	Q	F	I	N	A	N	C	E	W	N	V	S	A	I	M
D	P	H	D	G	M	I	E	H	O	U	H	E	T	L	U	A
E	C	W	A	A	P	T	W	H	F	U	C	R	O	L	U	N
S	O	R	Y	R	X	M	A	E	S	L	O	T	M	S	S	A
E	M	S	C	M	U	I	G	Q	Y	Q	N	I	E	T	W	G
C	P	B	T	P	A	D	N	U	A	J	T	S	R	R	I	E
R	E	H	Z	O	E	R	L	V	M	I	R	I	S	E	R	M
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S	T	O	B	O	V	H	H	H	T	C	T	R	P	L	S	T
V	I	E	N	F	S	V	J	O	P	I	E	O	O	Z	D	F
K	O	J	C	A	P	I	T	A	L	M	N	Q	R	C	A	N
I	N	V	E	S	T	M	E	N	T	D	C	G	Q	Y	Q	I
D	F	H	E	A	D	Q	U	A	R	T	E	R	S	H	W	W
W	R	E	A	L	E	S	T	A	T	E	A	R	L	X	O	I

ADVERTISING	CUSTOMERS	INVESTMENT	NASDAQ
CAPITAL	FINANCE	MANAGEMENT	REAL ESTATE
COMPETITION	HEADQUARTERS	MARKETING	STOCKHOLDER
CONTRACT	HEDGE FUND	MERGER	TRADE SECRETS
CORPORATION	INVENTORY	MONOPOLY	WALL STREET

**Crossword Source:** <http://www.wordsearchaddict.com/printables/bigbusiness.gif>

## → Leg 6. From Hong Kong to Auckland.

### OUTLINE Leg 6. Value Chain Analysis

01

**Key Concepts  
Value Chain  
Analysis**



02

**Value Chain  
Methodology  
Approach**



03

**Who Uses Value  
Chain Analysis?**



04

**Advantages and  
Disadvantages  
Value Chain**



05

**Innovating  
through Value  
Chain Analysis**



06

**Summary and  
Conclusions**



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**01**  
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**through Value**  
**Chain Analysis**

**06**  
**Summary and**  
**Conclusions**



**We are here!**





## → Leg 6. From Hong Kong to Auckland.

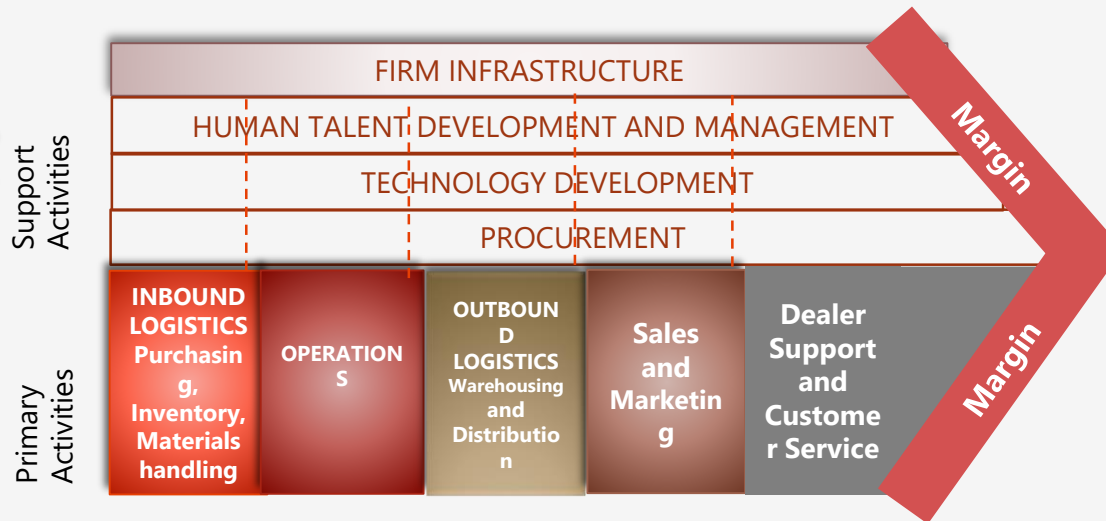
### Advantages and Disadvantages of the Value Chain Analysis

#### 04 Advantages and Disadvantages Value Chain

***The Value Chain Analysis has been used for more than 33 years. This tool has evolved over the years too. But it has advantages as pitfalls too.***



We are  
here!



- Porter's frameworks belong to the Positioning School of Strategy.
- Porter disrupted the business strategy ocean by showing us a field: Strategic Management.
- Porter was a disruptor in the 80s.
- His introduction of specific strategies available to organizations and the contexts in which these strategies work best, gave the "field of strategy, something to sink the teeth into".



## → Leg 6. From Hong Kong to Auckland.

### Advantages and Disadvantages of the Value Chain Analysis

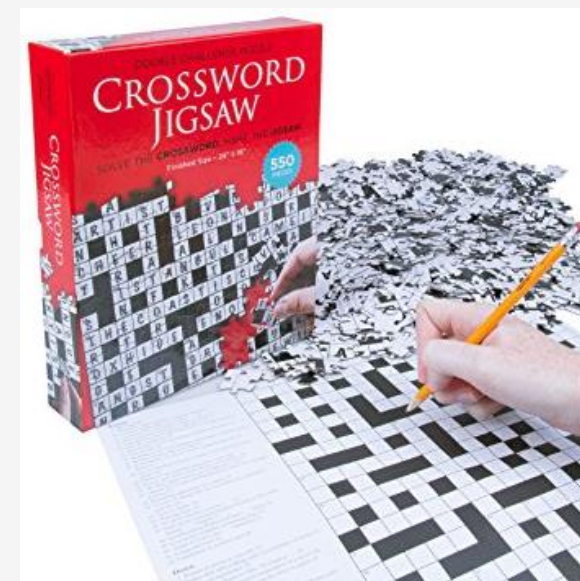
#### 04 Advantages and Disadvantages Value Chain



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***The Value Chain Analysis is one framework from the Positioning School of Strategy...***

- The premises of the positioning School are:
  1. Strategies are generic, specifically common, identifiable positions in the marketplace.
  2. The Marketplace (and its context) is economic and competitive.
  3. The strategy formation process is therefore one of selection of these generic positions based on analytical calculation.
  4. Analysts play a major role in this process, feeding the results of their calculations to managers and Corporate Superstructure (decision makers) who officially control the choices. External consultants emerge to help the decision makers to validate the choices.
  5. Strategies come out from this process full blown and are then articulated and implemented. In effect, market structure drives deliberate positional strategies that thrust organizational structure.



***Value Chain Analysis is  
like playing Crossword  
Jigsaw***



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### Advantages and Disadvantages of the Value Chain Analysis

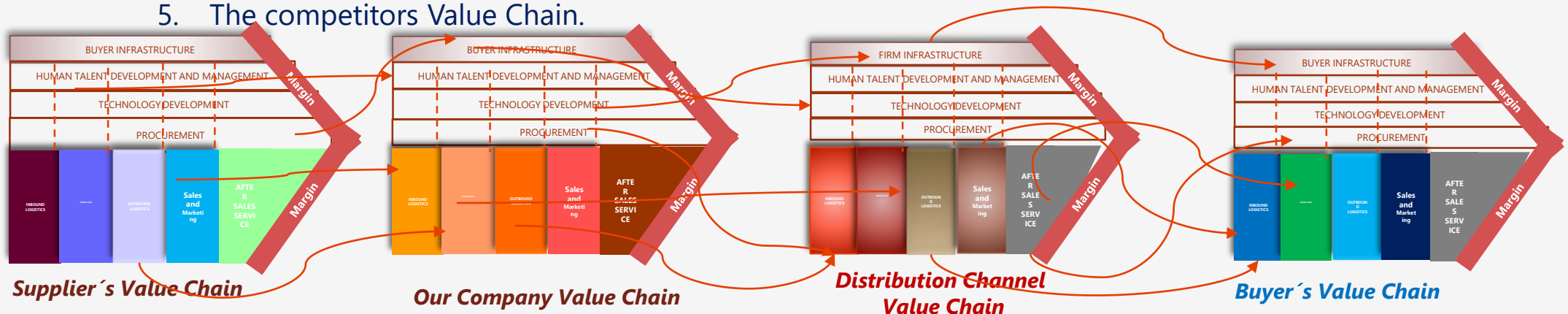
#### 04 Advantages and Disadvantages Value Chain



***We have seen how to use Value Chain Framework for Cost Analysis and Competitive Differentiation Analysis. It can be used to design Organizational Structures, and Evaluation and Planning.***

The Value Chain Framework can be used in addition for **evaluation and planning**. This is because the Value Chain offers a link between the company's own Value Chain and other value chains such as:

1. The Supplier Value Chain
2. The Buyer Value Chain
3. The Distribution Channel Value Chain (Direct Retailers, Indirect Retailers, Wholesalers, Distribution, Internet, Apps)
4. The company's Industry Value Chain
5. The competitors Value Chain.



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## → Leg 6. From Hong Kong to Auckland.

### Advantages and Disadvantages of the Value Chain Analysis

04

#### Advantages and Disadvantages Value Chain



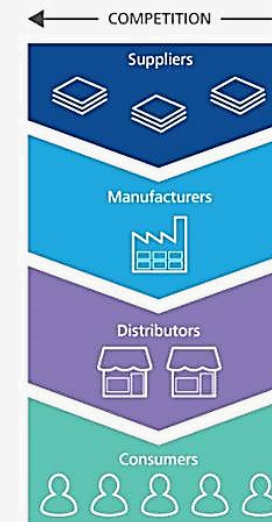
We are here!

#### ***The Value Chain can also play a role in designing organizational structures.***

- When we see the relationships between certain value activities and other value activities, we can see the links between people at different departments. The value chain tool helps to identify groups of teams which have to collaborate more, and understand why and how the company need to coordinate those teams. This effort of coordination is called integration.
- Organizational Structure designs using Value Chain Analysis are usually the best in the market, because organizational units tend to keep the linkages within it and with suppliers, buyers or channels.
- An organizational structure that corresponds to the value chain will improve the company ability to create and sustain competitive advantage.

Figure 1: Supply chains evolve into value webs

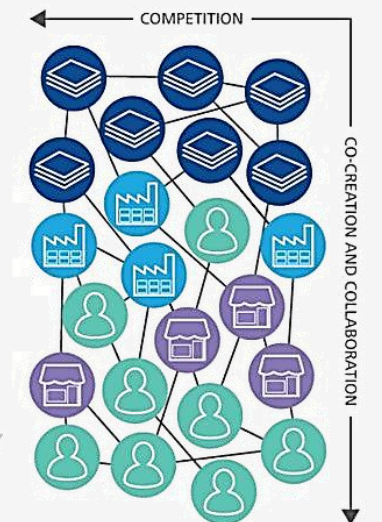
Linear supply chains are evolving into...



Value is based on the production of goods and services

Source: Deloitte analysis.

complex, dynamic, and connected value webs



Value is based on knowledge exchange that drives proactive production of goods and services

Graphic: Deloitte University Press | DUPress.com

*Value Chain helps to define organizational structures (of the past) and the future.*  
Source: Deloitte.





## Leg 6. From Hong Kong to Auckland.

### Advantages and Disadvantages of the Value Chain Analysis

#### 04 Advantages and Disadvantages Value Chain

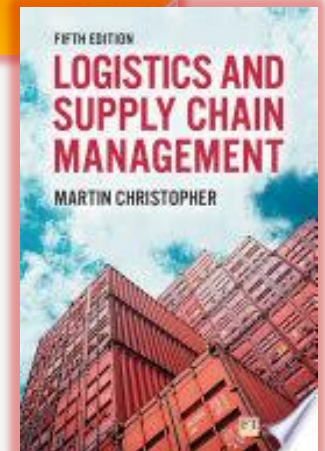
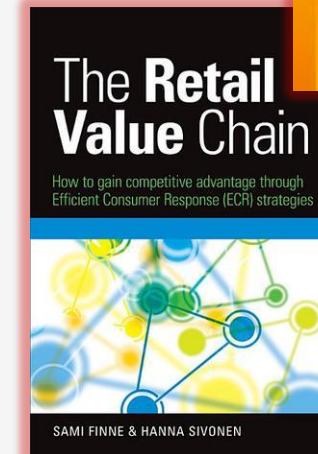
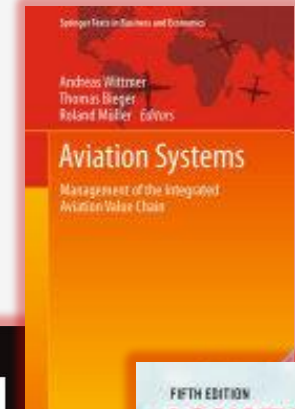


#### **Advantages of the Value Chain Analysis.**

1. "Value Chain Management involves an in-depth assessment of value drivers in an industry or organization and has many different commercial applications".
2. "Once a business understands its source of value (uniqueness) creation , it can make informed choices on how and where to grow, manage vertical and horizontal integration, identify the optimal distribution channels and push cost optimization".
3. Any industry that sells products or services to consumers can benefit from the Value Chain Analysis
4. Any company that wishes to remain competitive in the new global economy should consider to do a Value Chain Analysis as mandatory.
5. The uses of the Value Chain Analysis are multiple: to enhance value to buyers, to reduce costs, to decision making about growth and expansion or spinoffs, to understand linkages, company cost drivers and buyer's uniqueness drivers.



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*Innumerable books about Value Chain have been published. More than a million books on the topic!*







## Leg 6. From Hong Kong to Auckland.

### Advantages and Disadvantages of the Value Chain Analysis

#### 04 Advantages and Disadvantages Value Chain

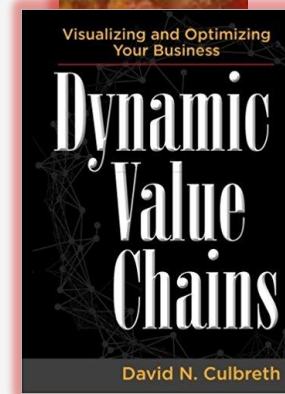
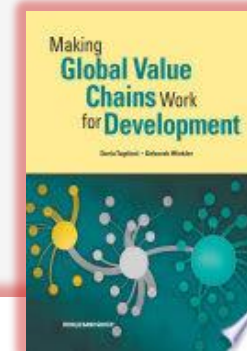
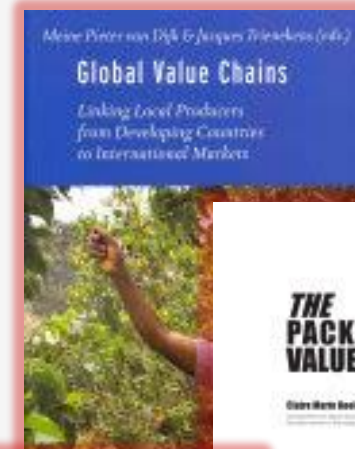


#### **Advantages of the Value Chain Analysis.**

6. The Value Chain tool is a versatile and flexible strategy tool which can be used as many times to review your business depending on the context, trends, life cycle or expansion plans.
7. It helps you to understand the organization issues.
8. Comparing your business model with your competitors using the value chain can give you a much deeper understanding on how to react and anticipate your strategy routes.
9. The Value Chain Analysis has evolved to be used in so many ways since its conception: Supply chain analysis, Global Value Chains, Industry Value Chains, Country Value Chains, Shared Value Chains, Digital Value Chains, Virtual Value Chains, etc. As it can be modified according to the value activities for each company, life stage or industry, we see several value chains in the global market place.
10. It can be adapted for any type of business – manufacturing, retail or service, big or small, global, etc.



We are  
here!



*Innumerable books about Value Chain have been published. More than a million books on the topic!*



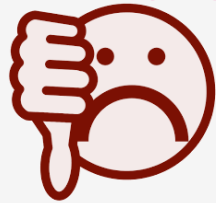
## Leg 6. From Hong Kong to Auckland.

### Advantages and Disadvantages of the Value Chain Analysis

#### 04 Advantages and Disadvantages Value Chain

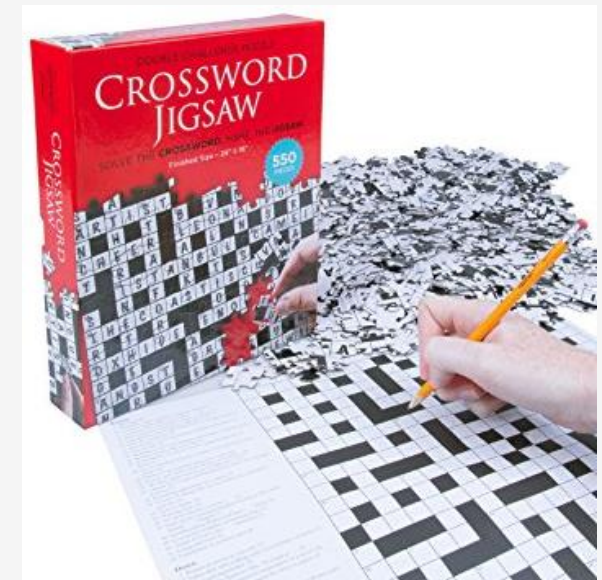


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#### *Disadvantages of the Value Chain Analysis.*

1. Conducting a thorough value chain analysis, properly assessing which measures are worth implementing, and then planning to action is not an easy task. It is not a "plug and play" tool.
2. It requires the help from an experienced external consultant, and a multidisciplinary commitment from all the company teams to build it step by step with "reliable information".
3. To do a Value Chain Analysis is not easy. The Process of evaluating a value chain can be lengthy. It requires time, patience and dedication.
4. I always compare the Value Chain Analysis as a Crossword puzzle. Why? Because every single sub-activities of a value activity of the Value Chain Analysis is connected with another sub activity, and it requires a strong level of dedication, observation, knowledge of the industry and buyers, attention to details, etc.



*Value Chain Analysis is like  
playing Crossword Jigsaw*

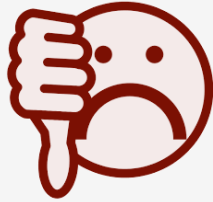




## Leg 6. From Hong Kong to Auckland.

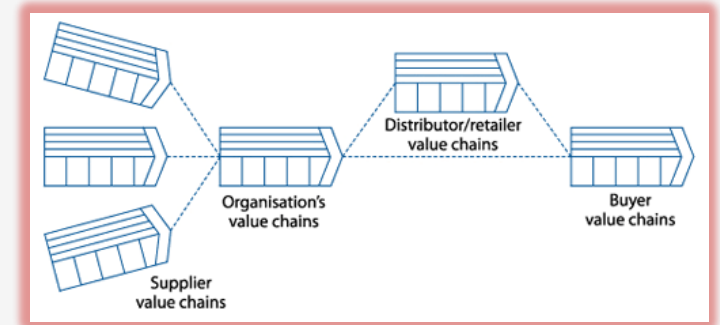
### Advantages and Disadvantages of the Value Chain Analysis

#### 04 Advantages and Disadvantages Value Chain



#### **Disadvantages of the Value Chain Analysis.**

5. There are several myths related to value chain analysis, given that is used many times only by the suppliers and operations experts.
6. In addition, many consultants only is the Value Chain for Cost Analysis, leaving the tool benefits cut in half because it is not used for "Uniqueness or Differentiation Analysis".
7. Detractors of the VCA may accuse this tool of being "out of date". It is not. The tool is a framework to be filled with information and data. If the companies evolve to become digital or based on "digital capabilities", the VCA can be modified perfectly with new contexts and it works.
8. Value Chain Analysis base discipline origin is Economics (Industrial Organizations). It requires analytical staff or specialized consultants to apply it. People from other social or human studies background may perceive it stiff, complex and too rigid or static.



*The Value Chain when used wrong or just partially (without considering the buyers, suppliers, complementors and distribution channels) can lead to wrong conclusions.*





## Leg 6. From Hong Kong to Auckland.

### Advantages and Disadvantages of the Value Chain Analysis

04

#### Advantages and Disadvantages Value Chain

#### ***Critique of the Positioning School are criticisms to Value Chain Analysis too.***

The positioning school is one of ten schools which have given us different “strategy process” views and models. The critiques of the positioning school can be grouped in three categories:



We are here!



##### Concerns about the Focus

- The focus is narrow (oriented to the economics, quantifiable as opposed to social or political aspects)
- It has been mis-utilized only for managing costs.



##### Concerns about the Context

- The context is also narrow, because it based on data.
- Paralysis-analysis
- Difficulty to balance the internal capabilities and external conditions of the business
- Industry representatives do not create nor protect or evolve their own value chains but the analysis is done by outsiders.



##### Concerns about the Process

- Massaging the numbers is what is expected. Strategists are supposed to deal in abstractions on paper, detached from the tangible world of making products, deliver and closing sales.
- The calculation of analysts can displace the commitment of the true actors.
- People from the business units and at the front line have to be included in VCA.



##### Concerns about the Strategies

- It promotes copycatting and “benchmarking” with competitors.
- It is “square” to try to categorize and fit everything in boxes of value activities
- Generic Strategies of low cost, differentiation, focus-differentiation or stuck in the middle are some of the strategies. There are more strategies.



## → Leg 6. From Hong Kong to Auckland.

### Advantages and Disadvantages of the Value Chain Analysis

04

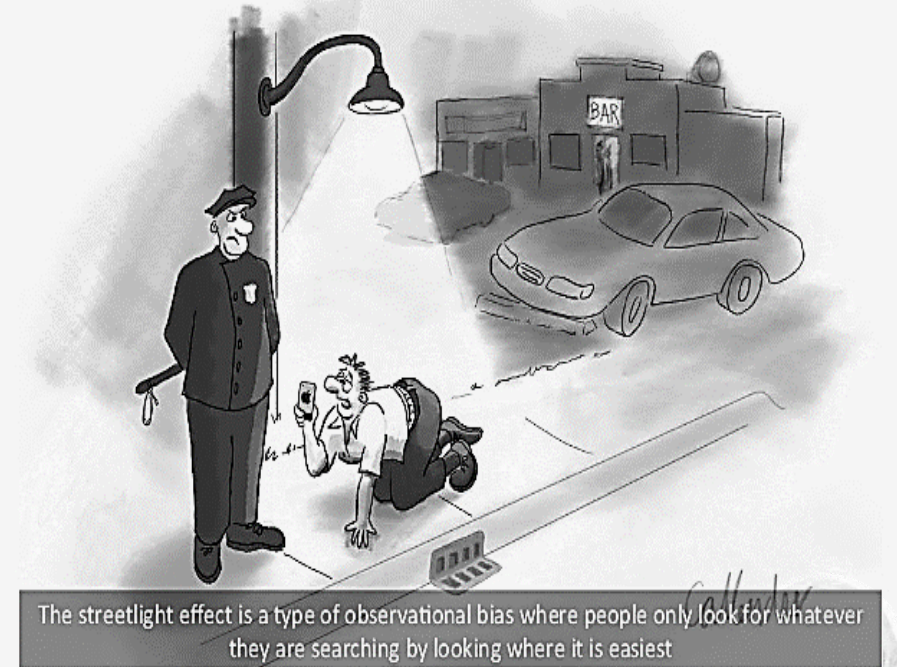
Advantages and  
Disadvantages  
Value Chain



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#### ***Pitfalls of Cost Leadership Strategies, when using the Value Chain Analysis.***

- Many CEO's have learned the concept of Value Chain. Nevertheless, it is usually related to "operations" or "supply", and what is worst it is used "wrong" exclusively on the "cost of manufacturing activities". ***It is a mistake to use the Value Chain, without considering other value chains linked to the company.***
- ***The Value Chain Analysis of one company is unique.*** No company can be the same, and in consequence we can't adapt the generic drawing of the value chain framework and fit it without a conscious analysis. The disadvantage of using generic Value Chains kill the opportunity to define our own value chain.
- ***Firms often misdiagnose cost drivers and calculations,*** because they think about costs as accountants.
- ***Overlooking indirect or small activities:*** cost reduction programs usually concentrate on large cost activities or direct activities. Indirect activities often escape attention altogether
- ***Linkages in the value chain are innumerable.*** Some companies fail when recognizing all the linkages that affect costs particularly with other value chains



The streetlight effect is a type of observational bias where people only look for whatever they are searching by looking where it is easiest

"I'm searching for my keys."

## → Leg 6. From Hong Kong to Auckland.

### Advantages and Disadvantages of the Value Chain Analysis

04

**Advantages and  
Disadvantages  
Value Chain**



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here!**

#### ***Pitfalls of Cost Leadership Strategies, when using the Value Chain Analysis.***

- **Contradictory Cost Reduction:** If we wish to reduce costs in one item of one value activity, don't dissipate it by using other antagonist action. Example: Try to gain market share to reap the benefits of scale economies and at the same time dissipating scale economies through model proliferation.
- **Unwitting Cross Subsidy:** Conventional accounting systems rarely measure all the cost differences among products, buyers, channels or geographic areas, and they often charge excessive prices on some items and subsidize prices charged on others.
- **Thinking Incrementally:** Cost reduction efforts often strive for incremental cost improvements in the existing value chain. Don't reconfigure the value chain when looking for cost reductions, the reconfiguration happens when as a final .
- **Undermining differentiation:** Cost reduction can undermine differentiation if it eliminates sources of uniqueness to the buyer.



*Incremental change brings  
incremental results.  
Radical change brings the  
potential for radical results.*





## Leg 6. From Hong Kong to Auckland.

### Advantages and Disadvantages of the Value Chain Analysis

04

#### Advantages and Disadvantages Value Chain



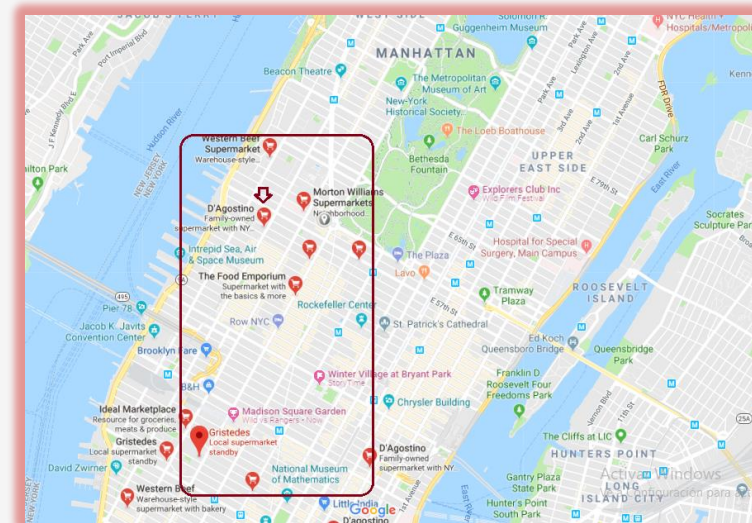
We are here!

#### Pitfalls of Differentiation Strategies, when using the Value Chain Analysis.

- **Uniqueness that is not valuable:** Uniqueness doesn't lead to differentiation unless it lowers "BUYER COST" or raises BUYER UTILITY. The most successful differentiation comes from sources of value the buyer can perceive and measure or from sources of value extensively signaled.

$$\text{Buyer's Value} = \text{Utility} \uparrow - \text{Total Price} \downarrow$$

- **Too Much Differentiation:** If product quality or service levels are higher than buyer's need, for example, a firm may be vulnerable to competitors with the correct level of quality at a lower price.
- **Lack of understanding** on how a firm's activities relate to the **buyer's** value chain. I will explain this in the next slide.
- **Too big a price premium:** A price premium from uniqueness is a function of the Buyer's Value and its sustainability. If the premium gets too high, the buyer will abandon the firm.



Example: The appropriate price premium for the fresh salmon filet at D'Agostino 10<sup>th</sup> Ave-54 street is a function not only of the extent of differentiation, but also of its overall relative cost position. D'Agostino has to keep its price in proximity to competitors around such as Whole Foods Market, Morton Williams, The Food Emporium and Gristedes.



## → Leg 6. From Hong Kong to Auckland.


### Advantages and Disadvantages of the Value Chain Analysis

#### 04 Advantages and Disadvantages Value Chain



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#### *Pitfalls of Differentiation Strategies, when using the Value Chain Analysis.*

- **Lack of understanding** on how a firm's activities relate to the **buyer's** value chain. By observing your clients, you have half of the story. It is important to KNOW YOUR CLIENTS. Let me explain this with a simple example.
  - If you have the opportunity to see me. you may think I like to use a lot of moisturizer (brilliance over my skin) or tons of makeup over my face.
  - By simply observation you may assume I like to buy cosmetics and get a wrong idea about my use criteria of these products.
- 
- If you have the opportunity to know me, you will understand that I practice swimming several days per week, and after my workouts my face, particularly my cheeks are tanned, burned and very red.
  - It has anything to do with cosmetics.
  - I usually don't use make up, and only natural earthy terracotta colors, just when is needed.

**KNOW YOUR CUSTOMER PLEASE**





## → Leg 6. From Hong Kong to Auckland.

### Advantages and Disadvantages of the Value Chain Analysis

#### 04 Advantages and Disadvantages Value Chain



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#### ***Pitfalls of Differentiation Strategies, when using the Value Chain Analysis.***

- ***Ignoring the need to signal value:*** Many firms ignore the need to signal value, basing their differentiation strategies ONLY on use criteria. Particularly when a recession happens, high-end clients tend to refrain about consumption of overpriced items, and it is not wise for the company to ignore signaling criteria. Other competitors can attack the company providing inferior value, but having a better understanding of the buyer's purchasing process in economic downturns or slowdowns.
- ***Not knowing the cost of differentiation;*** remember differentiation does not lead to superior utility unless its perceived value to the buyer exceeds its price.

$$\text{Buyer's Value} = \text{Utility} \uparrow - \text{Total Price} \downarrow$$

Don't assume that differentiation "can" make economic sense. Even if spending more on differentiation that will be recovered in the price premium. Failing to exploit ways of reducing the cost of differentiation by understanding its cost drivers happens very often.

- ***Focus on the product instead of the whole value chain;*** Some firms blame the value chain analysis when they only see it as a tool for understanding how to do a product. These companies fail to exploit opportunities to differentiate in other value activities.
- ***Failure to recognize buyer segments:*** Do you remember the topic Segmentation from Leg 3? Well, the buyer segments are important. The buyer purchase criteria and their ranking vary among buyers. Identify your clients, and understand the needs of the buyer very well.



## → Leg 6. From Hong Kong to Auckland.

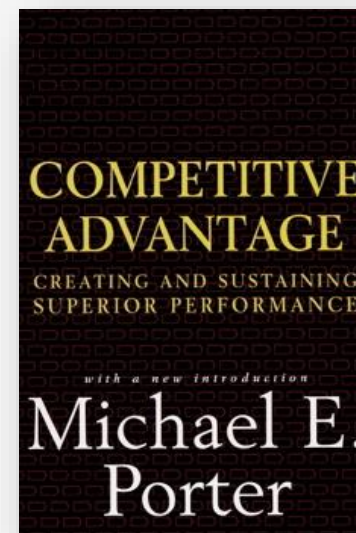
### Advantages and Disadvantages of the Value Chain Analysis

#### 04 Advantages and Disadvantages Value Chain

***On my next post we will continue sailing with the subject Innovations with Value Chain Analysis. We will also see the Shared Value Analysis as one of these innovations.***

Solution of  
the  
Crossword:

SOLUTION TO BIG BUSINESS PUZZLE



All the material  
shared today is  
based in the book  
***“Competitive  
Advantage,  
Creating and  
sustaining  
Superior  
Performance”***,  
From Michael  
Porter.

*Thank you!*



***Crossword Source: <http://www.wordsearchaddict.com/printables/bigbusiness.gif>***