CHAPTER 5 - Strategic position

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5.1 Introduction

The strategic position, often stated in terms of the strengths, weaknesses, opportunities, and threats (SWOT) analysis, brings the internal and external review together (Mintzberg, 1987; Marshall and Johnston, 2010). Strategies could be developed based on the environmental analysis, for example, noting a trend or gap in the market, or exploiting new technologies — what might be described as taking an outside-in approach to strategy (Day and Moorman, 2010). They could also be developed based on a key strength or competence of an organization, which could be described as the resource-based view (Barney, 1991).

SWOT is a widely used strategic tool (Fehringer et al., 2006; Gunn and Williams, 2007; Du Toit, 2016) but can often result in the extremes of either a very long wide-ranging list, or a very brief list of issues in general terms, neither of which is very useful for strategy development (Hill and Westbrook, 1997). Ideally, the SWOT should consist of a prioritized list of key strengths, weaknesses, opportunities, and threats arrived at by the process of consensus. It should not be a series of checklists (Valentin, 2001). It is also worth consulting external experts to assist in identifying the key trends in the environment.

This chapter reviews the process and use of SWOT analysis in developing strategies that help to close the gap between what the organization wants to achieve and the likely outcome if it continues with the existing strategy.

5.2 Learning outcomes

After studying this chapter, you will be able to:

- Evaluate the use of a SWOT analysis in the strategic management process
- Undertake a SWOT analysis for a given organization based on information provided
- Understand and discuss the concept of GAP analysis
- Discuss the contribution that management accounting can make to the analysis of an organization's strategic position

5.3 The strategic position and SWOT analysis

Active reading. Note the process of developing the SWOT and how it can be used in practice, but also note the subjective nature of deciding what factors to include and where on the cruciform chart they are placed. Also note the potential sources of the strengths, weaknesses, opportunities, and threats and how other models and frameworks can be used to aid their identification.

Video link [SWOT and GAP analysis](https://www.youtube.com/watch?v=t9L6IBW16z0)

[https://www.youtube.com/watch?v=t9L6IBW16z0]

The strategic position is also known as the SWOT analysis—strengths, weaknesses, opportunities, and threats. Primarily strengths and weaknesses come from the internal appraisal, and opportunities and threats come from the environmental analysis.

Changes in the business environment are identified during the environmental analysis phase. Still, it is only when these are matched against the organization's ability to deal with the change that it becomes evident whether the change represents an opportunity or a threat (Hofer and Schendel, 1978).

For example, proposed changes to the regulatory environment could present opportunities for expansion and product or market development if the organization has the resources to take advantage of the opportunity. However, if the organization has few resources, such that dealing with the changes will be problematic, it could pose a threat to its ability to meet the strategic objectives. It is significant for competitor analysis as understanding the potential impact of changes in the environment on competitors compared to the organization is a key part of developing a sustainable competitive strategy. The deregulation of financial services that occurred in many world financial markets during the 1980s illustrates the importance of understanding the consequences of an environmental development opening up the potential for new competitors to enter the market. This deregulation led to organizations other than financial institutions, such as supermarket chains, being able to diversify into offering banking facilities. In contrast, existing small financial organizations with fewer resources at their disposal began to find it difficult to compete, often leading to their acquisition by larger institutions.

The cruciform diagram shown in Figure 5.1 is often used to construct a SWOT. The cruciform chart ideally limits the number of elements that are eventually included. In practice, there will be many elements that could be included, some of which are subjective (Mintzberg, 1987). The key is that the SWOT elements are prioritized and reduced to a manageable number.

Figure 5.1 Typical cruciform chart layout for SWOT

The axes denote that strengths and weaknesses are relative to the competition. This relativity is significant in determining what the actual strength or weakness might be. For example, if an organization considers that it has a very experienced and highly skilled workforce, it may classify this as a strength. But if the competitor organizations in the industry also have a very experienced and highly skilled workforce, then this may not be the real source of strength and hence a competitive advantage. The organization that manages its workforce more effectively may be able to achieve a competitive advantage indicating that its real strength is the ability to manage the workforce more effectively than the competition, not the highly skilled workforce itself. This example illustrates that SWOT can be entirely subjective; however, where possible, it is best to base the analysis on evidence gathered from factual sources. That said, SWOT elements are often a mix of both factually supported ideas and subjective judgment.

Strengths can be ascertained by conducting a brainstorming session with functional managers. This brainstorming can, however, produce a long list, but it provides a comprehensive view of the organization's capabilities from those that know the functions well. Indeed, strengths and weaknesses can sometimes come from surprising sources. The use of technology within the provision and dissemination of management information, even management accounting information, could mean that managers are better informed than some of their competitors. Speedy provision of information means they can act promptly to changes in the local environment and customer demands, or keep costs under control more effectively due to prompt information supporting a cost led strategy. Sadly, this could also be the source of a weakness in that the provision of management accounting information is such that managers have no clue as to which are the profitable products or profitable customers. Or, the time lag between incurring the cost, reporting it, and their ability to take action, means that costs are not always under control.

The initial list can then be reduced by the process of discussion based around asking what the organization does well or any unique resources it possesses. It is sometimes difficult to assess the aspect of “relative to the competition” as it is difficult to gain enough accurate information about the inside workings and competencies of competitors to be able to make an objective judgment. Therefore, in practice, the strengths and weaknesses are not always assessed against the competition.

It is useful to think in terms of core competencies and distinctive competencies. Core competencies are those competencies that are essential to overall performance and success in the industry sector. A distinctive competence is any competence that distinguishes an organization from its competitors and hence is a source of competitive advantage (Mooney, 2007). A strength might emanate from a strong presence of a core competence but would undoubtedly arise from the presence of a distinctive competence. In contrast, any areas where these can be improved upon might signify a weakness.

Competitor analysis can aid the strengths and weaknesses aspects of SWOT. For example, attempting to identify the portfolio analysis of the competitors or the efficiency of its value creation system and comparing it to the analysis of the organization’s portfolio and value system can help to identify areas where it has the potential for competitive advantage. Where a competitive advantage existed, it is always worth reviewing whether the organization has retained its competitive advantage as competitors will respond. There is no guarantee that where a competitive advantage used to exist, it remains forever. Techniques such as competitor benchmarking (see section 10.9), which compare aspects of an organization’s performance to that of its competitors, can also help assess the relative strengths or weaknesses.

The opportunities and threats originate in the environment and thus are available to all industry members. The analysis conducted from the PESTEL or Porter’s five forces can provide the basis for identifying the opportunities or threats. As with the strengths and weaknesses, there is a degree of subjectivity and discretion in the practical determination of opportunities and threats. There is a subtle difference between what might be described as a strategic option available to one organization and an opportunity that is present for all industry members. For practical purposes, an opportunity is something that presents itself from the environmental analysis as being a possible strategic option that the organization can pursue.

Another area of subjectivity that arises is deciding whether issues identified present a threat or represent a weakness. The best way to decide between the two is to determine whether the organization has direct control over the outcome. If it does, then it is probably internal and represents a weakness as the organization can address the issue directly. If, however, the source is external, the organization may be able to influence, but not directly control the event. In this case, it is best viewed as a threat for which there is still some uncertainty about the outcome. Hence the organization needs to formulate, and be prepared to implement, an appropriate response.

Phadermrod et al. (2019) suggest linking the SWOT with an Importance-Performance Analysis (IPA). An IPA measures the satisfaction from customer satisfaction surveys based on two components of a product's or service's attributes, that is, the importance of a product or service to a customer and the performance of the organization in providing the product or service (Martilla and James, 1977). The technique suggested by Phadermrod et al. is that the strengths and weaknesses can be identified from the IPA matrix of the organization. This has the advantage of making it very customer focused.

The IPA analysis entails undertaking a customer survey in which questions can be asked about the competitors' products or services, and this provides the basis for comparing the organization with competitors. This comparison will also provide input to the strengths and weaknesses relative to the competitors but also helps to identify opportunities to gain a competitive advantage or forewarning of a potential threat from competition. Strategies can then be developed to take advantage of opportunities and minimize potential threats. Focusing on customers and competitors has the potential to miss opportunities and threats from sources other than competitors but has a benefit of focusing (for part of the analysis) on the competitive advantage aspect of strategy development.

An example of a SWOT containing some elements that relate to finance and accounting, illustrating that these can be viewed as strengths or weaknesses, is shown in Table 5.1. The opposite situation to the example given would turn a strength into a weakness.

Table 5.1 Example of SWOT elements

Strengths	Weaknesses
• Strong brand image rated as 2nd highest valued brand in the sector by recently published consumer survey • Established business for over 150 years • Strong product portfolio in global markets – contains recently acquired brands recognized for sustainability • Successful track record of growth via acquisition and merger. • Strong balance sheet and ability to secure future finance. • Maintained or increased dividend levels for the last 20 years – seen as 'invest and hold' by city analysts. • Ranked 2nd in the Times, 'Good Employer' survey of 2020.	• High cost structure • Declining profitability of significant brands over the past 2 years. • Poor integration of management information and accounting systems from recent acquisitions. • Lack of internal innovation and R & D capability • The senior management team has been in place for many years – no succession plan in place.

Opportunities	Threats
• Deregulation of some markets where governments are seeking to offset a recession by attracting foreign direct investment. • The growing affluence of emerging economies increasing the potential demand for products. • Changing customers' habits towards sustainable products.	• Strong and growing competition from global companies. • Rising raw material prices for some leading brands in markets where competition is strong. • Overseas economies are beginning to experience recession and declining living standards. • New technologies could reduce the need for some key products currently sold in developing countries.

5.3.1 Developing strategies from SWOT

Active reading. Note how the elements of SWOT can be combined to develop strategic options, and the use of factor analysis to aid the prioritization process.

The reason why the cruciform chart presentation is adopted is to aid the process of developing potential strategies. For example, ideally, the intension would be to match the strengths with the opportunities as the resource capability enables the organization to take advantage of the opportunity. It would also be desirable to address the weaknesses. One of the reasons why a change in the environment might pose a threat is because the organization does not have the resources capability to deal with it due to a weakness; therefore, the environmental change poses a threat. If the weakness is addressed, it may be that the environmental change no longer presents a threat as it can now be dealt with successfully. It may even turn the threat into an opportunity. Based on the SWOT analysis, a good strategy will build on the strengths, address the weaknesses, grasp the opportunities, and avoid or minimize the threats.

Weihrich (1982) suggested a TOWS matrix that could be used to develop strategic options from the SWOT. This analysis creates potential options shown in Figure 5.2.

SO Use strength to take advantage of an opportunity	WO Minimize or remedy a weakness to take advantage of an opportunity
ST Use strength to deal with a threat	WT Minimize weakness and avoid or minimize threat

Figure 5.2 Potential options from a SWOT analysis

The SO represents a maxi maxi situation, in which the strength can be used to take advantage of the opportunity. For example, a retail organization with a large customer base taking advantage of the deregulation of financial services to launch their branded credit cards.

The WO is a mini maxi situation where the weakness is minimized, which may present opportunities. For example, the use of outsourcing may enable an organization to take advantage of an opportunity by accessing an external resources capability that it does not possess itself.

The ST is a maxi mini situation where a strength is used to deal with a potential threat. For example, a pharmaceutical company applying its financial muscle to acquire one of the leading U.S. Health Maintenance Organizations (a medical insurance organization that provides health services) to counter increasing buyer power.

The WT represents a mini mini situation where the intension is to minimize both the weakness and the threat. For example, withdrawing from an overseas market in the face of intense competition from more established local players due to an economic recession in that country, and thus focusing attention on the organization's domestic market where it occupies a strong market position.

The use of the cruciform chart helps in the prioritization of the strengths, weaknesses, and so on so that it provides a focus for competitive advantage and management attention. The technique of strategic factor analysis can be used to aid the development and evaluation of strategic options. In this technique, the elements of the SWOT are prioritized, ranked, and given a weighting. The importance of the strengths and weaknesses is assessed and given a number anywhere from 0.01 (not very important) to 1 (very important). These can be converted to percentages or left as decimal numbers. In any event, the total of the values assigned to the strengths should equal 1 or 100%, as should the values that have been assigned to the weaknesses. The strengths and weaknesses are then prioritized and ranked. Some forms of this analysis suggest rating them with a value 1 – 3 with 1 being a minor strength or weakness and 3 being a significant strength or weakness. Whichever method is used, it allows for a prioritization of the strengths and weaknesses, as shown in Table 5.2 for the strengths. Note the ranking is between 1, being the least significant to 4 the most significant.

Table 5.2 Factor analysis and weighting of strengths

Factor—Strengths (examples)	**Importance Weighting**	**Priority Ranking**	**Weighted ranking score**
Strong brand identity	20%	3	0.6
Strategic locations	10%	4	0.4
Innovative product range	30%	1	0.3
Highly skilled workforce	40%	2	0.8
Total			2.1

The same process would be done for weaknesses.

For the opportunities and threats, the importance becomes the potential impact on the business ranging from 0.01 low impact to 1 being a high impact on the organization. The ranking becomes the probability of the opportunity or threat occurring. For example, 1 equals low probability, to 3 (or 4) equals high probability. As with the strengths and weaknesses, a rating is calculated for each opportunity and threat to arrive at a prioritization.

This analysis can then be developed further to help evaluate various strategies from the combinations of SWOT. For example, the overall assessment of the strategic option A may be represented in Table 5.3. Here we could imagine that two key strengths come into play to take advantage of an opportunity, while a weakness is addressed to avoid a threat. The weighting and ranking are taken from the tables constructed for each SWOT element.

Table 5.3 Factor analysis score for strategy A

Factor	**Weighting**	**Ranking**	**Weighted ranking score**
Key strength 1	30%	1	0.3
Key strength 2	40%	2	0.8
Key weakness 1	40%	1	0.4
Key opportunity 2	30%	2	0.6
Key threat 1	50%	1	0.5
Total strategy A			2.6

The various strategies developed from the analysis could be compared and used as part of the decision-making process. However, a problem with this approach is that strategy cannot be reduced to a set of numbers. Therefore, although providing some information on likely outcomes, it should never be the sole basis for deciding the future strategy. It also carries with it a high degree of subjective judgment despite being represented by a numerical analysis.

Weihrich (1982) also makes the point in the discussion of the TOWS analysis that the timing of strategies needs to be considered as the environment, and resource capabilities can be dynamic.

Learning activity. Pick an organization with which you are familiar and construct a SWOT. You could consider undertaking an environmental analysis of the industry first to help identify any opportunities or threats.

You may be able to think of potential strengths and weaknesses from your knowledge of the organization, but try reviewing news articles about the organization and its webpages, as this will help you think of what it is good at and areas where it needs to improve. Remember, this is a subjective exercise.

You could also access the latest set of financial accounts from its webpages and conduct a financial analysis to see if there are any potential strengths and weaknesses that arise, for example, high levels of gearing, poor financial performance, or other areas of good or poor financial management.

Do not worry about trying to balance the elements so that you have the same number of ideas under each of the SWOT headings. In practice, there may be more Ss and Ws than Os and Ts.

5.4 GAP Analysis

Active reading. Note what the gap represents and the role of the accountant in the gap analysis.

GAP analysis is concerned with identifying whether there is a gap between what the organization wants to achieve and the likely outcome if it continues with the existing strategy. It can be illustrated, as shown in Figure 5.3.

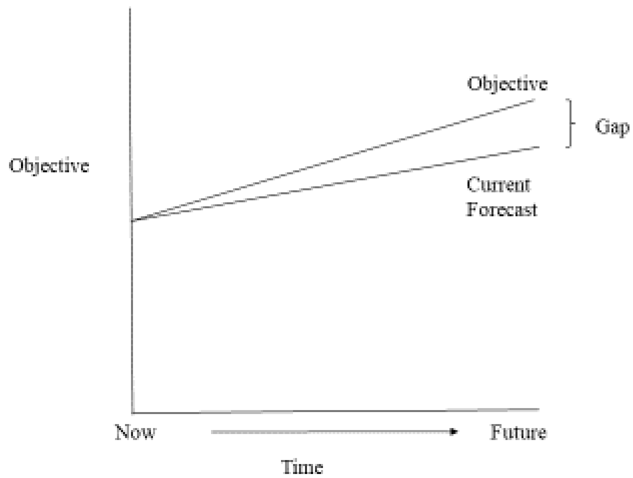

Figure 5.3 GAP analysis

The starting point is the current situation, that is, now. The objective is plotted over time, which is usually expressed in years with a time frame of three to five years or possibly longer. Obviously, the level of accuracy reduces the further ahead the forecast extends into the future. The objective can be anything that can be quantified. It is often a profit objective, or sales growth, but could equally be that the organization needs to increase the number of skilled employees over five years. For example, in the health care industry or hospitals, there may be targets to recruit and train a specific number of new nurses and health professionals over the next five years. The objective is, therefore, the number of new health care professionals to be recruited. The strategy is the recruitment and retention strategy and concerned with the pay and benefits package.

The next step is to look at the current strategy and to forecast or extrapolate what will happen if the organization continues down that path. In the instance of a profit objective, this would be the estimated profit. For the recruitment of nurses, however, the forecast would relate to how many additional nurses would be recruited if the organization follows the existing recruitment strategy with the same pay and benefits package. Invariably the result is that there is a gap between the objective and projected outcome. The accountant can provide valuable advice in determining how big the gap is, particularly when assessed as a profit gap, and the potential impact if the gap is not addressed.

The next phase is to evaluate the various strategic options to see how far they go to closing the gap. Gaps can arise due to internal or external factors, which is why the strategic management process is iterative and a continuous or periodic process, not a one-off exercise. For example, suppose that the strategic option chosen to close the gap is to launch a new product or enter a new market. Competitors will respond, and therefore, although there is a short-term closing of the gap, it begins to open again due to competitor response. It is therefore advisable to undertake continuous gap analysis, whereby the review is being conducted frequently, such as once every quarter or six months.

Another possibility is to take a realistic view and reassess the objectives. It is not cheating or moving the goalposts, but realistically assessing the objectives given the changes in the business environment. For example, when the financial crisis occurred in 2008, many organizations were suddenly in survival mode rather than moving forward on a growth trajectory, as may have been planned initially. The same is undoubtedly true for organizations after the covid-19 pandemic in 2020. Often political changes in many countries impact an organization's ability to achieve current objectives and change their view of the future, perhaps putting growth plans and investment decisions on hold until the outcome becomes more evident. Thus, organizations may be reassessing the strategic objectives for the next few years and setting more realistic or amended targets.

Following the implementation of a strategy to close the initial gap, the analysis can be completed again, at a quarterly or six-monthly review, depending on how fast the environment changes. This evaluation of the success of the strategy is often built into the latest estimated forecast or trend forecast as part of the management information provided to managers (see sections 9.3 and 9.4 of this learning resource for a discussion of updating forecasts). If the gap is closing, then managers gain confidence that the strategy is working, however, as competitors will respond and changes to the environment may have occurred, a gap of some sort may still be registered. This illustrates the need for organizations to innovate continually and find ways of retaining a competitive advantage. The speed at which this needs to occur will vary between industry sectors. Still, many organizations now see the need to exhibit a degree of agility to be able to respond appropriately to changes.

5.5 Summary

Management accounting can contribute to assessing the strategic position in the following ways.

Strengths and weaknesses

The accountant can assist in the evaluation of strengths and weaknesses, particularly in terms of financial strengths and weaknesses. It could be via the financial analysis undertaken as part of the internal review.

Financial impact

Identifying the potential financial impact of environmental changes helps to determine whether changes represent an opportunity or a threat.

Size of gap

Accountants are good at identifying the size of any gap that exists between the objectives and forecast outturn in financial terms, given the current strategy.

Evaluation of options

Evaluating the potential options based on combinations of strengths and weaknesses can help determine the most successful options to close the gap. This can include strategies such as implementing a cost reduction exercise.

5.6 Review questions

(1) Discuss why it is important for organizations to undertake a SWOT analysis.
(2) Discuss the process of undertaking a SWOT analysis and illustrate how strengths, weaknesses, opportunities, and threats can be determined.
(3) What is the significance of identifying a GAP between original objectives and the forecast outturn?
(4) Discuss the contribution that management accounting can make to the analysis of the strategic position.

5.7 Case study activity 8 – HW Inc. SWOT analysis

The following activities relate to the case study in Appendix A of this learning resource.

(a) Undertake a SWOT analysis for HW Inc. (Hint: Use the environmental analysis undertaken from the activity in Chapter 3 and the portfolio analysis, value creation system, and financial analysis activities in Chapter 4 of this learning resources to help you).
(b) Identify what you consider to be the main elements within each heading; that is, the key strengths, weaknesses, opportunities, and threats.

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