Portfolio Management

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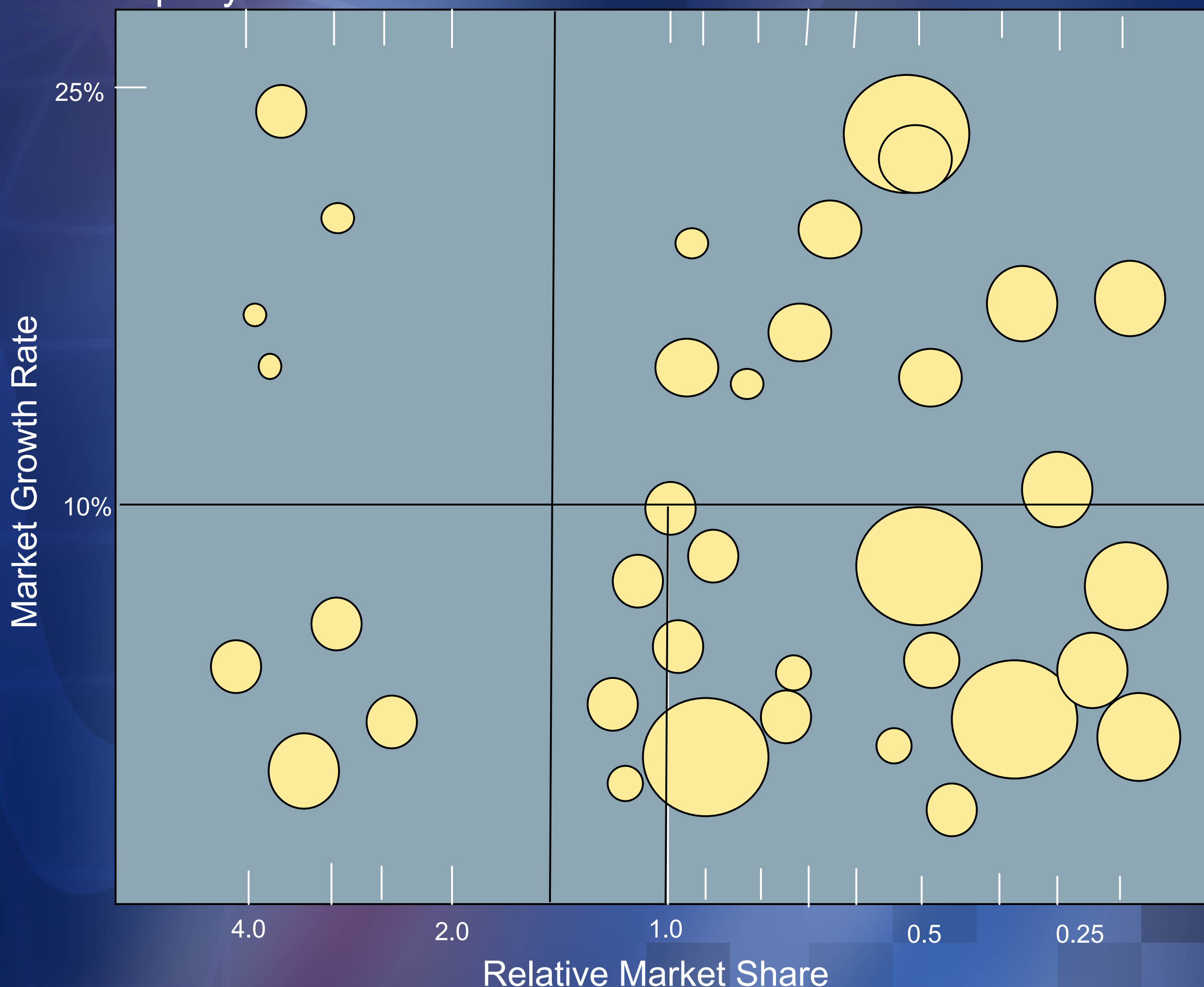
- It is top management responsibility that requires the assessment of strengths and weaknesses of the current portfolio of businesses, in order to define the priorities for resource allocation among businesses, and the identification of opportunities for diversification and divestment.
- Portfolio analysis requires an analysis of each business in terms of
  - External factors to determine industry opportunities and threats
  - Internal factors to determine internal strengths and weaknesses

Basic Tools for Portfolio Management

Tools	External Factors	Internal Factors
Growth-Share Matrix	Market growth potential	Relative market share
Industry Attractiveness-Business Strength Matrix	Overall industry attractiveness • Critical structural factors • Five-forces model	Sources of competitive advantage • Critical success factors • Value chain
Life-Cycle Matrix	Industry maturity	Overall measurement of business position
Profitability Matrix	Market growth potential Cost of capital	Profitability Cash generation

The Growth-Share Matrix

A typical Product Portfolio Chart (Growth-Share Matrix) of a Comparative Strong and Diversified Company

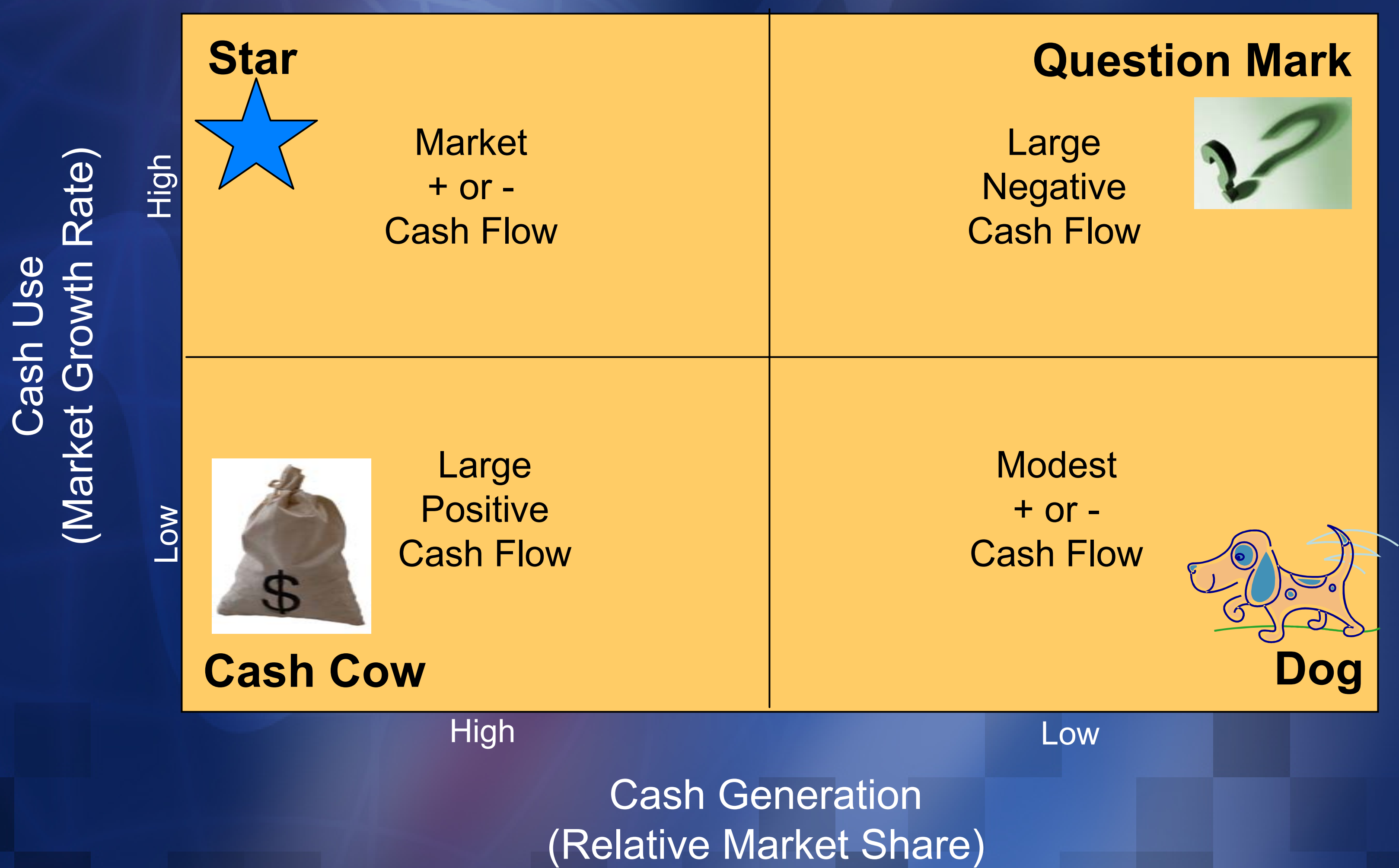


Recognizing the firm as composed by largely independent SBUs, with different growth, profitability and cash flow potentials.

Implications for Strategic Positioning Emerging from the Growth-Share Matrix

Business Category	Market Share Thrust	Business Profitability	Investment Required	Net Cash Flow
Stars	Hold/Increase	High	High	Around zero or slightly negative
Cash Cows	Hold	High	Low	Highly positive
Question Marks	Increase Harvest/Divest	None or Negative Low or Negative	Very High Disinvest	Highly Negative Positive
Dogs	Harvest/Divest	Low or Negative	Disinvest	Positive

Cash-Flow Characteristics of Business Categories in the Growth-Share Matrix



The Industry Attractiveness-Business Strength Matrix

Industry Attractiveness **

Business Strength*	High	Medium	Low
High	Investment and Growth	▪ Selective Growth	Selectivity
Medium	▪ Selective Growth	Selectivity	Harvest/ Divest
Low	Selectivity	Harvest/ Divest	Harvest/ Divest

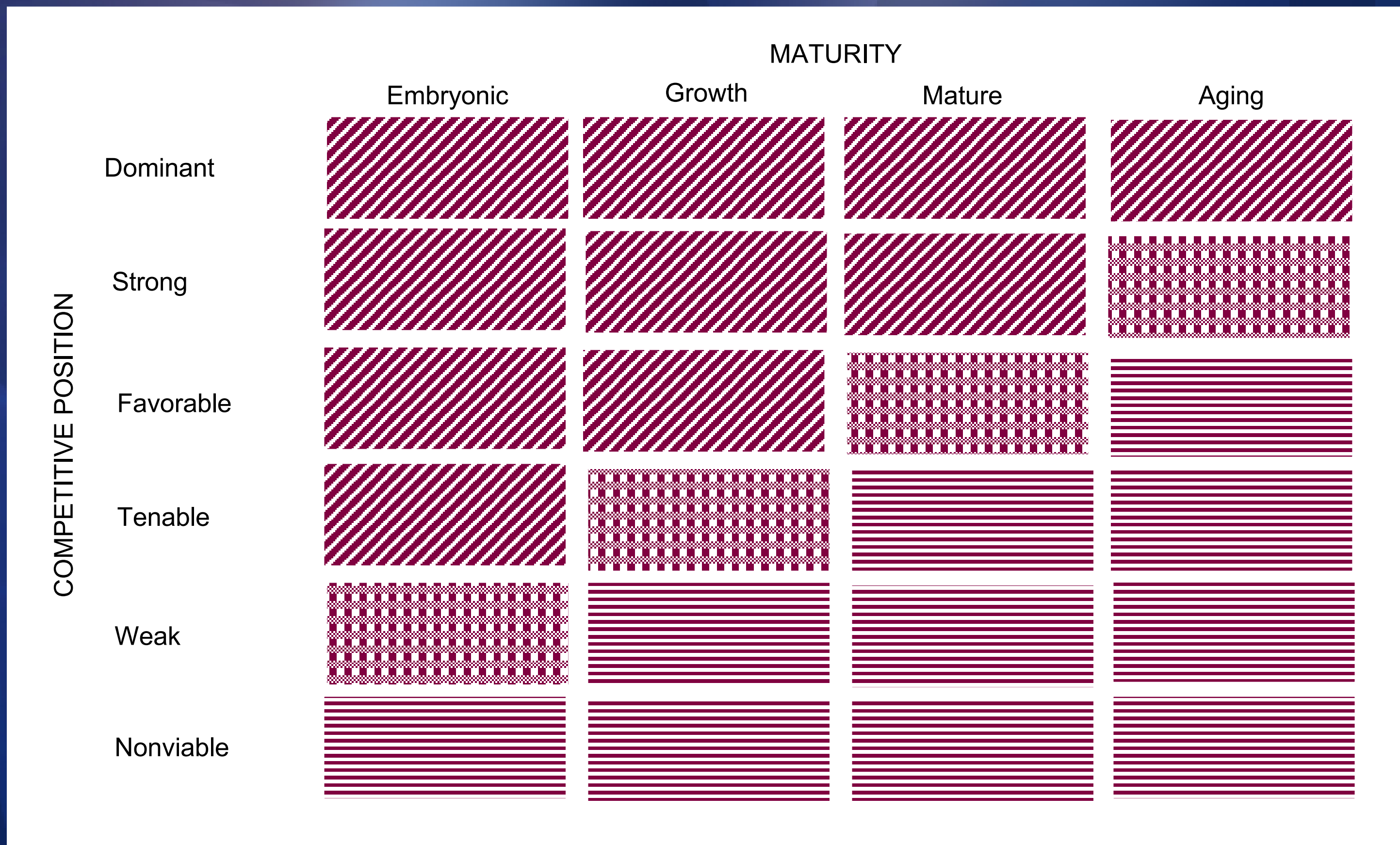
* Internal Factors
- Market Share
- Sales Force
- Marketing
- Customer service
- R&D
- Manufacturing
- Distribution
- Financial resource
- Image
- Breadth of product line
- Quality/Reliability
- Managerial Competence

** External Factors
- Market size
- Market growth rate
- Cyclicality
- Competitive structure
- Barriers to entry
- Industry profitability
- Technology
- Inflation
- Regulation
- Manpower availability
- Social issues
- Environmental issues
- Political issues
- Legal issues

Strategic Implications from the Industry Attractiveness-Business Strength Matrix -
Suggested by A. T. Kearney

Business Strengths \ Industry Attractiveness	High	Medium	Low
High	• Grow • Seek dominance • Maximize investment	• Identify growth segments • Invest strongly • Maintain position elsewhere	• Maintain overall position • Seek cash flow • Invest at maintenance level
Medium	• Evaluate potential for leadership via segmentation • Identify weaknesses • Build strengths	• Identify growth segments • Specialize • Invest selectively	• Prune lines • Minimize investment • Position to divest
Low	• Specialize • Seek niches • Consider acquisitions	• Specialize • Seek niches • Consider exit	• Trust leader's statesmanship • Sic on competitor's cash generates • Time exit and divest

The Life-Cycle Portfolio Matrix



Strategic Positioning in Terms of Market Share Suggested by the Life-Cycle Portfolio Matrix

	Embryonic	Growth	Mature	Aging
Dominant	All Out Push for Share Hold Position	Hold Position Hold Share	Hold ▪ Position Grow with Industry	Hold Position
Strong	Attempt to Improve Position All Out Push for Share	Attempt to Improve Position Push for Share	Hold Position Growth with Industry	Hold Position or Harvest
Favorable	Selective or All Out Push for Share Selectively Attempt to Improve Position	Attempt to Improve Position Selective Push for Share	Custodial or Maintenance Find Niche and Attempt to Protect	Harvest or Phased Withdrawal
Tenable	Selectively Push for Position	Find Niche and Protect It	Find Niche and Hang on Or Phased Withdrawal	Phased Withdrawal or Abandon
Weak	Up Or Out	Turnaround Or Abandon	Turnaround or Phased Withdrawal	Abandon

Strategic Positioning in Terms of Investment Requirements Suggested by the Life-Cycle Portfolio Matrix

	Embryonic	Growth	Mature	Aging
Dominant	**Invest Slightly Faster Than Market Dictates**	**Invest to Sustain Growth Rate (and Preempt New (?) Competitors)**	**Reinvest as Necessary**	**Reinvest as Necessary**
Strong	**Invest as Fast as Market Dictates**	**Invest to Increases Growth Rate (and Improve Position)**	**Reinvest as Necessary**	**Minimum Reinvestment or Maintenance**
Favorable	**Invest Selectively**	**Selective Investment to Improve Position**	**Minimum and/or Selective Reinvestment**	**Minimum Maintenance Investment or Disinvest**
Tenable	**Invest (Very Selectively)**	**Selective Investment**	**Minimum Reinvestment or Disinvest**	**Disinvest or Divest**
Weak	**Invest or Divest**	**Invest or Divest**	**Invest Selectively or Disinvest**	**Divest**

The terms invest and divest are used in the broadest sense and are not restricted to property, plant & equipment.

Strategic Positioning in Terms of Profitability and Cash-Flow Suggested by the Life-Cycle Portfolio Matrix

	Embryonic	Growth	Mature	Aging
Dominant	**Probably Profitable, But Not Necessary** **Net Cash Borrower**	**Profitable** **Probably Net Cash Producer (But Not Necessary)**	**Profitable** **Net Cash Producer**	**Profitable** **Net Cash Producer**
Strong	**May Be Unprofitable** **Net Cash Borrower**	**Probably Profitable** **Probably Net Cash Borrower**	**Profitable** **Net Cash Producer**	**Profitable** **Net Cash Producer**
Favorable	**Probably Unprofitable** **Net Cash Borrower**	**Marginally Profitable** **Net Cash Borrower**	**Moderately Profitable** **Net Cash Producer**	**Moderately Profitable** **Cash Flow Balance**
Tenable	**Unprofitable** **Net Cash Borrower**	**Unprofitable** **Net Cash Borrower or Cash Flow Balance**	**Minimally Profitable** **Cash Flow Balance**	**Minimally Profitable** **Cash Flow Balance**
Weak	**Unprofitable** **Net Cash Borrower**	**Unprofitable** **Net Cash Borrower or Cash Flow Balance**	**Unprofitable** **Possibly Net Cash Borrower or Net Cash Producer**	**Unprofitable (Write-off)**

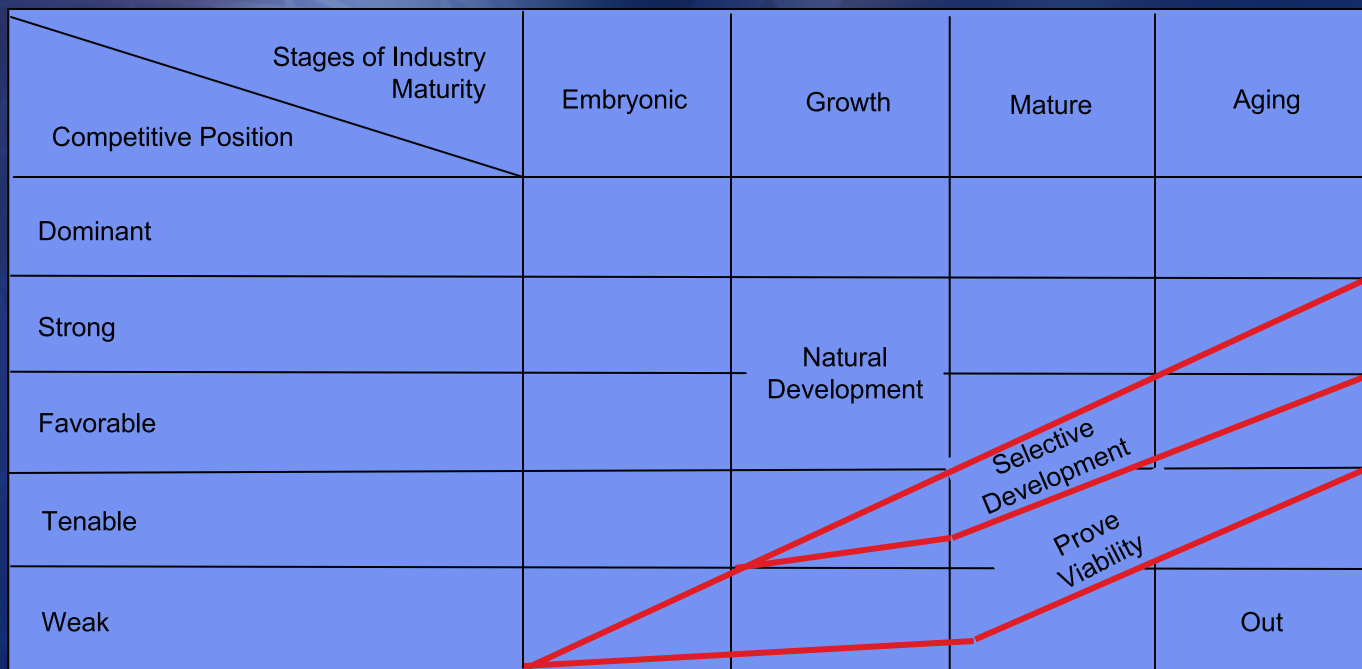
Industry Maturity Guide

	DEVELOPMENT STAGE			
DESCRIPTORS	EMBRYONIC	GROWTH	MATURE	AGING
Growth Rate	Accelerating; meaningful rate cannot be calculated because the base is too small.	Faster than GMP, but constant or decelerating.	Equal to or slower than GNP; cyclical	Industry volume cycles but declines over long term
Industry Potential	Usually difficult to determine.	Substantially exceeds the industry volume, but is subject to unforeseen developments.	Well-known; primary markets approach saturation industry volume.	Saturation is reached; no potential remains.
Product Lines	Basic product line established.	Rapid proliferation as product lines are extended.	Product turnover, but little or no change in breadth.	Shrinking.
Number of Participants	Increasing rapidly.	Increasing to peak; followed by shakeout and consolidation.	Stable.	Declines; but business may break up into many small regional suppliers.
Share Distribution	Volatile.	A few firms have major shares; ranking can change, but those with minor shares are unlikely to gain major shares.	Firms with major shares are entrenched.	Concentration increases as marginal firms drop out; or shares are dispersed along small local firms.
Customer Loyalty	Little or none.	Some; buyers are aggressive.	Suppliers are well-known; buying patterns are established.	Strong; number of alternatives decreases.
Entry	Usually easy, but opportunity may not be apparent.	Usually easy; the presence of competitors is offset by vigorous growth.	Difficult; competitors are entrenched, and growth is slowing.	Difficult; little incentive.
Technology	Concept development and product engineering	Product line refinement and extension	Process and materials refinement; new product line development to renew growth.	Role is minimal.

Criteria for Classification of Competitive Position

1. Dominant: Dominant competitors are very rare. Dominance often results from a quasi-monopoly or from a strongly protected technological leadership.
2. Strong: Not all industries have dominant or strong competitors. Strong competitors can usually follow strategies of their choice, irrespective of their competitors' moves.
3. Favorable: When industries are fragmented, with no competitors clearly standing out, the leaders tend to be in a favorable position.
4. Tenable: A tenable position can usually be maintained profitable through specialization in a narrow or protected market niche. This can be a geographical specialization or a project specialization.
5. Weak: Weak competitors can be intrinsically too small to survive independently and profitable in the long term, given the competitive economics of their industry, or they can be larger and potentially stronger competitors, but suffering from costly past mistakes or from a critical weakness.

Natural Strategic Thrusts



Source: Arthur D. Little, Inc.

Natural Strategic Thrusts

STRATEGIES / THRUSTS	A	B	C	D	E	F	G	H	I	J	K	L	M	N	O	P	Q	R	S	T	U	V	W	X
	NATURAL DEVELOPMENT																							
Startup					E				I			L												
Growth with industry	A	B	C			F	G			J				N		P				T	U			
Gain position gradually							G					L								T				
Gain position aggressively		B	C		E		G					L		N	O	P				T		V		
Defend position	A		C											N							U	V	W	
Harvest				D				H			K		M				Q	R			U		W	
	SELECTIVE DEVELOPMENT																							
Find niche	A						G		I			L	M					R		T				
Exploit niche		B	C		E							L		N		P					U	V		
Hold niche			C	D										N			Q				U			
	PROVE VIABILITY																							
Catchup				D	E							L	M			P	Q	R						
Renew				D									M		O	P	Q	R			U			
Turnaround				D								L	M	N			Q	R				V	W	
Prolong existence	A			D		F				J	K		M	N			Q	R	S	T			W	
	WITHDRAWAL																							
Withdraw				D									M				Q	R					W	
Divest				D							K						Q	R	S					
Abandon																								X

Generic Strategies

<u>Strategy Code</u>

A *Backward Integration* - To incorporate within the business organization the functions, operations, or products that were previously external and that served to supply and support existing business operations.

B *Development of Overseas Business* - To establish overseas a separate business unit in the same industry as the domestic business unit, but in a market with different characteristics.

C *Development of Overseas Facilities* - To invest in offshore production plants for products to be sold in domestic markets by domestic business unit.

D *Distribution Rationalization* - To prune back the distribution system to a more effective network; this may include cutting back to the highest volume distributors or shaping by geography or type.

E *Excess Capacity* - To provide additional capacity or existing products beyond current needs - not incremental capacity - in order to meet anticipated future growth.

F *Export/Same Product* - To invest in marketing selected products of the domestic business unit in foreign markets; these may or may not have the same competitors and market dynamics as the domestic market.

G *Forward Integration* - To incorporate within the business organization external functions between the current business and the ultimate consumer so that more effective distribution or increased control over the marketplace can be achieved.

Generic Strategies (cont'd.)

Strategy Code

H *Hesitation* - To slow down or establish a 1-year moratorium on new capital investment and new expenses; does not prohibit expense or capital investment for normal maintenance of the business, e.g., because of capital limitations, dangers of overextending management, or market uncertainties.

I *Initial Market Development* - To invest in creating a primary demand for a brand-new product; typically undertaken by the first company to develop a new market, often when that company has a clear technological edge.

J *Licensing Abroad* - To exploit through licensing in foreign countries the use of domestic technology, patents, know-how, brand franchise, etc., belonging to the domestic business unit.

K *Complete Rationalization* - To strip down a business to currently most profitable piece and reinvest the proceeds of divestments in the successful operations retained.

L *Market Penetration* - To increase market share through manipulating the marketing mix; e.g., lower price, product line breadth, increased product and sales service, increased advertising.

M *Market Rationalization* - To prune back the market served by the business unit to most profitable segments and/or higher volume segments, or by particular type of geography, in order to concentrate marketing focus.

Generic Strategies (cont'd.)

Strategy Code

N *Methods and Functions Efficiency* - To invest in new ways of doing existing tasks by adding new "soft" technology - e.g., new patterns of work flow, computer-aided production planning and inventory control, etc., - so as to improve effectiveness or efficiency.

O *New Products/New Markets* - To invest in developing, manufacturing, and marketing products related or unrelated to the present product line for new markets that are different in geography or by type from the present markets served by the business unit.

P *New Products/Same Market* - To develop, broaden, or replace products in the present product line, selling them into the existing market served.

Q *Production Rationalization* - To increase standardization of designs, components, and manufacturing processes and/or concentrating facilities and/or subcontracting out elements of production.

R *Product Line Rationalization* - To narrow the product line to the most profitable products.

S *Pure Survival* - To maintain existence of the business unit in periods of extremely adverse business conditions by eliminating functions, products, or by under-financing any activity.

Generic Strategies (cont'd.)

Strategy Code

T *Same Products/New Markets* - To expand existing domestic market by geography or type for the existing product line.

U *Same Products/Same Markets* - To execute those strategies required to maintain the present competitive position of the existing business unit … with the existing products in existing markets.

V *Technological Efficiency* - To improve operating efficiency through technological improvements in physical plant, equipment, or processes.

W *Traditional Cost Cutting Efficiency* - To reduce costs uniformly through management edicts.

X *Unit Abandonment* - To divest a business unit because of its inability to remain viable within the corporation or because the unit may be of greater value to someone else.

The Use of the M/B Model at the Business Level

An Alternative Profitability Matrix

p = Reinvestment rate