

***Master of Science
in Innovation and Entrepreneurship
2007/2008***

***ENT 4400:
Innovation Strategy and Management***

2n meeting



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Overview

- 1st meeting: strategic choice – content and process
- 2nd meeting: evaluation of strategic alternatives and criteria for choice
- 3rd meeting: growth alternatives and the M&A process
- 4th meeting: rise and fall of businesses via M&A



Agenda for 2nd meeting

- **Evaluation of strategic alternatives based on suitability**
 - Strategic logic
 - Cultural match
 - Empirical support
- **Strategic choice – two main criteria**
 - Feasibility
 - Accept
- **Discussion: case 2:**
”Strategic choice in Aker Biomarine ASA”
- **Recommended reading:**
 - Johnson & Scholes (2004): ch. 5-6 ”Strategic Choices”
Case example: The Virgin Group (pp. 333)
 - Christensen (2003): ”The Innovator’s dilemma”

Strategic choice related to innovation

- radical change

- ***Characteristics***

Collapse, break trough – or disruption in a development process
– related to market, technology and/or regulations

- Sustaining innovations: improve the existing and addresses today's (profitable) customers
- Disruptive innovations: improve performance along some dimensions and reduce performance along other, and give cheaper and simpler products that are initially adopted by others than today's (profitable) customers

- ***Follow-up question***

"Why do established players fail in situations with radical change despite abundance of competence and resources?"

- ***Answer***

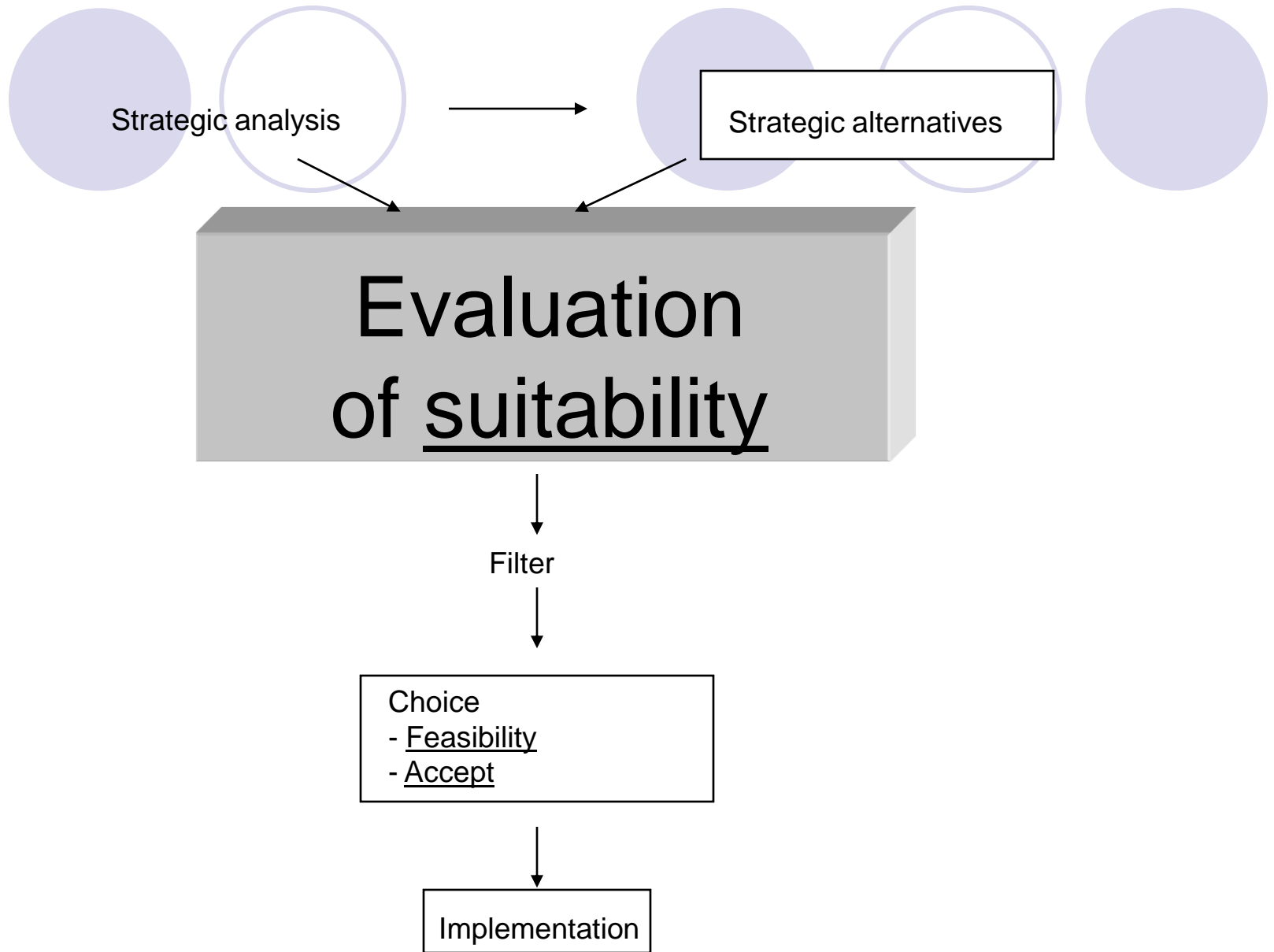
They typically focus on sustaining innovations

”But after all...”

- **The established players have a lot of advantages:**
 - Ownership of infrastructure
 - Knowledge of how to work with regulators
 - Resources
 - Have historically survived disruptive threats
 - Unchanged and un-challenged vertically integrated business model with centralised control and coordination
- **Even if they in principle can meet any change**, they will meet competitive threats in niches- that in sum can represent a major threat
- **Worst scenario:** sudden change where they remain kings in an old world that will be more and more irrelevant
- **Winners and losers**
 - The winners will be those who take the opportunities early and seek to exploit opportunities for new growth
 - The losers will be those who sit and wait too long

To see what is next...

- Prepare along three dimensions
 1. *Signals of change*
 - Are there any signs that current or new players exploit new opportunities related to over/under served customers or “non-consumers”?
 2. *Competitive battles*
 - How do new entrants penetrate the market (based on asymmetrical motivation and skills) without reaction from established players, and how will they manage in direct competition?
 3. *Strategic choices*
 - Do the players make decisions related to resources, competence and network that influence their chances of success?
- Organise for separate units
 - Small enough to celebrate small victories, but with enough resources to survive
 - Do not expect to succeed at once



Evaluation of alternatives

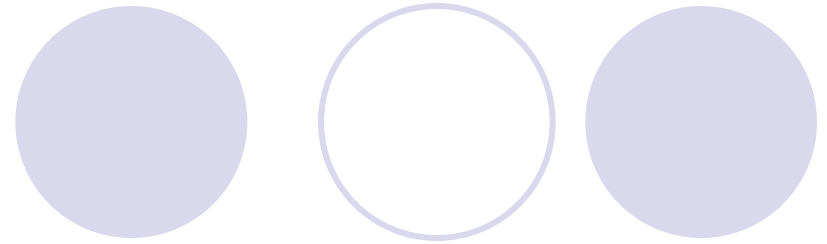
- ”Suitability” defines if a strategic alternative is realistic and matches the situation the business is in, and contributes to improve its competitive position
- Approach
 - (a) Strategic logic
 - (b) Cultural match
 - (c) ”Empirical support”

(a) Strategic logic



- Portfolio analysis
- Relation to product life cycle
- Potential synergies
related to value creation logic

Network effects - speed matters



Growth per year

4.0%

3.0%

2.0%

1.0%

0%



Growth: no of years to achieve 25 % of the US population

(b) Cultural match

- Head vs. heart
- Matures over time

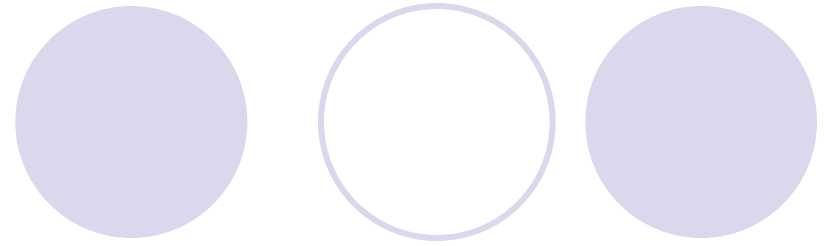
(c) "Empirical support"



- Companies in the same industry
- Other industries
- Other regions

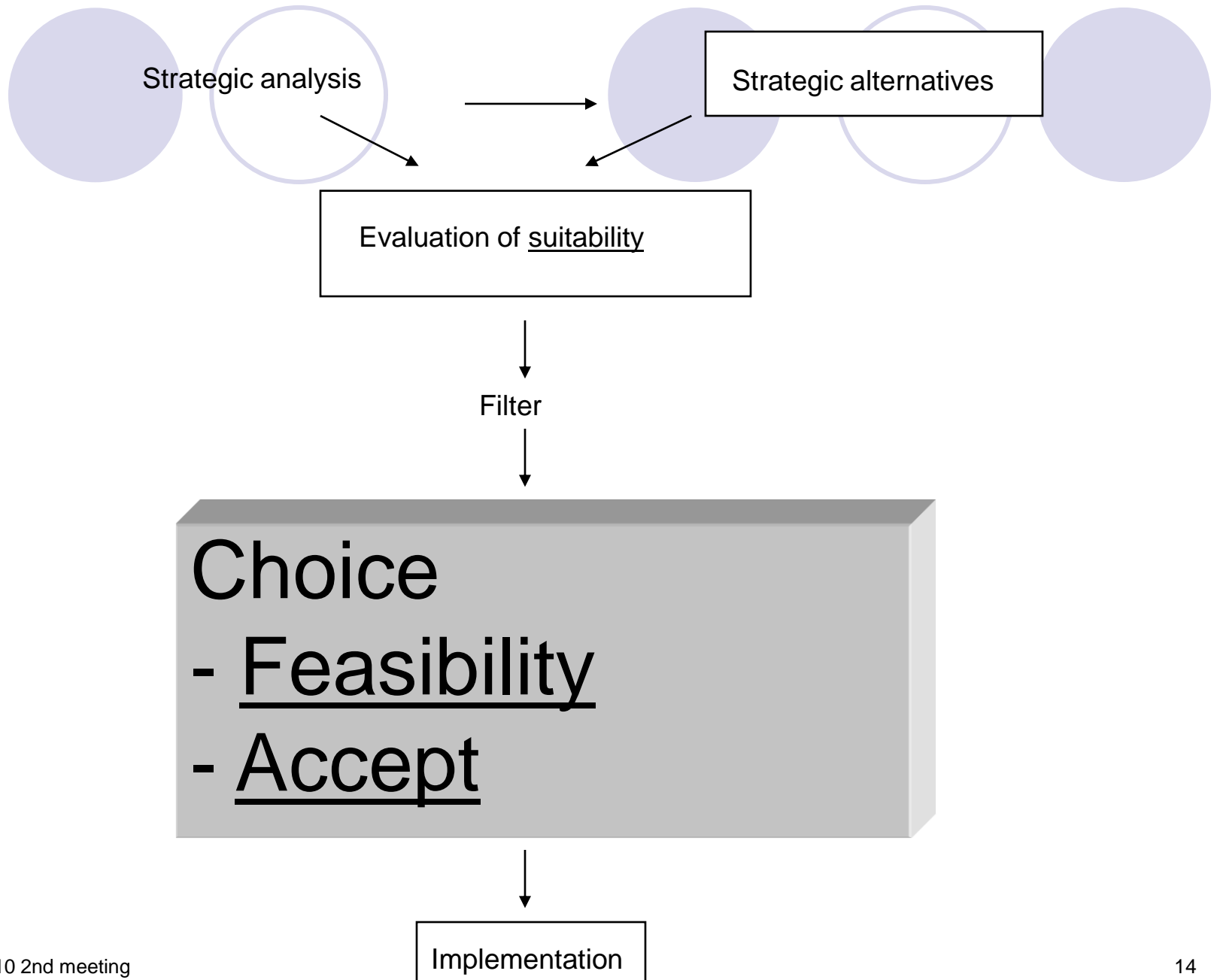


Filter



Short listing

- Prioritisation
- Decision trees
- Scenarios



Strategic choice



- Exact science?
- Quality
 - Opens eyes of decision makers
 - Highlights the logic behind
- NB! Iterations and continuous processes

Key criteria

Given the evaluation of the logic in the strategic alternatives and the potential for suitability and match with current strategy

(a) Feasibility

- Funding
- Break-even
- Resources

(b) Accept

- Return on investments
- Risk
- Key stake holders' expectations

(a) Feasibility as criteria

- Is the strategy realistic to fund?
- Is the organisation capable of perform?
- Can necessary competence and resources be secured?
- Can necessary market position be achieved?
- How can response from competitors be handled?
- Is necessary technology available?

Analysis of feasibility

- Funding

- Necessary capital investment
- Accumulated profit
- Increase in working capital

- Break-even

- Alternative ways of utilising resources

(b) Accept as criteria

- *Owners* will consider
 - Return on investment (cost/benefit)
 - Financial risk
 - Effects on capital structure
- Influence the *organisation's* (individuals and groups) expectations
- Effects on other *stake holders*
 - Creditors
 - Suppliers
 - Customers
 - Government

Evaluation of return on investments

- Analysis of profitability
 - Pay-back time
 - Discounted cash-flow
 - Market valuations

- Analyses of cost/benefit
 - Qualitative
 - Quantitative (if possible)

Evaluation of risk



○ **Financially**

- Influence on capital structure
- Time to break-even
- Influence on liquidity

○ **Sensibility analyses**

“What if” critical assumptions are changed

○ **Scenarios**

Situation in pessimistic, optimistic, and realistic cases

○ **Heuristic models**

«Good enough»

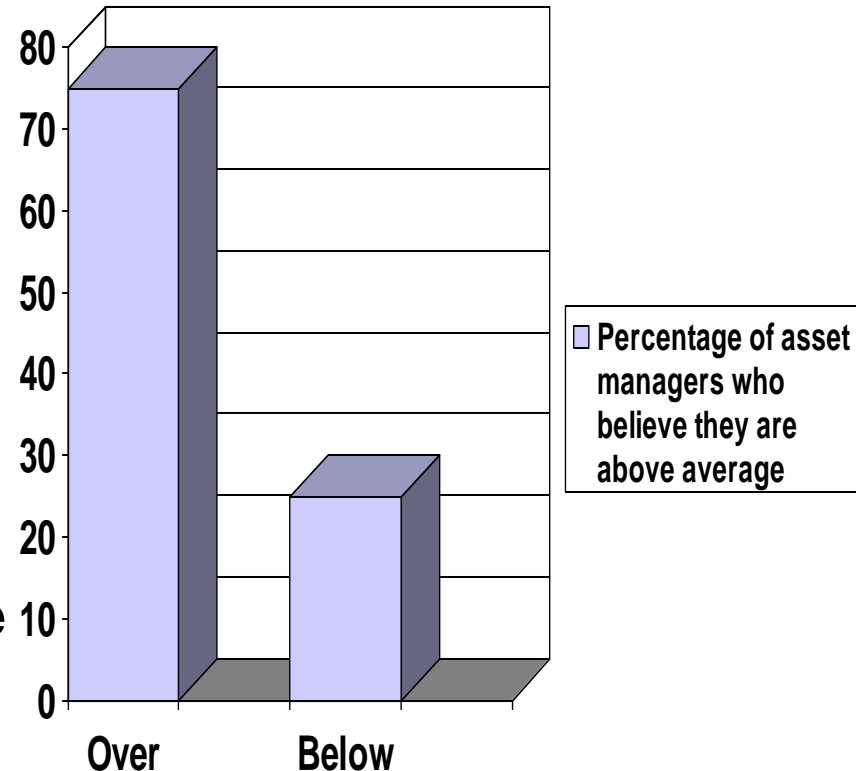
The practical choice



- Criteria are not always established
-and they are not always used
- Higher authorities play a more or less visible role
- Implementation is more or less intense
- External conditions often play a role...

Why do estimates often fail?

- Momentum driven
 - Over-optimistic in bull times
 - Over-pessimistic in bear times
- Too self-confident
 - "I know that everyone believe that they are above average, but i know that I AM."
 - Experts (especially in finance!) over-estimate their knowledge more than others



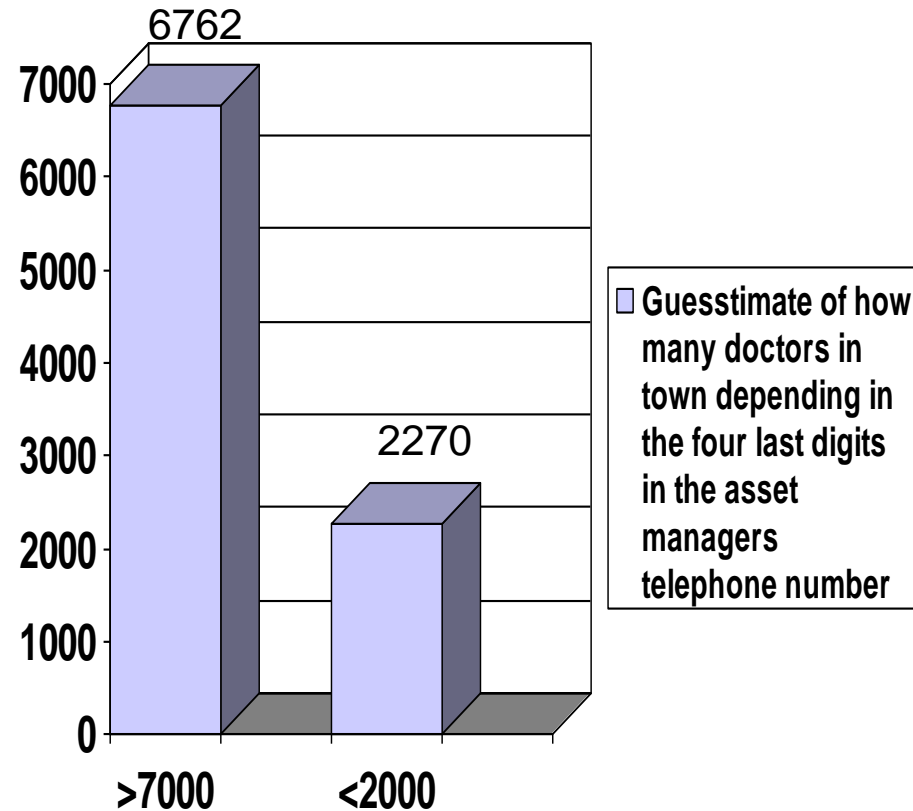
Kilde: DrKW/Macro Research/Finansavisen

Why are estimates followed anyway?

- Lack of skills
 - The ability to produce the right answers are practically the same as those to evaluate the answers
 - If people lack the ability to give the right answers, they are also cursed with a lack of ability to know if answers are right or wrong
- Pride and bad excuses
 - If only ("...Norges Bank had increased the interest rate earlier")
 - Everything else equal ("but imports from China made clothes cheaper")
 - I was almost right ("But the market was up just before it closed")
 - It has not happened yet ("But the market will crash soon")

So why are estimates used after all?

- The hope of beating efficient markets through information others don't have
- Anchoring: with uncertainty you will stick to what is known, although irrelevant
- What else can we do?



Kilde: DrKW/Macro Research/Finansavisen

Example: new growth for the energy companies?

● External analysis

- Electricity becomes more and more of a "cost-plus game"
- Necessary to build barriers of entry for electricity
- Other utility markets such as telecom grow

● Internal analysis

- Brand power (especially locally)
- Customer information (90 % market share)
- Competence and resources related to infrastructure (100 years of history)

Energy players (ctd.) – strategic response

- New arena: from supplier of electricity to "multi-service-provider"
 - *Energy*: gas
 - *Telecom*: broadband (triple play) and mobile
 - Next: alarm, insurance, financing...
- Instruments: long term organic growth combined with acquisitions
- Differentiators: clear and unique customer values
 - *Local*
 - Lower price
 - *Simpler*: one bill etc.
 - Addresses the family segment (1/3 of the market)
- Consequences of new economic logic by establishing separate units
- Conscious staging: signs up customers before building infrastructure

Energy players (ctd.) – success factors

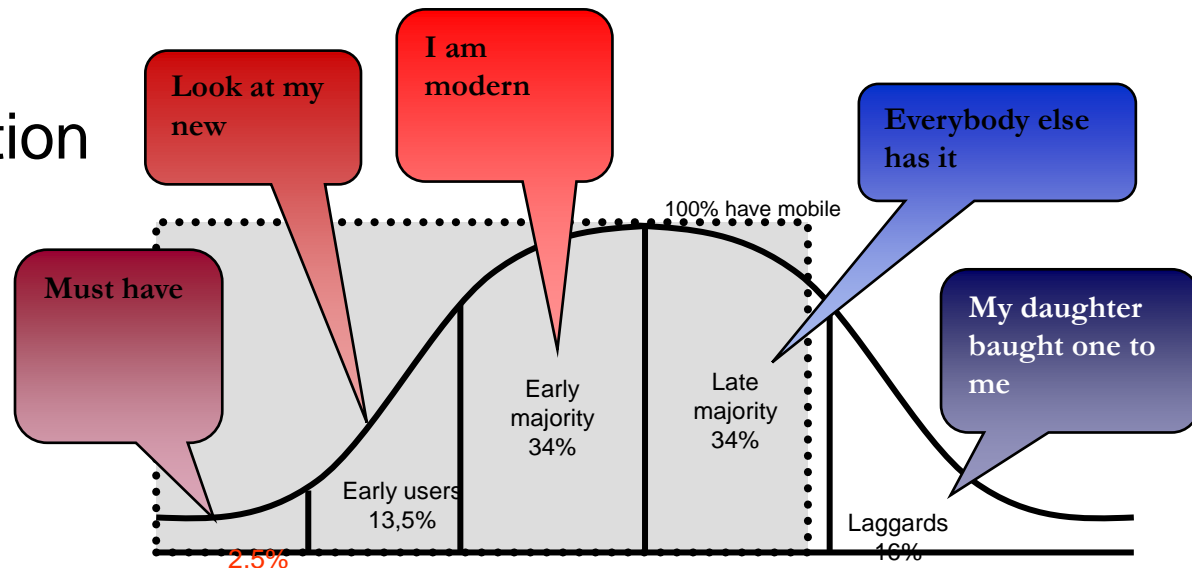
- Clear value proposition

- Low price
- Local
- Simple

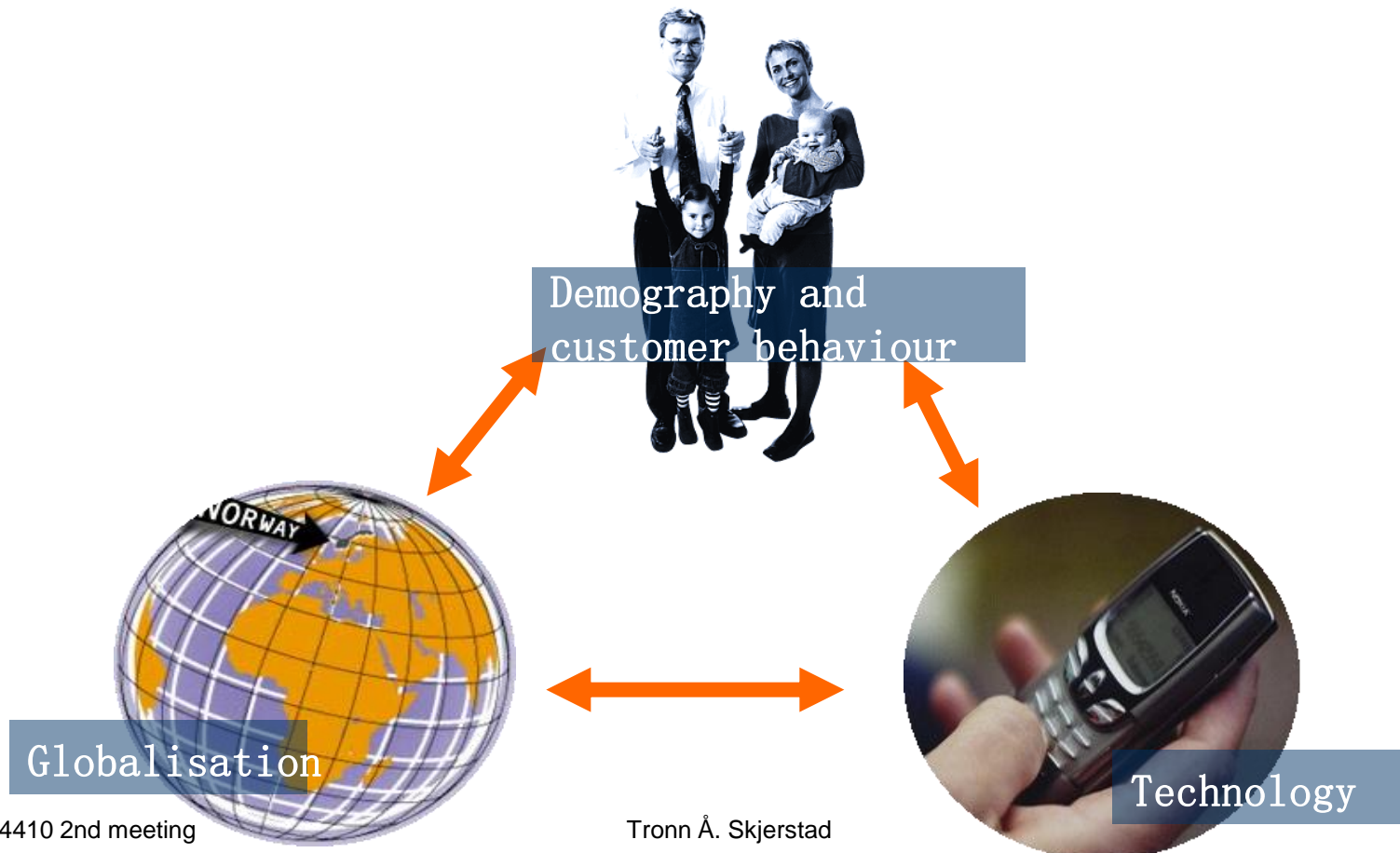


- Careful segmentation

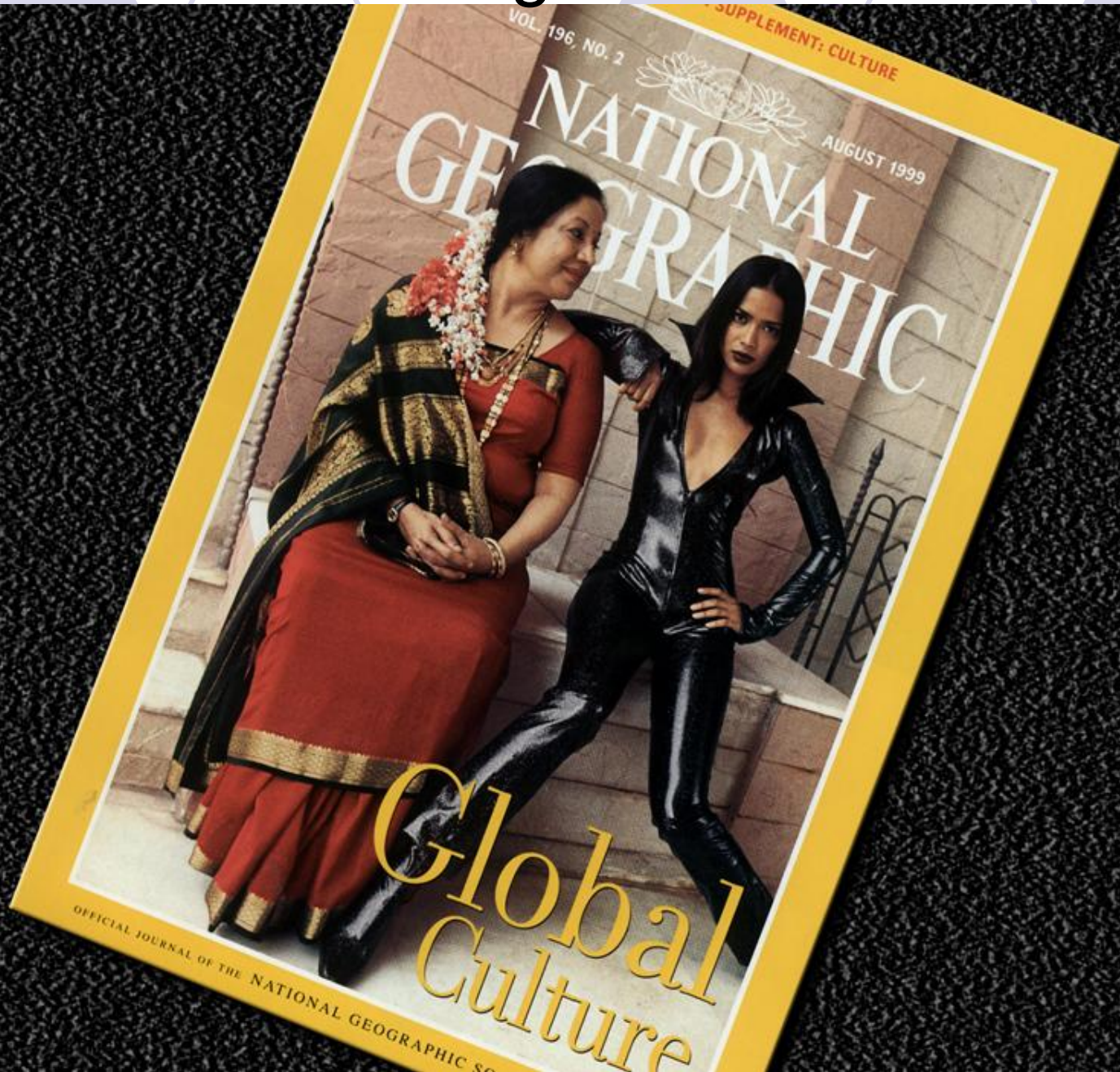
- Young families
- With kids



The general drivers for change



Globalisation challenges us...



It is hard to predict the future...

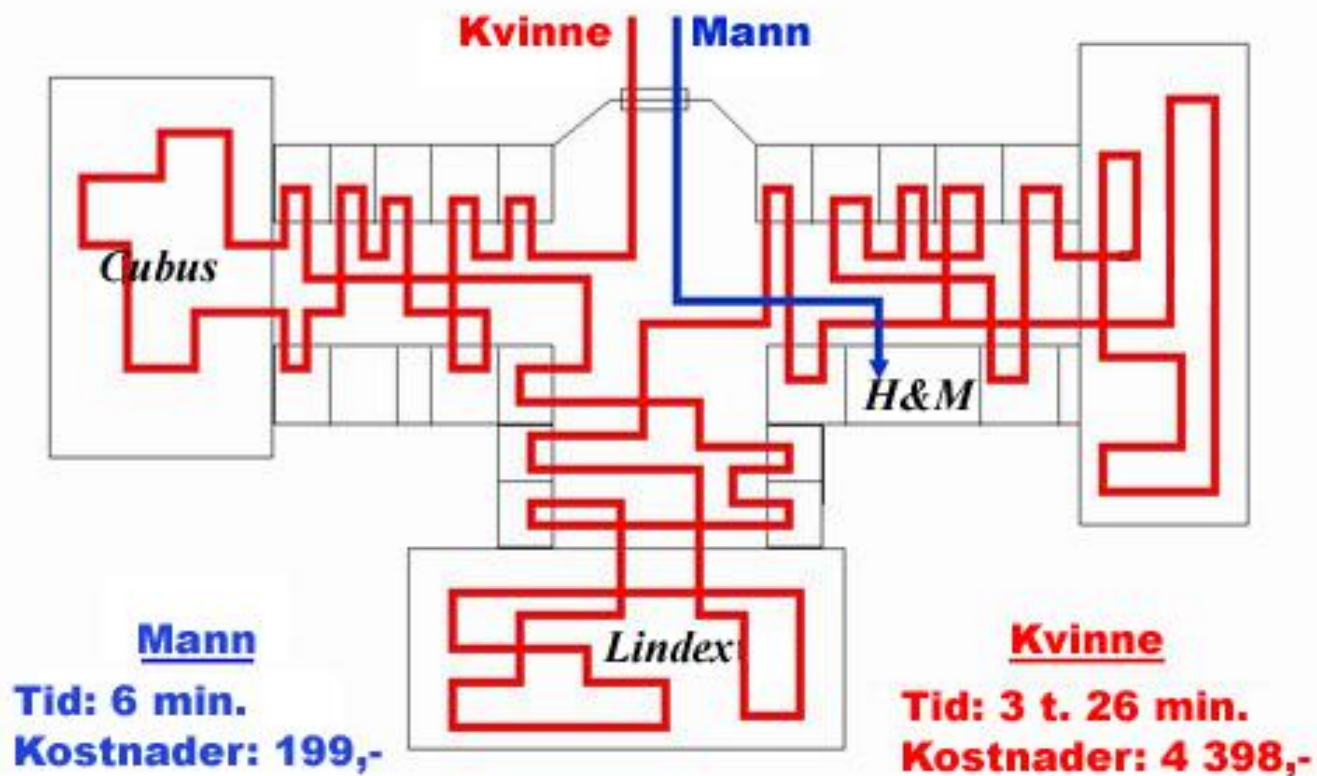
There will never be a big market for cars.
In Europe you can sell maybe 1.000 cars
– more private drivers are not available.



Spokesman from
Daimler in the late 1800s

And customers needs and behaviour are different

Oppdrag: Gå til H&M og kjøp en bukse



But some things are also stable...

Education	NTNU (1910) NHH (1936) UiO (1811)
Chocolate	Freia Melk (1906) KvikkLunsj (1937) Stratos (1936) Firkløver (1926)
Bank	DnB NOR (1822) Nordea (1848) Fokus Bank (1859)

Case Aker Biomarine part 3 (to 3rd meeting)

- assessment of the growth plan

1. What has been the major ingredients in Aker Biomarine's strategy until now with respect to: arena, growth instruments, differentiators, economic logic, and staging?
2. What role has individual entrepreneurs played in different phases of the development of the company? What role have alliances and partnerships played, and in what way has the listing on the stock exchange influenced the company's organisation and profile?
3. What are the major market trends that Aker Biomarine should exploit over the next three years, and what will be the major threats?
4. What should be the major priorities in Aker Biomarine's strategy towards 2010 with respect to: arena, growth instruments, differentiators, economic logic, and staging?