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## Chapter 2-- xternal Analysis: The Identification of Opportunities and Threats

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5. The bottled water industry created new competitors for Coca-Cola, but did not change the basic industry boundaries.  
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6. In Porter's framework, the stronger the five forces, the more limited the ability of established companies to raise prices and earn greater profits.  
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7. Fortunately, substitute products are not a threat if a company is the market leader.  
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8. The personal computer industry is uniquely dependent upon a powerful supplier, Intel.  
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9. Access to cheaper capital is an example of an economy of scale.  
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10. Even when entry barriers are very high, new firms may still enter an industry if they perceive that the benefits outweigh the costs of entry.  
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11. In general, the more that an industry's product is like a commodity, the lower the intensity of any price war that may develop.  
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14. Government deregulation of telephone service lowered the barriers to entry and lowered industry profit margins.  
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15. When buyers are in a weak bargaining position, companies in the supplying industry must lower their prices to increase profits.  
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18. Starbucks and an independent local caf~ both sell coffee and therefore belong to the same strategic group.  
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- A. substitute.
  - B. market segment.
  - C. sector.
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  - E. industry.
32. United Airlines, Amtrak, and Greyhound are all companies in the transportation
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  - D. Greater bargaining power of suppliers
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36. Which of the following is not one of Porter's five forces, as proposed in his original model?
- A. Threat of complementors
  - B. Bargaining power of suppliers
  - C. Rivalry among established companies
  - D. Threat of new entrants
  - E. Threat of market changes

37. Which of the following components was an extension of Porter's original five forces model?
- A. Risk of entry by potential competitors
  - B. The intensity of rivalry among established companies within an industry
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38. Which of the following is not a barrier to entry?
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  - B. Brand loyalty
  - C. Absolute cost advantages
  - D. High customer bargaining power
  - E. High customer switching costs
39. If economies of scale are an industry's primary entry barrier, a new entrant's major risk is
- A. its inability to access labor and materials.
  - B. the inferior quality of its products.
  - C. its inability to match the innovation of the established firm.
  - D. its inability to produce in sufficient volume to match the cost advantages of established producers.
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- A. continuous advertising of brand and company names.
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  - C. cost reductions that arise from the mass production of standardized output.
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41. Which of the following industry structures consists of a large number of small and medium-sized companies, none of which is in a position to determine industry price?
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  - D. Monopoly
  - E. Sector
42. Which of the following industry structures is dominated by a small number of large companies?
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  - B. Demand conditions
  - C. The cost structure of firms in an industry
  - D. Exit barriers
  - E. The power of buyers
44. The extent of rivalry among established companies is lowest when
- A. the industry's product is a commodity.
  - B. demand is growing rapidly.
  - C. exit barriers are substantial.
  - D. the industry is entering a decline stage.
  - E. the industry is dominated by a small number of large companies.
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- A. compete directly with members of other strategic groups.
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  - C. follow a business model that is similar to that pursued by other companies in the group.
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53. Historically, government reputation has
- A. encouraged new entrants into an industry.
  - B. constituted a major entry barrier into major industries.
  - C. neither hampered nor encouraged new entrants into an industry.
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54. Rivalry refers to
- A. competition.
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  - C. a struggle among firms using price, product design, and advertising.
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55. The competitive structure of an industry refers to the
- A. number of segments in the industry.
  - B. number and size distribution of companies in the industry.
  - C. the number of consumers in the industry.
  - D. number of competing products in the industry.
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- A. prevent movement within a strategic group.
  - B. inhibit the movement of companies between strategic groups in an industry.
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  - D. include exit barriers of the strategic group that a company wants to enter.
  - E. are low when exit barriers in the strategic group that a company is a member of are high.
58. In growth industries,
- A. replacement demand is increasing rapidly.
  - B. technological expertise is the most important entry barrier.
  - C. rivalry is high.
  - D. distribution channels are poorly developed.
  - E. buyers are familiar with the industry's product.
59. Entry barriers in the embryonic stage are frequently based on
- A. brand loyalty.
  - B. economies of scale.
  - C. absolute cost advantages.
  - D. economies of scope.
  - E. technological know-how.
60. Growth industries
- A. typically suffer from high mobility barriers.
  - B. tend to be characterized by weak rivalry.
  - C. have high rivalry among established companies.
  - D. increase prices because customers are more aware of the industry's product.
  - E. provide economies of scale to existing companies.

61. An industry's buyers have high bargaining power when
- A. buyers purchase in large quantities.
  - B. switching costs are low.
  - C. it is economically feasible for buyers to purchase inputs from several companies at once.
  - D. buyers can threaten to enter an industry and produce the product themselves.
  - E. all of these.
62. Demand reaches total saturation in the EEEE stage of the industry life cycle.
- A. embryonic
  - B. growth
  - C. shakeout
  - D. maturity
  - E. decline
63. The threat from new entrants is greatest in the EEEE stage of the industry life cycle.
- A. embryonic
  - B. growth
  - C. shakeout
  - D. maturity
  - E. decline
64. Which of the following is not one of the factors in the economic forces of the macroenvironment?
- A. Interest rates
  - B. Inflation
  - C. Regulation
  - D. Currency exchange rates
  - E. Economic growth rate
65. Suppliers in an industry are most powerful when
- A. there are few substitutes for the product suppliers sell.
  - B. switching costs are low.
  - C. companies in the industry can threaten to enter the suppliers' industry.
  - D. substitute products are readily available.
  - E. all of these choices
66. Julian is asked to examine the demographic environment facing his employer, a clothing manufacturer. Which of the following should Julian examine?
- A. Government regulations
  - B. Inflation
  - C. Manufacturing technology
  - D. Aging of the population
  - E. Society's growing interest in exercise

67. Beverage makers are finding that water sales are increasing due to consumers' preferences for healthy drinks. Which part of the macroenvironment does this represent?
- A. Economic forces
  - B. Demographic forces
  - C. Embryonic forces
  - D. Political forces
  - E. Social forces
68. The level of industry demand
- A. has little effect on competition in the industry.
  - B. is one of the determinants of the intensity of rivalry in the industry.
  - C. increases as the number of customers grows.
  - D. is influenced by bankruptcy regulations.
  - E. all of these.
69. The Internet is an example of a
- A. technological force.
  - B. social force.
  - C. political and legal force.
  - D. demographic force.
  - E. global force.
70. Due to a recent relaxation in pollution standards, Ford Motors is withdrawing its electric-powered cars from sales in the U.S. market. Ford is responding to a change in which of the following macroenvironmental forces?
- A. Economic
  - B. Demographic
  - C. Political and legal
  - D. Social
  - E. Strategic
71. As an industry enters the shakeout stage,
- A. rivalry among companies declines.
  - B. demand is still growing at a high rate.
  - C. prices rise.
  - D. excess capacity emerges.
  - E. new entrants come into the market.

72. Eventually most industries enter a decline stage where
- A. growth becomes negative.
  - B. rivalry among established companies usually decreases.
  - C. competitive pressures abate.
  - D. excess capacity declines.
  - E. demand continues to hold steady.
73. Leslie is the owner of Crafts and Things, a local craft store that sells homemade gifts such as jewelry and quilts. Recently, there has been an increase in the price of the items that Leslie uses to make her crafts, such as beads and yarn. The rising cost of these items represent a(n) EEEEE to Leslie's business.
- A. opportunity
  - B. threat
  - C. cost advantage
  - D. rivalry
  - E. strength
74. When shopping for clothing such as shirts and jeans, Tyrone will only buy products sold by the Eastern Clothing Company, even if other brands are cheaper. Eastern Clothing Company has EEEEE with Tyrone.
- A. switching costs
  - B. bargaining power
  - C. risk of entry
  - D. brand loyalty
  - E. economies of scale
75. In the early 1900s, when the automobile was first manufactured, the automobile industry would have been considered a(n)
- A. mature industry.
  - B. industry stakeout.
  - C. embryonic industry.
  - D. growth industry.
  - E. declining industry.
76. In part due to advances in medicine, Americans are currently living longer now than in the past. As a result, the sale of products that meet the needs of older individuals, such as devices that assist in walking and movement, have increased. Age can be referred to as a
- A. technological force.
  - B. demographic force.
  - C. social force.
  - D. political force.
  - E. legal force.

77. Philip Morris capitalized on the growing health consciousness trend when it acquired Miller Brewing Company, and then redefined competition in the beer industry with its introduction of low-calorie beer (Miller Lite). This health trend represents a EEEEEforce.
- A. social
  - B. political
  - C. legal
  - D. technological
  - E. demographic
78. Why is it important to understand the external environment in order to think strategically?
79. Define and then relate the concepts of sectors, industries, market segments, and strategic groups.
80. Using the industry life cycle model, explain how the threats and opportunities for existing firms in an industry change over time.

81. Describe one major limitation of each of the following models for competitive analysis: the five forces model, the strategic groups model, and the industry life cycle model. Does the existence of these limitations mean that the models are not useful? Why or why not?
82. Consider the macroenvironment facing a large, international airline headquartered in the United States (such as American or United). Give at least three examples of important trends or events from each of the five segments of the airline's macroenvironment (macroeconomic, technological, demographic, social, political, and legal), and explain whether each represents a threat or an opportunity for the firm.

## Chapter 2--External Analysis: The Identification of Opportunities and Threats **Key**

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FALSE
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  - C. rivalry is high.
  - D. distribution channels are poorly developed.
  - E. buyers are familiar with the industry's product.
59. Entry barriers in the embryonic stage are frequently based on
- A. brand loyalty.
  - B. economies of scale.
  - C. absolute cost advantages.
  - D. economies of scope.
  - E. technological know-how.
60. Growth industries
- A. typically suffer from high mobility barriers.
  - B. tend to be characterized by weak rivalry.
  - C. have high rivalry among established companies.
  - D. increase prices because customers are more aware of the industry's product.
  - E. provide economies of scale to existing companies.

61. An industry's buyers have high bargaining power when
- A. buyers purchase in large quantities.
  - B. switching costs are low.
  - C. it is economically feasible for buyers to purchase inputs from several companies at once.
  - D. buyers can threaten to enter an industry and produce the product themselves.
  - E. all of these.
62. Demand reaches total saturation in the EEEE stage of the industry life cycle.
- A. embryonic
  - B. growth
  - C. shakeout
  - D. maturity
  - E. decline
63. The threat from new entrants is greatest in the EEEE stage of the industry life cycle.
- A. embryonic
  - B. growth
  - C. shakeout
  - D. maturity
  - E. decline
64. Which of the following is not one of the factors in the economic forces of the macroenvironment?
- A. Interest rates
  - B. Inflation
  - C. Regulation
  - D. Currency exchange rates
  - E. Economic growth rate
65. Suppliers in an industry are most powerful when
- A. there are few substitutes for the product suppliers sell.
  - B. switching costs are low.
  - C. companies in the industry can threaten to enter the suppliers' industry.
  - D. substitute products are readily available.
  - E. all of these choices
66. Julian is asked to examine the demographic environment facing his employer, a clothing manufacturer. Which of the following should Julian examine?
- A. Government regulations
  - B. Inflation
  - C. Manufacturing technology
  - D. Aging of the population
  - E. Society's growing interest in exercise

67. Beverage makers are finding that water sales are increasing due to consumers' preferences for healthy drinks. Which part of the macroenvironment does this represent?
- A. Economic forces
  - B. Demographic forces
  - C. Embryonic forces
  - D. Political forces
  - E. Social forces
68. The level of industry demand
- A. has little effect on competition in the industry.
  - B. is one of the determinants of the intensity of rivalry in the industry.
  - C. increases as the number of customers grows.
  - D. is influenced by bankruptcy regulations.
  - E. all of these.
69. The Internet is an example of a
- A. technological force.
  - B. social force.
  - C. political and legal force.
  - D. demographic force.
  - E. global force.
70. Due to a recent relaxation in pollution standards, Ford Motors is withdrawing its electric-powered cars from sales in the U.S. market. Ford is responding to a change in which of the following macroenvironmental forces?
- A. Economic
  - B. Demographic
  - C. Political and legal
  - D. Social
  - E. Strategic
71. As an industry enters the shakeout stage,
- A. rivalry among companies declines.
  - B. demand is still growing at a high rate.
  - C. prices rise.
  - D. excess capacity emerges.
  - E. new entrants come into the market.



72. Eventually most industries enter a decline stage where
- A. growth becomes negative.
  - B. rivalry among established companies usually decreases.
  - C. competitive pressures abate.
  - D. excess capacity declines.
  - E. demand continues to hold steady.
73. Leslie is the owner of Crafts and Things, a local craft store that sells homemade gifts such as jewelry and quilts. Recently, there has been an increase in the price of the items that Leslie uses to make her crafts, such as beads and yarn. The rising cost of these items represent a(n) EEEEE to Leslie's business.
- A. opportunity
  - B. threat
  - C. cost advantage
  - D. rivalry
  - E. strength
74. When shopping for clothing such as shirts and jeans, Tyrone will only buy products sold by the Eastern Clothing Company, even if other brands are cheaper. Eastern Clothing Company has EEEEE with Tyrone.
- A. switching costs
  - B. bargaining power
  - C. risk of entry
  - D. brand loyalty
  - E. economies of scale
75. In the early 1900s, when the automobile was first manufactured, the automobile industry would have been considered a(n)
- A. mature industry.
  - B. industry stakeout.
  - C. embryonic industry.
  - D. growth industry.
  - E. declining industry.
76. In part due to advances in medicine, Americans are currently living longer now than in the past. As a result, the sale of products that meet the needs of older individuals, such as devices that assist in walking and movement, have increased. Age can be referred to as a
- A. technological force.
  - B. demographic force.
  - C. social force.
  - D. political force.
  - E. legal force.

77. Philip Morris capitalized on the growing health consciousness trend when it acquired Miller Brewing Company, and then redefined competition in the beer industry with its introduction of low-calorie beer (Miller Lite). This health trend represents a EEEEEforce.
- A. social
  - B. political
  - C. legal
  - D. technological
  - E. demographic

78. Why is it important to understand the external environment in order to think strategically?

Strategic thinking allows managers to select those strategies that allow their companies to establish competitive advantage and outperform rivals. As the external environment continues to change in rapid and unpredictable ways, it is important for managers to understand the conditions that exist and that impact their performance and profitability. Without an understanding of the external environment, the strategy process would be arbitrary and performance would be lower than it should be. By understanding the dynamics that drive industries and the macroenvironmental forces that present both opportunities and threats, managers are in a position to craft strategies that allow them to effectively steer their companies through challenging times.

79. Define and then relate the concepts of sectors, industries, market segments, and strategic groups.

All of these concepts are useful in terms of understanding the nature of competition and the forces in the industry environment that affect performance. A skilled strategic manager must take all of these into account when developing strategies.

A sector refers to a group of closely related industries. In terms of scope, sectors encompass the broadest set of firms. A sector is typically composed of several interrelated industries. An industry refers to a group of companies offering products and services that are close substitutes for each other. Market segments refer to a distinct group of customers within an industry market that can be differentiated from each other on the basis of their distinct attributes and specific demands. A strategic group is a group of companies within an industry in which each company follows a business model that is similar to that pursued by other companies in the group. A useful way to look at a strategic group is as an intersection of market segments and industries. The concept of a strategic group is especially useful in the strategy process because it helps a company determine its direct competition.

80. Using the industry life cycle model, explain how the threats and opportunities for existing firms in an industry change over time.

In the embryonic stage of the industry life cycle, barriers to entry come from access to technological know-how (a threat). Rivalry is relatively low due to the fragmented nature of the industry (an opportunity). Suppliers tend to be large and powerful relative to existing companies, as do buyers (threats). Substitute products may be plentiful, inexpensive, and better known to consumers (a threat).

In the growth stage, barriers to entry are typically quite low (a threat). Rivalry is low because the growing industry creates plenty of demand (an opportunity). Buyers and suppliers are somewhat less powerful relative to the larger companies of the growth stage (moving toward opportunities). Substitute products may be few or plentiful (an opportunity or threat).

In a mature industry, barriers to entry rely on economies of scale and brand loyalty, and they are quite high (an opportunity). Rivalry becomes much more intense (a threat). Buyers and suppliers become even less powerful relative to the large existing companies (opportunities). Substitute products may be few or plentiful (opportunity or threat).

In the decline stage, there are few new entrants (an opportunity). Rivalry remains very intense (a threat). Buyers and suppliers become more powerful relative to existing firms (moving toward threats). Substitute products are likely to be plentiful and appealing to consumers (a threat).

81. Describe one major limitation of each of the following models for competitive analysis: the five forces model, the strategic groups model, and the industry life cycle model. Does the existence of these limitations mean that the models are not useful? Why or why not?

All three of these models fail to account for the impact that radical change and innovation can have on an industry. Radical change can alter the impact of the five forces; it can shift the strategic groupings within an industry; and it can speed, slow, or disrupt an industry's progress through the stages of the life cycle model. Because these three models all rely on historical evidence to project future trends, the possibility and impact of radical discontinuity is not incorporated into them.

Another limitation of each of these models is the lack of accounting for firm-specific characteristics and actions. These three models all assume that the environment is a major determinant of firm performance and that every firm in the industry (or the strategic group) experiences the industry structure in the same way. Yet empirical evidence demonstrates that firms within the industry have widely differing levels of performance, so there must be other explanatory variables. According to some studies, industry characteristics account for no more than 20 percent of the variance in performance across firms.

A limitation of the life cycle model is that not every industry moves through the same steps or in the same order or at the same rate. Empirical evidence shows that industries vary tremendously in the rate and way in which they mature.

82. Consider the macroenvironment facing a large, international airline headquartered in the United States (such as American or United). Give at least three examples of important trends or events from each of the five segments of the airline's macroenvironment (macroeconomic, technological, demographic, social, political, and legal), and explain whether each represents a threat or an opportunity for the firm.

Students don't need to conduct research to answer this question; they should be able to answer from their own understanding and general knowledge. Examples of the types of answers they should write are given below.

- [ The airline industry benefits from low interest rates, part of the macroeconomic environment, because it enables airlines to borrow the funds for purchasing new planes at lower cost.
- [ Americans are taking shorter but more frequent vacations. This social trend presents an opportunity for airlines to sell more tickets.
- [ Technological advances have allowed railroads to use fast, fuel-efficient bullet trains, which can economically substitute for planes on short, heavily-traveled commuter routes, such as along the Boston-New York-Washington corridor. This development threatens airlines because it reduces the number of tickets they can sell and the prices they can charge in those markets.