



STRATEGIC VALUE ANALYSIS

Competitive interactions to be considered in investment decisions

SVA™ Methodology

Selection of slides

Strategy

Management

Organization

Finance

- **Foundations of Strategic Value Analysis methodology and SVA™ tool**
 - The industry cost curve
 - Introduction to imperfect competition (investments // price & volumes)
 - SVA foundations
 - Illustrations

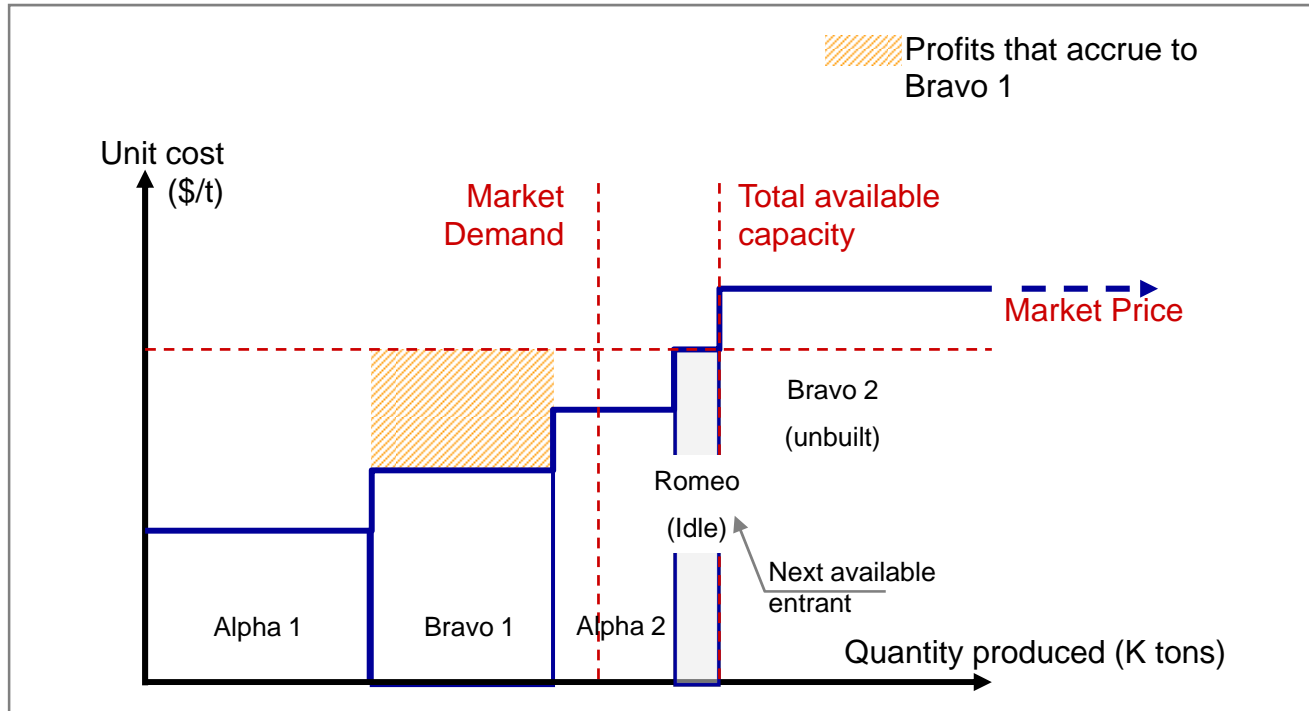
- How to deal with the threat of entry?
 - Contexts that favour / limit entry
 - Case of a new entrant more competitive than the local firm
 - Judo economics : Case of a new entrant less competitive than the local firm

- Demand growth and market structuring
 - Pre-emption and acquisitions
 - Retaliation threat
 - Free-riding

- New business models for commodities
 - International development issues
 - Corporate finance issues

Starting point : Industry Cost Curve, *cf Watters, Mc Kinsey, 1981*

Market share predictions do not fit with empirical evidence in multi-markets industries

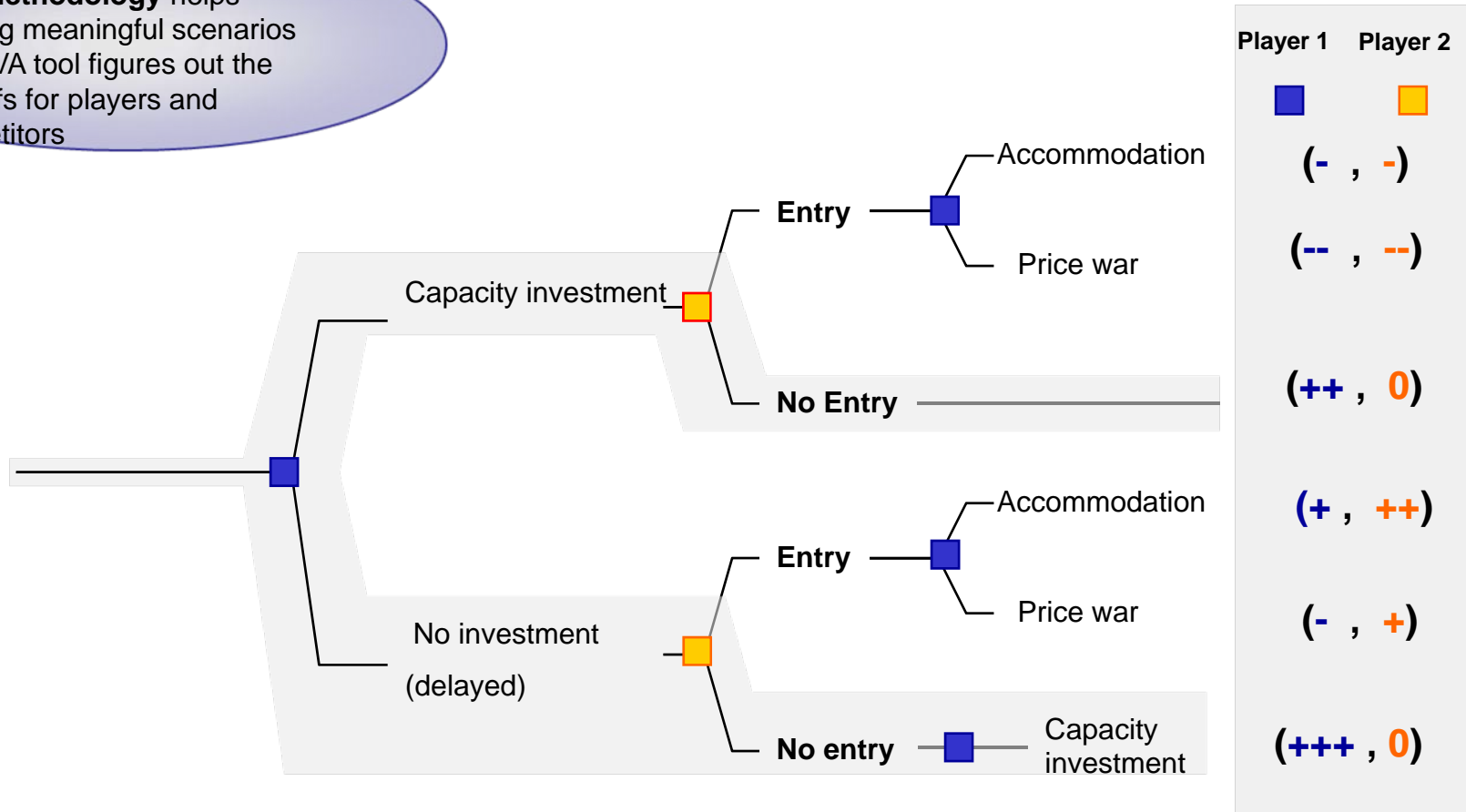


- Why do Alpha2 not seek to undercut the price for improving its utilization ratio ?
- What if cost curves differ from one market to another while capacity constraints are limiting the total available volume ?
- How to quit the world of perfect competition (allocation that maximizes the efficiency of the whole industry) ?

Example of a competition issue (game theoretical approach)

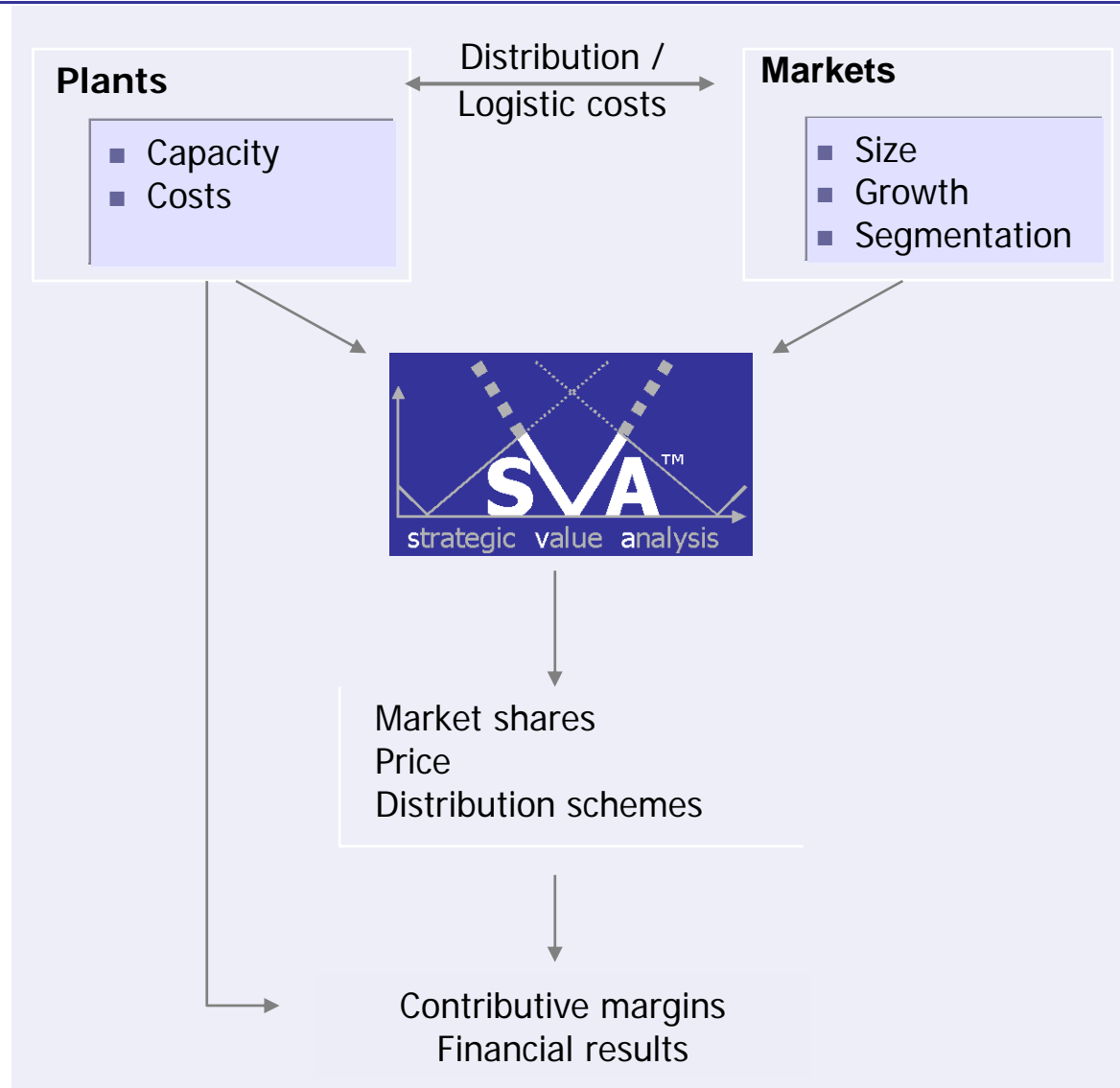
Scenarios building and selection

SVA methodology helps building meaningful scenarios and SVA tool figures out the pay-offs for players and competitors



How to figure out Payoffs of players ? (3/6)

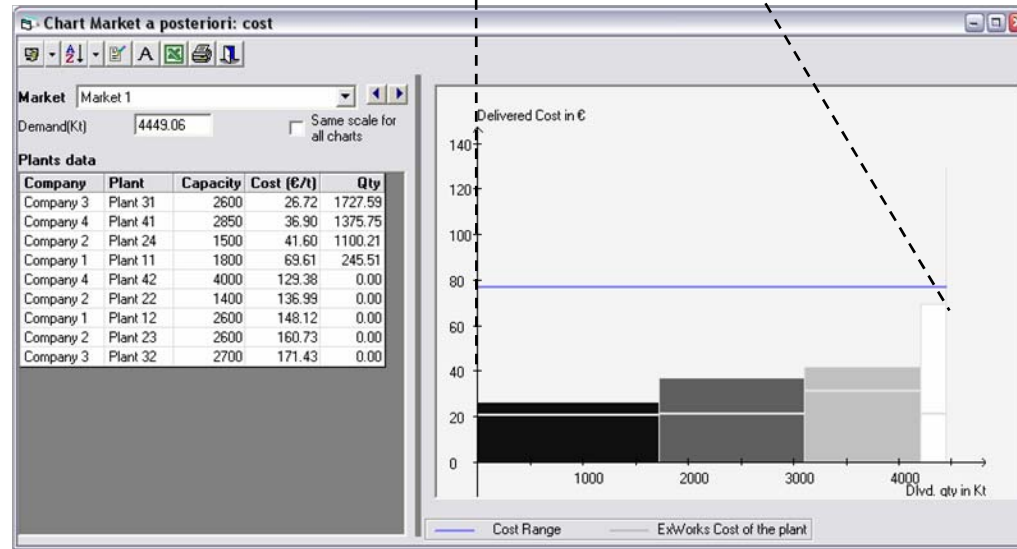
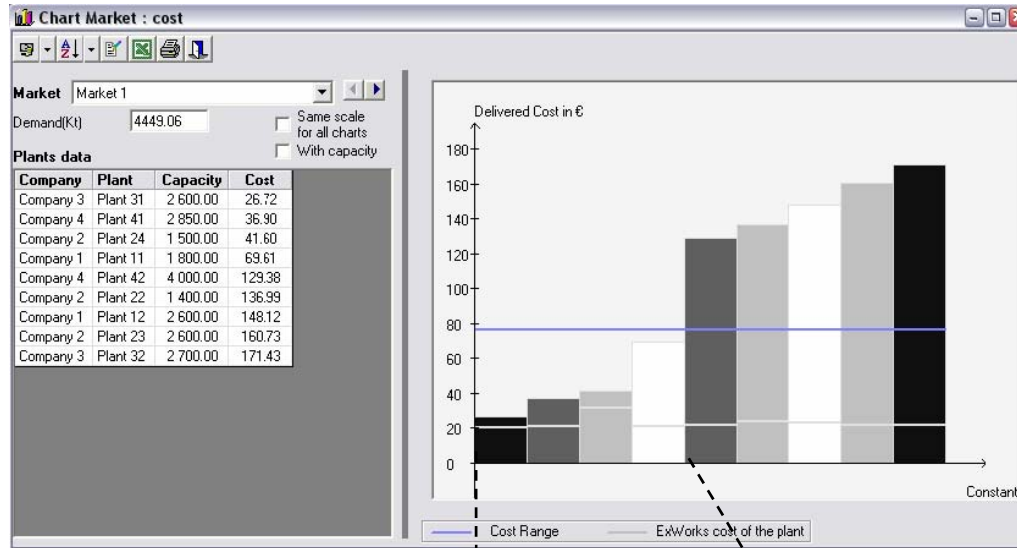
SVA deals with multi-market / capacity constraints problem



How to figure out Payoffs of players ? (4/6)

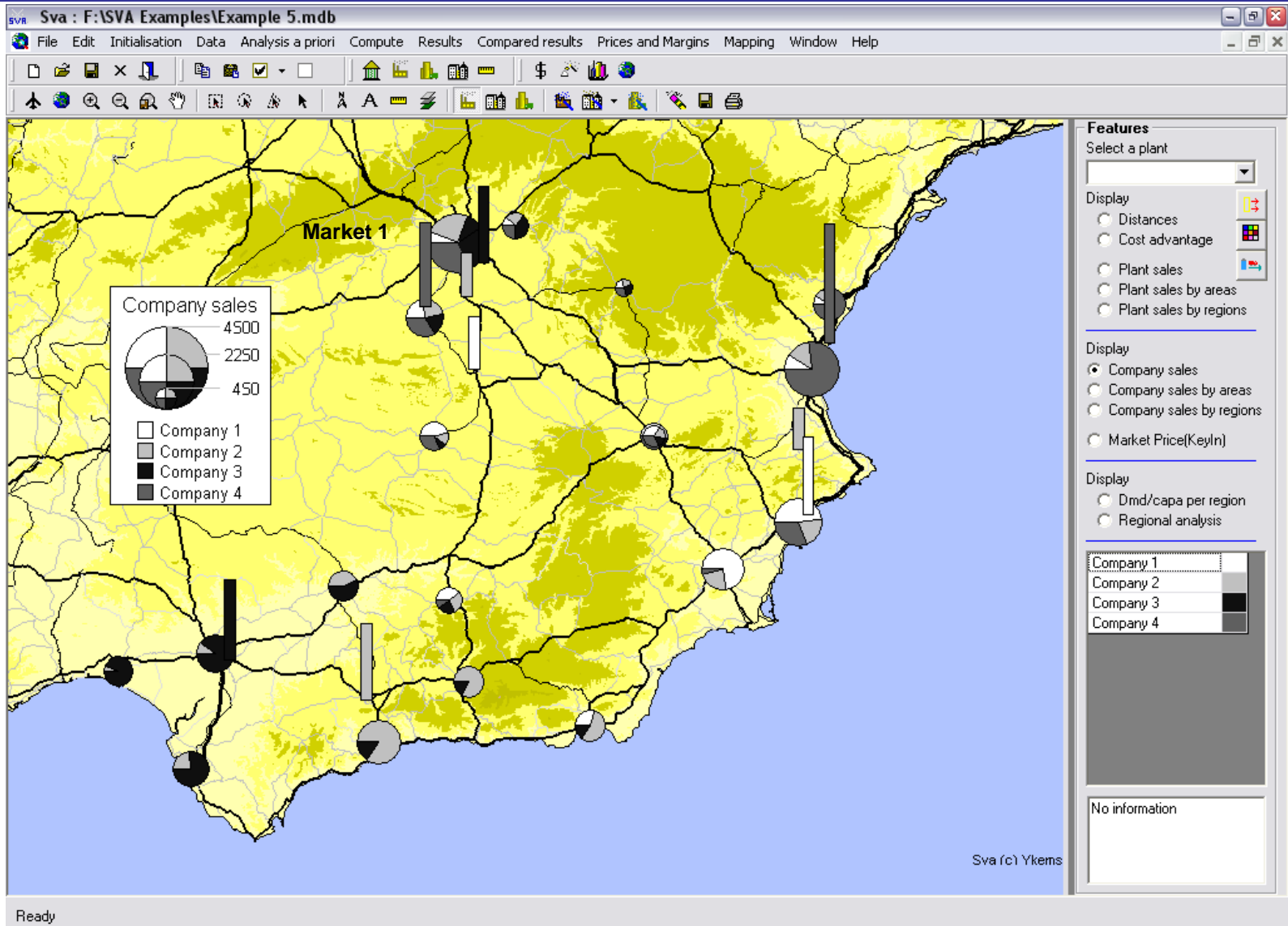
Competitors delivered costs on one market and SVA allocation of market shares under capacity constraints

Market 1



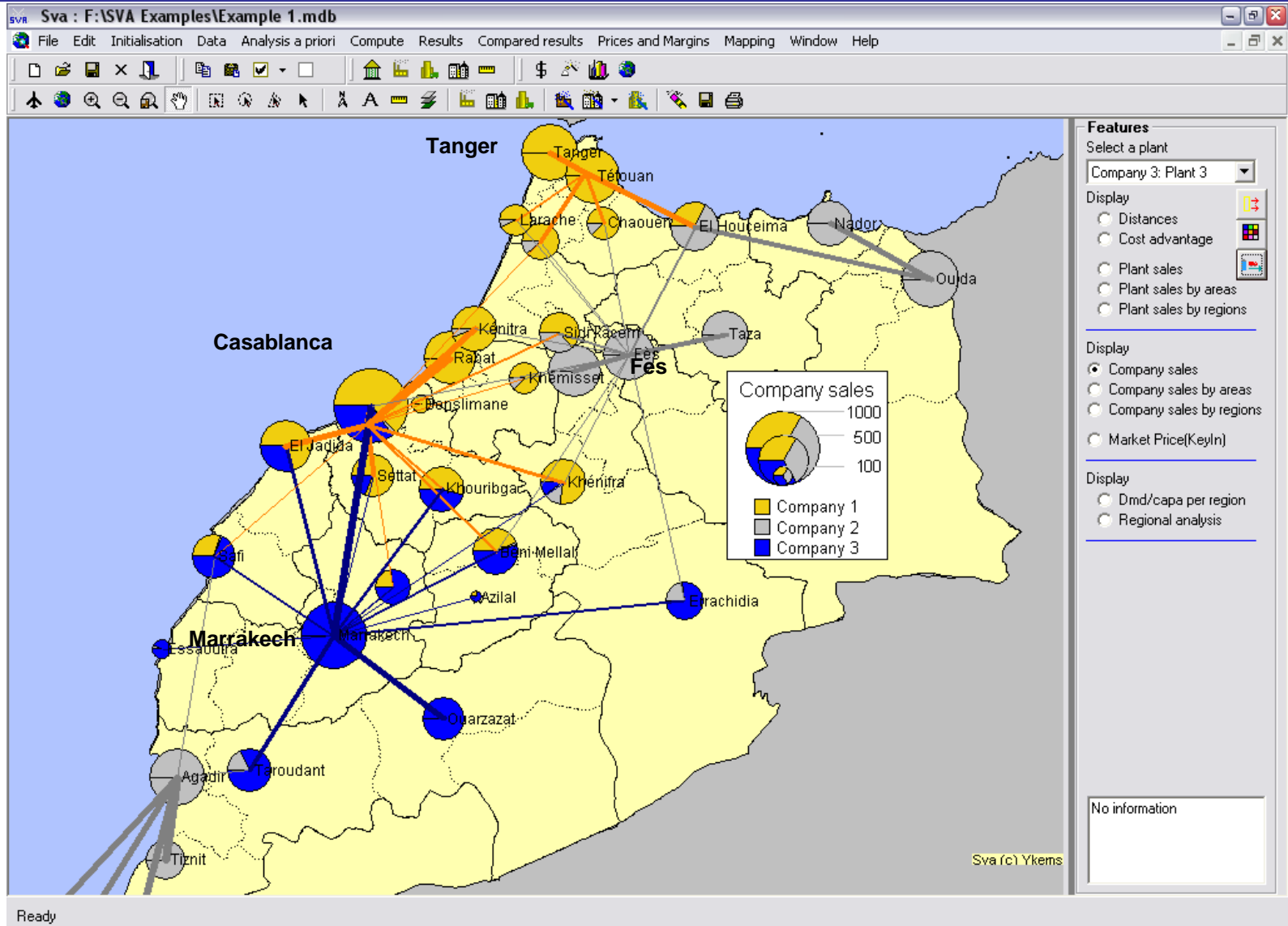
How to figure out Payoffs of players ? (5/6)

Plants' capacity and location par company and competitors market shares



How to figure out Payoffs of players ? (6/6)

Market shares allocation and plant-to-market flows



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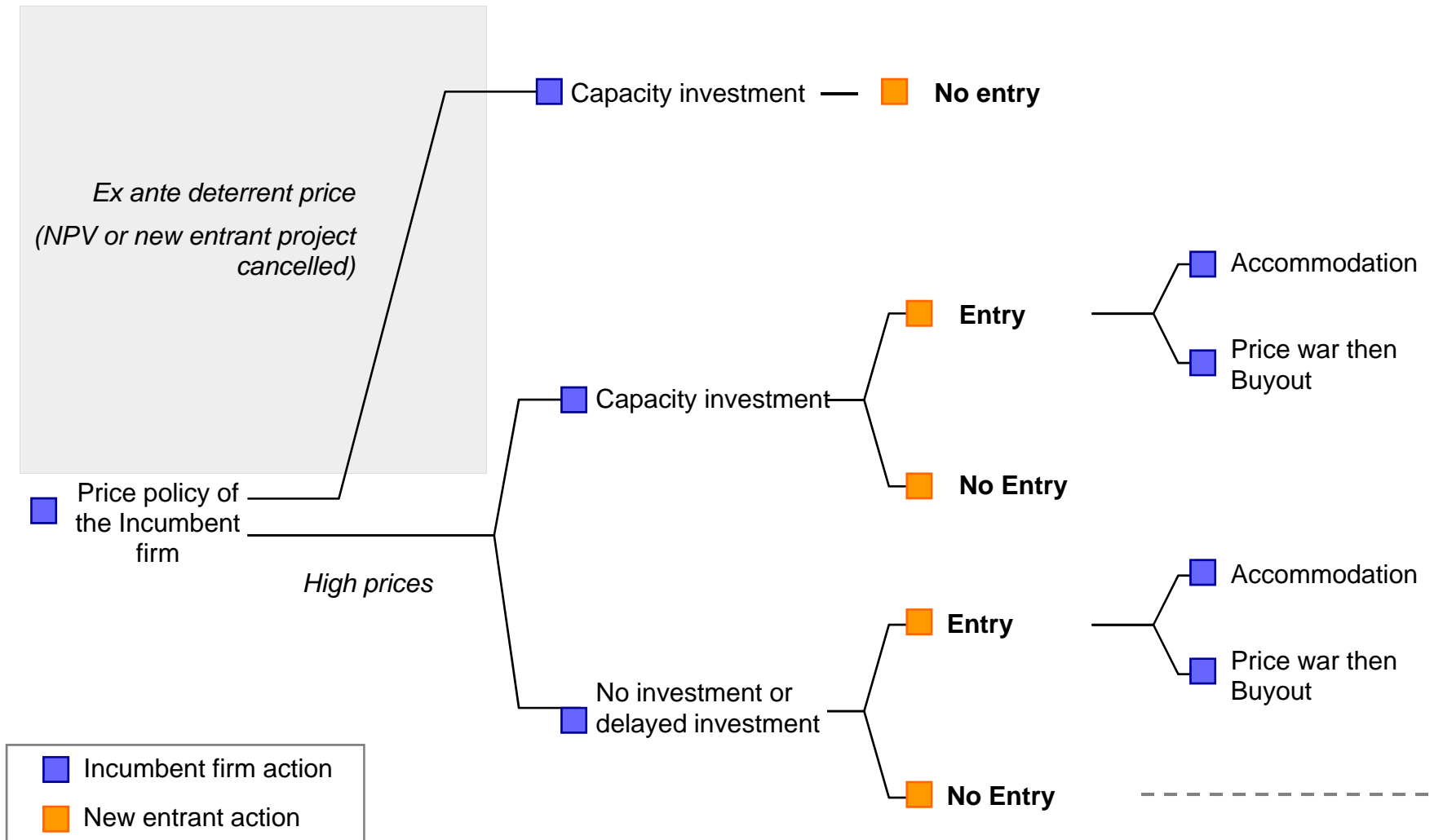
Some contexts support new competitors entry

- **Some markets characteristics** may create entrance opportunity for new competitors (importers or new domestic investment projects)
 - A high growth
 - The existence of power buyers (distributors) which could turn away from their usual suppliers
 - An easy access to raw materials or technologic alternatives (new raw materials or new process)
 - Custom duties reduction

- **Incumbent firms behavior** can contribute to increase entry risks :
 - High prices, resulting from abuse of dominant position or production costs too high
 - Difficulties to supply clients (who may look for alternative sourcing schemes)
 - Lack of capacity
 - Frequent under coverage, low service rate
 - Weakness of services associate to the product (credit)
 - Weak control of downstream supply chain and distribution structure
 - Weak control of upstream sourcing in case of non-vertical integration.

- **Finally, a bad coordination between domestic players** may facilitate the entry : if the firm facing directly the new entrant mistakenly responds, firms which were not “a priori” concerned can be severely hurt by the propagation of the price war, that nobody can stop...But in some contexts, “weak entrants are welcomed”

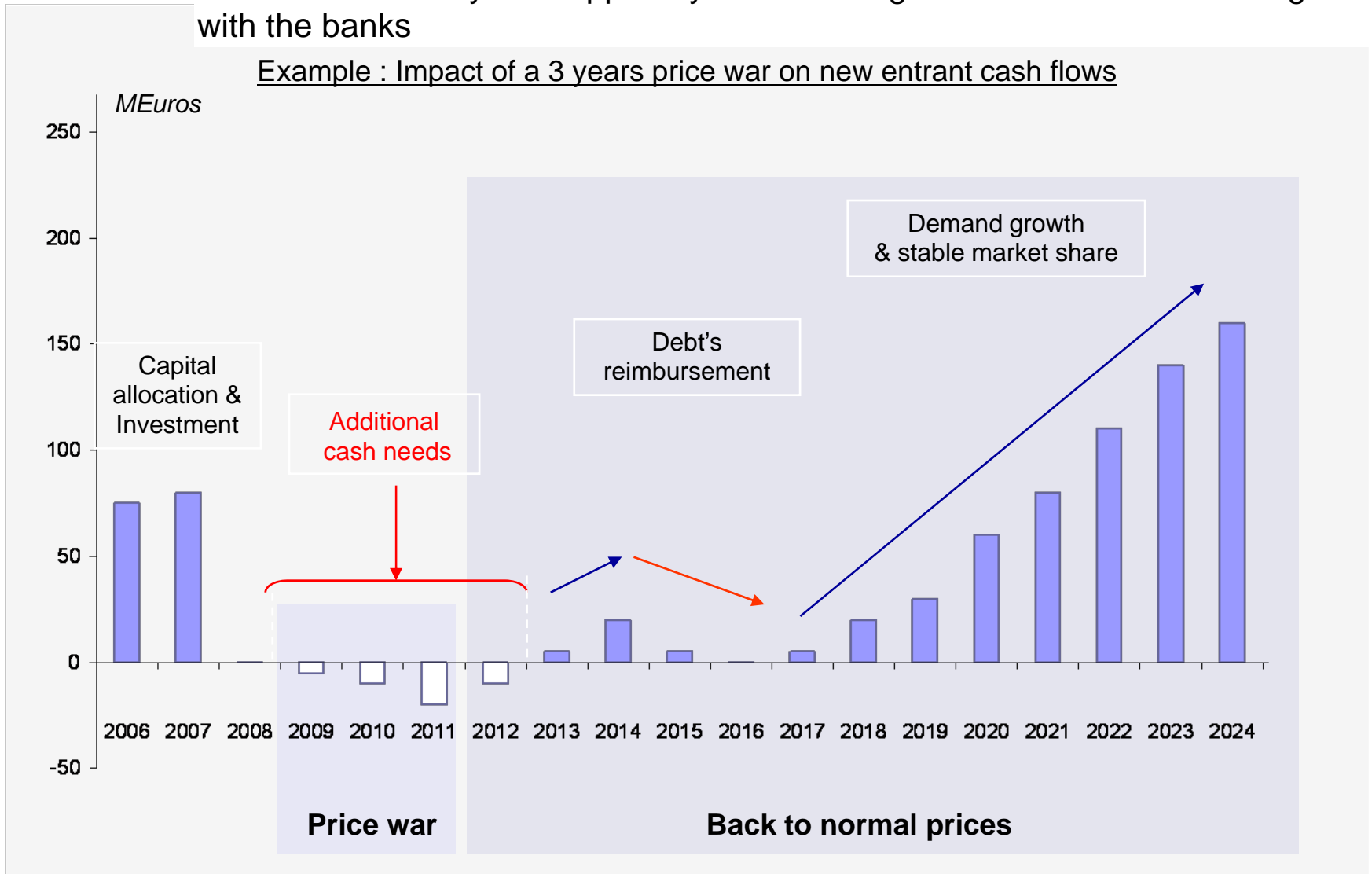
Judo economics : Case of a new entrant less competitive than the local firm (1/3)



Judo economics : Case of a new entrant less competitive than the local firm (3/3)

Once the investment is sunk, the incentives to sustain a price war while pushing volumes can hardly be stopped by cash shortages that could not be re-negotiated with the banks

Example : Impact of a 3 years price war on new entrant cash flows



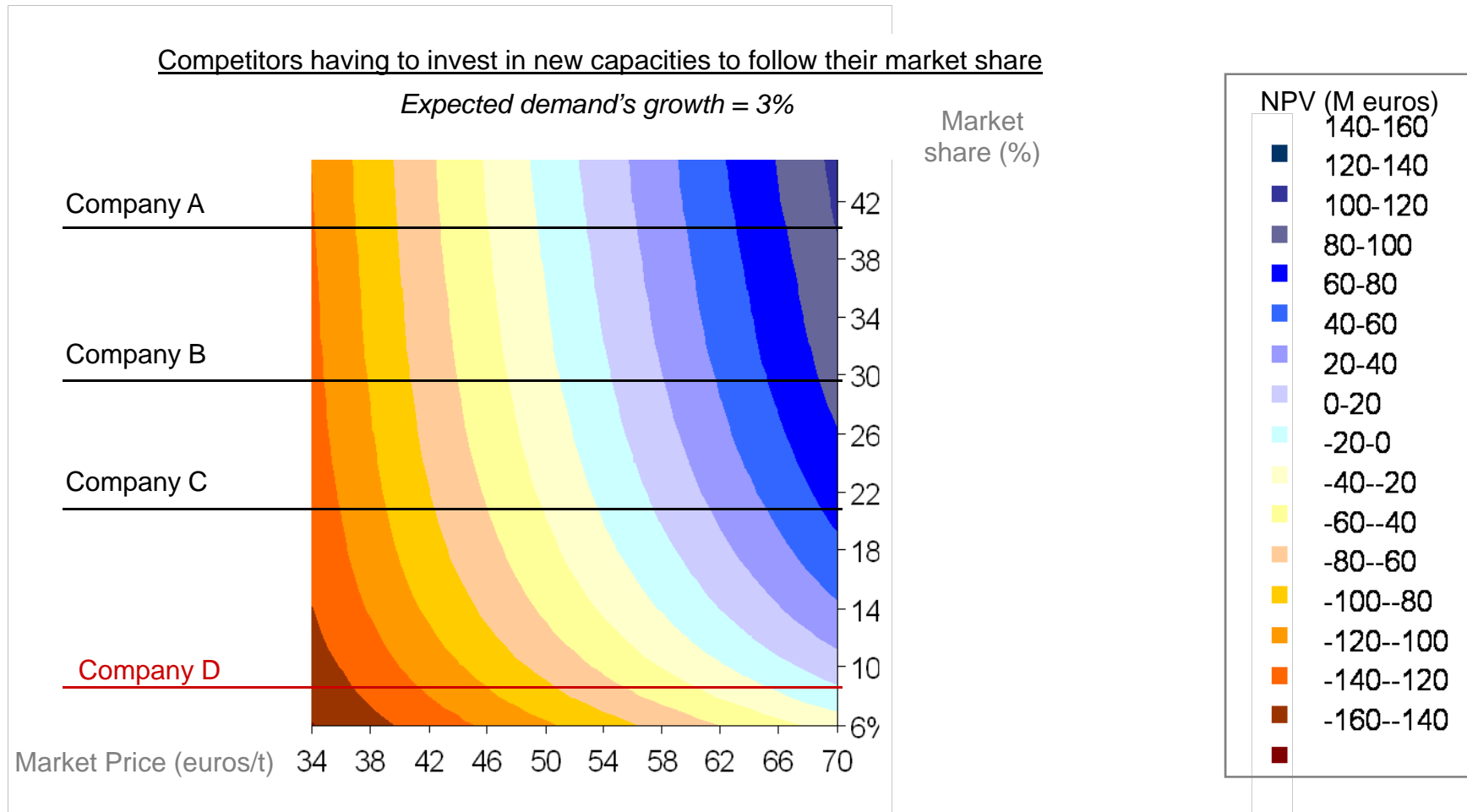
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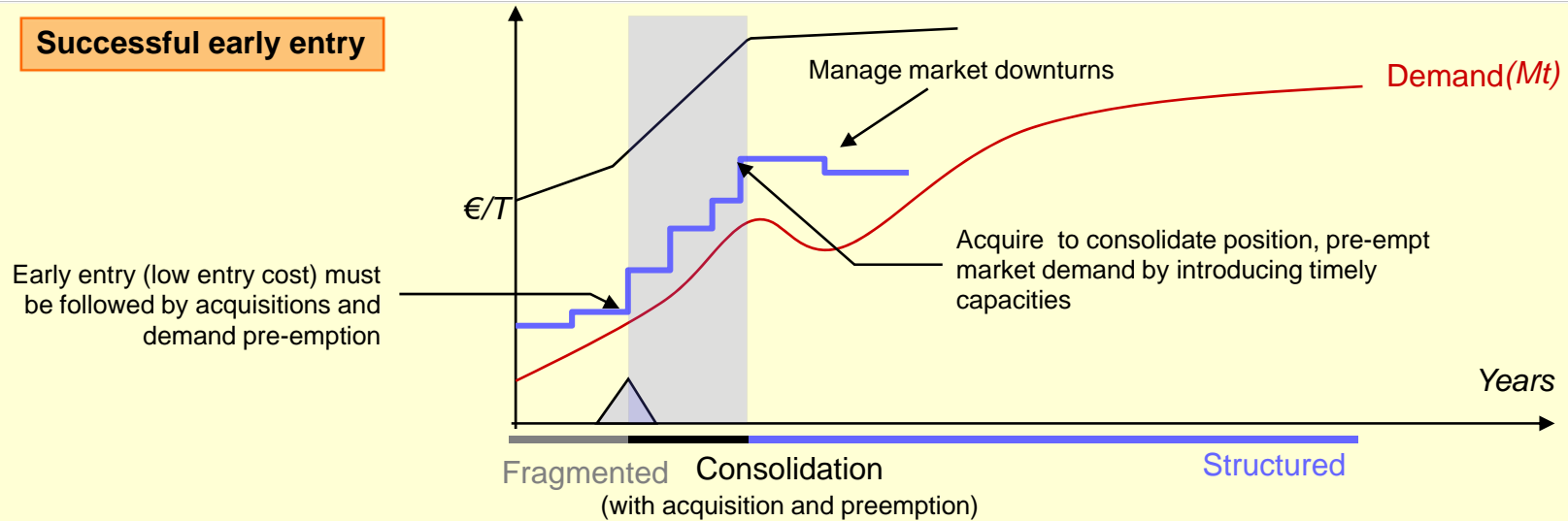
- With market prices around 65€/T, **Company D** is the only one who cannot justify a new capacity investment, unless begging on an aggressive strategy (catch volumes to other competitors) or seeking to pre-empt demand's growth and dissuade another company to invest.



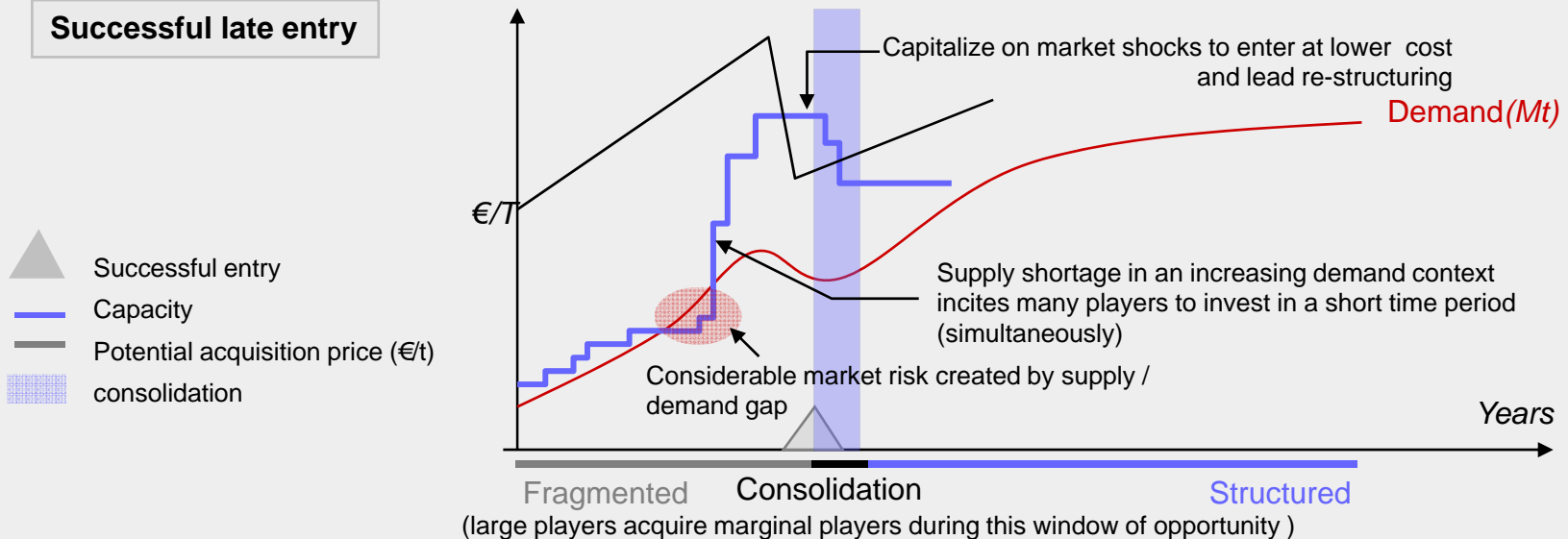
Offer/Demand cycles evolution offer various types of entry strategy

Early entry requires pro-active capacity/consolidation management, while late entry requires opportunistic timing and parallel competitive efforts

Successful early entry



Successful late entry



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