SWOT

Idea In Short

SWOT Analysis is a business framework that helps assess a wide variety of factors that impact a business's performance. These factors may be either internal or external to a business. These factors may either be favourable/helpful or unfavourable/harmful to a business. By combining these dimensions - Strengths, Weaknesses, Opportunities and Threats – a business can assume a strategic posture.

SWOT is a simple and widely accepted tool that helps focus on the key issues that affect a business. The SWOT helps identify the strengths and weaknesses that are relevant to meet opportunities and threats in particular scenarios. A business can directly manage its strengths and weaknesses as these are factors internal to the business. Likewise, a business can only anticipate and react to opportunities and threats that emerge from forces external to the business.

Origins

SWOT analysis was invented in the 1960s by a management consultant named Albert Humphrey at the Stanford Research Institute. Previously, corporate planning had not met with much success. Fortune 500 companies needed a way to produce long-term planning that was executable and reasonable. Humphrey and his research team proposed the SWOT model to bring accountability and objectivity to the planning process, and it has been popular ever since. Albert Humphrey advocated performing SWOT analysis on specific criteria, such as products, process, customers, distribution, finance, and administration. Since it was invented, SWOT analysis has grown in popularity. Today, it is a part of every consultant's toolkit.

Strengths

A business's strengths are its characteristics that give it an advantage over its competitors.

These strengths go by different names, such as unique selling points (USPs), firm-specific advantages [FSAs] or competitive advantage. The source of these strengths are resources and capabilities that are valuable, rare, hard-to-imitate and organization-wide supported. The VRIO framework is a useful tool to evaluate a business's resources. Patents, a strong brand, innovative products, large financial reserves, etc. are examples of valuable business resources. Value Chain Analysis is another approach to assess a business's strengths. By mapping out a business's complete value chain, from the purchasing of raw materials to the marketing and sales of the end-products, a business can better identify where it creates value.

Weaknesses

Weaknesses are characteristics that place a business at a disadvantage relative to its competitors. In other words, weaknesses harm a business. Examples of weaknesses include a lack of patent protection, poor reputation among customers, limited working capital, poor leadership and inefficient production processes. Adequate feedback loops, both internal and external to the business environment, help discovered weaknesses. Examples of such feedback loops include customer surveys, monthly employee All-Hands meetings, etc. To summarize, strengths and weakness analyses constitute the internal scope of SWOT analyses. Altogether, these analyses help businesses understand their internal factors.

Opportunities

Opportunities are factors external to a business that positively impacts its performance. To assess opportunities, a business seek out elements in its environment that it could exploit to its advantage. PESTLE analysis helps understand businesses' macro-environment. Similarly, Porter's Five Forces helps understand the industry dynamics. Both these tools help asses factors external to a business. PESTLE looks at political, economic, social, technological, environmental and legal trends in the macro-environment. Examples are the increasing purchasing power of customers, governmental subsidies, more favorable international trade policies, and general lifestyle changes among the population. On the other hand, Porter's Five Forces looks at industry factors, such as current competition, supplier power, buyer power, potential new entrants, and substitutes (products or services).

Threats

Threats are factors external to a business that negatively impacts its performance. As with opportunities analysis, PESTLE analysis and Porter's Five Forces model help identify the environmental factors that could potentially harm the organization. Examples of detrimental macro-environmental developments include increasing unemployment rate, disruptive technologies, socio-demographic shifts, changing consumer behavior, increasing government corruption levels, unfavorable regulations, etc. Examples of industry specific threats include new competitors entering the competitive landscape, increasing number of substitutes, growing bargaining power from suppliers, etc. To summarize, opportunities and threats analyses constitute the external scope of SWOT analyses. These analyses help businesses understand their external factors.

Summary

SWOT analysis is a robust framework that combines different frameworks and perspectives, such as Resource Based View [RBV] and Industrial Organization (I/O). Porter's Five Forces focuses on the external environment, whilst the VRIO framework focuses on the internal environment as sources for competitive advantage to determine a business's profit potential. Combining both, internal and external factors, will help truly understand businesses' operating environment. Hence, a SWOT analysis offers businesses a good starting point to assess the current situation and formulate a strategy.