

PAK Study Manual

Strategic Decision Making (SDM) Exam
Spring 2021 Edition

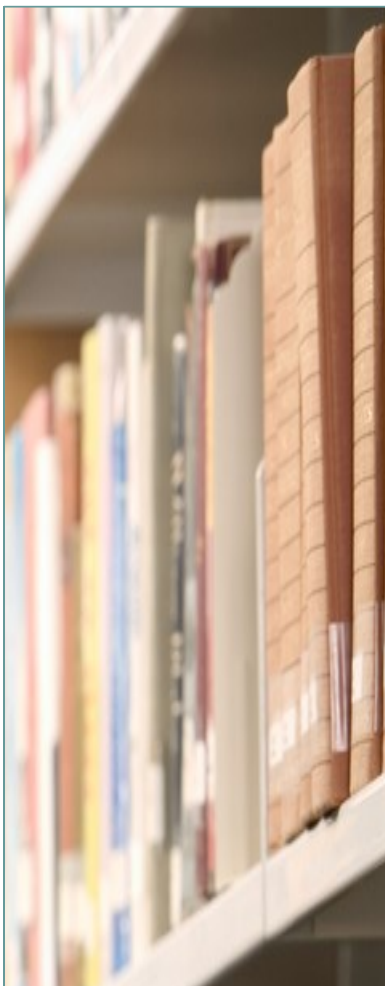


PAK Study Manual for SDM Spring 2021



PRODUCT FEATURES

Features	PAK Study Manual	PAK Exam Aid	PAK Flash Cards	PAK Test Aid	PAK Video of the Week	PAK Study Manual Basic Package	PAK Study Manual Premium Package	PAK Online Seminar
Summaries	X					X	X	
Relevant Past Questions (List)	X					X	X	
500+ Practice Questions	X					X	X	
Case Study Analysis	X					X	X	
10 Mock Questions	X					X	X	
Suggested Schedule (Detailed)	X					X	X	
Email Support	X					X	X	
110 Mock Questions		X				X	X	
700+ Practice Questions		X				X	X	
Case Study Questions		X				X	X	
Past Questions (Sorted PDFs)		X				X	X	
Electronic Flash Cards			X				X	
Audio Flash Cards + Anki			X				X	
Condensed Summary			X				X	
Mock Exam				X			X	
Weekly Videos					X	X	X	
Bonus materials							X	
Online Videos								X
Past Question Video								X
Mock Questions								X



PAK STUDY MANUAL

A **printed** copy of the manual can be purchased separately.

1. Summary

The PAK Study Manual covers the entire SDM syllabus. Not only does it give you the detailed explanations on conceptual, calculation, and exam materials, but it also fills in the gaps among the topics that are not covered in the source readings. It helps you better understand and master the confusing logics and difficult materials.

In addition, it links the similar topics across readings together and connects them to the syllabus so that you can see the whole picture of this exam.

2. Relevant Past SDM SOA Exam Questions (List)

For each reading, we compose a list of relevant past exam questions (if any) so that you can locate the questions quickly and practice them immediately. This saves your time on searching what materials are relevant to this exam.

3. Case Study Analysis

This set connects the case study materials to the study materials so that you can see the picture on how they can be tested.

4. 500+ Practice Questions

One key point to pass this exam is to "practice" (Practice makes perfect!). Due to this reason, we include many practice questions in each reading to refresh the materials just learnt and to strengthen your knowledge. More practice will be available in the PAK Exam Aid.

5. 10 Mock Exam Questions

The mock exam questions mimic the same difficulty level of the real exam questions. 10 mock exam questions and solutions are included in the PAK Study Manual to challenge your understandings. More practice will be available in the PAK Exam Aid.

6. Suggested Study Schedule (Detailed)

The syllabus is huge. It is very easy to lose track on your study. A clearly defined study schedule and some useful tips are included to help you better manage your schedule.

7. Email Support

Get questions? Please send us an email

"The study materials were very helpful in preparing me for the exam. Most importantly I was better able to apply the things that I learned to exam style questions." By Marc Roberts

[Read the whole story](#)

DO YOU KNOW?

The PAK Study Manual and related aids are updated EVERY exam sitting.

You will see the most updated materials, examples, and explanations to help you master the concepts and pass this exam in the first attempt.

PAK FLASH CARDS

A **printed** copy of the flash cards can be purchased separately.

1. Electronic Flash Cards

- ◇ Summarize the key points in organized format.
- ◇ Include pros/cons, definition/description, etc.
- ◇ Contain around 400+ front/back flash cards (or 800+ slides) .
- ◇ Read them in your smart phone device, tablet device, and/or computer.
- ◇ PDF version is also available.

2. Audio Flash Cards + Anki

- ◇ You can load them to your smartphone device and listen to them anytime/ anywhere you want.
- ◇ An Anki version is available.

3. Electronic Condensed Summary

- ◇ Summarize the key points in outline format
- ◇ Quickly refresh all the important topics in the readings

PAK TEST AID

1. Mock Exam

- ◇ This set of mock exam is different from those mock questions available in the PAK Exam Aid. You can write down your answers and send them to me. I will give you detailed feedbacks on how to improve your exam score.

PAK EXAM AID

1. 110 Mock Exam Questions and Solutions

The mock exam questions mimic the same difficulty level of the real exam questions. 100 mock exam questions and solutions (10 mock question sets) are included to challenge your understandings.

2. 700+ Practice Questions

One key point to pass this exam is to "practice" (Practice makes perfect!). Due to this reason, we include many practice questions in each reading to refresh the materials just learnt and to strengthen your knowledge. They are different from the practice question set in the manual.

3. Case Study Practice Questions

A set of case-study-related practice questions is included to help students better understand how to answer case study questions.

4. Past SOA Exam Questions (from All FSA Tracks) Relevant to This Exam

This set not only includes the past exam questions from the SDM exam, but also includes the past exam questions from all the other FSA exam tracks (e.g. FETE, APM, CSP, DP, etc). It helps you better understand how the materials were tested and gets you familiar with the SOA exam question style.

PAK VIDEO OF THE WEEK

1. Videos discussing confusing topics and concepts.
2. Videos explaining calculation-related examples.
3. Video reviewing the case study.
4. Weekly video answering common students' questions.

DO YOU KNOW?

You can find the most updated information about the PAK Study Manual and related aids under the "Announcement" section on the front page of the PAK website.

"The Mock questions, Mock exam and Exam Aid are also very beneficial to make sure you're abilities are up to par before the real exam." By Wes Smith

Read the whole story

RELEASE SCHEDULE

Features	PAK Study Manual	PAK Exam Aid	PAK Flash Cards	PAK Test Aid	PAK Video of the Week	PAK Study Manual Basic Package	PAK Study Manual Premium Package	PAK Online Seminar
Summaries	11/15 + 1/15					11/15 + 1/15	11/15 + 1/15	
Relevant Past Questions (List)	1/15					1/15	1/15	
500+ Practice Questions	1/15					1/15	1/15	
Case Study Analysis*	2/15					2/15	2/15	
10 Mock Questions	11/15					11/15	11/15	
Suggested Schedule (Detailed)	11/15					11/15	11/15	
Email Support	Anytime					Anytime	Anytime	
110 Mock Questions*		2/15				2/15	2/15	
700+ Practice Questions		2/15				2/15	2/15	
Case Study Questions*		2/15				2/15	2/15	
Past Questions (Sorted PDFs)		12/15				12/15	12/15	
Electronic Flash Cards			1/15				1/15	
Audio Flash Cards + Anki			2/15				2/15	
Condensed Summary			1/15				1/15	
Mock Exam*				3/15			3/15	
Weekly Videos					12/15	12/15	12/15	
Bonus materials							To Be Announced	
Online Videos								11/15 + 2/15
Past Question Video								3/15
Mock Questions*								3/15

* The release schedule of these items may be changed. It depends on when the SOA will release the new case study.



PAK ONLINE SEMINAR

1. Over 80 videos to clarify and explain the key concepts/calculations in the readings of the entire syllabus
2. Discuss the past exam questions and what questions might be asked on the upcoming exam
3. Videos reviewing exam tips and techniques that can help you to maximize your score
4. Review the new version of the case study and discuss which sections are important, and how they might be tested
5. Contain condensed outlines for each reading
6. Review the lectures and study at your own pace, on any PC, Mac, smartphone, and/or tablet device
7. All videos are available in MP3 (audio) format
8. Instructor support via email and PAK Forum support to help you to clarify any section of the syllabus
9. Free access for 2nd attempt (only for those who scored 2-5)
10. Include PAK Study Manual, PAK Flash Cards, and 7 Mock Question Sets (from PAK Exam Aid)

SAMPLES?

You can find more samples on the [PAK](#) website.

IMPORTANT NOTES

1. Please note that all products are in electronic (PDF) format. **No** hard copy is provided.
2. Once you make a purchase (please use your work email address), we will send you a confirmation email within 1 business days. Once the files are available, we will send them to you through email. Please make sure that you put the correct email address when you purchase the PAK products. **If you do not receive the confirmation email, please send us an email (services@pakstudymanual.com).**
3. Please check your “junk” mailbox. Sometimes, our email is blocked.

MORE INFORMATION

Want more information? Please contact me at eddy.chan@pakstudymanual.com, paulpeterson@pakstudymanual.com or visit www.pakstudymanual.com

COMMENTS FROM THE PAST CANDIDATES

You can find more comments from the past candidates here: [PAK Testimonials](#).

WHERE TO PURCHASE PAK PRODUCTS

The PAK products are available at [Actex](#), and [Actuarial Bookstore](#).

DO YOU KNOW?

If you are not sure which exam track to take, or how it can advance your career, you can send an email to Paul or Eddy and discuss your situation with them. They will share their work experience with you so that you can make your decision informatively.

Frequent Answer Questions

Do You Need to Read the Source Readings?

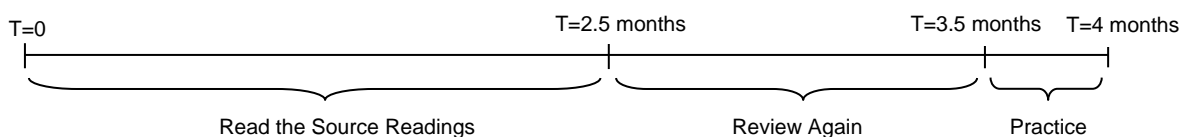
Unlike the preliminary exams, reading the source readings (textbooks, SOA study notes, and online readings) is ***a must*** in the FSA exams. PAK Study Manual can help you understand the materials faster and memorize them quickly so that in the time-limited environment, you can be well-prepared for the exam.

How Much Time is Needed to Study for This Exam?

This varies by person. Usually it will take one 350-400 hours to study for a FSA exam (5-hour). Please expect to spend the same amount of time for the SDM exam.

Study Schedule

From the date the SOA release the new syllabus to the exam date, there are around 4 months to study. How to plan your study schedule?



Read the Source Readings

Assume you take the SDM exam in this exam sitting. In general, it will take one 2 to 2.5 months to finish them. To study more efficiently, we highly suggest you following the steps below:

Step 1: Define Your Own Study Schedule

- Use the suggested study schedule as a reference
- Prepare your own study schedule (*Target 20-30 pages @weekday and 50-60 pages @weekend*)
- Expect to read the whole syllabus and the past exams 2 or 3 times before the exam

Step 2: Read the Source Readings Together with the PAK Study Manual

- Write down your notes in the study manual
- Highlight all the key points there (*Will be used for memorization later*)
- Label any calculations that you will go over again later
- Go over the related past exam questions once you finish that reading

Step 3: Practice the SOA Past Papers

- Practice them once you finish your first-round of readings (*use the PAK Exam Aid*)
- Understand how the topics were tested and how the questions were answered

Review Again

After completing the three steps above, you probably have a general idea about how the exam looks like. Now you should review the source readings again but this time focus more on the key topics, clarify the confusing concepts/calculations, think of what can be tested and read them carefully (use my mock exam questions)

Practice

The last month is the most critical month. Here are the steps:

- Practice the past exams and my mock questions to identify what you still do not know
- Go back to the readings and find your answers (*or send us an email if you need help*)
- Start memorizing the key points (*use the PAK Flash Cards*)
- Use the PAK Test Aid to test your knowledge (*Send us your answers and we will give you detailed feedbacks on how to improve your score in the exams*)

More Information

We will explain how to prepare for this exam in much more details in the PAK Study Manual.

Any Questions?

We know you probably have a lot of questions in your mind regarding the exam or choosing study aids. Please feel free to contact us at eddy.chan@pakstudymanual.com or paulpeterson@pakstudymanual.com.

Key points

Key Points in This Reading

1. Explain the importance of analyzing and understanding the firm's external environment
2. Define and describe the general environment and the industry environment
3. Discuss the four activities of the external environmental analysis process
4. Name and describe the general environment's seven segments
5. Identify the five competitive forces and explain how they determine an industry's profit potential
6. Define strategic groups and describe their influence on the firm
7. Describe what firms need to know about their competitors and different methods used to collect intelligence about them

Ch.2 The External Environment: Opportunities, Threats, Industry Competition, and Competitor Analysis

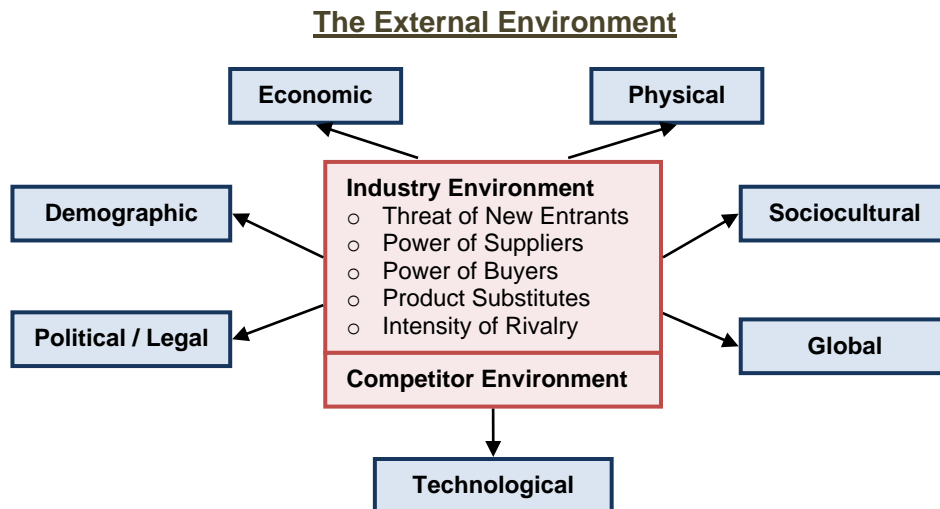
Introduction

External Environment

- A firm's external environment creates both opportunities and threats
- Opportunities and threats affect a firm's strategic actions
- Since its external environment is filled with uncertainty, the firm must be aware of and fully understand the different segments of the external environment to successfully deal with this uncertainty and to achieve strategic competitiveness and thrive

New Information

- Firms understand the external environment by acquiring information about competitors, customers, and other stakeholders to build their own base of knowledge and capabilities
- On the basis of the new information, firms take actions, such as building new capabilities and core competencies, in hopes of buffering themselves from any negative environmental effects and to pursue opportunities as the basis for better serving their stakeholders' needs
- A firm's strategic actions are influenced by the conditions in the three parts (the general, industry, and competitor) of its external environment



The General, Industry, and Competitor Environments

The General Environment

- The general environment is composed of dimensions in the broader society that influence an industry and the firms within it
- Firms cannot directly control the general environment's segments, but the segments are influencing the actions the firms are taking
- Because firms cannot directly control the segments of their external environment, successful ones learn how to gather the information needed to understand all segments and their implications for selecting and implementing the firm's strategies

Seven Environmental Segments in the General Environment

1. Demographic
2. Economic
3. Political / Legal
4. Sociocultural
5. Technological
6. Global
7. Physical Environment

The Industry Environment

- The industry environment is the set of factors that directly influences a firm and its competitive actions and responses
- The challenge for a firm is to locate a position within an industry where it can favorably influence the five factors or where it can successfully defend against their influence
- The greater a firm's capacity to favorably influence its industry environment, the greater the likelihood that the firm will earn above-average returns

Five Factors Determine an Industry's Profit Potential

1. The threat of new entrants
2. The power of suppliers
3. The power of buyers
4. The threat of product substitutes
5. The intensity of rivalry among competitors

The Competitor Environment

- Understanding the firm's competitor environment complements the insights provided by studying the general and industry environments
 - o Analyze the general environment → Focus on environmental trends
 - o Analyze the industry environment → Focus on the factors and conditions influencing an industry's profitability potential
 - o Analyze the competitors → Focus on predicting competitors' actions, responses, and intentions
- In combination, the results of these three analyses influence the firm's vision, mission, and strategic actions

External Environmental Analysis

External Environmental Analysis

- To cope with often ambiguous and incomplete environmental data and to increase understanding of the general environment, firms engage in external environmental analysis

Four Parts of External Environmental Analysis

Component	Description
Scanning	<ul style="list-style-type: none"> o It identifies early signals of environmental changes and trends o It often reveals ambiguous, incomplete, or unconnected data and information o Many firms use special software to help them identify events that are taking place in the environment and that are announced in public sources o The Internet provides significant opportunities for scanning
Monitoring	<ul style="list-style-type: none"> o It detects meaning through ongoing observations of environmental changes and trends o Critical to successful monitoring is the firm's ability to detect meaning in environmental events and trends o Effective monitoring requires the firm to identify important stakeholders and understand its reputation among these stakeholders as the foundation for serving their unique needs
Forecasting	<ul style="list-style-type: none"> o It develops projections of anticipated outcomes based on monitored changes and trends o Forecasting events and outcomes accurately is challenging o Forecasting demand for new technological products is difficult because technology trends are continually driving product life cycles shorter
Assessing	<ul style="list-style-type: none"> o It determines the timing and importance of environmental changes and trends for firms' strategies and their management

Opportunity and Threat

- Identifying opportunities and threats is an important objective of studying the general environment
 - o An opportunity is a condition in the general environment that, if exploited effectively, helps a company achieve strategic competitiveness
 - o A threat is a condition in the general environment that may hinder a company's efforts to achieve strategic competitiveness

Segments of the General Environment

Seven Environmental Segments in the General Environment

1. Demographic
2. Economic
3. Political / Legal
4. Sociocultural
5. Technological
6. Global
7. Physical Environment

#1: The Demographic Segment

- The demographic segment is concerned with a population's size, age structures geographic distribution, ethnic mix, and income distribution
- Demographic segments are commonly analyzed on a global basis because of their potential effects across countries' borders and because many firms compete in global markets

Component	Description
Population Size	<ul style="list-style-type: none"> ○ The world's population doubled between 1959 and 1999 and it will continue to grow in the 21st century ○ Firms seeking to find growing markets in which to sell their goods and services want to recognize the market potential that may exist for them ○ While observing the population of different nations and regions of the world, firms also want to study changes occurring within different populations to assess their strategic implications
Age Structure	<ul style="list-style-type: none"> ○ The world's population is rapidly aging ○ In North America and Europe, millions of baby boomers are approaching retirement ○ Data suggest that baby boomers are struggling to meet their retirement goals and are uncertain if they will actually be able to require as originally expected
Geographic Distribution	<ul style="list-style-type: none"> ○ Firms should consider the effects of the geographic shift in demographics ○ The trend of relocating from metropolitan to nonmetropolitan areas continues in the U.S. ○ These trends are changing local and state governments' tax bases ○ Business firms' decisions regarding location are influenced by the degree of support that different taxing agencies offer as well as the rates at which these agencies tax businesses
Ethnic Mix	<ul style="list-style-type: none"> ○ The ethnic mix of countries' populations continues to change (e.g. Hispanics are now the largest ethnic minority (16%) in the U.S. ○ Changes in the ethnic mix also affect a workforce's composition (e.g. the population and labor force will continue to diversify)
Income Distribution	<ul style="list-style-type: none"> ○ Understanding how income is distributed within and across populations informs firms of different groups' purchasing power and discretionary income ○ Studies of income distributions suggest that although living standards have improved over time, variations exist within and between nations

#2: The Economic Segment

- The economic environment refers to the nature and direction of the economy in which a firm competes or may compete
- Firms seek to compete in relatively stable economies with strong growth potential
- Firms must scan, monitor, forecast, and assess the health of their host nation and the health of the economies outside their host nation

#3: The Political/Legal Segment

- The political / legal segment is the arena in which organizations and interest groups compete for attention, resources, and a voice in overseeing the body of laws and regulations guiding interactions among nations as well as between firms and various local governmental agencies
 - This segment represents how organizations try to influence governments and how they try to understand the influences of those governments on their strategic actions
- Firms must carefully analyze a new political administration's business-related policies and philosophies
 - Antitrust laws, taxation laws, industries chosen for deregulation, labor training laws, and the degree of commitment to educational institutions are areas in which an administration's policies can affect the operations and profitability of industries and individual firms across the globe
 - To deal with those issues, firms should develop a political strategy to influence governmental policies that might affect them

#4: The Sociocultural Segment

- The sociocultural segment is concerned with a society's attitudes and cultural values
 - Because attitudes and values form the cornerstone of a society, they often drive demographic, economic, political/legal, and technological conditions and changes
- Societies' attitudes and cultural values appear to be undergoing possible changes
 - Examples include healthcare, labor force (more working women), contingency workers (part-time, temporary, and contract employees)
- Each country and culture has unique values and trends
 - National cultural values affect behavior in organizations and thus also influence organizational outcomes
 - Likewise, the national culture influences to a large extent the internationalization strategy that firms pursue relative to one's home country

#5: The Technological Segment

- The technological segment includes the institutions and activities involved in creating new knowledge and translating that knowledge into new outputs, products processes, and materials
- Given the rapid pace of technological change and risk of disruption, it is vital for firms to thoroughly study the technological segment
- The importance of these efforts is suggested by the finding that early adopters of new technology often achieve higher market shares and earn higher
- Both large and small firms should continuously scan the external environment to identify potential substitutes for technologies that are in current use, as well as to identify newly emerging technologies from which their firm could derive competitive advantage

#6: The Global Segment

- The global segment includes relevant new global markets, existing markets that are changing, important international political events, and critical cultural and institutional characteristics of global markets
- When studying the global segment, firms should recognize that globalization of business markets may create opportunities to enter new markets as well as threats that new competitors from other economies may also enter their market
- Because of the threats and risks, some firms choose to take a more cautious approach to competing in international markets

Two Ways to Limit Risks in International Market

Way	Description
Global-focusing	<ul style="list-style-type: none"> o Global-focusing often is used by firms with moderate levels of international operations who increase their internationalization by focusing on global niche markets o In this way, they within build on and use their special competencies and resources while limiting their risks within the niche market
One-region-focusing	<ul style="list-style-type: none"> o Another way in which firms limit their risks in international market is to focus their operations and sales in one region of the world o In this way, they can build stronger relationships in and knowledge of their markets

#7: The Physical Environment Segment

- The physical environment segment refers to potential and actual changes in the physical environment and business practices that are intended to positively respond to and deal with those changes
- Concerned with trends oriented to sustaining the world's physical environment, firms recognize that ecological, social, and economic systems interactively influence what happens in this particular segment
- There are many parts or attributes of the physical environment that firms should consider (e.g. global warming, energy consumption, etc)
- Because of increasing concern about sustaining the quality of the physical environment, a number of companies are developing environmentally friendly policies

Industry Environment AnalysisIndustry

- An industry is a group of firms producing products that are close substitutes
- An industry's profit potential is a function of five forces of competition:
 1. The threats posed by new entrants
 2. The power of suppliers
 3. The power of buyers
 4. Product substitutes
 5. The intensity of rivalry among competitors

#1: The Threats Posed By New Entrants

- Identifying new entrants is important because they can threaten the market share of existing competitors
 - o One reason new entrants pose such a threat is that they bring additional production capacity
 - o Unless the demand for a good or service is increasing, additional capacity holds consumers' costs down, resulting in less revenue and lower returns for competing firms

Two Factors Affect the Likelihood that Firms Will Enter an Industry

Factor	Description
Barriers to Entry	<ul style="list-style-type: none"> Entry Barriers make it difficult for new firms to enter an industry and often place them at a competitive disadvantage even when they are able to enter High entry barriers tend to increase the returns for existing firms and discourage potential competitors from deciding to enter the industry
The Retaliation Expected from Current Industry Participants	<ul style="list-style-type: none"> An expectation of swift and vigorous competitive responses reduces the likelihood of entry Vigorous retaliation can be expected when the existing firm has a major stake in the industry Locating market niches not being served by incumbents allows the new entrant to avoid entry barriers

Different Kinds of Entry Barriers

	Description
1. Economies of scale	<ul style="list-style-type: none"> Economies of scale are derived from incremental efficiency improvements through experience as a firm grows larger Therefore, the cost of producing each unit declines as the quantity of a product produced during a given period increases Increasing economies of scale enhances a firm's flexibility New entrants face a dilemma when confronting current competitors' scale economies Small-scale entry places them at a cost disadvantage Some competitive conditions reduce the ability of economies of scale to create an entry barrier (e.g. provide customized products)
2. Product differentiation	<ul style="list-style-type: none"> Over time, Customers may come to believe that a firm's product is unique and this will increase the customers' loyalty This belief can result from the firm's service to the customer, effective advertising campaigns or being the first to market a good or service Customers valuing a product's uniqueness tend to become loyal to both the product and the company producing it In turn, customer loyalty is an entry barrier for firms thinking of entering an industry and competing against the existing firms
3. Capital requirements	<ul style="list-style-type: none"> Competing in a new industry requires a firm to have resources to invest In addition to physical facilities, capital is needed for inventories, marketing activities, and other critical business functions Even when a new industry is attractive, the capital required for successful market entry may not be available to pursue the market opportunity
4. Switching costs	<ul style="list-style-type: none"> Switching costs are the one-time costs customers incur when they buy from a different supplier The costs of buying new ancillary equipment and of retraining employees, and even the psychic costs of ending a relationship, may be incurred in switching to a new supplier A decision made by manufacturers to produce a new, innovative product creates high switching costs for the final consumer Customer loyalty programs are intended to increase the customer's switching costs If switching costs are high, a new entrant must offer either a substantially lower price or a much better product to attract buyers The more established the relationships between parties, the greater the switching costs
5. Access to distribution channels	<ul style="list-style-type: none"> Over time, industry participants develop effective means of distributing products Once a relationship with its distributors has been built, a firm will nurture it, thus creating switching costs for the distributors Access to distribution channels can be a strong entry barrier for new entrants
6. Cost disadvantages independent of scale	<ul style="list-style-type: none"> Established competitors have cost advantages that new entrants cannot duplicate Proprietary product technology, favorable access to raw materials, desirable locations, and government subsidies are examples
7. Government policy	<ul style="list-style-type: none"> Through licensing and permit requirements governments can also control entry into an industry Also, governments often restrict entry into some industries because of the need to provide quality service or the need to protect jobs Alternatively, deregulation of industries allows more firms to enter

#2: Bargaining Power of Suppliers

- Increasing prices and reducing the quality of their products are potential means suppliers use to exert power over firms competing within an industry
- If a firm is unable to recover cost increases by its suppliers through its own pricing structure, its profitability is reduced by its suppliers' actions

A Supplier Group is Powerful When:

1. It is dominated by a few large companies and is more concentrated than the industry to which it sells
2. Satisfactory substitute products are not available to industry firms
3. Industry firms are not a significant customer for the supplier group
4. Suppliers' goods are critical to buyers' marketplace success
5. The effectiveness of suppliers' products has created high switching costs for industry firms
6. It poses a credible threat to integrate forward into the buyers' industry (credibility is enhanced when suppliers have substantial resources and provide a highly differentiated product)

#3: Bargaining Power of Buyers

- Buyers (customers of an industry or a firm) want to buy products at the lowest possible price
- To reduce their costs, buyers bargain for higher quality greater levels of service, and lower prices
- These outcomes are achieved by encouraging competitive battles among the industry's firms

Customers (Buyer Groups) are Powerful When:

1. They purchase a large portion of an industry's total output.
2. The sales of the product being purchased account for a significant portion of the seller's annual revenues
3. They could switch to another product at little, if any, cost
4. The industry's products are undifferentiated or standardized, and the buyers pose a credible threat if they were to integrate backward into the sellers' industry

#4: Threat of Substitute Products

- Substitute products are goods or services from outside a given industry that perform similar or the same functions as a product that the industry produces
- Product substitutes present a strong threat to a firm when customers face few switching costs and when the substitute product's price is lower or its quality and performance capabilities are equal to or greater than those of the competing product
- Differentiating a product along dimensions that customers value (such as quality, service after the sale, and location) reduces a substitute's attractiveness

#5: Intensity of Rivalry among Competitors

- Competitive rivalry intensifies when a firm is challenged by a competitor's actions or when a company recognizes an opportunity to improve its market position
- Common dimensions on which rivalry is based include price, service after the sale, and innovation

Factors that Affect the Intensity of Firms' Rivalries

1. Numerous or equally balanced competitors
2. Slow industry growth
3. High fixed costs or high storage costs
4. Lack of differentiation or low switching costs
5. High strategic stakes
6. High exit barriers

#1: Numerous or equally balanced competitors

- With multiple competitors, it is common for a few firms to believe they can act without eliciting a response, but most of the times, other firms are aware of competitors' actions, often choosing to respond to them
- The large and similar-sized resource bases of these firms permit vigorous actions and responses

#2: Slow Industry Growth

- Growing markets reduce the pressure to take customers from competitors
- However, rivalry in no-growth or slow-growth markets becomes more intense as firms battle to increase their market shares by attracting competitors' customers

#3: High Fixed Costs or High Storage Cost

- When fixed costs are high, firms maximize the use of their productive capacity to spread costs across a larger volume of output
- This will create excess capacity if many firms do the same at the same time
- To reduce inventories, firms will cut their prices, offer rebates, and other special discounts to customers
- This will intensify competition

#4: Lack of Differentiation or Low Switching Costs

- When buyers find a differentiated product that satisfies their needs, they frequently purchase the product loyally over time
- Industries with many companies that have successfully differentiated their products have less rivalry, resulting in lower competition for individual firms
- However, when buyers view products as commodities (i.e., as products with few differentiated features or capabilities), rivalry intensifies

#5: High Strategic Stakes

- Competitive rivalry is likely to be high when it is important for several of the competitors to perform well in the market
- High strategic stakes can also exist in terms of geographic locations

#6: High Exit Barriers

- Sometimes companies continue competing in an industry even though the returns on their invested capital are low or negative
- Firms making this choice likely face high exit barriers, which include economic, strategic, and emotional factors causing them to remain in an industry when the profitability of doing so is questionable

Common Exit Barriers

Barrier	Example
Specialized assets	o Assets with values linked to a particular business or location
Fixed costs of exit	o Labor agreements
Strategic interrelationships	o Relationships of mutual dependence, such as those between one business and other parts of a company's operations, including shared facilities and access to financial markets
Emotional barriers	o Aversion to economically justified business decisions because of fear for one's own career, loyalty to employees, and so forth
Government and social restrictions	o Often based on government concerns for job losses and regional economic effects; more common outside the United States

Interpreting Industry Analyses**Interpreting Industry Analyses**

- Firms can use industry or international data to conduct industry analyses to better understand the market
- Analysis of the five forces in the industry allows the firm to determine the industry's attractiveness
- An attractive industry has high entry barriers, suppliers and buyers with little bargaining power, few competitive threats from product substitutes, and relatively moderate rivalry

Strategic Groups**Strategic Groups**

- A set of firms that emphasize similar strategic dimensions and use a similar strategy is called a strategic group
 - o Intra-strategic group competition (the competition between firms within a strategic group) is more intense than is inter-strategic group competition (the competition between a member of a strategic group and companies outside that strategic group)
- High mobility barriers, high rivalry, and low resources among the firms within an industry limit the formation of strategic groups
 - o After strategic groups are formed, their membership remains relatively stable over time
- Using strategic groups to understand an industry's competitive structure requires the firm to plot companies' competitive actions and competitive responses along strategic dimensions such as pricing decisions, product quality, distribution channels and so forth
 - o This type of analysis shows the firms how certain companies are competing similarly in terms of how they use similar strategic dimensions

Strategic Groups Have Several Implications

1. Because firms within a group offer similar products to the same customers, the competitive rivalry among them can be intense (higher intensity leads to lower profitability)
2. The strengths of the five Industry forces differ across strategic groups
3. The closer the strategic groups are in terms of their strategies, the greater is the likelihood of rivalry between the groups

Competitor AnalysisCompetitor Analysis

- Competitor analysis focuses on each company against which a firm directly competes
- In a competitor analysis, the firm seeks to understand the following:
 1. Its future objectives
 2. Its current strategy
 3. Its assumptions
 4. Its strengths and weaknesses
- Information about these four dimensions helps the firm prepare an anticipated response profile for each competitor
- The results of an effective competitor analysis help a firm understand, interpret and predict its competitors' actions and responses

Competitor Intelligence

- Critical to an effective competitor analysis is gathering data and information that can help the firm understand its competitors' intentions and the strategic implications resulting from them
- Useful data and information combine to form competitor intelligence, the set of data and information the firm gathers to better understand and anticipate competitors' objectives, strategies, assumptions, and capabilities

Complementors

- When gathering competitive intelligence, firms must also pay attention to the complementors of its products and strategy
- Complementors are companies or network of companies that sell complementary goods or services that are compatible with the local firm's good or service
- When a complementors' good or service adds value to the sale of the local firm's good or service, it is likely to create value for the local firm

Ethical ConsiderationsEthical Considerations

- Firms must follow relevant laws and regulations as well as carefully articulated ethical guidelines when gathering competitor intelligence
- Practices considered both legal and ethical include (1) obtaining publicly available information and (2) attending trade fairs and shows to obtain competitors' brochures, view their exhibits, and listen to discussions about their products
- In contrast, certain practices are widely viewed as unethical and often are illegal
- An appropriate guideline for competitor intelligence practices is to respect the principles of common morality and the right of competitors not to reveal certain information about their products, operations, and strategic intentions

SOA SDM Past Exam Question Related To This Reading

SOA SDM Spring 2019 Q3a	(Must Read)
SOA SDM Spring 2018 Q6	(Must Read)
SOA SDM Fall 2016 Q5c-e	(Must Read)
SOA SDM Fall 2016 Q6a-d	(Must Read)
SOA SDM Spring 2016 Q2	(Must Read)
SOA SDM Fall 2014 Q7d-e	(Must Read)
SOA SDM Spring 2014 Q7	(Must Read)
SOA SDM Fall 2013 Q6	(Must Read)

PAK Study Manual (Practice Questions)
for SDM Spring 2021
(Sample)

Note

1. 500+ Practice Questions/Solutions are included in the PAK Study Manual.

Textbook Reading: Accounting for Decision Making and Control Ch. 11
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Data for Q1-Q8

ABC Factory produces 3 models of a product: Base, Standard, and Premium:

	Base	Standard	Premium
Unit volume	80,000	70,000	60,000
Selling price	\$120	\$140	\$160
Raw materials	\$3,000,000	\$2,900,000	\$2,800,000
Unit volume	80,000	70,000	60,000
Direct labor hours per unit	3	4	5
Direct labor cost	\$10	\$10	\$10

Overheads

Depreciation	\$3,000,000
Indirect labor	150,000
Scrap	2,400,000
Other	450,000
Total	<u>\$6,000,000</u>

Q1: Calculate the direct labor cost for each product.

Q2: Calculate the overhead cost for each product using direct labor cost.

Q3: Calculate the profit per unit for each product.

Q4: Which line of product is the most profitable?

You are given the following data:

	Base	Standard	Premium
Total scrap	\$1,000,000	\$800,000	\$600,000

Q5: Calculate the scrap cost for each product.

Since the scrap costs for Base and Standard products are much higher than the scrap cost for Premium, you suggest that ABC Factory should directly charge the scrap costs to the profits.

Q6: Re-calculate the overhead cost for each product.

Q7: Calculate the unit cost and the profit per unit for each product.

Q8: Which line of product is the most profitable?

Q9-Others are not shown in this sample.