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INDEX

1 MANAGING COST STRATEGICALLY

'Anything which can be measure, can also be controlled and managed'. Therefore, earlier cost control and now cost management are applied realities for optimisation as an extension of cost accounting.

Cost accounting deals with only the ascertaining and recording of costs, not the control or management thereof; it is management accounting that empowers the management of organisations with an information & support system to make efforts and attempts to control and manage the costs.

Cost management focused only on cutting or reducing cost, whereas the focus is now widening and aiming for either reducing cost while maintaining the same quality level (value) or increasing value at the same or reduced cost level. In a contemporary set-up, Cost Management is much more than just cost reduction; it has gained strategic importance in aligning the cost to business strategies.

Evolution of Cost Concepts Over Time Horizon

Cost Ascertainemnt - Recoding of Cost	»	Cost Control - Containment of Cost	»	Traditional Cost Management - Cost Reduction	»	Strategic Cost Management - Alligning costs to strategies

When techniques of cost management are practiced as strategic driver in context of organisational objectives and vision, this is termed as Strategic Cost Management. In other words, strategic cost management deals with measuring and managing costs and aligning them to the business strategy.

2 Traditional Cost Management & Its Limitation

- Traditional Cost Management aims at cost reduction.
- It revolved around the central theme 'that cost cutting always results in enhanced profits'

It ignores competition, market growth, and customer requirements, because it is largely concerned with the quantitative factors inside the organisation	It places excessive focus on cost reduction. It ignores the strategic importance of individual cases. Broad cost reduction leads to inferior quality.	It ignores the dynamics of marketing and economics because it relies on financial accounting data that is static and historical in nature.
It has a limited focus on review and investigation, only of those variances & deviations that are quantitative in nature.	It is a reactive approach. It can be seen as a corrective function rather than a preventive one.	It has a short-term outlook and may focus on the upcoming year, quarter, or even month.

The above specified limitations of traditional cost management, in themselves emphasise o the need for Strategic Cost Management. The need for strategic cost management als observed due to-

The requirement for detailed cost analysis is essential to gain an in-depth understanding of cost structure.	Strategic use of cost data to gain and sustain a competitive advantage.	To assimilate cost management into strategy and vice versa.	To comprehend the big picture (a canvas that can showcase the business model), to have a holistic analysis of cost relations among the different activities and empower the management in managing those relations.

Let's consolidate the above answer by considering the following illustrations -

- Reducing cost by not performing preventive maintenance as and when it becomes due as per the maintenance schedule may lead to major breakdown and therefore results in high corrective maintenance cost and lower profitability.
- In order to reduce cost, if any automobile business decides to close some of the service stations, it may end up losing customers due to poor after-sale services, which in turn leads to a reduction in the top line (i.e., revenue) as well as the bottom line (i.e., profit).

According to industry leaders, service (after-sale services) is key in the automotive industry and effectively makes a difference in the car buying decision too. Therefore, most automobile companies in India are striving for expanding their dealers' network which helps them showcase their presence in the market and act as positive decision stimuli for buyers of the class.

3 Strategic Cost Management (SCM)

Strategic cost management is the implementation of cost management techniques to sustain & improve the organisation's strategic position as well as reduce costs. It also deals with the collection, processing, analysis and dissemination of cost data with a view to feed information to the system for decision-making to support the organizational strategy as a whole.

Hence, Strategic Cost Management is the use of cost information in developing & deploying the strategy to practice superior performance that leads to sustainable competitive advantage.

Strategic Cost Management can be applied in service and manufacturing settings, as well as in not- for-profit environments. Strategic Cost Management deals with the assimilation of both quantitative and qualitative information in decision making.

Strategic Cost Management is the application of cost management techniques so that they simultaneously improve the strategic position of a firm and reduce costs.

3.1 Underneath Pillars of Strategic Cost Management

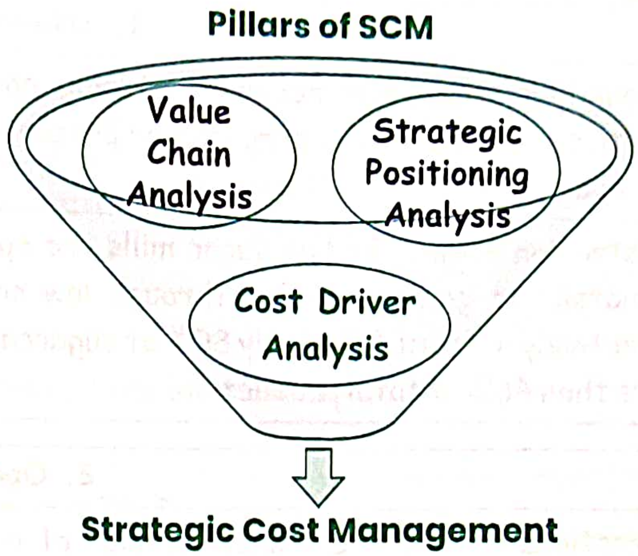
Strategic cost management has three important pillars:

1) Strategic positioning,

2) Cost driver analysis,

3) Value chain analysis.

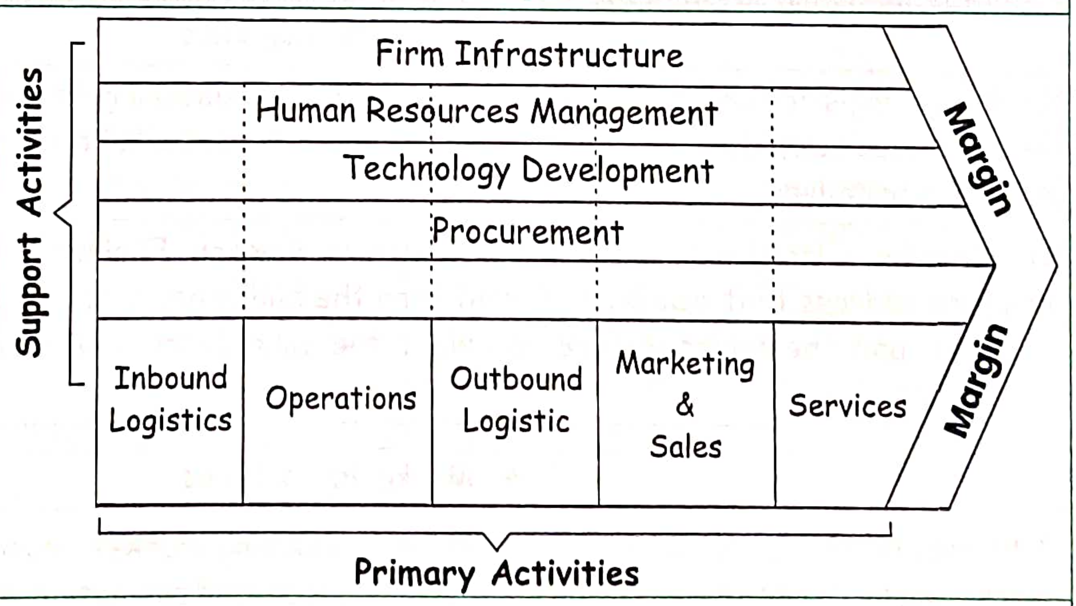
'Understanding the value chain will help in defining the optimal strategic position (positioning strategy), and eventually both will help in identifying relevant cost drivers'.



Strategic Cost Management is the managerial use of cost information explicitly directed at one or more of the four stages (strategy formulation, communicating the strategy, implementing the strategy, and controlling) of strategic management. Overall recognition of the cost relationships among the activities in the value chain and the process of managing those cost relationships to attain the firm's strategic objectives are the main focal points of Strategic Cost Management.

4 Value Chain Analysis

Michael E. Porter, the Value Chain is the sequential chain of activities that leads to the delivery of the final product to the customer; it also depicts how value (utility) accumulates for the customer.



The Value chain comprises the activities in two sets, the first being **primary activities** (vertical), which are directly involved in the transformation of a product or provisioning of a service, whereas the second set is **support activities** (horizontal), which ensure support to perform primary activities. Margin is the excess of the value that a customer is willing to pay over the cost incurred by the firm for the product.

4.1 Primary Activities comprising of

1. Inbound logistics

Inbound logistics Cover receiving, storing, and handling raw material inputs. Mind it, inbound logistics don't cover the purchase or procurement. Inbound logistics are deeply impacted by the location of business operations.

Illustration – Most Indian sugar mills are operating in the states of UP, Maharasthra, and Karnataka to generate value through low cost on inbound logistics because these states collectively account for nearly 80% of sugarcane production in India, UP leading the chart with more than 46% of total production.

2. Operations

Operations include the transformation of raw materials into finished goods and services; operations must be seen in depth; it may or may not be possible for an organisation to be master of all the activities that are required to render the service or to convert raw material into finished goods; the organisation may take the decision to outsource those activities which are not its core competences.

Illustration – Apple only designs and sells the iPhone; it doesn't manufacture its components. Outsourcing manufacturing to locations with lower resource costs is the main source of value for Apple operations.

3. Outbound Logistics

Outbound logistics covers storing, distributing, and delivering finished goods to customers. This includes how, when, and where for customer reference. Where to deliver, how to deliver, and when to deliver.

Illustration – Many e-retail platforms, such as Amazon, Flipkart, etc., offer delivery at a shipping address that may be different than the billing address; they also offer contactless delivery, and the buyer is free to select the time frame within which delivery shall be attempted.

4. Marketing & Sales

I.Marketing and sales activities comprise conducting market research to determine the marketing mix8 that comprises product, price, place, and promotion. McCarthy's concept was further developed by Booms and Bitner9 into the 7Ps of the marketing mix by adding three more Ps, i.e. People, Process, and Physical evidence (sometime referred to positioning). The newly added 3Ps have a relatively grater bearing on the provisioning and supply of services than goods. The marketing and selling activities broadly comprise the aspects pertaining to these 7Ps.

It is worth noting that if we keep the customer at the focal point then 4Ps can be replaced by the 4Cs, which are consumer wants and needs (for products); Cost to satisfy (for price); convenience to buy (for place); and communication (for people).

Marketing and sales effort are truly of significant importance to let the customer, perceive value of the product. Brands often use taglines that create impact. A Noodles brand may choose any of the following taglines or keep changing its tagline from time to time -

- 2 mins noodles ... to focus on convenience.
- Taste Bhi Health Bhi ... to emphasis at health.
- 2-minute mein Khushiyan (Happiness in 2 minutes) ... to collaborate on fun and happiness

5. After sales service

I. After sales service includes all those activities that occur after the point of sale, such as installation, training, and repair. It is important to note that the importance of after sale services is higher in the case of durable products in comparison to products falling into the FMCG category. In the service industry after sale service depends on the nature of the service.

Illustration - Service station network, time taken to service the vehicle, and quality of service (coverage of what is asked for to check or repair and manner to do so) are key aspects for creating value for its customers in the automobile industry. Even service costs become part of cost ownership and shall be a deciding factor for making purchases in the automobile sector.

4.2 Support activities also referred as to secondary activities; it comprises of

1. Firm infrastructure	I. Firm infrastructure deals with how the firm is organised. It basically describes the activities pertaining to legal, general management, administrative, accounting, finance, public relations , and quality assurance in the organisation apart from who will perform these and how.
2. Technology development	I. Technology development describes how the firm uses technology. Activities such as research and development, IT management, and cybersecurity that build and maintain an organization's use of technology.
3. Human resource management	Human resource management describes how people contribute to competitive advantage. Basically, it deals with the management of human capital. Human resource functions such as hiring, training, building and maintaining an organizational culture, and maintaining positive employee relationships.
4. Procurement	Procurement signifies purchasing, but not just limited to materials. Finding new external vendors, maintaining vendor relationships, negotiating prices, and other activities related to bringing in the necessary materials and resources used to build a product or service.

Value Chain Analysis is a process of identifying Key Value Drivers (can be referred to as equivalent to CSFs) that add substantial value and contribute most towards a firm's competitive advantage by categorising the activities into value-added and non-value-added activities, with the objective of eliminating non-value-added activities to obtain cost leadership and focusing (by further resource deployment) on value-added activities to improve product differentiation.
Hence, Value Chain Analysis is a means of evaluating each of the activities in a firm's value chain to understand where opportunities for improvement lie. Conducting a value chain analysis prompts you to consider how each step adds or subtracts value from your final product or service. Value chain analysis can help you realise some form of competitive advantage, such as cost reduction (becoming cost leader) and product differentiation.

Value Chain Analysis requires a framework (strategic framework), which can collect a variety of information strategically. Three essential analyses to collect such strategic information are-

- Industry Structure Analysis - to determine industry profitability and the basis of competition.
- Core Competencies Analysis - to determine whether organisation possess the desired key success factors.
- Segmentation Analysis - to understand customers and markets.

Practical Insight
Primary activities at Apple Inc.

Inbound logistics - Apple collects its raw materials from China, America, Europe, and various Asian countries. Although it doesn't apply the Just-in-Time principle in inbound logistics, its supply chain practices are a benchmark for efficiency for global businesses. The main source of value is economies of scale due to the massive scope and scale of business operations. This helps them to be cost-effective.

Operations - Apple operations are conducted by around 150k full-time equivalent employees worldwide. Apple designs and sells; it hardly manufactures the components of the product it is selling. Outsourcing manufacturing to locations with lower resource costs is the main source of value for Apple operations. Apart from a few models of Mac that are manufactured in the USA and Ireland, the rest are outsourced to manufacturing units based in Asia, largely in China. This strategy provides advantages such as a focus on the core competencies of the business, such as research and development and designing new products. It tries to keep operations lean, but it does not apply the six sigma principles like its competitor, Samsung.

One may appreciate to note that Apple's operations are divided into the following reportable operating segments: America, Europe, Greater China, Japan, and the Rest of Asia Pacific.

Outbound logistics - For technology items such as smartphones, tablets, and laptops inventory depreciation rates are very high due to short product life cycles. The company tries to keep minimum inventory in their warehouses.
The company ships finished products to Apple Stores, that are typically located at high-traffic locations in quality shopping malls and urban shopping districts. But currently, the company is focusing on E-Commerce sales because E-Commerce is more cost-effective compared to sales via Apple Store.

One may appreciate to note - In the US, in terms of size of e-commerce business, Apple is only behind Amazon.com and Wal-Mart Stores Inc.
The massive source of value addition also lies in Apple's market penetration into Asia in general and China in particular, because selling in this particular geographical market would not involve massive outbound logistics expenses (as assembly took place in China largely), and this cost advantage can be passed on to customers to increase the overall appeal of offers.

Marketing and Sales - Apple sells its products through the following seven sales channels i.e., retail stores; online stores; direct sales force, third-party cellular network carriers, wholesalers, retailers, and value-added resellers.
Apple is consistently increasing its share of sales through direct sales channels as opposed to indirect sales channels. In 2020, the company's net sales through its direct and indirect distribution channels accounted for 34% and 66%, respectively, of the total net sales.

After sale service - Apple is famous for the exceptional quality of customer service during all three stages: pre-purchase, during the purchase, and post-purchase. Apple sales assistants are usually trained and polite young males and females who are technically savvy and happy to demonstrate product features and capabilities. Products can be returned within 14 calendar days after the purchase. Post-purchase customer service is also impressive, with unique iPhone tradein programs that allow iPhone users to upgrade their phone to newer models with additional payment.

4.3 Value Shop Model Or Service Chain Model

(Value chain analysis for service sector.)

Approach designed to solved customer problems rather than creating value by producing outp
It aims to cater to service sector companies. Best applies telecommunication company.

INFRASTRUCTURE

HUMAN RESOURCE MANAGEMENT

TECHNOLOGY DEVELOPMENT

PROCUREMENT

Primary Activities

- Problem finding and acquisition.
- Problem solving.
- Choosing among solution.
- Executive and control evaluation.

Secondary Activities

- Same as porter's value chain.
- Infrastructure
- Human Resource Management
- Technology Development
- Procurement

Value Shop Model is similar to value chain but with differences in 2 aspects.:
- Rather than focusing on creating value, value shop model focuses on solving problems.
- Primary activities are described as Problem Finding and Acquisition, Problem Solving, Choi
  Execution, Control, and Evaluation.

Value is created in the shop by several mechanisms that allow the organization to so problems better or faster than the client. These are variables such as:
- The organization is in possession of more information about the problem than the client.
- The organization is specialized to deal with the problem at hand with specific methods analysis.
- Strong expertise from expert professionals is available.

5 Strategic Position and Strategic Positioning Analysis

- Understanding the strategic position is concerned with the impact of the external environment, internal resources and competences, and the expectations and influence of stakeholders on strategy.
- Strategic Positioning Analysis is the analysis of the company's relative position within that strategic segment of industry that matters for the purpose of establishing performance targets (while attaining competitive advantage) in addition to determining the means (strategies and plans) of attaining the same and then the measurement of performance as well as the evaluation thereof. Basically, the intent seen in where the firm is positioned in context to its true peer group (which can be referred to competitor) or how it is performing in comparison to others who are operating in the same segment.
- To illustrate, Tata Motors' performance or standing shall be analysed in the context of Maruti, Toyota, Honda, and Hyundai, which offer the same products in the same price range with similar features.
- Strategic positioning reflects choices a company makes about the kind of value it will create and how that value will be created differently than rivals. Strategic positioning should translate into either one of two things: a premium price (i.e., differentiation) or a lower cost (i.e., cost leadership)

Note: Driving up prices is one way to increase profitability. To command a premium price, a company must deliver distinctive value to customers.... differentiation. Driving down costs is another way to increase profitability. To compete on cost, companies must balance price with acceptable quality...cost leadership.

6 Strategic positioning analysis includes the study of

I	II	III	IV
Culture, beliefs, & assumptions of the organisation	Stakeholders' influence and expectations	Task Environemnt in context of capability i.e., resources, core competences	Environment in context of competitors, markets, regulations, etc.
↓	↓	↓	↓
Vision and Values	Mission and Objectives	Strengths and Weaknesses	Opportunities and Threats

6.1 Culture, beliefs, and assumptions of the organisation

Culture, beliefs, and assumptions of the organisation help in appraising the vision and values. Vision is aspiration statement, while values are the guiding principle that will be observed to attain such an aspiration (vision). Culture is the beliefs, values, mindsets, and practices of a specific group of people. It includes behaviour patterns and norms.

Illustration - Google's vision statement is "to provide access to the world's information in one click". The nature of company's business is a direct manifestation of this vision statement. For instance, Google's most popular product is its search engine service. Further, as part of their value system, Google is committed to significantly improving the lives of as many people as possible.

6.2 Stakeholders' influences and expectations

Stakeholders' influences and expectations shall be considered in order to determine what the shareholders want and how much they will cooperate. So that the same can be reflected in the mission statement and objectives of the organisation. It also needs to be seen whether we are able to meet their expectations or not while appraising strategic position.

Different stakeholder groups have their own set of forces and tactics that have a strong bearing on organisations mission and objectives and, in turn, on its strategic position.

Illustration - Google's key stakeholders are its users, and they will continue using google more and more if it is convenient to use, freely accessible, and user friendly. This is reflected in Google's mission statement. Google's mission is to organize the world's information and make it universally accessible and useful14. That's why search makes it easy to discover a broad range of information from a wide variety of sources.

6.3 Strategic capabilities in terms of resources and core competences

Strategic capabilities in terms of resources and core competences shall be analysed in the context of the task environment (which may be referred to as the microenvironment) in which organisation is operating to assess the strengths and weaknesses to appraise the strategic position.

Strengths shall be used aggressively to exploit opportunities to capture competitive advantage, whereas weaknesses need to be analysed at the root-cause level, and those causes shall either be removed or reduced (if they can't be reduced).

6.4 Macro Environment

The macro environment (beyond the control of organisation), especially the basis of competition, industry profitability, industry key success factors, customers' behaviour, markets and regulations, etc., shall be analysed to assess Opportunities and Threats to appraise the strategic position.

Opportunities need to be exploited, whereas a defence mechanism shall be created against threats that can be mitigated. Risk management is of key importance to protect the organisation from threats to sustain its strategic position and make the most of opportunities. This will improve its strategic position, apart from ensuring it realizes the benefits of competitive advantages.

EXAMPLE

Do we need to consider all the stakeholders or only those who are significant enough? If only those limited chunk of stakeholders exist, then how do we identify them?

Solution

Mendelow's Matrix helps in considering the attitude of stakeholders while setting out strategic objectives. Mendelow's Matrix consists of four boxes representing stakeholders with:

High Interest and High Power

These will be considered key stakeholders, and a business will need to actively engage this group. This group is likely to have a significant influence; they may be the driver behind the change or strategy. They will likely have the power to stop the change or strategy from going ahead if they are unhappy.

This is the group that requires most focus. Keep them both updated on any strategic changes and empowered to steer the direction of change (or at least feel that they have the opportunity to input into the direction of the project).

High Interest and Low Power

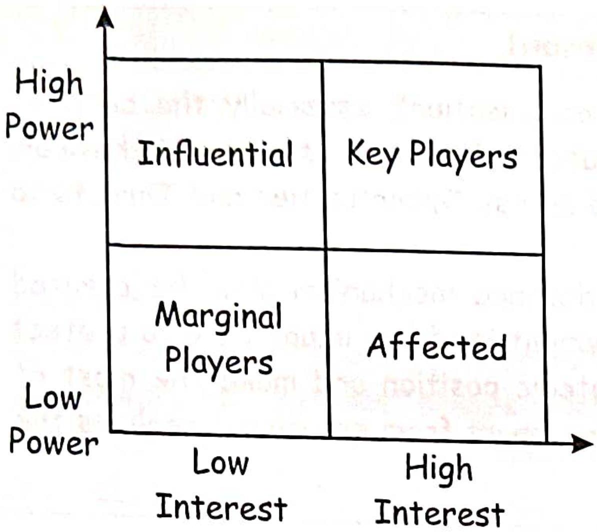
This group has an interest in what is happening; however, they are unlikely to have the power to influence change. This group should be kept informed. While, they have little power themselves, they could attempt to join forces with a group with power.

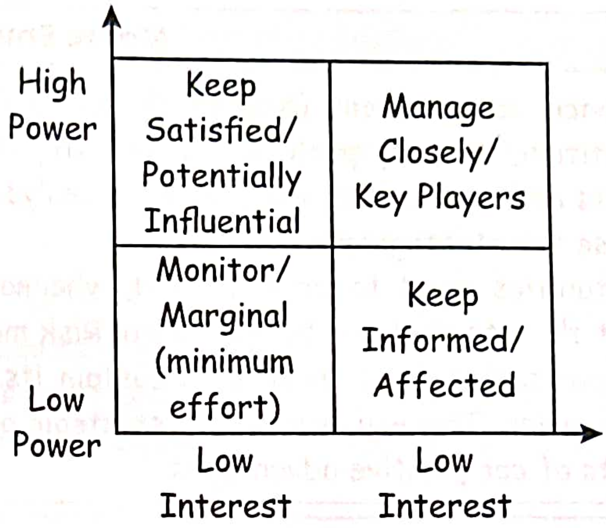
Low Interest and High Power

This group of stakeholders has the potential to move into the 'High Interest and High Power' group, so it is essential that they are kept satisfied. By keeping them satisfied, they are less likely to gain interest and exercise their power of influence.

Low Interest and Low Power

This group is unlikely to have an interest in the organization and its strategic direction. This is often due to their lack of power to influence a situation. They are likely to accept the position and show little, if any, resistance.





6.6 What tools are handy for conducting strategic position analysis?

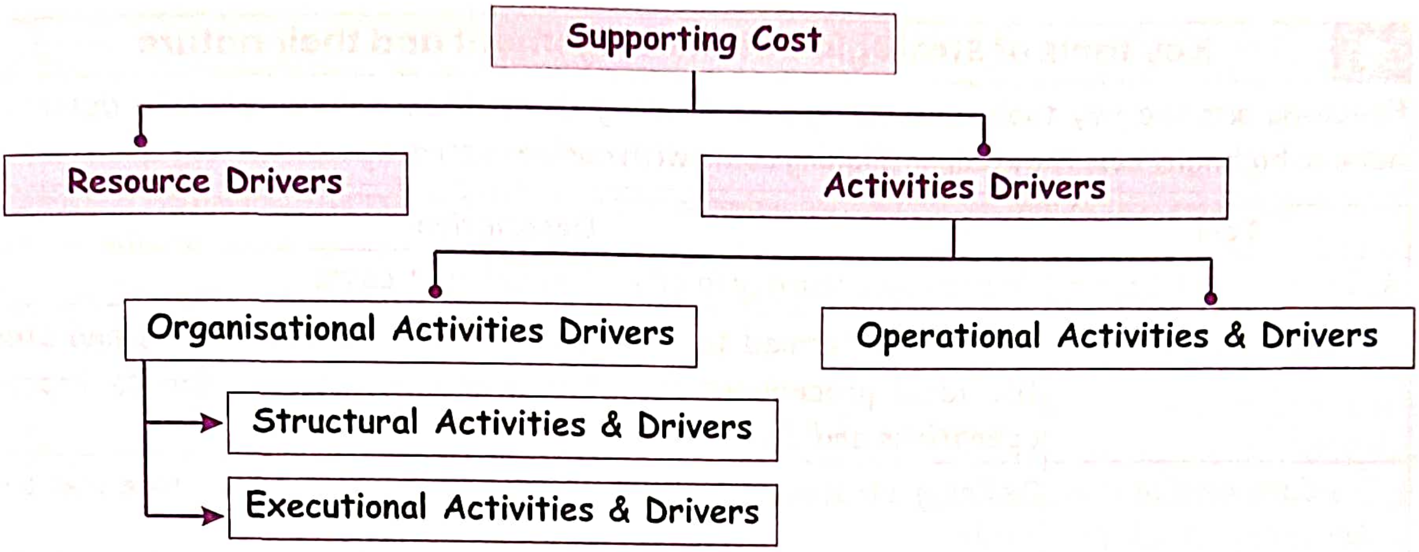
SWOT analysis is the focal tool for Strategic Position Analysis supported by PESTEL Analysis (specifically relied on for the analysis of remote environmental factors), Porter's Five Forces (for industry analysis), Porter's Diamond Studies, etc. for external environment analysis. Porter's Value Chain, Critical Success Factors and Core Competencies, Product Lifecycle, McKinsey 7S, etc. for internal environment analysis.

7 Cost Driver Analysis

Cost driver is the unit of that activity that causes costs to be incurred. Hence, cost driver is trigger of change in cost, meaning thereby more frequency/ runs of cost driver led to more cost. Cost Driver Analysis includes the examination, quantification, and explanation of the monetary effects of cost drivers associated with an activity.
It is an in-depth review of the cost drivers to make sure that your firm correctly allocates the supporting production and service costs to all goods and services. There are different cost driver analysis methods, including a cost accounting system review, industry analysis, and internal activity analysis.

In traditional costing, the cost driver used to allocate overhead costs (supporting cost) to cost objects only relates to the quantity/ volume of output. But under Strategic Cost Management cost driver for short-term overhead costs (that occur once in a while) may be the volume of output or activity. But
for long-term overhead costs, a variety of cost drivers are used.

Based upon the nature of supporting cost (overhead cost), appropriate drivers can be identified and categorised into the following classes-



Structural Cost Drivers	**Structural cost drivers** relate to business strategic choices about an organization's underlying economic structure, such as scale and scope of operations, use of technology, and complexity of products (it is not necessary that more is better).

Executional cost drivers	**Executional cost drivers** relate to the execution of the business activities, such as the utilization of employees in terms of involvement, the provision of quality service, product design and manufacturing, and links with suppliers and clients (higher is the better).

8 Key tools of Strategic Cost Management and their nature

Following are the key tools of strategic cost management; their nature is briefly described here to highlight how they help in aligning costs with business strategies -

Tool	Description
Activity Based Costing	To provide accuracy in allocating indirect costs.
Benchmarking	Process performed to determine critical success factors and study the ideal procedures of other organizations in order to improve operations and dominate the market.
Competitive Advantage Analysis	Defining strategies that an organization could adopt to excel over rivals.
Just-in-Time	A comprehensive system to buy materials (JIT Purchase) or produce commodities (JIT Production) when needed at the appropriate time.
Kaizen - Continuous Improvement	Conducting continuous improvements in quality & other critical success factors.
Target Costing	Cost that an organization is willing to incur according to a competitive price that could be used to achieve the desired profit.
Theory of Constraints	A tool to improve the rate of transferring material into finished goods.
Total Quality Management	Adapt the necessary policies and procedures to meet customers' expectations.
Value Chain Analysis	Add value to customers, reducing costs & understanding relationship between business organization and customers.

9 Traditional vs. Strategic Cost Management

Basis of Difference	Traditional Cost Management	Strategic Cost Management
Allocation of cost	Volume (per unit produced).	Allocation will be w.r.t. relevant cost driver - Activity Based Costing.
Nature	Reactive (risk averse) approach.	Proactive and dynamic approach.
Objective	Cost control and reduction.	Product differentiation (apart from cost containment).
Risk Appetite	Risk-averse approach.	Risk taking approach and ability to adapt itself to changing environment.
Scope	Internal business environment.	Both internal and external.
Term	Short term focus.	Long span or perpetual focus.

10 ORGANISATIONAL CONTEXT

Strategic Cost Management is the analysis of cost in a broader context (Organisational as well as External Environment Context), where the strategic elements become more conscious, explicit, and formal. The cost data is used to develop superior strategies in route to gaining a sustainable competitive advantage. Strategic Cost Management gives a clear understanding of the firm's cost structure in search of sustainable competitive advantage through cost reduction or differentiation.

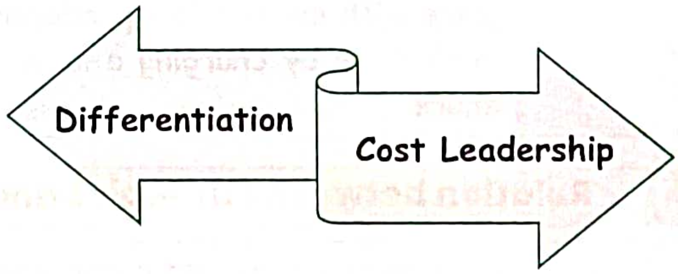
10.1 Gaining Competitive Advantage

A Competitive advantage is the ability of an organisation to outperform its competitors and make more profits than its competitors do from an equivalent set of activities through superior performance. Gaining and maintaining a competitive advantage over a period of time is challenging for organisations in the global economy with the speed of competition and information exchange possible today.

The role of the strategist (including the management accountant as a cost engineer) is to engineer superior performance within a given industry in which organisation is operating.

10.2 How can a strategist increase profitability?

The answer lies in having a competitive advantage. Companies must search out "white space" in the industry, which usually means competing on either one of two fronts-



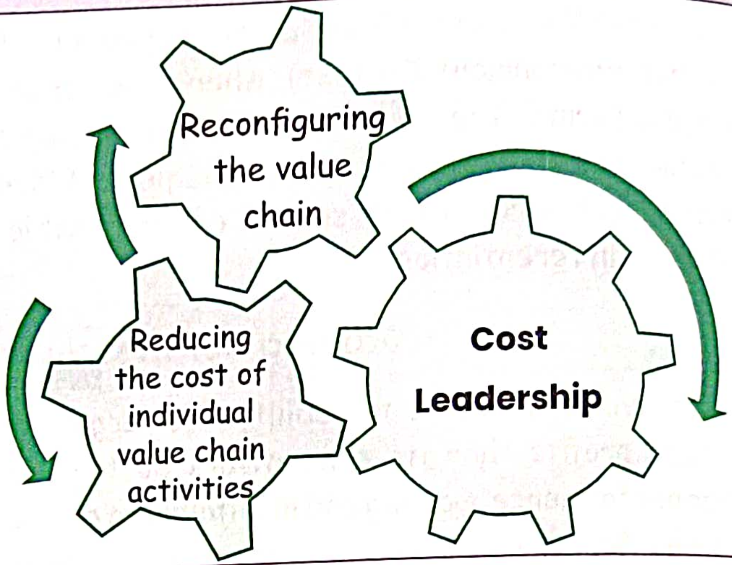
11 Differentiation

- Driving up prices is one way to increase profitability. To command a premium price, a company must deliver distinctive value to customers. A customer may perceive the high value of any product and be ready to pay a premium due to the differentiation it offers.
- E.g., Apple. Product differentiation is achieved by investing more time and resources into activities like research and development, design, or marketing that can help the organisation's product stand out.

Source	Differentiation can be sourced from quality (design, knowhow or performance), innovation, customer relations/ response (including after sale services), a wide-product range etc.
Benefits	Differentiation helps either earn a huge margin by charging the top price or build market share by charging lesser than premium price.

12 Cost Leadership

Driving down costs is another way to increase profitability. To compete on cost, firm must balance price with acceptable quality and become the lowest cost producer in an industry. A firm can create a cost advantage in two different ways, by reducing the cost of individual value chain activities and by reconfiguring the value chain as shown:



Source	Cost Leadership can be sourced from cost effective inputs, proces innovation or re- engineering, low-cost distribution channel, superio operation management, learning curve, and the economics of scale.
Benefits	By producing at the lowest possible cost, the manufacturer can compete o price with every other producer in the industry and earn the highest uni profits, or by charging a lower price than others, it can capture marke share.

12.1 Relation between strategies and cost management Emphasis

Strategic emphasis on different aspects under Product Differentiation and Cost Leadership is enumerated below –

Aspects	Strategic Emphasis	
	Product	Cost Leadership
Role of standard costs in assessing performance	Not very important	Very important
Importance of concepts such as flexible budgeting for manufacturing cost control	Moderate to low	High to very high
Perceived importance of meeting budgets	Moderate to low	High to very high
Importance of marketing cost analysis	Critical to success	Relatively less importar
Importance of product cost as an input to pricing decisions	Low	High
Importance of competitor cost analysis	Low	High

13 How to conduct a Value Chain Analysis?

There are three steps involved in conducting value chain analysis -

- Identify Value Chain Activities
- Determine the Cost and Value of Activities
- Identify Opportunities for Competitive Advantage

13.1 Identify Value Chain Activities

The first step in conducting a value chain analysis is to understand all of the primary and secondary activities that go into your product or service creation. If your company sells multiple products or services, it's important to perform this process for each one.

13.2 Determine the Cost and Value of Activities

Once the primary and secondary activities have been identified, the next step is to determine the value that each activity adds to the process, along with the costs involved.

When thinking about the value created by activities, an organisation needs to ask itself following questions -

- How does each activity increase the end user's satisfaction?
- How does it create value for the firm?

To be more specific, the organisations need to answer

- Does constructing the product out of certain materials make it more durable or luxurious for the user?
- Does including a certain feature make it more likely your firm will benefit from network effects and increased business?

Similarly, it's important to understand the costs associated with each step in the process. Depending on the situation, lowering expenses may be an easy way to improve the value each transaction provides.

14 The Value Chain Approach For Assessing Competitive Advantage

- Internal Cost Analysis
- Internal Differentiation Analysis
- Vertical Linkage Analysis

14.1 Internal Cost Analysis

Identify the firm's value creating processes	Determine the portion of the total cost of the project or service attributable to each value creating process	Identify the cost drivers for each processes.	Identify the links between processes.	Evaluate the opportunities for achieving relative cost advantage
Eg: Procurement process.	Eg: New ERP system reduce logistic cost but increase IT cost.	Eg: Ordering cost.	Eg: Mobile.	Eg: Reduce cost under all head by 15%..

14.2 Internal Differentiation Analysis

Identify the customer's value creating processes.	Evaluate differentiation strategies for enhancing customer value.	Determine the best sustainable differentiation strategies.
Eg: Apple earphones without wire.	Eg: Apple/Google Superior Features, Marketing Channels, Customer Service, Quality Product, Brand Image.	Eg: Starbucks provide variety of coffees in eco-friendly glasses.

14.3 Vertical Linkage Analysis

Creating an extendable organisation by extending the value chain across the firms of suppliers and users.

We already discussed in the previous section of this chapter that Value Chain Analysis (three steps explained above) requires a strategic framework that can collect a variety of strategic information that will be used while performing the above three steps (especially the third one). Three essential analyses to collect such strategic information are -.

- ***Industry Structure Analysis*** – to determine industry profitability and the basis of competition.
- ***Core Competencies Analysis*** – to determine whether organisation possess the desired key success factors.
- ***Segmentation Analysis*** – to understand customers and markets.