

Porter, Michael E. – Competitive Strategy*Free Press, 1980 [Business] Grade* ★★★★★

A concept that Warren Buffett has popularized in the world of investing is circle of competence. It describes what industries and businesses the investor understands well enough to be able to make an informed investment decision. It may be easy to understand the notion but its realization surely is harder than it seems. An integral part is to grasp the inner workings of an industry and the competitive situation of the specific business. A book that has stood the test of time and that will give the reader some well-needed guidance on the subject is *Competitive Strategy* by Michael E. Porter.

Porter is a Professor of Harvard University and Head of the Institute of Strategy and Competitive Strategy. He has written several pioneering books and papers and is possibly most renowned for *Competitive Strategy* and *Competitive Advantage* written five years later. He is a thought-leader and his material is widely used in academia worldwide and by practitioners as managers, consultants and investors. Porter has throughout his career worked as a consultant to help businesses improve their skills in making strategic decisions. He has studied hundreds of businesses in his research while teaching at Harvard Business School and has used much of that experience to produce his groundbreaking writings.

Competitive Strategy is divided into three parts. In the first part covering chapters one to eight, Porter presents a framework for how to analyze an industry and its competitors. His famous five forces, the key concept of the book, act as a base for the analysis. Chapters one, two, seven and eight are essential reading for both the investor and the manager as they present a foundation for how to think about competitive advantages on various levels while chapters three to six are more tilted towards managers and management consultants by giving hands-on information on how to devise strategies. The management's task is to develop strategies to strengthen the competitive advantage while the investor's job is to analyze if management is doing the right things. In other

words, management builds the competitive advantage and investors measure it. The second part of the book covers strategies for different industry structures as for example fragmented industries with many competitors and no dominating leader as well as emerging industries lacking stable rules. In the last part, again more interesting for managers and consultants, Porter presents several important strategic decisions that firms need to take and applies the ideas and lessons earlier described. Appendix 2 is also useful as it presents a hands-on way on how to conduct an analysis.

Investors, arguing that it's too difficult to use his material in practice, sometimes criticize Porter. Conducting the strategic analysis is an assignment that ranges from weeks to months depending on the investor's prior knowledge and network and it includes a lot of footwork and reading. On the other hand, investing is a full-time job and who is to say that it should be easy? Furthermore, investors who apply the five forces get criticism from Porter for being too superficial when using the model. Reading the book is tough and applying the lessons from it is even tougher which drives investors to take shortcuts. Porter also stresses that change is vital while many use the five forces in a static way. One could argue that it's understanding whether the future of the business will be better or worse than the consensus view has it, that is the key question for investors as the rest should be built into the current share price.

My recommendation to the reader is to compile a couple of case studies of businesses while reading the book as this will lead to a better understanding of the framework. Before I read the book, I had heard that it was challenging - which was confirmed. I had also heard that it would be worth the effort, which I agree on as well. Fully grasping the ideas will potentially make the investor recognize the challenges of a business before the information is public which will lead to an important analytical edge.

Niklas Sävås, October 13, 2018