Conducting your SWOT Analysis

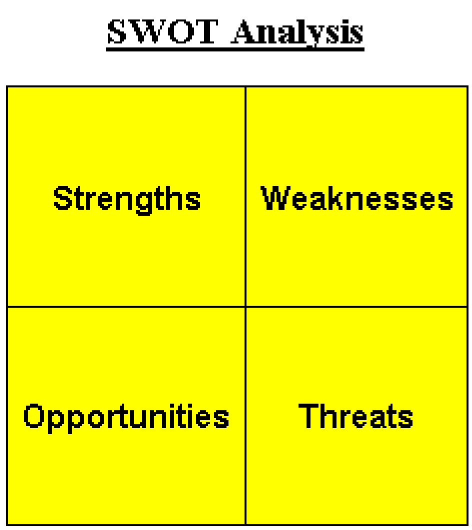
***SWOT Analysis*[1]**

What is a 'SWOT Analysis'

SWOT analysis is a process that identifies an organization's strengths, weaknesses, opportunities and threats. Specifically, SWOT is a basic, analytical framework that assesses what an entity (usually a business, though it can be used for a place, industry or product) can and cannot do, for factors both internal (the strengths and weaknesses) as well as external (the potential opportunities and threats). Using environmental data to evaluate the position of a company, a SWOT analysis determines what assists the firm in accomplishing its objectives, and what obstacles must be overcome or minimized to achieve desired results: where the organization is today, and where it may be positioned in the future.

For example, back in 2015, a Value Line SWOT analysis of The Coca-Cola Company noted strengths like its well-known brand name and vast distribution network and opportunities like emerging markets, but also weaknesses and threats such as foreign currency fluctuations, a growing taste for "healthy" beverages (vs. soft drinks) and the subsequent competition from providers of such beverages. Coca-Cola took steps to address these concerns, ramping up its marketing, advertising, and promotional activities, and expanding into other beverage categories. As a result, within a year its dividend-per-share rose from $.33 to $.35 and its stock, which was hovering around $39 per share, climbed to $46; it's fallen down since, but remains up nearly 8% over the past three-year period.

A Visual Overview



BREAKING DOWN 'SWOT Analysis'

[1] "SWOT Analysis." Investopedia, Investopedia, LLC, 9 Mar. 2017, www.investopedia.com/terms/s/swot.asp.

A SWOT analysis is usually presented as a square with each of the four areas making up one quadrant. This visual arrangement of the information provides a quick overview of the company's position. Although all the points under a particular heading may not be of equal importance, there are some insights to be had in seeing how the number of opportunities measures up to the number of threats, and so forth.

Elements of a SWOT Analysis

When using SWOT analysis, an organization needs to be realistic about its good and bad points. Analysis needs to be kept specific by avoiding gray areas and analyzing in relation to real-life contexts. For example, how do the organization's products and services compare to those of competing firms? SWOT analysis should be short and simple, and should avoid complexity and over-analysis, as much of the information is subjective. Thus, companies should use it as a guide and not a prescription.

- ***Strengths*** *describe what an organization excels at and separates it from the competition: things like a strong brand, loyal customer base, strong balance sheet, unique technology and so on. For example, a hedge fund may have developed a proprietary trading strategy that returns market-beating results; it must then decide how to use those results to attract new investors.*
- ***Weaknesses*** *stop an organization from performing at its optimum level. They are areas where the business needs to improve to remain competitive: things like higher-than-industry average turnover, high levels of debt, an inadequate supply chain or lack of capital.*
- ***Opportunities*** *refer to favorable external factors that an organization can use to give it a competitive advantage. For example, a car manufacturer may be able to export its cars into a new market, increasing sales and market share, if tariffs in a country are substantially reduced – the "opportunity" in this case.*
- ***Threats*** *refers to factors that have the potential to harm an organization. For example, a drought is a threat to a wheat-producing company, as it may destroy or reduce the yield of the crop. Other common threats include things like rising costs for inputs, increasing competition, tight labor supply and so on.*

Advantages of SWOT Analysis

A SWOT analysis is a great way to guide business-strategy meetings. It can be very powerful to have everyone in the room to discuss the core strengths and weaknesses of the company and then move from there to defining the opportunities and threats, and finally to brainstorming ideas. Often the SWOT analysis that you envision before the session changes throughout to reflect factors you were unaware of and would never have captured if not for the group's input.

SWOT can be used for overall business strategy sessions, but it can also be used to for a specific segment like marketing, production, or sales. This way you can see how the overall strategy developed off the SWOT analysis will filter down to the segments below before committing to it. You can also work in reverse and do segment specific SWOT analysis that feeds into an overall SWOT analysis.

Executing a SWOT Analysis

Pre-SWOT Homework

Before you set out to do a SWOT analysis with your management team or other group, there is some preparation. The first step is to take a stab at creating a company profile. This is simply a description of what the business does and who the main customers are. If time allows or your company is sprawling and complex, you may need to profile each segment to capture what they add to the business. It also helps to outline strengths, weaknesses, opportunities and threats that you've perceived so you can prompt the group if needed.

Leading the Process

When performing a SWOT analysis, it is best to start with a clean chart. Lay out the four quadrants and outline the content you are looking to populate it with as above, but let the group lead off. Again, in highly segmented business you will probably find that the leads in the separate areas have more specialized knowledge as to the strengths and weaknesses in their areas. In extreme cases, you may need to do a segment-by-segment SWOT and then feed it up into the larger one. For most companies, however, a single SWOT chart is sufficient to capture the current condition of the business.

At first, you want to capture everything you can from the group in a rush. When the pace of input trickles off, you can go over the chart and eliminate duplicate/overlapping entries and ensure each entry is in the right category. Walk the group through your reasoning if you are outright eliminating an entry or combining concepts. This is basic courtesy and it shows that their input is being valued. The group can also help in adding and removing entries within the SWOT chart to distil it down to a mutually agreed upon core.

Working with the Chart

At this point in the process, you will likely have an imbalance between internal and external factors. People are much more aware of the current state within the company and less likely to be thinking of the direction of the business sector as a whole. If needed, you can prompt more entries under opportunities by encouraging them to think about how a current strength can be leverage to create new opportunities or how fixing a weakness could lead to a larger opportunity in the future. Likewise, in what situations (threats) will your current strengths and weaknesses endanger the company?

Examples of SWOT Analysis

Let's take a practical look at SWOT analysis by applying it to two fictional companies.

Al's Ice Cream: The Case for Expansion

Al's Ice Cream is a wholly-owned ice cream shop that leverages founder Al's food science training to create hand crafted ice cream with local ingredients. Al's company is profitable with strong margins on its premium priced cones, but Al is wondering if the single store approach isn't limiting his growth. We'll take this first SWOT analysis in two steps so we can see how the exercise builds on itself.

Strengths and weaknesses are internal factors unique to the business in question. Some may be a result of external factors like a weak economy or tight labor market, but they are still company-specific. Here are the strengths and weaknesses for Al's Ice Cream:

Strengths

- *Superior product with unique flavors that are difficult to duplicate*
- *Loyal customer base supplying word of mouth marketing*
- *Strong sales and a generous profit margin*

Weaknesses

- *Limited market penetration due to a single location*
- *Time and labor intensive production process*
- *Limited capital for expansion*
- *Have trouble finding capable ice cream artisans*

Opportunities and threats are external to the company. They represent things that could happen in the right conditions. Of course, that is a awfully broad guideline, so we can use the strengths and weaknesses above to narrow in on opportunities and threats that follow naturally from them. Here are some opportunities and threats facing Al's Ice Cream:

Opportunities

- *Increase the number of stores to access more customers*
- *Focus on production and sell into retail food service*
- *Buy new equipment to lower production time and labor*
- *Start an artisanal ice cream class to train and recruit employees*
- *Partner up to access more capital, raise it from private investors, or apply for government grants*

Threats

- *Big ice cream brands are experimenting with artisanal ice cream*
- *Consumers are increasingly health-conscious*
- *Local ingredients may become more expensive as restaurants and other big buyers focus on local food*
- *Competitors have more marketing dollars*

The purpose of a SWOT analysis is to present possible routes for a company. Potential strategies can be created by combining and recombining different factors. For example, Al's could apply for government grants to install new equipment, reducing labor needs, and then raise capital to open an additional concept store staffed with graduates of the artisanal ice cream class. This an ambitious plan – and it will likely change in implementation – but it provides Al's Ice Cream with a potential path forward.

Ed's Carpets: Sell More to Your Customers

Ed's Carpets is a mature business with a warehouse and a storefront. Carpets are a low margin business that depends on value. Ed's enjoys steady business due to his installation guarantee and high quality standards, but things aren't as good as they were 20 years ago.

Here is the SWOT analysis:

Strengths

- *Established brand with loyal customers*
- *Deep knowledge of carpets and flooring*
- *Dedicated and efficient employees who take pride in their work*

Weaknesses

- *Basic web presence with no inventory images or online ordering*
- *Main focus on carpets with a small amount of linoleum*
- *A lot of capital is tied up in warehouse inventory*

Opportunities

- *Adopt a leaner model with less inventory on hand*
- *Increase the range of flooring products offered (laminate, tile, cork, etc)*
- *Increase the range of services offered (repair, maintenance, design, etc.)*
- *Use knowledge to sell carpet over the internet without installation services*

Threats

- *Move towards less carpet and more diverse types of flooring*
- *Consumers are more price conscious in the down economy*
- *Competition from online only stores that don't have the same overhead costs*
- *Better flooring materials is increasing the time span between flooring changes.*

Again, we see natural combinations within the quadrants and even between quadrants. Ed's Carpets can benefit from exploring several of the opportunities and some of those will help to address weaknesses. For example, adopting a leaner inventory model will address some of the capital concerns and wholesaling existing inventory online without installation can potentially clear the backlog. Less carpet in the warehouse then frees Ed's up to look at different flooring products for the local market.

Using SWOT Analysis to Evaluate Investments

Most commonly used as a business planning tool, SWOT analysis can also be used as an investment tool, giving you a handy snapshot of the potential advantages or disadvantages of buying stock in a company. Broadly speaking, the strengths and weaknesses should reflect "what is" about the company today, while opportunities and threats are more about what could happen to it in the future.

***Strengths** are characteristics that form the basis of above-average performance potential of shares. Not only do strengths consider what a company does well, but why or how it does it well. In the case of a mining company, for instance, a valuable mineral asset in a politically stable country may be listed as a strength, while a major consumer company may have some of its greatest strengths in the value of its brands. It is important to note that above-average revenue growth or superior margins are not in and of* *themselves strengths – it is the popularity of the products or the relative efficiency of a manufacturing process that represent the real strengths.*

Weaknesses *are vulnerabilities to the company's competitive position and/or opportunity to post positive returns on investment. An industry heavily burdened with competition, for example, would be considered a potential weakness of the firm.*

Opportunities *represent scenarios or options where the company can meaningfully improve itself. The introduction of a significant product can be an opportunity, as well as a restructuring or acquisition. Another type of opportunity presents itself from an untapped customer demographic. For example, if an independent pizza restaurant introduces a delivery service, it has the opportunity to expand its customer base beyond only those living in the neighborhood.*

Threats *should answer the question "what could change for the worse?" with a particular company. Like opportunities, threats may be prospective or even theoretical, but they should offer more specificity than "something might go wrong." Increased government regulation, a failure to secure approval/acceptance for a major new product, or the introduction of a rival product/service would all represent meaningful threats to a company's competitive standing and returns. Threats can also refer to how the company is affected by economic conditions: If it is especially sensitive to a change in interest rates, inflation, etc.*

Limits of Using SWOT for Investing

There are key limitations that investment-oriented users of SWOT analysis should understand. To start, SWOT totally ignores valuation and other significant fundamental metrics like return on capital, margins, cost of capital and so on. A SWOT analysis will not tell an investor what price is fair for a stock, or if a stock is presently undervalued.

SWOT analysis also does not tend to offer much scope or scale to the size or significance of various opportunities and threats. It stands to reason that the creator of a SWOT analysis would not bother with non-material opportunities or threats, but it is nevertheless important to try to quantify the impact of these items on a company's returns.

The largest limitation of SWOT analysis is that it is subjective and self-directed. The entire process relies solely on the analyst's knowledge and judgment, and there is an inherent potential for bias. In the case of a biotech, for instance, a bullish investor may well see an experimental therapy as a major opportunity while a bearish one will see a weakness or threat in the vast amounts of money that are to spent developing a doomed therapy. Likewise, an optimist may well see an emerging brand as a major asset (a strength), while the bear sees little value in a brand and major threats from competition from more established brands/companies.

Advantages to Using SWOT for Investing

What SWOT analysis does do, however, is force some discipline and systematic, quantifying thinking into the investment evaluation process. A careful and thoughtful analysis should bring into focus the balance of a company's advantages and vulnerabilities, and also give the investor a benchmark to evaluate the company in future years. On balance, SWOT analysis is best used by investors as a way of crystallizing and the thought process that goes into an investment decision. The entire process can, and should, make *an investor think more deeply about the weaknesses of and threats to a company, while also helping to tease out what is really important and distinctive about one company versus its rivals.*

SWOT analysis also works best when it is done consistently. By using it on a regular basis and keeping track of the information, SWOT analysis can allow for better comparisons across industry participants, and more frequent use can also help limit some of the dangers of bias and selective (or incomplete) analysis.

Investors can look at SWOT analysis as a good screening tool for ideas and investment prospects that merit further research, as well as a useful means of tracking current holdings and comparing the development and evolution of those companies to the original purchase plans.

The Bottom Line

SWOT analysis provides a visual overview that prompts discussion around a company's situation. It is a bird's-eye view meant to flesh out the viability of a concept or strategy from the inside out – a more macro review than that of other analytic tools, such as Porter's 5 forces (see What's the difference between Porter's 5 forces and SWOT analysis?).

The speed at which you can do a SWOT analysis and the flexibility of the format to evaluate different ideas and strategies are key reasons why this tool remains popular in business circles, and can be useful to investors as well.

The most important factor in successfully using SWOT analysis is the quality of the data. If you don't accurately capture your company's core strengths and weaknesses, then SWOT analysis won't be much help. A SWOT analysis is only as good as the data coming in. If a company over-represents its strengths, weaknesses, opportunities or threats, SWOT analysis will potentially provide support in the wrong direction.

The SWOT analysis is never the end goal of the discussion. The next steps, for either a group or an individual investor, are to pull out action items from the analysis to work on further.

Read more: SWOT Analysis Definition | Investopedia http://www.investopedia.com/terms/s/swot.asp#ixzz4plV3dgGZ