

Strategic Valuation of Investment Under Competition

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The most serious problem with the widely used discounted-cash-flow (DCF) methods of investment valuation is that they are commonly applied without explicit regard to competition. As a result, the prescriptions they afford are often inconsistent with those given by competitive strategy frameworks. To remedy this, we show how such frameworks can be integrated with DCF methods to value investments (and disinvestments) in competitive and uncertain contexts. We recommend that the DCF analysis be carried out within a framework that includes the following three analytical steps: positioning, which focuses on competitive advantages; sustainability, which focuses on competitive dynamics; and flexibility, which focuses on options to revise the initial investment plan in the face of uncertainty. Valuers using this framework will reduce the likelihood that the DCF analysis misses relevant competitive-strategy considerations. Firms that have used this framework for positioning, sustainability, and flexibility have shaped and clarified their choices, solving apparent inconsistencies between DCF results and the competitive-strategy argument.