

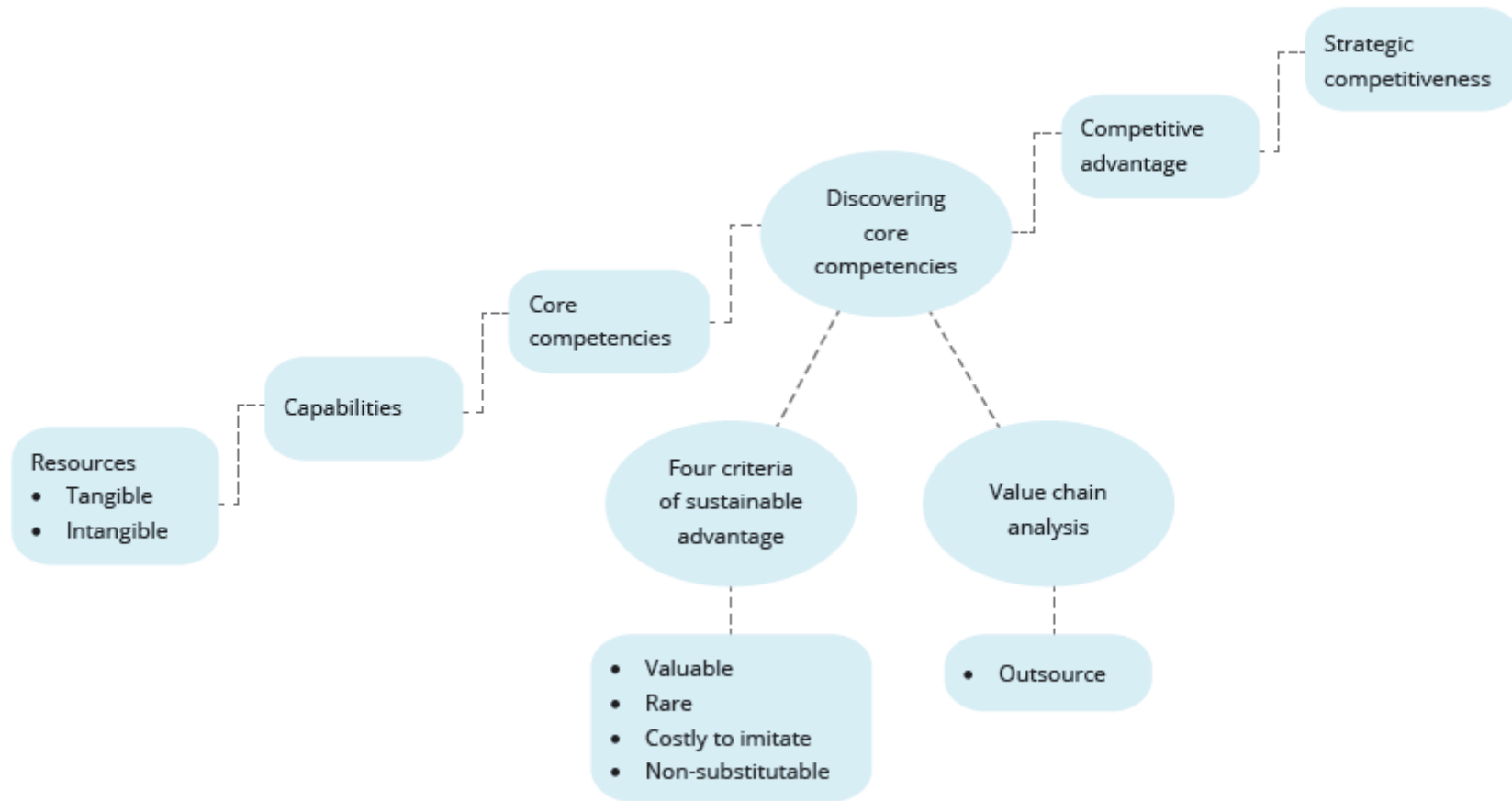
Week 3 Part B: Chapter 3

INTERNAL ENVIRONMENT OF ORGANISATIONS

WHEN STRATEGIC COMPETITIVENESS AND ABOVE-AVERAGE RETURNS OCCUR



Figure 3.1 Components of an internal analysis



COMPETITIVE ADVANTAGE: KEY POINTS

- No competitive advantage lasts forever.
- Over time, rivals use their own unique resources, capabilities and core competencies to duplicate a firm's ability to create value for customers.
- With globalisation, sustainable competitive advantage is especially challenging.

COMPETITIVE ADVANTAGE: KEY POINTS

- Firms must exploit their current advantages while simultaneously using their resources and capabilities to form new advantages that can lead to future competitive success.
- Innovation and people are critical resources for organisations in their quest for competitive advantage.

COMPETITIVE ADVANTAGE: SUSTAINABILITY

- The sustainability of a competitive advantage is a function of:
 - rate of core competence obsolescence due to environmental changes
 - availability of substitutes for the core competence
 - imitability of the core competence
 - ability to change the capabilities (i.e. how dynamic are they?).

ANALYSING THE INTERNAL ORGANISATION

▪ **Creating value**

- By innovatively bundling and leveraging their resources and capabilities and by exploiting their core competencies or competitive advantages, firms create value.
- Value is measured by:
 - product performance characteristics
 - product attributes for which customers are willing to pay.

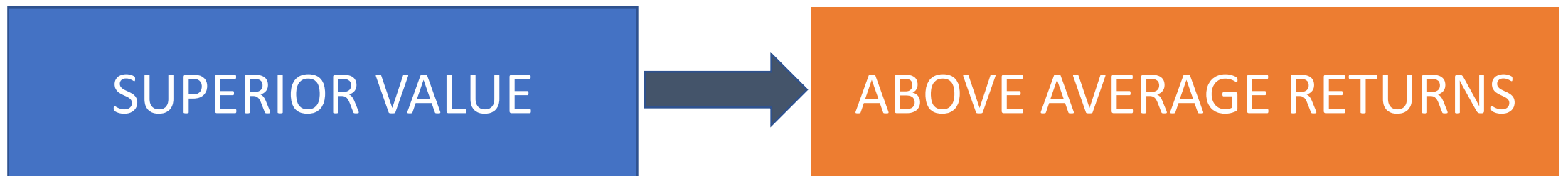
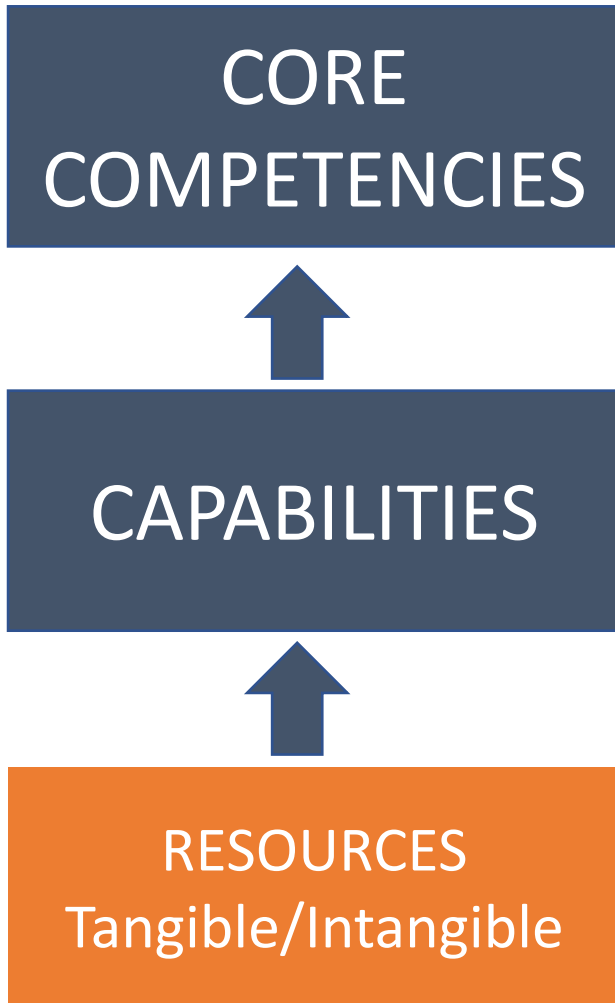


Figure 3.2 Conditions affecting managerial decisions about resources, capabilities and core competencies



Source: Adapted from R. Amit & P. J. H. Schoemaker, 1993, Strategic assets and organizational rent, *Strategic Management Journal*, 14: 33.

RESOURCES, CAPABILITIES & CORE COMPETENCIES



■ Resources:

- are the source of a firm's capabilities
- are broad in scope
- cover a spectrum of individual, social and organisational phenomena
- represent inputs into a firm's production process
- do not yield a competitive advantage or create value that results in above-average returns on their own (e.g. a brand is no use unless you use it).

TABLE 3.1

**RESOURCES,
CAPABILITIES AND
CORE COMPETENCIES:
Tangible Resources**

Financial resources	<ul style="list-style-type: none"> • The organisation's capacity to borrow • The organisation's ability to generate funds through internal operations
Organisational resources	<ul style="list-style-type: none"> • Formal reporting structures
Physical resources	<ul style="list-style-type: none"> • The sophistication of an organisation's plant and equipment and the attractiveness of its location • Distribution facilities • Product inventory
Technological resources	<ul style="list-style-type: none"> • Availability of technology-related resources such as trade secrets

Sources: Adapted from J. B. Barney, 1991, Firm resources and sustained competitive advantage, *Journal of Management*, 17: 101; R. M. Grant, 1991, *Contemporary Strategy Analysis*, Cambridge, UK: Blackwell Business, 100-2.

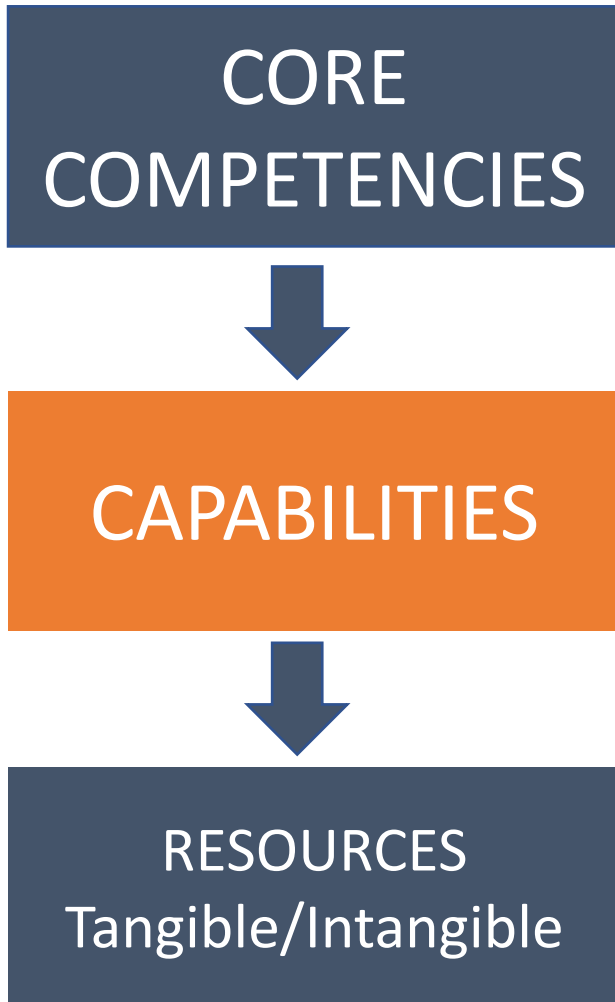
TABLE 3.2

**RESOURCES,
CAPABILITIES AND
CORE COMPETENCIES:
Intangible Resources**

Human resources	<ul style="list-style-type: none"> • Knowledge • Trust • Skills • Abilities to collaborate with others
Innovation resources	<ul style="list-style-type: none"> • Ideas • Scientific capabilities • Capacity to innovate
Reputational resources	<ul style="list-style-type: none"> • Brand name • Perceptions of product quality, durability and reliability • Positive reputation with stakeholders such as suppliers and customers

Sources: Adapted from R. Hall, 1992, The strategic analysis of intangible resources, *Strategic Management Journal*, 13: 136-9; R. M. Grant, 1991, *Contemporary Strategy Analysis*, Cambridge, UK: Blackwell Business, 101-4.

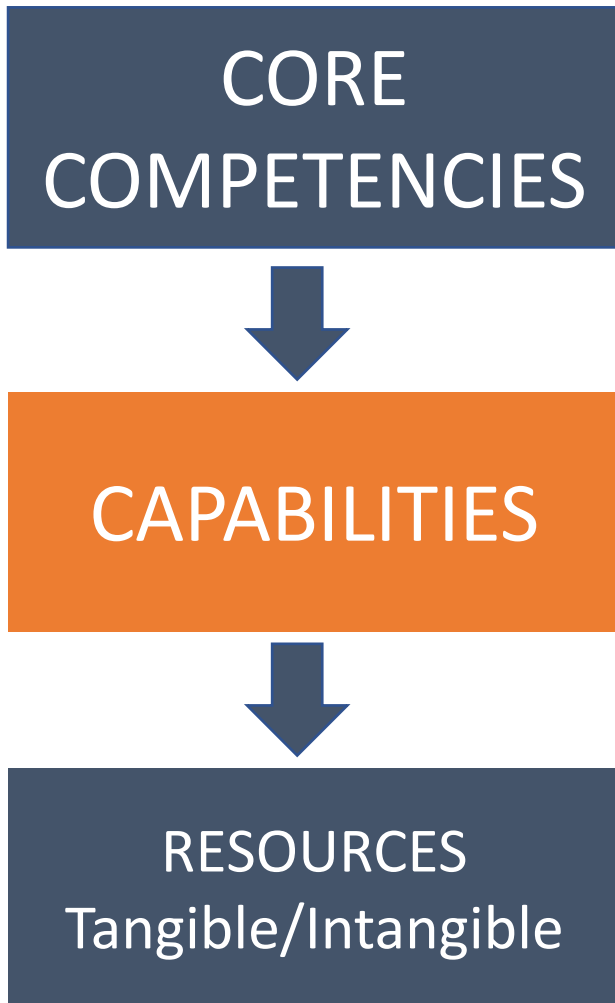
RESOURCES, CAPABILITIES & CORE COMPETENCIES



■ **Capabilities:**

- emerge over time through complex interactions among tangible and intangible resources
- stem from employees' unique skills, knowledge and functional expertise
- are activities that a firm performs exceptionally well relative to its rivals
- are activities through which a firm adds unique value to its goods or services over an extended period.

RESOURCES, CAPABILITIES & CORE COMPETENCIES



■ **Capabilities:**

- exist when resources have been purposefully integrated to achieve a specific task or set of tasks
- are often developed in specific functional areas
 - distribution
 - human resources
 - management information systems
 - marketing
 - management
 - manufacturing
 - research and development.

TABLE 3.3

**RESOURCES,
CAPABILITIES AND
CORE COMPETENCIES:
EXAMPLES OF FIRMS'
CAPABILITIES**

Functional areas	Capabilities	Examples of organisations
Distribution	<ul style="list-style-type: none"> • Effective use of logistics management techniques 	<ul style="list-style-type: none"> • Woolworths • IKEA
Human resources	<ul style="list-style-type: none"> • Motivating, empowering and retaining employees 	<ul style="list-style-type: none"> • Microsoft • Southwest Airlines
Management information systems	<ul style="list-style-type: none"> • Effective and efficient control of inventories through point-of-purchase data-collection methods 	<ul style="list-style-type: none"> • Coles
Marketing	<ul style="list-style-type: none"> • Effective promotion of brand-name products • Effective customer service • Innovative merchandising 	<ul style="list-style-type: none"> • Procter & Gamble (P&G) • Ralph Lauren Corp. • McKinsey & Co. • RM Williams
Management	<ul style="list-style-type: none"> • Ability to envision the future of clothing 	<ul style="list-style-type: none"> • Zara
Manufacturing	<ul style="list-style-type: none"> • Design and production skills yielding reliable products • Product and design quality • Miniaturisation of components and products 	<ul style="list-style-type: none"> • Komatsu • Sony
Research and development	<ul style="list-style-type: none"> • Innovative technology • Development of sophisticated lift-control solutions • Rapid transformation of technology into new products and processes • Digital technology 	<ul style="list-style-type: none"> • Caterpillar • Otis Elevator Co. • Cochlear • Apple • Amazon • Netflix • Google • Alphabet • Facebook

BUILDING CORE COMPETENCIES



- Tools firms use to identify and build core competencies
 - **Four specific criteria of sustainable competitive advantage** can be used to determine which capabilities are core competencies.
 - **Value chain analysis** helps select the value-creating competencies that should be maintained, upgraded or developed and those that should be outsourced.

BUILDING CORE COMPETENCIES

- **The four criteria of sustainable competitive advantage**
 - Capabilities that fulfil the four criteria of sustainable competitive advantage are considered core competencies.

TABLE 3.4

**RESOURCES,
CAPABILITIES AND
CORE COMPETENCIES:
BUILDING CORE
COMPETENCIES**

Valuable capabilities	<ul style="list-style-type: none">• Assist an organisation to neutralise threats or exploit opportunities
Rare capabilities	<ul style="list-style-type: none">• Are not possessed by many others
Costly-to-imitate capabilities	<ul style="list-style-type: none">• Historical: a unique and valuable organisational culture or brand name• Ambiguous cause: the causes and uses of a competence are unclear• Social complexity: interpersonal relationships, trust and friendship among managers, suppliers and customers
Non-substitutable capabilities	<ul style="list-style-type: none">• No strategic equivalent

BUILDING CORE COMPETENCIES

- **Sustainable competitive advantage:**
 - exists only when competitors cannot duplicate a firm's strategy or when they lack the resources to attempt imitation
 - exists until competitors can successfully imitate a good, service or process
 - lasts for a relatively long period if all four criteria of sustainable competitive advantage are satisfied.

Table 3.5**Outcomes from combinations of the criteria for sustainable competitive advantage**

Is the capability valuable?	Is the capability rare?	Is the capability costly to imitate?	Is the capability non-substitutable?	Competitive consequences	Performance implications
No	No	No	No	Competitive disadvantage	Below-average returns
Yes	No	No	Yes/no	Competitive parity	Average returns
Yes	Yes	No	Yes/no	Temporary competitive advantage	Average returns to above-average returns
Yes	Yes	Yes	Yes/no	Sustainable competitive advantage	Above-average returns

BUILDING CORE COMPETENCIES

■ Value chain analysis

- Both value chain (primary) and support activities should be analysed.
- The competitive landscape demands that value chains and supply chains be examined in a global context.
- Each activity should be examined relative to competitor's abilities and rated as superior, equivalent or inferior.

BUILDING CORE COMPETENCIES

■ Value chain analysis

To become a core competence and a source of competitive advantage, a capability must allow a firm to do one of the following:

- perform an activity in a manner that provides superior value relative to competitors; OR
- perform a value-creating activity that competitors cannot perform.

BUILDING CORE COMPETENCIES

■ **Value chain analysis**

Value chain activities:

- Completed by a firm in order to produce products and then sell, distribute and service those products in ways that create value for customers

Support functions:

- Completed by a firm in order to support the work being done to produce, sell, distribute and service the products the firm is producing

Figure 3.3 A model of the value chain

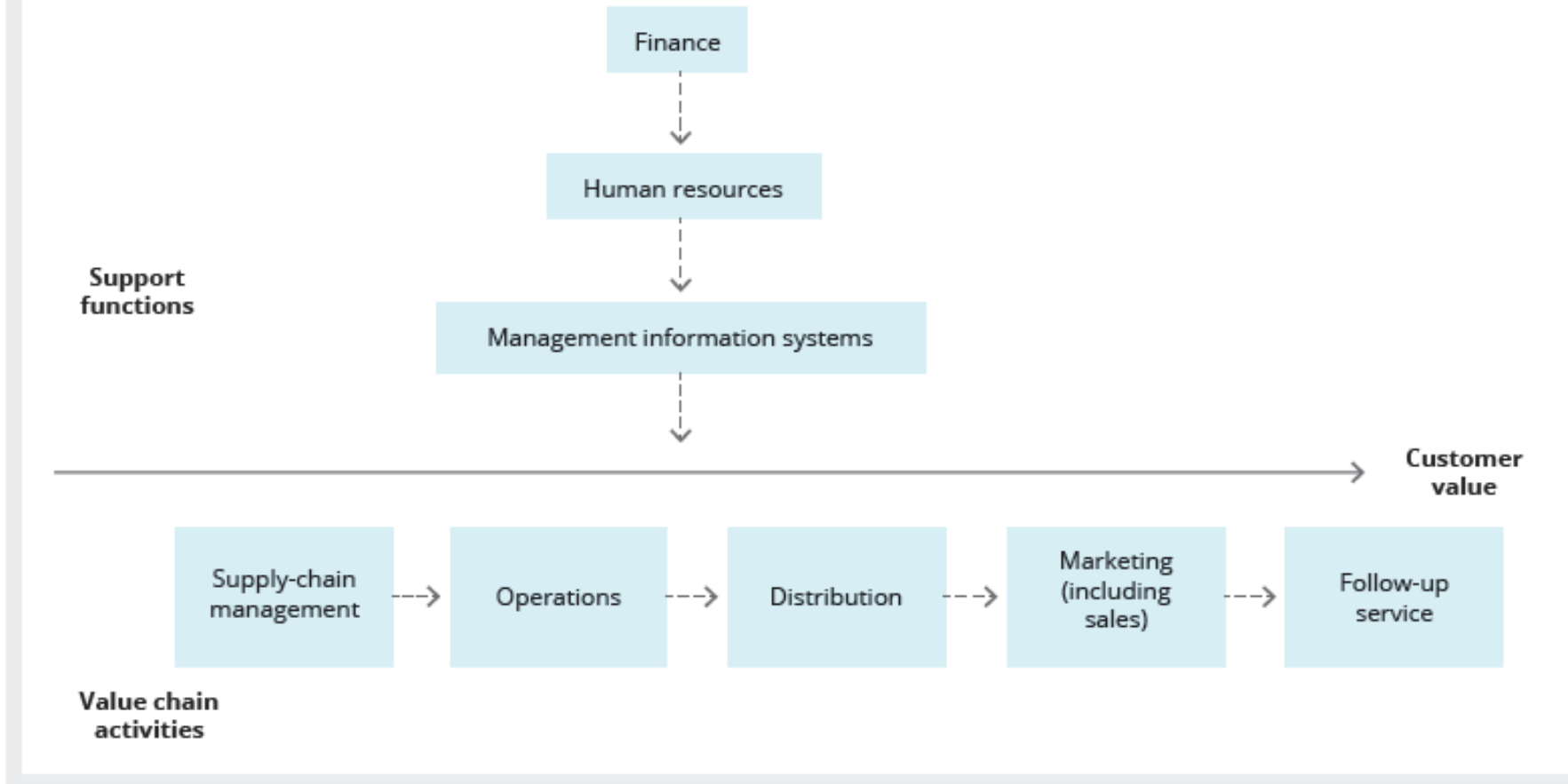


Figure 3.4 Creating value through value chain activities

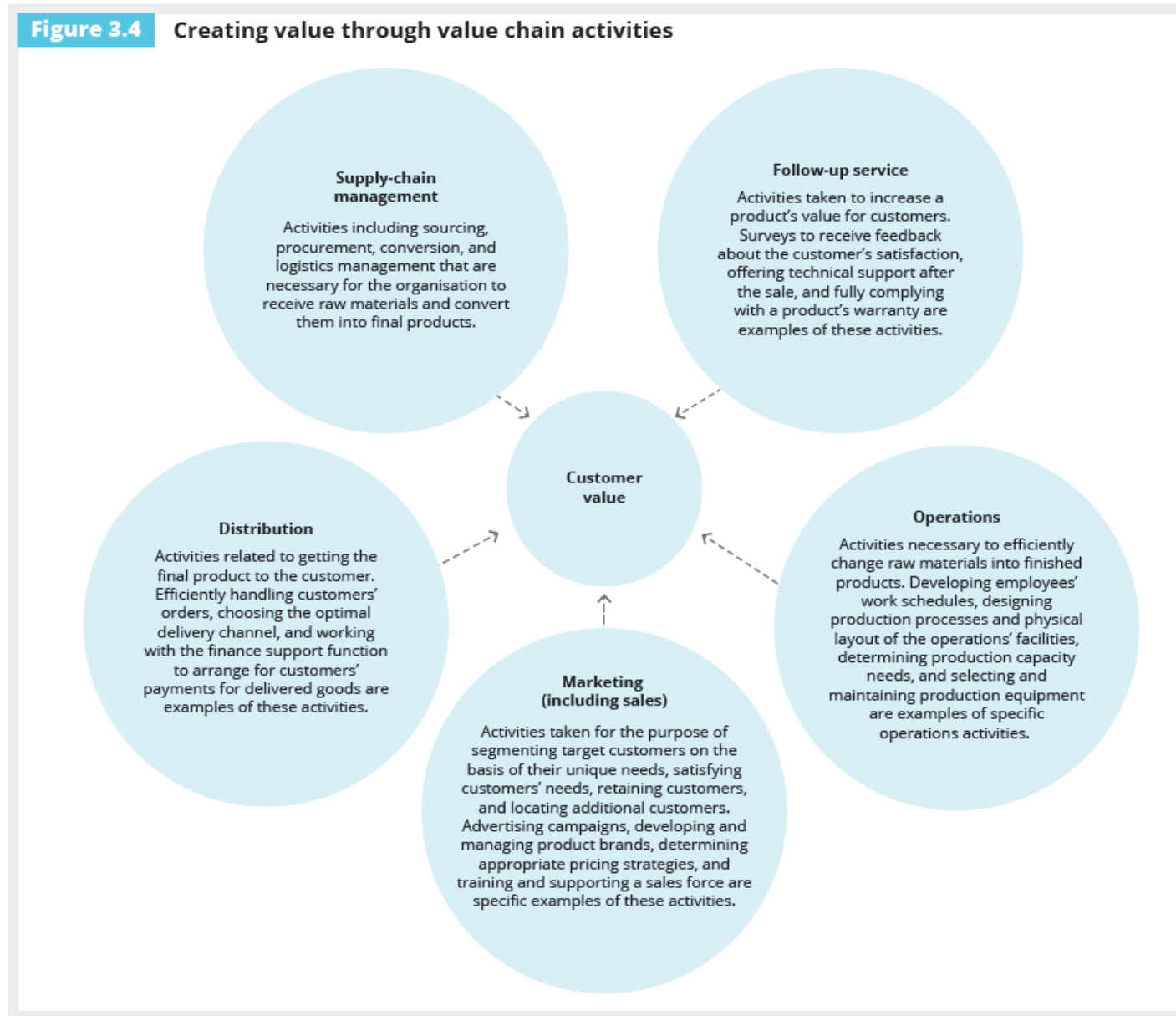
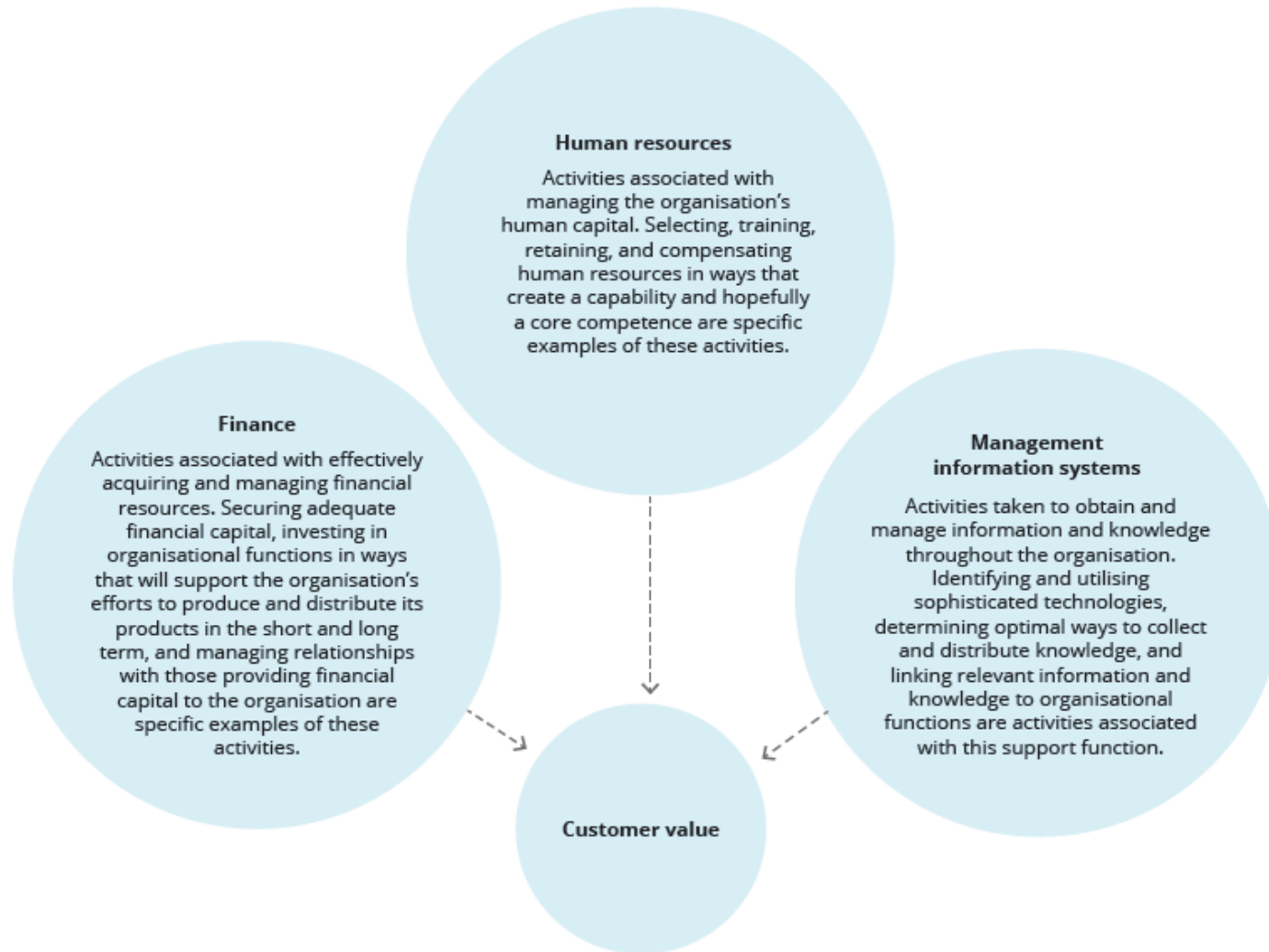


Figure 3.5 Creating value through support functions



OUTSOURCING

The purchase of a value-creating activity or support function from an external supplier –

- Effective execution includes an increase in flexibility and risk mitigation as well as a reduction in capital investment.
- Firms must outsource activities where they cannot create value or are at a substantial disadvantage compared to competitors.

STRATEGIC RATIONALE FOR OUTSOURCING

- Few organisations are competitively superior in all value chain activities and support functions.
- By outsourcing activities where it lacks competence, a firm can fully concentrate on those areas in which it can create value.
- Freeing resources for other purposes redirects efforts from non-core activities towards those that serve customers more effectively.

STRATEGIC RATIONALE FOR OUTSOURCING

- Specialty suppliers can perform outsourced capabilities **more efficiently**.
- **Sharing risks** reduces investment requirements and makes firms more flexible, dynamic and better able to adapt to changing opportunities.
- The **specialised resources** of outsourcing providers makes world-class capabilities available to firms.

COMPETENCIES, STRENGTHS, WEAKNESSES AND STRATEGIC DECISIONS

Firms must identify their strengths and weaknesses.

- Strengths are core competencies and strong capabilities.
- Weaknesses are what the value chain indicates are weak links relative to competitors.