Building Competitive Advantage

Chapter 4

Success and Strategy

Within an industry some companies outperform others. What is the basis of their competitive advantage?

Competitive Advantage

- Occurs when a company’s profitability is greater than the industry’s average profitability
- Competitive advantage over several years is considered Sustained
Company Profitability

Two basic conditions:
1. **Amount of Value** that customers place on a good or service
   - Value creation is at the heart of competitive advantage
   - The greater the value customers place on a product, the more the company can charge.
   - A product’s price is usually less than the value placed on it by the average customer.
   - This causes customers to capture consumer surplus.

Company Profitability (cont’d)

2. The company’s **cost of production**
   - A company will look for ways to increase productivity of capital and labor through:
     - Economies of Scale
     - Spread fixed cost over large product volume
     - Greater division of labor and specialization

Two Basic Strategies for Creating Value

- **Low Cost**: Drive down cost structure
- **Differentiation**: Consumers value the product and are willing to pay a premium price
Value Creation

Building Competitive Advantage

Four Factors:
1. Efficiency
2. Quality
3. Innovation
4. Customer Responsiveness

These are the generic building blocks of competitive advantage that any company in any industry can adopt.

Resource-Based View of Competitive Advantage...

...suggests that competitive advantage is attained through firm resources that are:
- **Valuable** - they enable a firm to implement strategies that improve its efficiency and effectiveness
- **Rare** - not available to other competitors
- **Imperfectly imitable** - not easily implemented by others
- **Non-substitutable** - not able to be replaced by some other non-rare resource
Comparing Toyota and General Motors

Building Blocks of Competitive Advantage

Efficiency

- Efficiency = outputs/inputs
- Employee Productivity: output per employee
- Capital Productivity: Output per unit of investment capital
- High Productivity = greater efficiency and low costs
Quality (as Excellence)

• **Superior Quality**: customers perceive attributes of a product to be better than rival’s attributes, in:
  – Design,
  – Style,
  – Aesthetic appeal,
  – Features and functions, and / or
  – Level of service that comes with the product

• **Excellence**: when excellence is built into product offering, consumers have to pay more to own or consume the product

A Quality Map for Automobiles

Quality (as Reliability)

• A product is reliable if it:
  – Consistently does the job it was designed for
  – Does the job well
  – Rarely, if ever, breaks down

• Less time is spent of defective products and fixing mistakes

• Reliability increases the value a consumer gets from the product and increases the price that the company can charge
Innovation

• The act of creating new products or processes
  – Innovations give a company something unique that their competitors lack
  – In the long run, innovation is perhaps the most important part of competitive advantage

• **Product Innovation** - The development of products that are new to the world or have superior attributes to existing products.

• **Process Innovation** - The development of a new process for producing products and delivering them.

Customer Responsiveness

• If a customer’s need is satisfied better by a certain product, the customer will attribute more value to the product.
  – What’s involved with making this phenomenon happen?
  – What risks are there to this?

• More attributed value creates a differentiation and ultimately a competitive advantage

The Value Chain is the idea...

...that a company is a chain of activities for transforming inputs into outputs that customers value

• Consists of **primary** and **support** activities
Strategy, Resources, Capabilities, and Competencies

Functional Level Strategies (really tactics)

- Managers pursue improvement in business functions by:
  - Increasing efficiency
  - Increasing quality
  - Increasing innovation
  - Achieving superior customer responsiveness

Distinctive Competencies

- A unique firm-specific strength that allows a company to better differentiate or achieve lower cost than rivals
- These arise from Resources and Capabilities
Resources

• Financial, physical, social or human, technological, and organizational factors that create value to customers.
• Can be **Tangible or Intangible**
  Example:
  Tangible = land, building, equipment
  Intangible = brand names, reputations

Capabilities

• A company’s skills at coordinating its resources and putting them into productive use.
• Capacities are needed to utilize resources

Durability

• When a company has superior profitability, other companies are inclined to imitate the successful strategy.
• Durability of competitive advantage depends on the ease or difficulty to copy distinctive competencies.
• **Barriers of Imitation** are the factors that make copying difficult for competitors.
• Even if a company’s distinctive competencies are protected by higher barriers to imitation, it should act as if rivals are continually trying to nullify its source of advantage