chapter 3 Analyzing Internal Strategic Resources and Capabilities

Knowledge management is critical. It's one of our core processes – sell work, do work, manage people and manage knowledge.

JOHN PATZ, CKO OF ERNST AND YOUNG

Only consider managers that you admire and trust.

WARREN BUFFET, CHAIRMAN OF BERKSHIRE CORP.

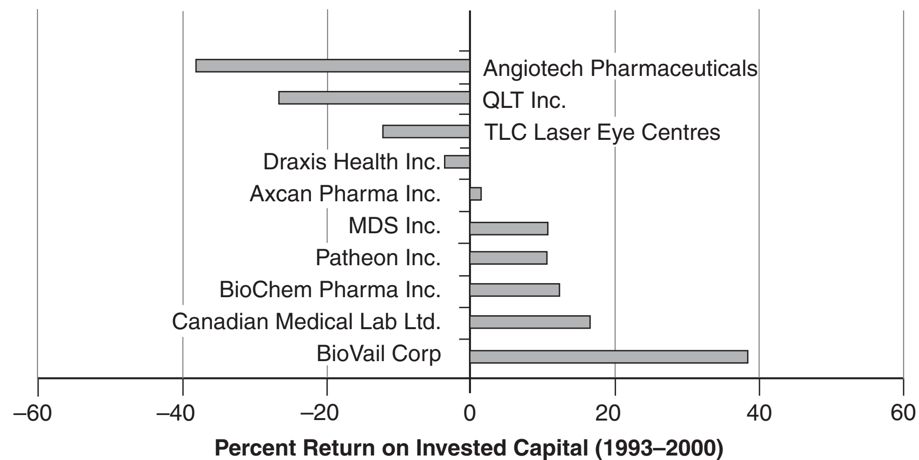
In this chapter, we examine the development of a firm's internal competitive advantages. In Chapter 2, exhibit 2-1 illustrated how the external competitive environment can influence industry sector performance. In exhibit 3-1, we examine the performance of companies in firms within a specific industry, the Canadian biotech and pharmaceutical industry. The performance differences are large, as is shown in exhibit 3-1, and this variance in firm performance is consistent in most industry sectors studied. The question that is examined in this chapter is, why is there such a variance in performance between individual firms in an industry?

The differences in performance are due to several factors. First, the firms may be in slightly different competitive positions (i.e., belong to different strategic clusters in the industry) and some positions may be more attractive than others. However, the more important difference is the disparity in competitive advantages between the various firms. Competitive advantages are abilities, assets, skills, capabilities, etc., that enable a company to compete more effectively in its industry.

In the biotech and pharmaceutical industries, illustrated in exhibit 3-1, firms that have higher return on invested capital tend to have stronger technological capabilities, including patented products and other functional competences, such as marketing and manufacturing abilities.

A comparison of the best and worst performing companies, in exhibit 3-1, illustrates how a firm's competitive advantages can influence performance. These companies, Angiotech and Biovail, have very similar competitive positions (i.e., both specialize in proprietary time-release drug technologies in the pharmaceutical industry), yet they have very different levels of performance. This performance difference is a result of the differences in each firm's competitive advantages. The poorer performing company, Angiotech, is in the early stages of drug product development—discovery and clinical trials—while Biovail is in the latter stages—clinical trials, approval, and commercialization. Therefore, all of Angiotech's efforts have been aimed at developing the necessary technical capabilities to move its products through to the approval

exhibit 3-1 Performance in the Biotech and Pharmaceutical Industry in Canada*



* Notes
From the Financial Post Corporate Reports 2001
RIC was calculated s an average for the years 1993 to 2000

and commercialization stages. However, Biovail has not only developed competitive advantages related to technical product development, but has also manufacturing and marketing abilities. Furthermore, Biovail's active marketing effort has created considerable brand recognition in the market place. In conclusion, Biovail's competitive advantages have produced much greater return on invested capital relative to Angiotech, which is just starting to build its competitive advantages. This example illustrates the importance of building competitive advantages continuously and in a focused manner.

TOOLS FOR ASSESSING A FIRM'S COMPETITIVE ADVANTAGES

A basic tool for analyzing a firm's competitive position and advantages is SWOT analysis, as was indicated in Chapter 1. However, before we examine the various tools for assessing competitive advantage, we should make sure we understand the concept and the different types of competitive advantages that are available to the firm.

WHAT ARE COMPETITIVE ADVANTAGES?

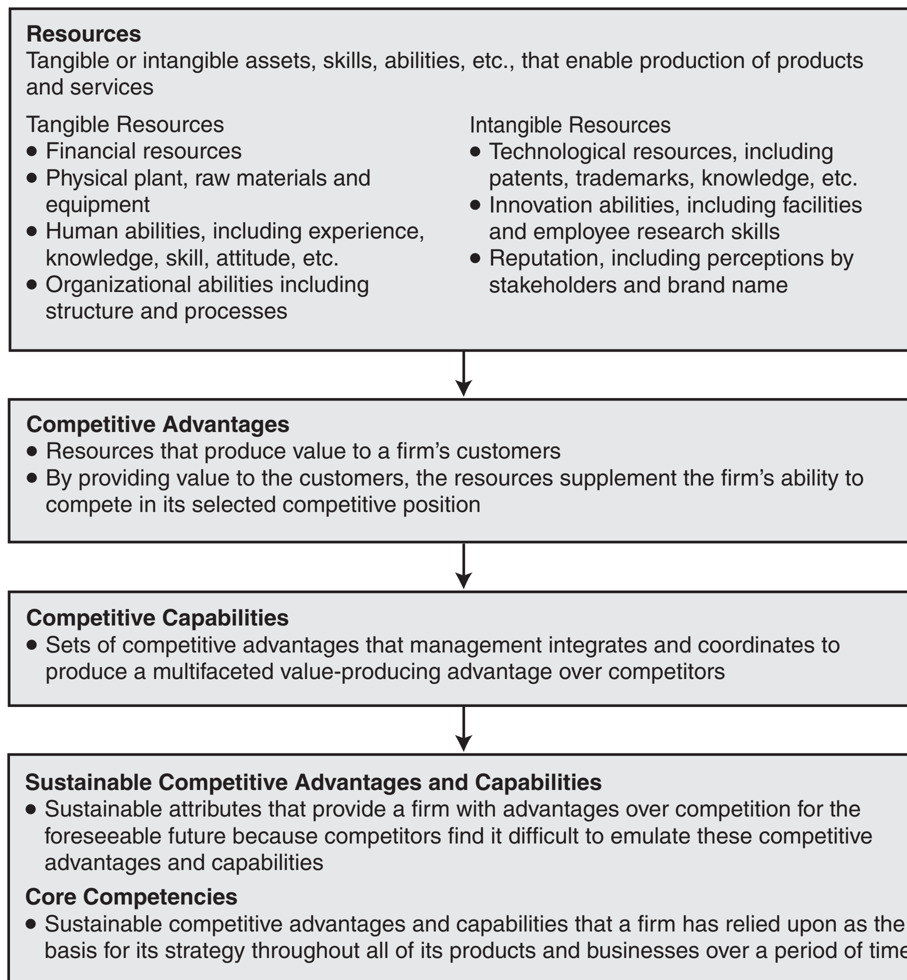
A firm's competitive advantages evolve from the resources available to the firm. Resources are physical assets (e.g., land, equipment, buildings, cash, etc.), intangible resources (e.g., brand name, market share, product patents, technological know-how, etc.), or capabilities (e.g., learning proficiencies, product development processes, fast delivery times, managerial abilities, etc.). Analyzing a firm's resources is an important step for a manager when formulating and implementing strategy. Strong resources must support a successful strategy, and when a strategy changes, accompanying changes in competitive advantages and, therefore, resources are usually necessary.

When formulating strategy, managers must decide what resources are necessary for a firm's strategy, and how to develop or acquire these resources overtime.

How managers evolve resources into competitive advantages and capabilities, and then eventually into sustainable competitive advantages are illustrated in exhibit 3-2. The hierarchy of development illustrates how managers select and develop specific resources available to them, then slowly shape them into competitive advantages, and sometimes competitive capabilities and sustainable competitive advantages and capabilities. The definitions of these competitive attributes are briefly described in exhibit 3-2.

Exhibit 3-2 also provides examples of the different types of resources a firm uses competitively. For example, a corner store uses its location as a competitive advantage because corner stores tend to compete on convenience. An example of a competitive capability is Microsoft's development of its brand image, something that results from a number of competitive advantages including technological, marketing, distribution as well as its ownership of the Windows operating system and the Office desktop applications. Something that provides continuous advantages competitively is

exhibit 3-2 The Hierarchy of Development of Competitive Advantages



a sustainable competitive advantage. An example of a sustainable competitive advantage is Intel's continuous ability to upgrade its product technically and market it faster than its competition. This ability to stay continuously ahead of the competition is one of the most valuable advantages a firm can have.

Very often, sustainable competitive advantages evolve into core competencies in a company. Core competencies are competitive advantages and capabilities that emerge over time as being central to a firm's overall strategy, and they are competitive advantages upon which the firm's strategy is based over time. For example, Intel's core competency is the ability to produce the fastest chip in the world. Intel has built its strategy around this core competency for the past decade. More recently, it has begun to stress efficiency in manufacturing because they realize this will become a more important strategic factor in the future as this industry matures. Multi-business firms build their businesses around a core competency and this enables them to effectively and efficiently execute their strategy in all of their businesses. An example of this is Bombardier, which has developed a core competency around its relationship building capabilities. This core competency has enabled Bombardier to market to key customers, more effectively gain financing from government, integrate acquisitions adeptly, and gain access to technology developed by other firms through alliances.

DEVELOPING RESOURCES INTO COMPETITIVE ADVANTAGES

One of the key strategic decision-making judgments managers face is deciding what resources to develop or acquire. Top managers spend an inordinate amount of time analyzing, selecting, acquiring, or developing the necessary resources to enable their firm to be competitive. These resources and competitive advantages must be constantly upgraded or altered to enable a firm to maintain its competitive advantage relative to other firms in the market.

Exhibit 3-3 illustrates the criteria that managers use to assess the quality of resources. As shown, resources must provide value to the customer (either directly or indirectly) or they are of no use to the firm. If it does not, then it should not be acquired or developed by the firm into a competitive advantage. Furthermore, a competitive

exhibit 3-3 Assessing Resource Characteristics and Quality

Quality	Explanation Question
Valuable	Is the resource or capability valuable in delivering the firm's service or product to its customer? This is a necessary resource quality.
Durable	Is the resource or capability temporal (i.e., will disappear over a period of time) in nature (e.g., a limited natural resource)?
Rare	Is the resource rare, or do many other firms have this competitive capability?
Inimitable or non-substitutable	Is the resource or capability unique to your firm relative to the competition? Can a resource or capability be substituted by another one in your business or industry?
Complex	Does a resource or capability have a breadth, scope, and complexity to make it difficult for others to both imitate and understand (e.g., organizational culture)?

advantage that should be further developed and improved is one that has the potential to be durable, rare, and so on. The more qualities the resource has, the more important it is as a competitive advantage. A competitive advantage that has characteristics of inimitability and complexity, an example being organizational culture in the advertising business, has qualities of sustainability. These latter competitive advantages and capabilities may be very effective at producing long-term competitive advantages and managers should focus considerable effort on developing them.

VALUE-CHAIN ANALYSIS

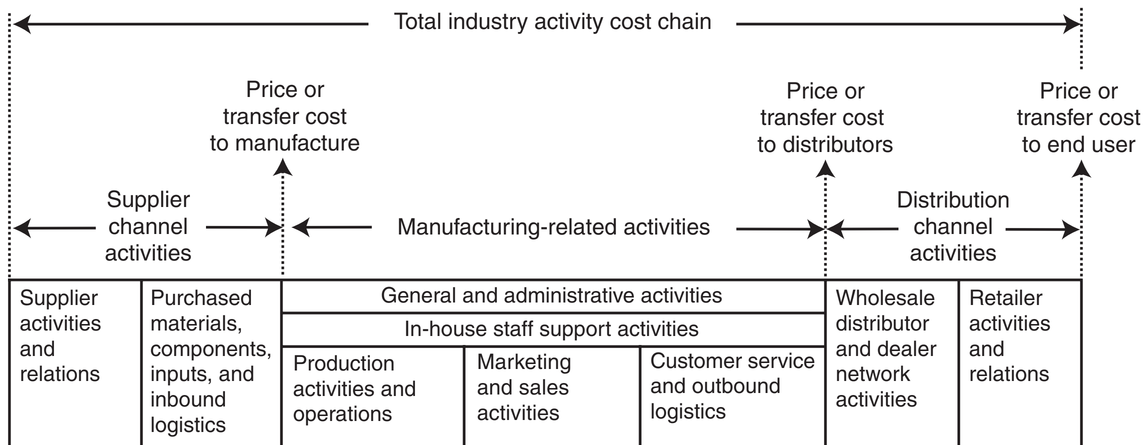
An important approach to identifying competitive advantages and capabilities in a firm is through value-chain analysis. A value chain is defined as the path upon which products or services progress along as value is added, prior to reaching the end consumer. A generic value chain is shown in exhibit 3-4. A value chain is made up of primary activities (inbound logistics, operations, outbound logistics, marketing and sales, and service) and support activities (firm infrastructure, human resource management, technology development, and procurement). Firms try to gain competitive advantage by increasing the value to customers in one or more activities relative to competitors. Value is defined as improving the worth of the product or service to the customer either through lowering the price or increasing the product or service characteristics. Managers must focus on increasing the value to the customer while attempting to minimize the costs to the firm—this maximizes total profits to the firm. These two issues are called *strategic value* and *cost analysis*.

Strategic value analysis focuses on a firm's relative value position vis-à-vis its rivals. The analytical approach must combine an analysis of the firm's total industry value chain and the firm's competitive position. The manager must appreciate the relationship between the firm's competitive position (i.e., its customers that are served by that competitive position) and the value provided to these customers by the various activities in the firm's value chain. The analysis must include value provided by assets possibly not owned and controlled by the firm, including such things as the quality of service provided by their chosen retail distribution channels, and the quality of raw materials provided by suppliers. All of these factors may influence customer value.

Strategic cost analysis focuses on a firm's relative cost position vis-à-vis its rivals. The primary analytical tool of strategic cost analysis is the construction of a total firm value chain showing the makeup of costs all the way from the inception of raw materials and components to the end price paid by ultimate customers. The activity-cost chain, thus includes more than just a firm's own internal cost structure; it includes the buildup of cost (and thus the "value" of the product) at each stage in the whole market chain of getting the product into the hands of the final user, as shown in exhibit 3-4. Constructing an integrated activity-cost chain is more revealing than restricting attention to just a firm's own internal costs. This is because a firm's overall ability to furnish end-users with its product at a competitive price easily depends on cost factors originating either backward in the suppliers' portion of the activity-cost chain or *forward* in the distribution channel portion of the chain.

It is important to note that value-chain analysis and decisions must be directed at the competitive position of the firm. In other words, increasing the value of an activity (or competitive advantage in an activity) must be related to a firm's competitive position (i.e., be valued by a company's customers). For example, if a firm is in an expensive and highly differentiated market position, customers may not want cheaper

exhibit 3-4 Generic Value Chain in an Industry



Activity	Specific Cost Activities and Cost Elements
Supplier activities and relations	• Managing and controlling suppliers • Ingredient raw materials and component parts supplied by outsiders
Purchased materials, components, inputs and inbound logistics	• Energy • Inbound shipping • Inbound materials handling • Inspection • Warehousing
General and administrative activities	• Finance and accounting • Legal services • Public relations • General management • Interest on borrowed funds • Tax-related costs • Regulatory compliance
In-house staff support activities	• Payroll and benefits • Recruiting and training • Internal communications • Computer services • Procurement functions • R&D • Safety and security • Supplies and equipment • Union relations
Production activities and operations	• Facilities and equipment • Processing, assembling, and packaging • Labour • Maintenance continued • Process and product design and testing • Quality control and inspection • Inventory management • Internal materials handling • Manufacturing supervision
Marketing and sales activities	• Sales force operations • Advertising and promotion • Market research • Technical literature • Travel and entertainment • Dealer/distributor relations
Customer service and outbound logistics	• Service representatives • Order processing • Service manuals and training • Spare parts • Transportation services • Other outbound logistics costs • Scheduling
Wholesale distributor and dealer network activities	• Includes all of the activities, associated costs and markups of distributors, wholesale dealers, retailers, and any other forward channel allies whose efforts are utilized to get the product into the hands of end-users/customers • Outbound logistics and transportation
Retailer activities and relations	• Sales support activities to retailers, including sales calls to retailers, promotions, marketing programs, etc.

activities, they may in fact just want higher value products and services that more thoroughly cover their needs.

The task of constructing a complete value-chain for a firm is not easy. It requires breaking a firm's own historical cost accounting data out into several principal cost categories and developing cost estimates for the backward and forward channel portions of getting the product to the end-user as well. It also requires the manager to estimate the same cost elements for one's rivals and then estimating their overall value chains—an advanced art in competitive intelligence in itself. But despite the tedium of the task and the imprecision of some of the estimates, the payoff in exposing the cost competitiveness of one's position and the attendant strategic alternatives makes it a valuable analytical tool.

In exhibit 3-4, observe that there are three main areas in the cost chain where important differences in the *relative* costs of competing firms can occur: in the suppliers' part of the cost chain, in their own respective activity segments, or in the forward channel portion of the chain. To the extent that the reasons for a firm's lack of cost competitiveness lie either in the backward or forward sections of the cost chain, then its job of reestablishing cost competitiveness may well have to extend beyond its own in-house operations. When a firm has a cost disadvantage in the area of purchased inputs and inbound logistics, five strategic options quickly emerge for consideration:

- Negotiate more favourable prices with suppliers.
- Integrate backward to gain control over material costs.
- Try to use lower priced substitute inputs.
- Search out sources of savings in inbound shipping and materials logistics costs.
- Try to make up the difference by initiating cost savings elsewhere in the overall cost chain.

When a firm's cost disadvantage occurs in the forward end of the cost chain, there are three corrective options:

- Push for more favourable terms with distributors and other forward channel allies.
- Change to a more economical distribution strategy, including the possibility of forward integration.
- Try to make up the difference by initiating cost savings earlier in the cost chain.

It is likely, of course, that a substantial portion of any relative cost disadvantage lies within rival firms' own activity-cost structures. Here, five options for restoring cost parity emerge:

- Initiate internal budget-tightening measures aimed at using fewer inputs to generate the desired output (cost-cutting retrenchment).
- Invest in cost-saving technological improvements.
- Innovate around the troublesome cost components as new investments are made in plant and equipment.
- Redesign the product or service to achieve cost reductions.
- Try to make up the internal cost disadvantage by achieving cost savings in the backward and forward portions of the cost chain.

The construction of a value chain is a valuable tool for competitive diagnosis because of what it reveals about a firm's overall cost/value competitiveness and the relative cost/value positions of firms in the industry. Examining the makeup of one's

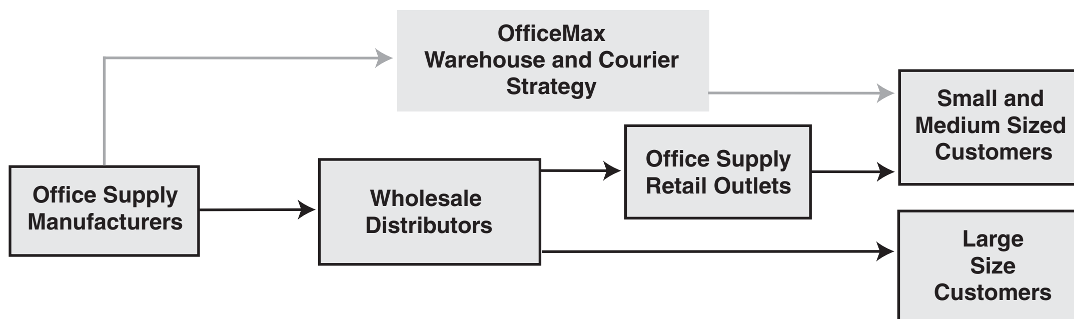
own value chain and comparing it against the chains of important rival firms indicates who has the most efficient and/or effective activities or competitive advantages and capabilities.

Assessing Supply and Distribution Chains

A manager analyzing his or her firm's value chain must also consider potential activities external to his or her firm because competitive advantages and capabilities can be attributable to a supplier or distributor. For example, Ikea's advantage of low cost is attributable to some degree to its suppliers who provide products at extremely low costs. The suppliers are able to provide this low cost because they have minimal overhead, no labour unions, and are focused on few activities and products. Ikea has restructured its value chain to provide these suppliers with many of the activities that would otherwise make their products expensive, such as product design and engineering. Therefore, restructuring activities in a value chain and coordinating activities with external activities can provide a firm with highly valuable and complex to imitate competitive advantages and capabilities.

Another example of an firm that reinvented its business activities, making use of the supply and distribution chain, is illustrated in exhibit 3-5. The solid lines in exhibit 3-5 illustrates how office supply products, such as stationary, staples, and pens were distributed in the early 1970s. Management in a company called OfficeMax noted that medium sized customers, such as law and medical offices, purchased their supplies through retail outlets where they incurred the high costs of retailing such as retail store overhead costs, stocking fees, and so on. OfficeMax setup a catalogue delivery service, which delivered from low cost warehouses located in rural sites using contracted overnight couriers. For the medium sized businesses, this provided lower cost products, and it improved the scope of products available and lowered delivery times to within 24 hours. OfficeMax has now evolved its strategy to include large retail box stores and the ability to order products through the Internet. It is notable that many other competitors have followed OfficeMax's strategy, which uses different supply chain channels to focus on, into the lower cost, medium sized customer in this market. Therefore, it is important that all of the various channels of supply, product flow, and distribution channels be identified in an industry, as certain approaches may provide competitive advantages to companies focusing on certain types of customers.

exhibit 3-5 A Business Supply and Distribution Chain for Office Supplies



Some of the more fundamental issues to be considered when developing and examining the business system are:

- What are the various distribution and/or supply channels in the industry?
- What are the most efficient and effective channels to use in the industry?
- Are specific channels more effective and efficient for targeting specific customers (i.e., competitive positions in the market place)?
- Have any of the firms vertically integrated into different activities of the business system and will this provide an advantage or disadvantage?
- Are there any new types of channels of supply or distribution that are not being used in the industry, but might prove to be effective?

DEFINING THE "BUSINESS MODEL"

A new jargon has arisen over the last several years and it is "business model." A business model is essentially a value chain, but it also incorporates advantages provided to the firm outside of the firm itself, unlike the classic value chain that looks only at internal activities in the firm. For example, supply and distribution chains would be part of a business model. In addition, the classic value chain is essentially an accounting or financial exercise in examining value. The business model examines the value delivered to the customer from both a pecuniary and non-pecuniary perspective. Non-pecuniary value may come in the form of higher quality, more service, greater features, a wider selection of product types, more convenient location, and so on. This assessment ensures that management in a firm is assessing the complete value provided to the customer as perceived by that customer and relative to the competition. Thus, it is a more complete perspective of how much value the customer perceives the company to be providing to them.

An analysis of a business model is essentially the approach discussed above that examined the value chain and supply and distribution chains. It is important in this analysis to look not only at costs as the product and service moves through the business model activities, but also the non-pecuniary value produced by the activities and competitive advantages that the firm uses.

BENCHMARKING AND BEST PRACTICES

Benchmarking is the process of examining the value and efficiency of activities in your firm and comparing them to similar activities in other firms. Best Practices is an approach used by many good companies to better their capabilities, and ultimately their competitive advantage. The process involves identifying companies with the "best" functional activities and capabilities, and then sending in teams to study these capabilities. A team is made up of key workers and managers in the activity that will implement these "best" practice procedures in their company. The team evaluates the methods, work activities, processes, responsibilities, organizational linkages, and so on, in the company that has the "best" activity. Then they assess how and what can be implemented in their company to improve their competitive advantages in their activity.

Best Practices is usually facilitated by an outside consultant company who identifies the "best practice" companies. Normally, the firm identified is not a competitor, although some best practices companies, such as Nucor, invite its competitors into its plant as long as a reciprocal visit is possible. However, the key is getting

an activity that is similar to the activity that is comparable and ultimately imitable in the target firm.

The objective of this approach is to install the best competitive advantages and capabilities into your company by copying not one firm, but by gathering the best competitive advantages from all firms both inside and outside their industry. Managers must, however, be aware that a Best Practices program is no substitute for developing one's own creative and unique competitive advantages and capabilities. The best capabilities are complex and abstruse, making them very difficult to imitate, and, therefore, poor candidates for a Best Practices program.

Finally, strategy involves developing competitive advantages built from resources and capabilities that uniquely fit the firm's competitive position. This fit must create a unique interaction and coordination between all of the parts, and selecting best practices from different firms may provide best individual capabilities that do not produce the best unified strategy.

THE PROCESS OF MANAGING THE DEVELOPMENT OF COMPETITIVE ADVANTAGES

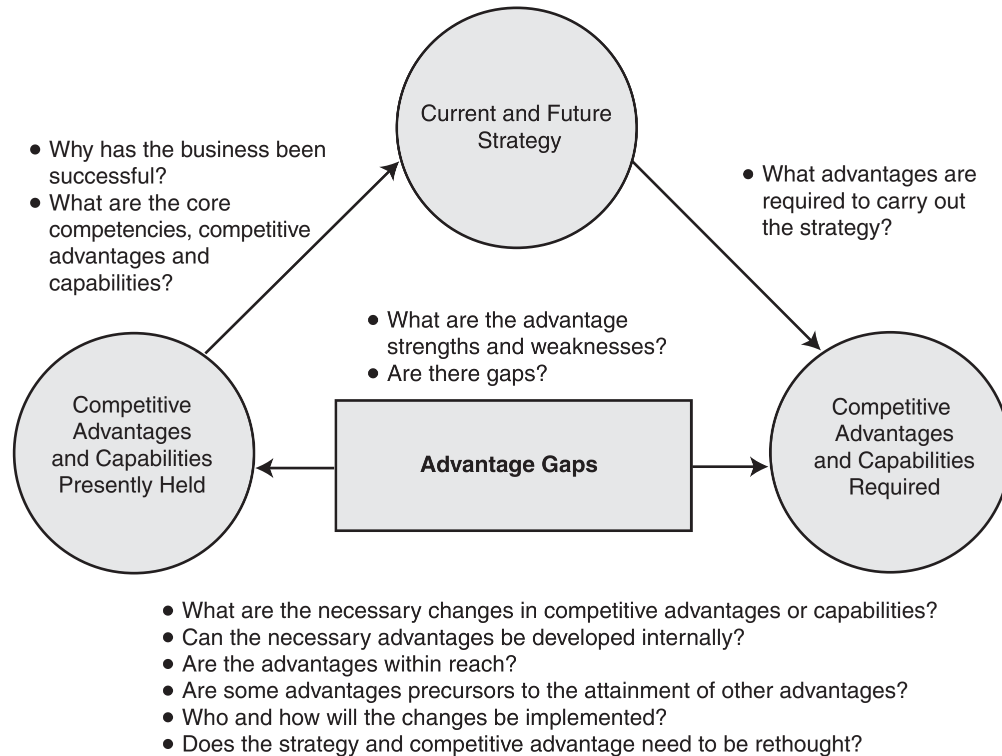
Managing the resource identification and development process requires that managers assess what resource gaps must be filled to ensure that the firm's present strategy is competitive in the future. Now it is important to evaluate the quality of competitive advantages and capabilities required by the present and future desired strategy and competitive position. In particular, managers analyze what advantages should be focused upon to improve activities that are weak or to develop sustainable advantages or core competencies in critical activities. Therefore, the assessments of gaps and weaknesses of competitive advantages in a firm are critical to the firm's competitiveness. Exhibit 3-6 illustrates the managerial thinking during this process.

Two questions must be kept in mind when determining the specific advantages required for a strategy: Do the advantages support the firm's competitive position and core competencies, and can they be implemented effectively? Starting with advantages held, the strategist determines the unique characteristics of the firm's current advantages—those that differentiate it from its competitors. These characteristics may include competitive advantages and capabilities, core competencies, or sustainable competitive advantages and capabilities. Having established what these critical advantages are, a strategy is then developed that makes good use of them.

Advantage gaps are the differences between the advantages required and the advantages held. If most of the gaps can be reduced, then the probability of executing the strategy successfully is improved. However, if the gaps are large and cannot be reduced, the strategy probably has to be revised so that the competitive advantages of the firm conform more readily to the competitive strategic position of the firm.

It should be noted that managers often are not immediately aware of the future advantages that their company requires. However, the drivers behind development of all long-term advantages are the people in the firm. Therefore, many firms put in place programs and processes that continuously attempt to upgrade the quality and abilities of their personnel. This enables firms to continually improve the abilities of their personnel and to guide their behaviour so that they develop core competencies or sustainable competitive advantages that are specific to the firm's competitive position and strategy. These programs and processes are discussed more thoroughly in Chapter 6.

exhibit 3-6 The Relationship Between Strategy and Assessing Advantage Requirements



EVALUATING COMPETITIVE ADVANTAGES HELD AND DETERMINING COMPETITIVE ADVANTAGES REQUIRED

Competitive advantages can be evaluated from several different perspectives. The most prevalent way of evaluating them is **by function**: finance, research and development, human resources, operations, marketing, and so forth. This really mirrors the value-chain analysis approach described earlier. Some of the important questions for such an approach are included in exhibit 3-7.

When a functional perspective is taken, the strategist also needs to consider the context within which the functions operate. The contribution of each function to the business's strategy needs to be addressed as some functions may be more important to the strategy than others. The interrelationships among the functions also need to be considered because what is done in one function may have a bearing on what can be done in another function.

A second way of evaluating resources is **by type**: financial, physical, human, and organizational. Financial resources are the funds that the company raises. They are the most basic and flexible resources of the business, and can be converted into other resources. Converting other resources into financial resources is less certain and more difficult. Physical resources are the buildings, raw material, and equipment that the company has to work with and what it can do with them. Human resources are the

exhibit 3-7 An Overview of the Functional Perspective

Function	A Partial List of Questions to Answer
Finance	• What is the apparent capacity of the firm to generate internal and external funds? • What funds are required for each strategic alternative?
Research and development	• How important is technology to the firm's processes and products? • What percentage of the firm's resources is devoted to research and development?
Human resources	• What is the ambition, depth, drive, loyalty, and skill of the managerial/administrative group in the firm?
Procurement	• What is the cost, flexibility, motivation, productivity, and skill of the work force? • How important is the procurement function to the firm?
Operations	• Does the firm have good relations with suppliers? What are the capacity, cost, and productivity of operations? • What is the age, condition, and flexibility of the plant and equipment? • What is the quality of the products produced?
Marketing	• Does the firm command a premium price, and, if so, why? • How well does the firm know its customers and its competitors?

number and type of people in the firm and what they are able to do. Organizational resources are the procedures and techniques the firm has developed that are necessary for success in the business.

A fourth way of evaluating resources is in terms of their **breadth**. A resource is essentially broad/wide when it is easily transferred to other situations and narrow/specialized when it is not. Sales staff with knowledge of many different products is an example of a broad resource, while specialized product knowledge is an example of a narrow resource. A broad resource base facilitates a business's expansion of its product, market, and industry scope, while a narrow resource base serves to limit the firm's ability to increase its scope.

A final way of evaluating resources is in terms of **location or business unit**. This is particularly useful when the firm has diverse businesses or locations. Other categorizing approaches may be useful if management in the firm identifies with the categorization methodology. Using different approaches to assessing competitive advantage gaps is useful because it forces managers to take new perspectives of their company's competitiveness.

RESOURCE GAPS

Rarely is the precise combination of resources needed to pursue a strategy in place. Furthermore, a firm is constantly trying to improve its competitive position and advantages, thus requiring new resources. This makes resource gap analysis critically important for a manager. When assessing the resources, a useful approach is to construct a table with entries down the side for the activities or functions, and with headings across the top for (1) current resources, (2) projected resources, (3) gaps between those two, and (4) how the gaps might be filled (exhibit 3-8). The body of this table is then filled in with the analytical details.

Resource gaps not only occur when a firm takes on a new strategy, but just by maintaining an ongoing strategy creates resource gaps. New resources must be developed when existing resources deteriorate, depreciate, or turn over. In addition, success with the existing strategy can create resource gaps as additional resources are required for growth. On occasion, more resources are generated than can be employed profitably in a business. Under utilization of existing resources is a negative form of resource gap analysis. Overproduction of resources can be problematic also. For example, when a firm generates more cash than it can use in the business making itself an attractive takeover target.

Identifying the Gaps

Resource gaps are identified through strength-and-weakness analysis as part of the SWOT analysis described earlier. Determination of strengths and weaknesses involves a relative comparison between those resources the company has and those it needs. In depth analysis of advantage gaps details the magnitude and type of resource needed, the availability of such a resource, methods for obtaining the advantage, and the timing or priority of need for such a resource. It should be noted that some resources may have to be sold and some acquired to meet the needs of one's competitive strategy.

Reducing the Gaps

The ability of the business to reduce advantage gaps is influenced by the magnitude and nature of the changes required, as well as the firm's ability to implement these changes. Reallocating, developing, buying, and selling advantages can reduce these gaps. Depending on how the gap is reduced, cost, ease, and timing will differ. Advantages can be acquired from the outside, but their high market cost can make it more desirable to develop them internally. Developing advantages is usually cheaper, but slower, but it can have other positive benefits, such as providing for the development of a continuous stream of advantages (e.g., managers). Moreover, development of advantages may be required if sufficient quantities or qualities are not available, either elsewhere in the business or in the marketplace. Of course, many tactical issues have to be addressed when considering how gaps might be filled.

It should also be noted that the ability to reduce an advantage gap will depend on the particular country in which the firm is located. A firm's advantage base is not simply

exhibit 3-8 Assessing Resource Gaps

Activity or Functional Area	Current Advantages	Required Advantages	Advantage Gaps	Filling the Gaps: Tactics and Risk
Finance				
R&D				
Human Resources				
Procurement				
Operations				
Marketing				

a function of its own operational regime, but a function of the location and country within which it operates. In other words, there is an interaction between firm-level and country-level sources of advantages and competitive advantage.

Changing a firm's advantages carries certain risks. These risks are associated with the number and magnitude of the advantages as well as the quality of advantages demanded by the strategic change. The manager must be careful that he or she does not make such a radical strategic so as to render the present firm advantages ineffectual and create advantage demands that are impossible for the firm to fulfill in the required time frame. It may be more acceptable for the firm to take a more incremental strategic approach to change where advantages are developed appropriate for the firm's intermediate competitive positions and associated competitive advantage.

EXAMPLE OF DEVELOPING COMPETITIVE ADVANTAGES

Loblaws developed considerable competitive advantages as it evolved into its new competitive positions, as described in Chapter 2. The following are some of the more important competitive advantages that Loblaws developed:

- Top management depth: Mr. Weston accomplished this by hiring a number managers who had MBAs from top business schools and extensive business experience in a number of different businesses. First-rate people are the underpinnings of any strong strategy because, ultimately, it is people who have to lead strategic development and execution. Most strong companies have strategically started this process by getting a first class upper management team.
- Loblaws closed store locations that were not in growth and middle to upper class residential areas. Loblaws also sold some other assets that were not key to its Canadian grocery strategy to get the capital to acquire other needed assets, such as new stores.
- The new stores were extremely well designed. They were larger than normal grocery stores and the design provided shoppers with a pleasant atmosphere. These stores improved the shopping experience immensely because they were physically pleasant, and the size allowed for a far wider product selection to be offered to the customer.
- Loblaws also began to develop a number of different types of stores that catered to different market sectors, including specialty sections in their main stores that catered to value added tastes and "no-frills" stores that sold lower cost and bulk items.
- Loblaws developed supplier relations with a far wider variety of suppliers, bringing in culturally diverse foods and a wider variety of fresh fish and vegetables. These relations enabled it to develop in-house brands of food that are manufactured to their specifications by suppliers.
- Many different types of branded foods were developed. The most prestigious was the President's Choice line of food, which was high quality food that has become the most widely recognized food brand in Canada. Loblaws also developed a "no-name" line of food that has become an economical brand despite the "no-name" title.
- Loblaws has slowly acquired competitors in regions in Canada in which it was not represented, and attempted to inject its value added, broad product scope strategy into these markets. This enabled Loblaws to become a truly across-Canada grocery chain.

The above list of advantages is a brief example of the continual development that Loblaws has developed over the past several decades. In fact, the key to its overall competitive advantage is its ability to continually innovate and become more efficient and effective.

SUMMARY

Finding an acceptable fit between the strategy and the advantages available to the business is a major step in formulating strategy. First, the firm's advantage must be examined in terms of what is available and what is needed. Advantages can be evaluated in several ways: by functional area, by type, by tangibility, by breadth, and by activity costs. Advantage gaps must be identified and evaluated to determine the likelihood of their being overcome. Whether they can be overcome depends on the gaps' size, number, and nature; the ways in which the gaps can be reduced; and the time available. When the likelihood of filling the advantage gaps poses too great a risk to be acceptable, the strategy has to be modified in order to bring its advantage requirements closer to current advantages.

Summary of The Competitive Resource and Advantage Analysis

Linking Competitive Position and Advantage

- It is critical that management examine competitive advantages relative to the demands for value by the customers in the firm's competitive position.

Analysis of Firm's Competition Resources and Advantages

- Define the characteristics of resources and advantages available to the firm, which can be categorized as one of the following:
  - Tangible or intangible resources
  - Competitive advantages
  - Competitive capabilities
  - Sustainable competitive advantages and capabilities
  - Core competencies
- Define the quality of the resources and advantages available to the firm, which should be done simultaneously with the above analysis. Determine if the resources and advantages are:
  - Valuable
  - Durable
  - Rare
  - Inimitable
  - Complex

Assess the Firm's Business Model

- What are the activities in the value chain and are they quality resources to the firm as defined by the previous quality categories? It is particularly important to look at the relationship and interlinkages between activities.
- Examine the firm's supply chain both from suppliers through to the eventual buyers. How does this business model compare to other competitors' business models?

Developing New Resources and Advantages

- Benchmark similar high quality activities, advantages, and resources in other high performance companies and compare them to your own.
- Assess the resource gaps that you have as a firm. What are the resources you require to acquire, or develop, to enable you to have the competitive advantages to effectively carry out your strategy?

Additional Notes and Recommended Readings

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