

PART **1**

STRATEGIC  
MANAGEMENT  
INPUTS

**CHAPTER 3**

*The Internal Environment:  
Resources, Capabilities,  
and Core Competencies*

**Strategic Management**

*Competitiveness and Globalization:  
Concepts and Cases*

Seventh edition

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PowerPoint Presentation by Charlie Cook  
The University of West Alabama

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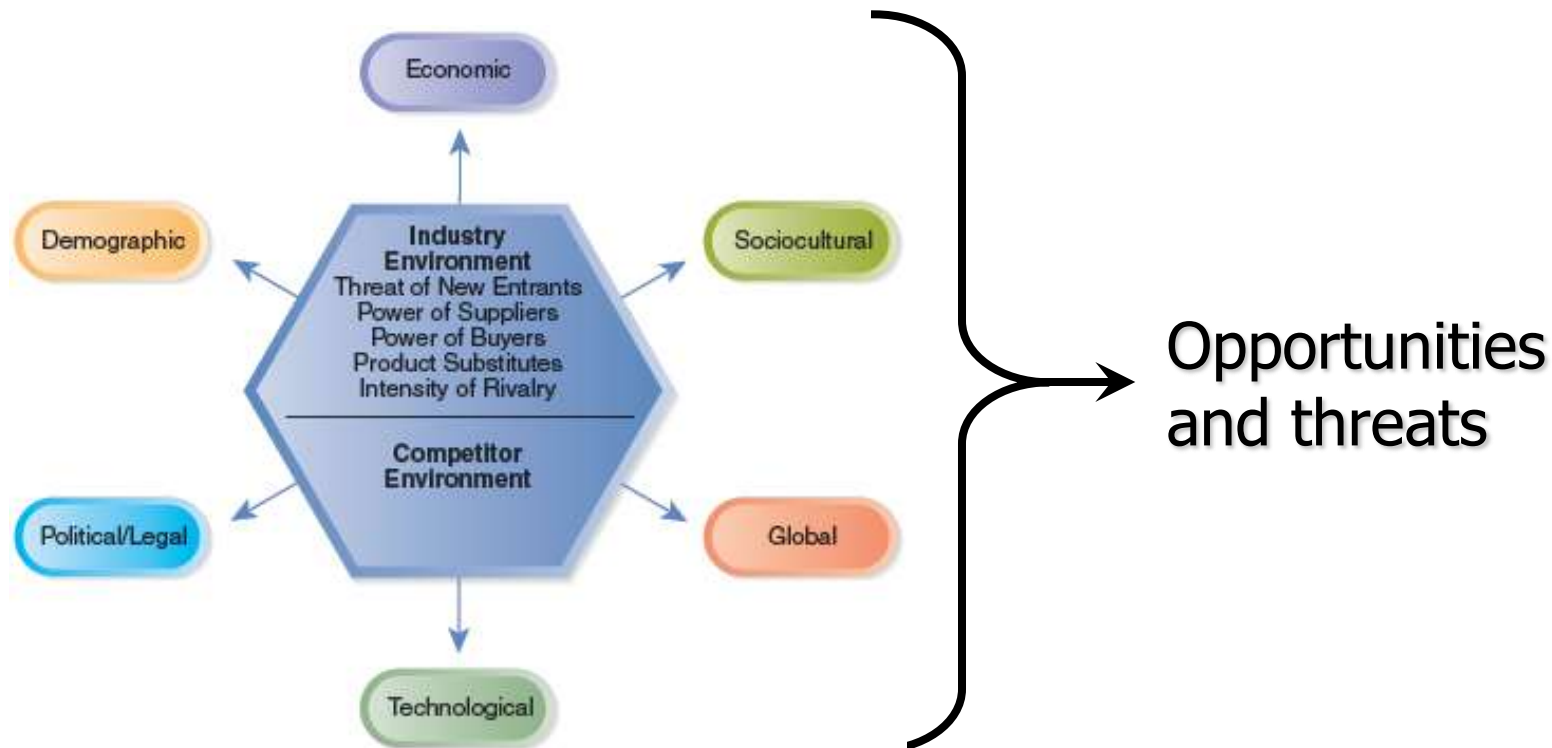
# Competitive Advantage

- Firms achieve strategic competitiveness and earn above-average returns when their core competencies are effectively:
  - Acquired.
  - Bundled.
  - Leveraged.
- Over time, the benefits of any value-creating strategy can be duplicated by competitors.

# Competitive Advantage (cont'd)

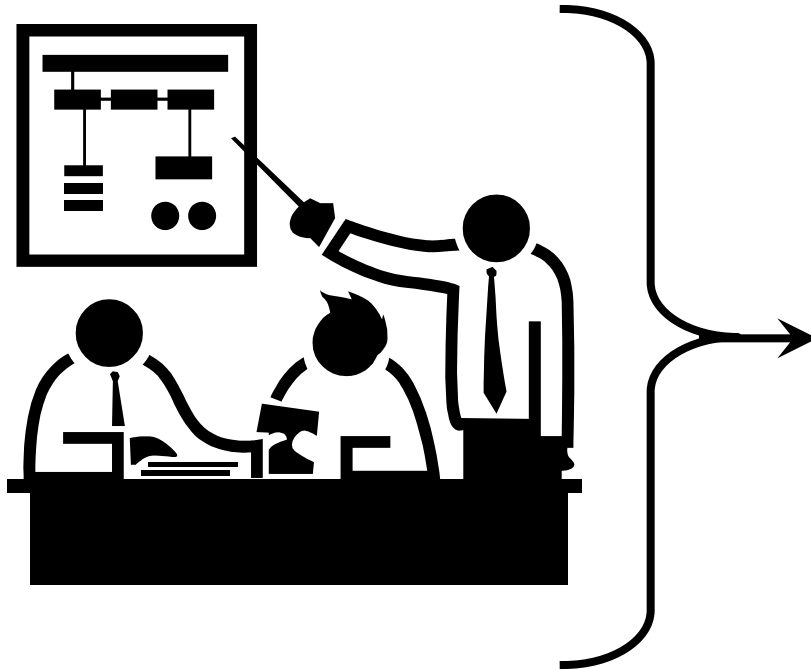
- Sustainability of a competitive advantage is a function of:
  - The rate of core competence obsolescence due to environmental changes.
  - The availability of substitutes for the core competence.
  - The difficulty competitors have in duplicating or imitating the core competence.

# External Analyses' Outcomes



By studying the external environment, firms identify what they *might choose to do*.

# Internal Analyses' Outcomes



Unique resources,  
capabilities, and  
competencies  
*(required for sustainable  
competitive advantage)*

By studying the internal environment,  
firms identify what they *can do*

# The Context of Internal Analysis

- Global Economy

- Traditional sources of advantages can be overcome by competitors' international strategies and by the flow of resources throughout the global economy.

- Global Mind-Set

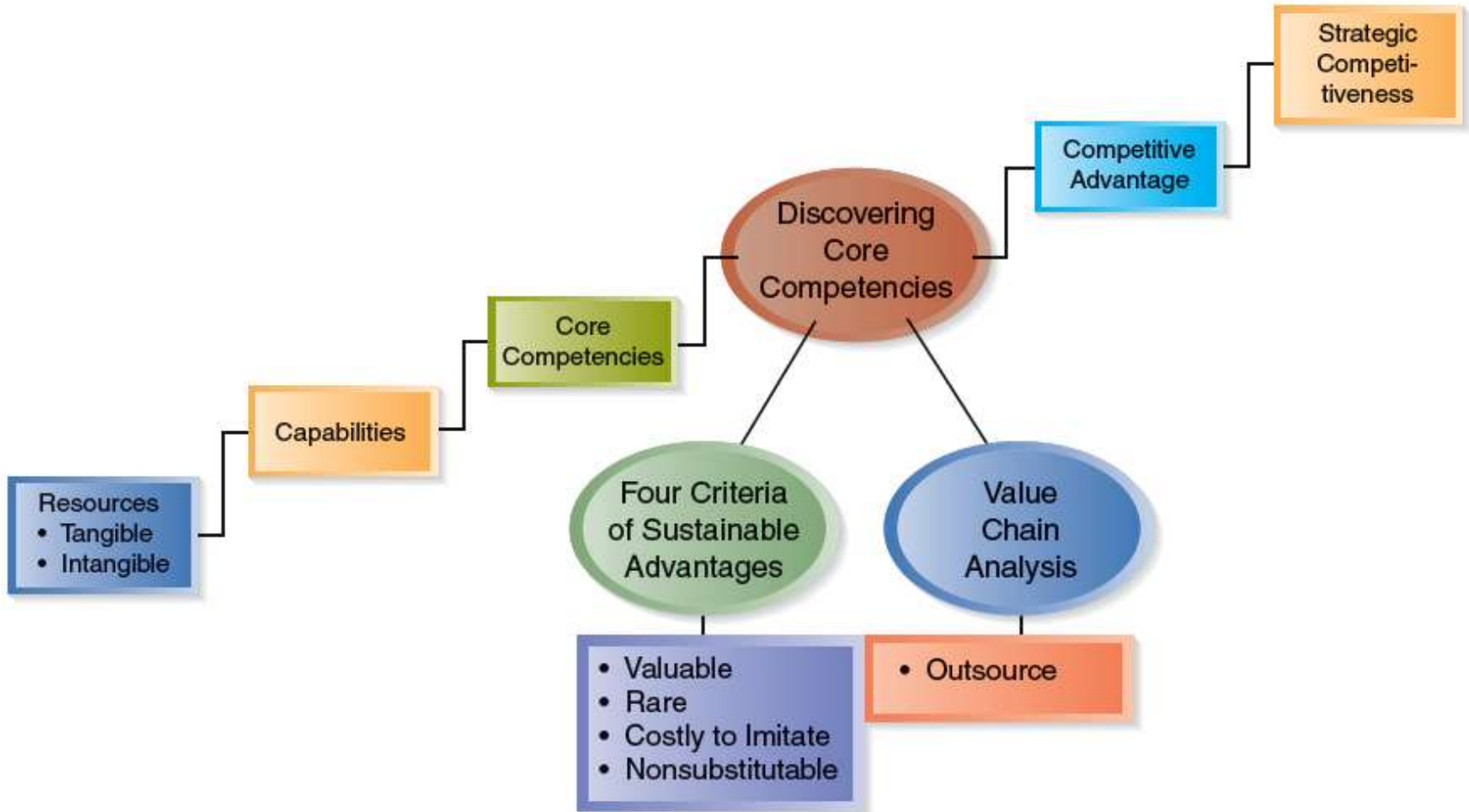
- The ability to study an internal environment in ways that are not dependent on the assumptions of a single country, culture, or context.

- Analysis Outcome

- Understanding how to leverage the firm's bundle of heterogeneous resources and capabilities.

FIGURE 3.1

## Components of Internal Analysis Leading to Competitive Advantage and Strategic Competitiveness



# Creating Value

- 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
- Firms create value by innovatively bundling and leveraging their resources and capabilities.
- Superior value → Above-average returns



# Creating Competitive Advantage

- Core competencies, in combination with product-market positions, are the firm's most important sources of competitive advantage.
- Core competencies of a firm, in addition to its analysis of its general, industry, and competitor environments, should drive its selection of strategies.

# The Challenge of Internal Analysis

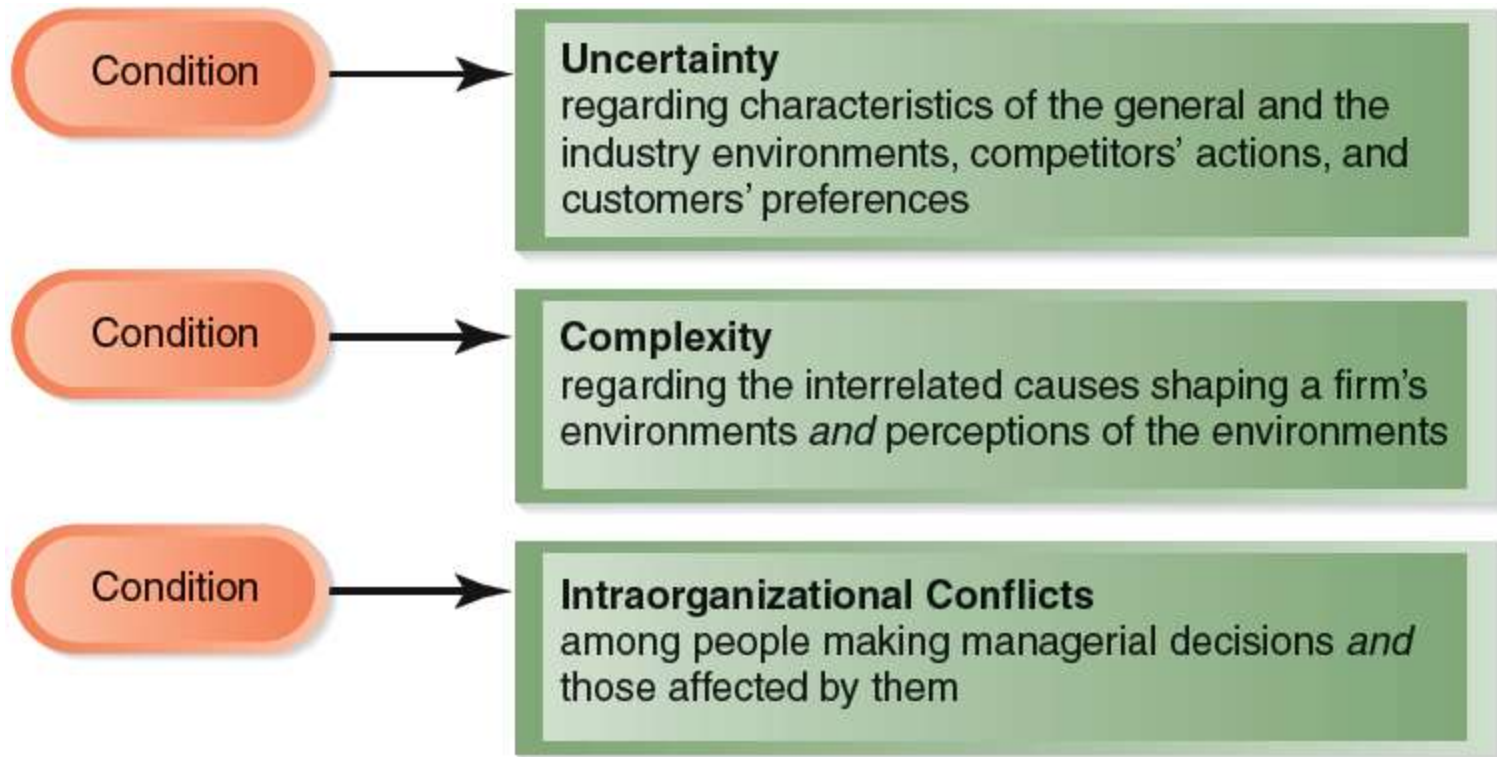
- Strategic decisions in terms of the firm's resources, capabilities, and core competencies:
  - Are non-routine.
  - Have ethical implications.
  - Significantly influence the firm's ability to earn above-average returns.

# The Challenge of Internal Analysis (cont'd)

- To develop and use core competencies, managers must have:
  - **Courage**
  - **Self-confidence**
  - **Integrity**
  - **The capacity to deal with uncertainty and complexity**
  - **A willingness to hold people (and themselves) accountable for their work**

FIGURE 3.2

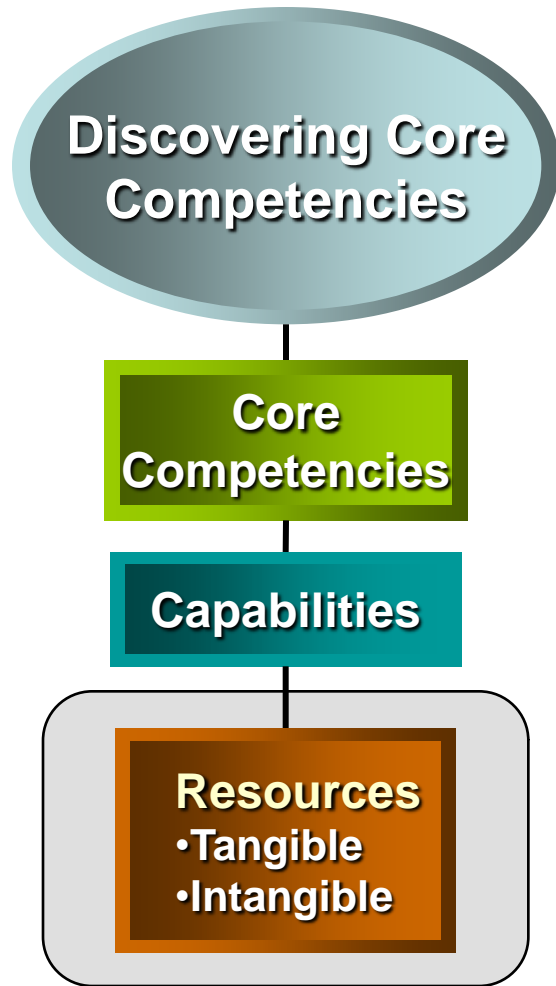
## Conditions Affecting Managerial Decisions about Resources, Capabilities, and Core Competencies



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

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# Resources, Capabilities and Core Competencies



## • Resources

- Are the source of a firm's capabilities.
- Are broad in scope.
- Cover a spectrum of individual, social and organizational phenomena.
- Alone, do not yield a competitive advantage.

# Resources

- Resources

- Are a firm's assets, including people and the value of its brand name.
- Represent inputs into a firm's production process, such as:
  - Capital equipment
  - Skills of employees
  - Brand names
  - Financial resources
  - Talented managers

- Types of Resources

- **Tangible resources**

- Financial resources
- Physical resources
- Technological resources
- Organizational resources

- **Intangible resources**

- Human resources
- Innovation resources
- Reputation resources

**TABLE 3.1**

## Tangible Resources

### **Financial Resources**

- The firm's borrowing capacity
- The firm's ability to generate internal funds

### **Organizational Resources**

- The firm's formal reporting structure and its formal planning, controlling, and coordinating systems

### **Physical Resources**

- Sophistication and location of a firm's plant and equipment
- Access to raw materials

### **Technological Resources**

- Stock of technology, such as patents, trademarks, copyrights, and 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, U.K.: Blackwell Business, 100–102.

**TABLE 3.2**

## Intangible Resources

### Human Resources

- Knowledge
- Trust
- Managerial capabilities
- Organizational routines

### Innovation Resources

- Ideas
- Scientific capabilities
- Capacity to innovate

### Reputational Resources

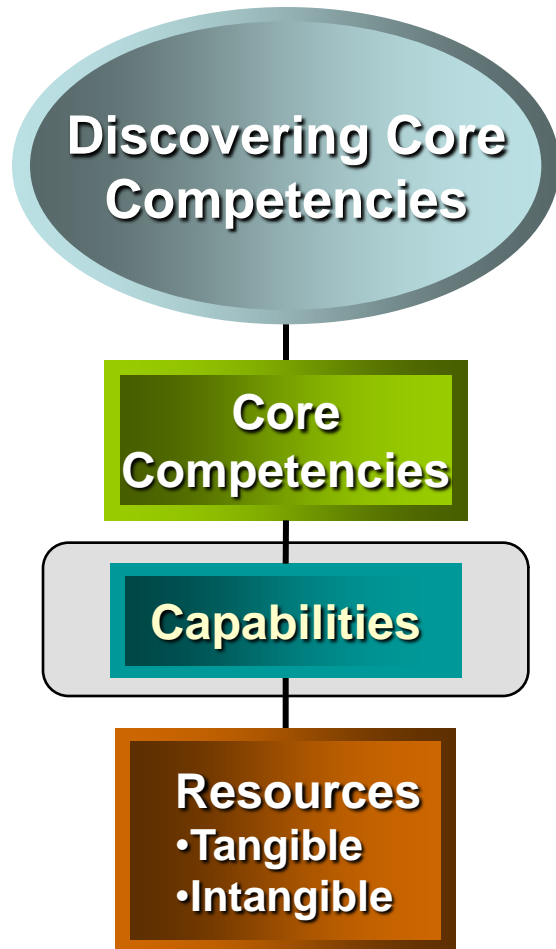
- Reputation with customers
- Brand name
- Perceptions of product quality, durability, and reliability
- Reputation with suppliers
- For efficient, effective, supportive, and mutually beneficial interactions and relationships

**Sources:** Adapted from R. Hall, 1992, The strategic analysis of intangible resources, *Strategic Management Journal*, 13: 136–139; R. M. Grant, 1991, *Contemporary Strategy Analysis*, Cambridge, U.K.: Blackwell Business, 101–104.

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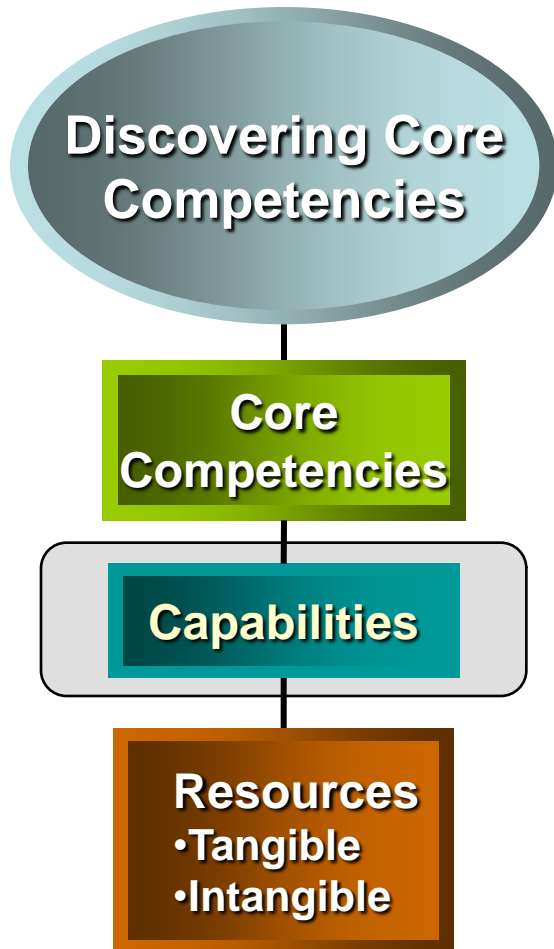
# Resources, Capabilities and Core Competencies



## • Capabilities

- Represent the capacity to deploy resources that have been purposely integrated to achieve a desired end state
- Emerge over time through complex interactions among tangible and intangible resources
- Often are based on developing, carrying and exchanging information and knowledge through the firm's human capital

# Resources, Capabilities and Core Competencies



- **Capabilities (cont'd)**
  - **The foundation of many capabilities lies in:**
    - The unique skills and knowledge of a firm's employees
    - The functional expertise of those employees
  - **Capabilities are often developed in specific functional areas or as part of a functional area.**

**TABLE 3.3****Examples of Firms' Capabilities****Functional Areas****Capabilities**

Distribution

Effective use of logistics management techniques

Human resources

Motivating, empowering, and retaining employees

Management

Effective and efficient control of inventories through

information systems

point-of-purchase data collection methods

Marketing

Effective promotion of brand-name products

Effective customer service

Innovative merchandising

Management

Ability to envision the future of clothing

Effective organizational structure

Manufacturing

Design and production skills yielding reliable products

Product and design quality

Miniaturization of components and products

Research &amp;

Innovative technology

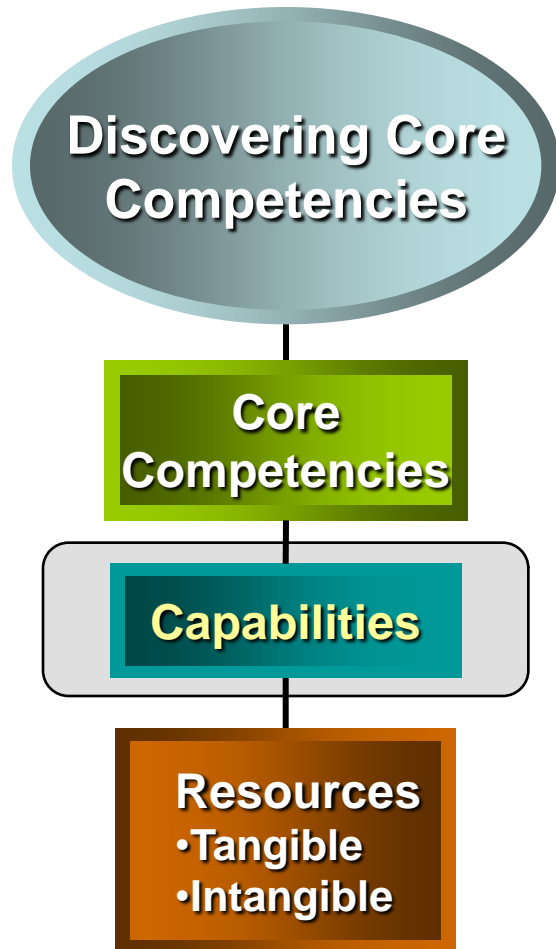
development

Development of sophisticated elevator control solutions

Rapid transformation of technology into new products and processes

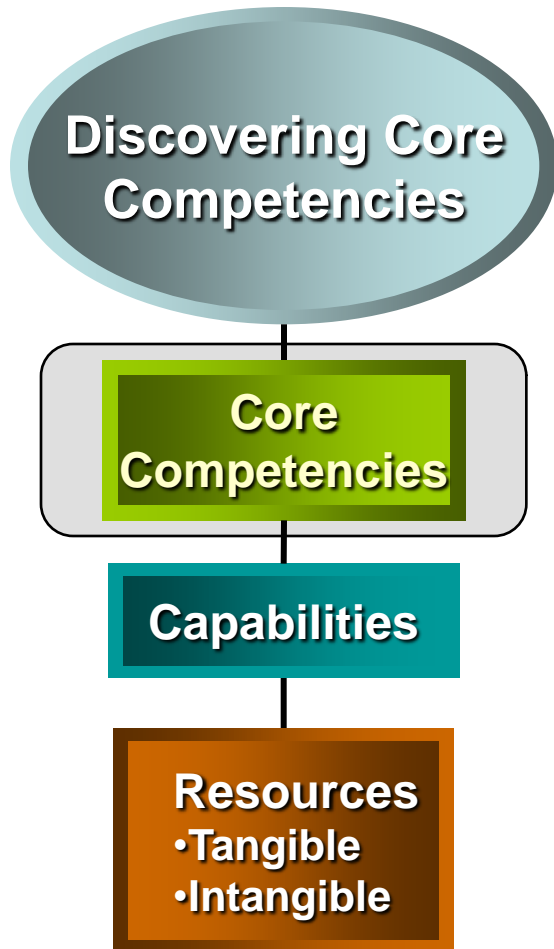
Digital technology

# Resources, Capabilities and Core Competencies



- Four criteria for determining strategic capabilities:
  - Value
  - Rarity
  - Costly-to-imitate
  - Nonsubstitutability

# Resources, Capabilities and Core Competencies

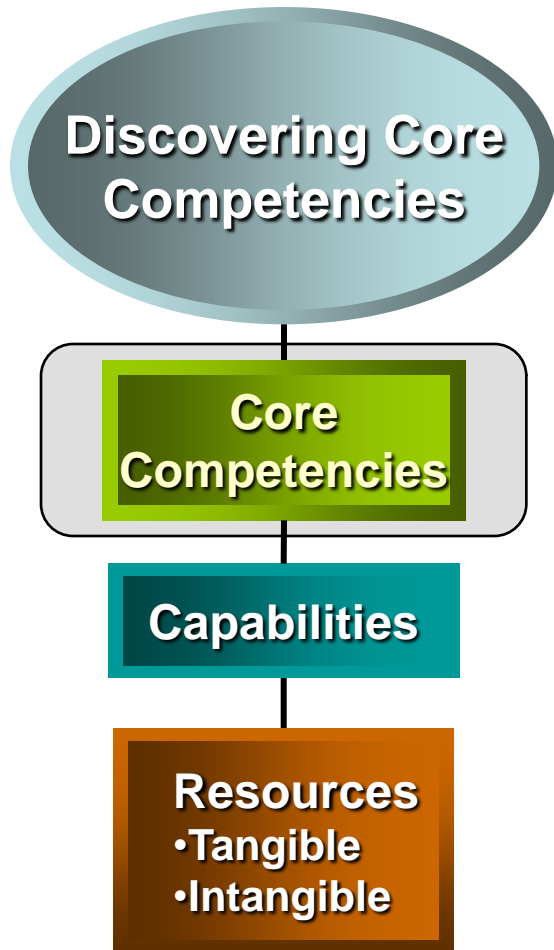


- **Core Competencies**

- **Resources and capabilities that are the sources of a firm's competitive advantage:**

- Distinguish a company competitively and reflect its personality.
- Emerge over time through an organizational process of accumulating and learning how to deploy different resources and capabilities.

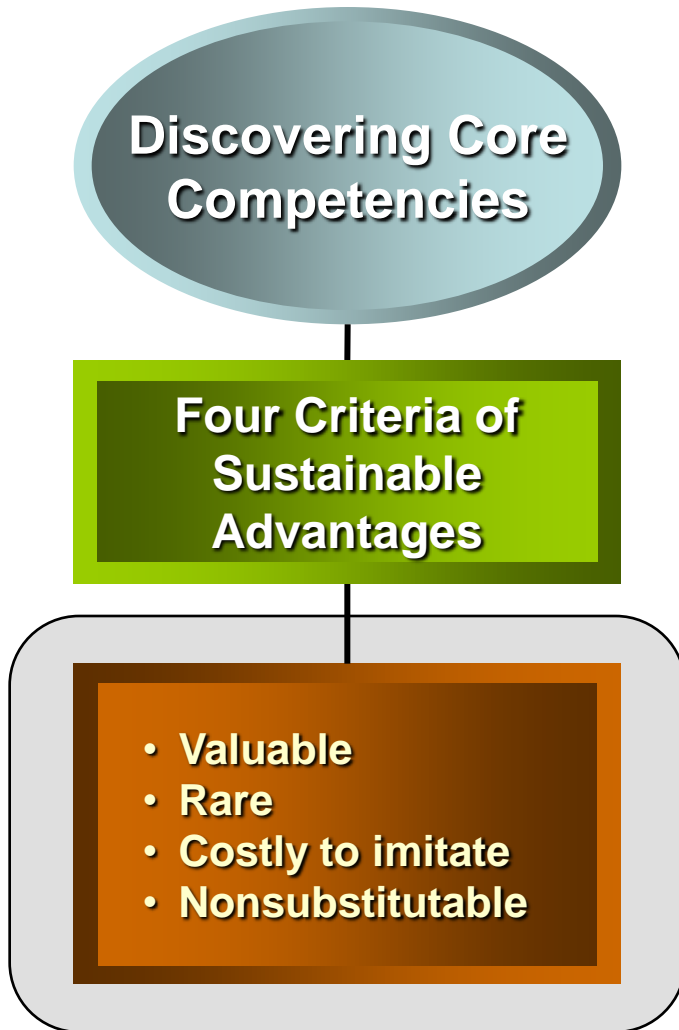
# Resources, Capabilities and Core Competencies



## • Core Competencies

- Activities that a firm performs especially well compared to competitors.
- Activities through which the firm adds unique value to its goods or services over a long period of time.

# Building Core Competencies



- Four Criteria of Sustainable Competitive Advantage

- Valuable capabilities
- Rare capabilities
- Costly to imitate
- Nonsubstitutable

**TABLE 3.4**

## The Four Criteria of Sustainable Competitive Advantage

### **Valuable Capabilities**

- Help a firm neutralize threats or exploit opportunities

### **Rare Capabilities**

- Are not possessed by many others

### **Costly-to-Imitate Capabilities**

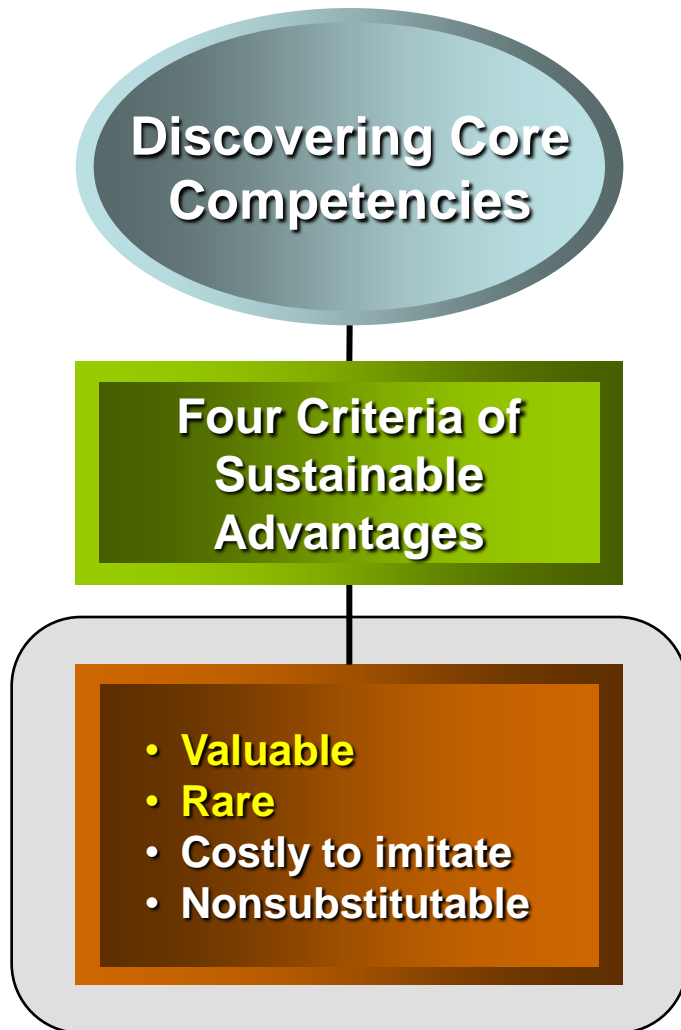
- Historical: A unique and a valuable organizational culture or brand name
- Ambiguous cause: The causes and uses of a competence are unclear
- Social complexity: Interpersonal relationships, trust, and friendship among managers, suppliers, and customers

### **Nonsubstitutable Capabilities**

- No strategic equivalent

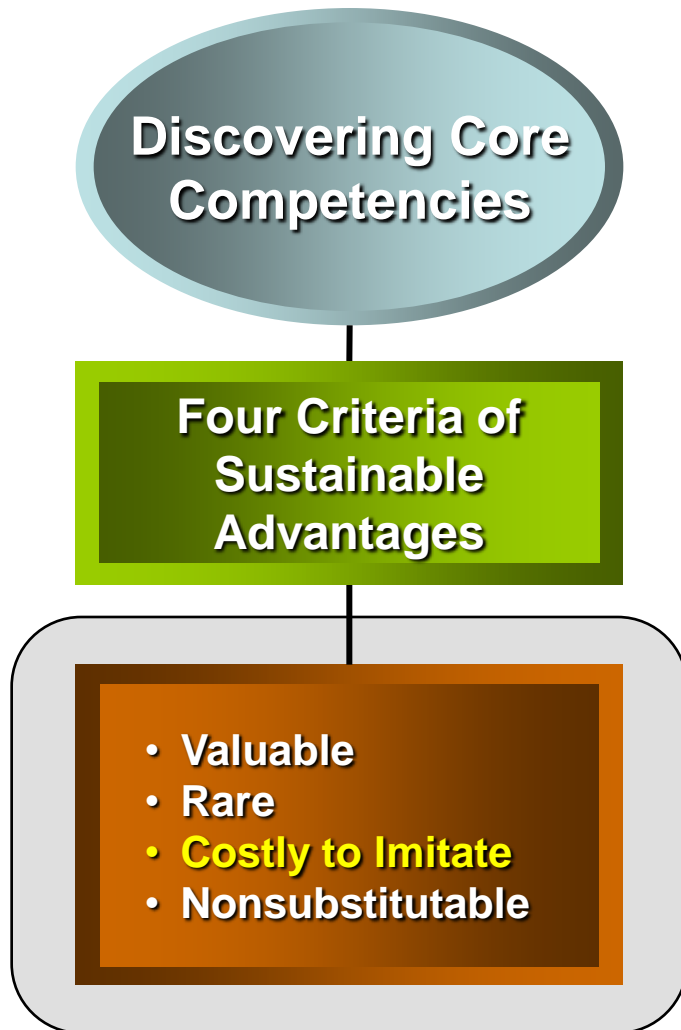


# Building Sustainable Competitive Advantage



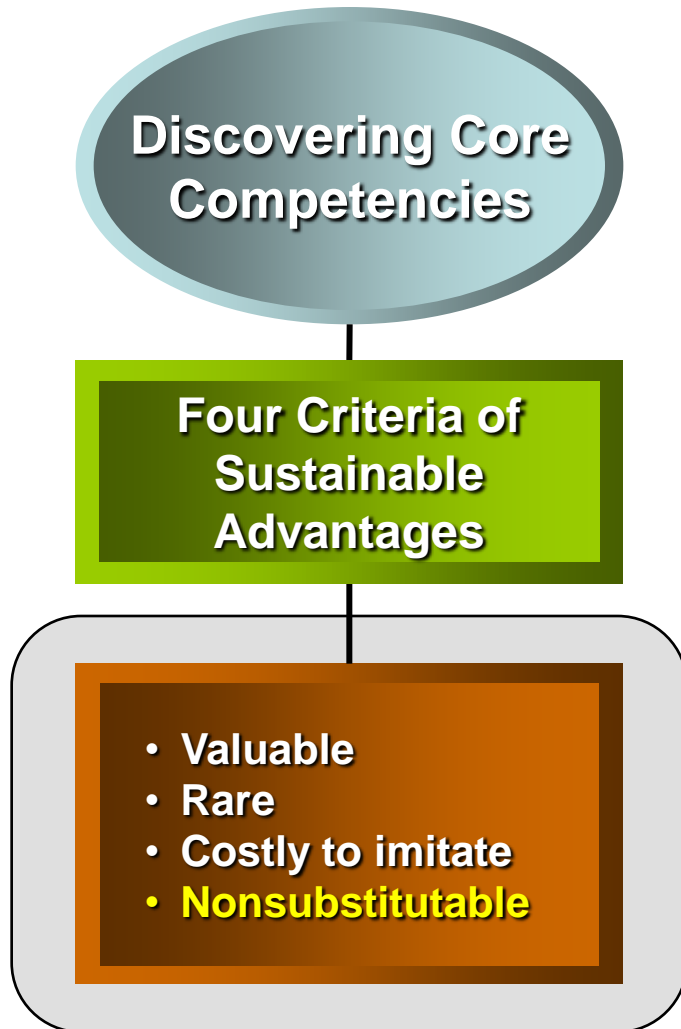
- Valuable capabilities
  - Help a firm neutralize threats or exploit opportunities.
- Rare capabilities
  - Are not possessed by many others.

# Building Sustainable Competitive Advantage



- **Costly-to-Imitate Capabilities**
  - **Historical**
    - A unique and a valuable organizational 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

# Building Sustainable Competitive Advantage



- **Nonsubstitutable Capabilities**

- **No strategic equivalent**

- Firm-specific knowledge
- Organizational culture
- Superior execution of the chosen business model

# Outcomes from Combinations of the Four Criteria

Valuable?	Rare?	Costly to Imitate?	Nonsubstitutable?	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	Above Average to Average Returns
Yes	Yes	Yes	Yes	Sustainable Competitive Advantage	Above Average Returns

**Table 3.5**

## Outcomes from Combinations of the Criteria for Sustainable Competitive Advantage

<b>Is the Resource or Capability Valuable?</b>	<b>Is the Resource or Capability Rare?</b>	<b>Is the Resource or Capability Costly to Imitate?</b>	<b>Is the Resource or Capability Nonsubstitutable?</b>	<b>Competitive Consequences</b>	<b>Performance Implications</b>
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	Sustainable competitive advantage	Above-average returns

# Value Chain Analysis

- Allows the firm to understand the parts of its operations that create value and those that do not.
- A template that firms use to:
  - Understand their cost position.
  - Identify multiple means that might be used to facilitate implementation of a chosen business-level strategy.

# Value Chain Analysis (cont'd)

- Primary activities involved with:
  - A product's physical creation
  - A product's sale and distribution to buyers
  - The product's service after the sale
- Support Activities
  - Provide the assistance necessary for the primary activities to take place.

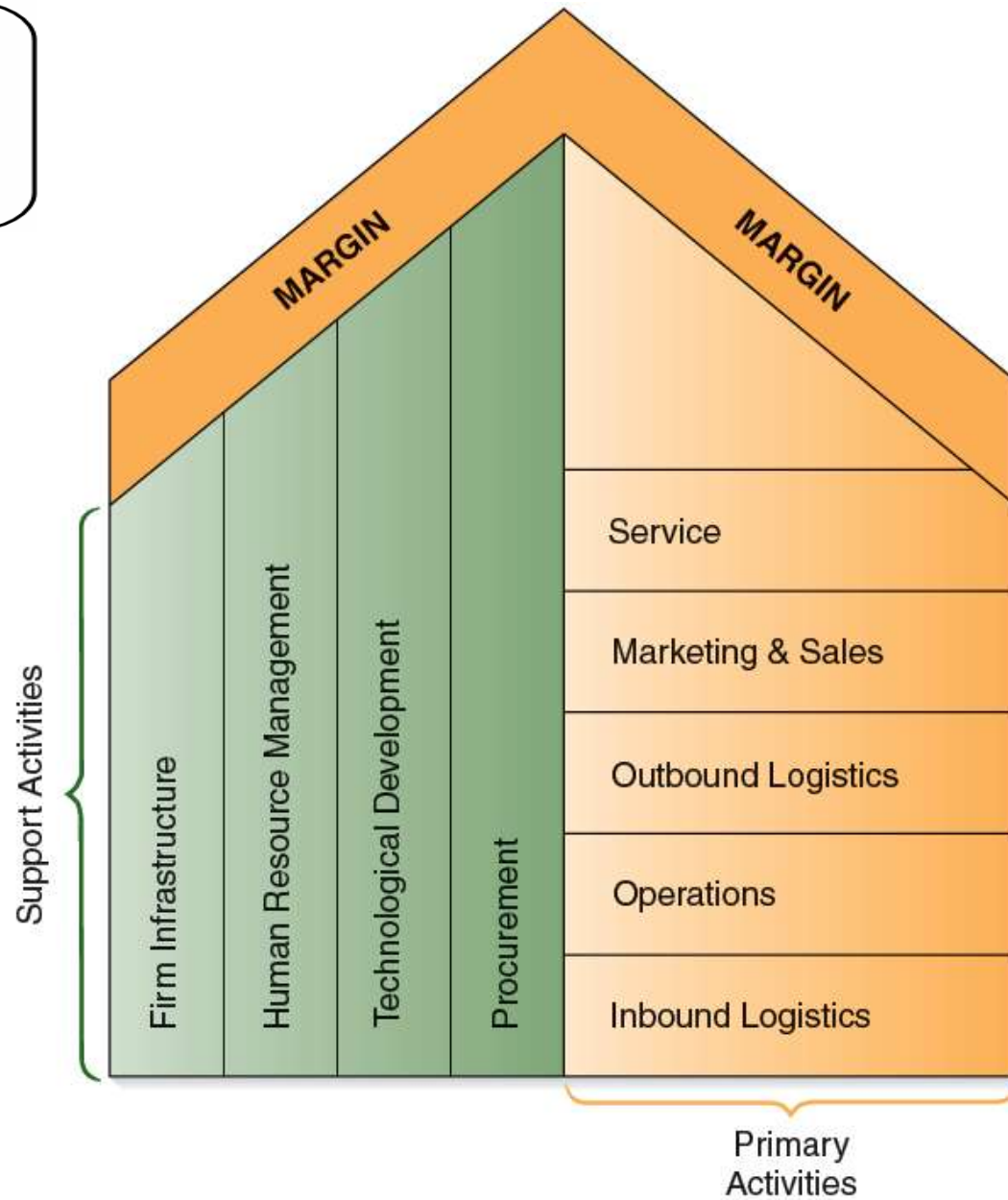
# Value Chain Analysis (cont'd)

- Value Chain
  - Shows how a product moves from the raw-material stage to the final customer.
- To be a source of competitive advantage, a resource or capability must allow the firm:
  - To perform an activity in a manner that is superior to the way competitors perform it, or
  - To perform a value-creating activity that competitors cannot complete



FIGURE 3.3

The Basic Value Chain



**Inbound Logistics**

Activities, such as materials handling, warehousing, and inventory control, used to receive, store, and disseminate inputs to a product.

**Operations**

Activities necessary to convert the inputs provided by inbound logistics into final product form. Machining, packaging, assembly, and equipment maintenance are examples of operations activities.

**Outbound Logistics**

Activities involved with collecting, storing, and physically distributing the final product to customers. Examples of these activities include finished goods warehousing, materials handling, and order processing.

**Marketing and Sales**

Activities completed to provide means through which customers can purchase products and to induce them to do so. To effectively market and sell products, firms develop advertising and promotional campaigns, select appropriate distribution channels, and select, develop, and support their sales force.

**Service**

Activities designed to enhance or maintain a product's value. Firms engage in a range of service-related activities, including installation, repair, training, and adjustment.

***Each activity should be examined relative to competitors' abilities. Accordingly, firms rate each activity as superior, equivalent, or inferior.***

### **Procurement**

Activities completed to purchase the inputs needed to produce a firm's products. Purchased inputs include items fully consumed during the manufacture of products (e.g., raw materials and supplies, as well as fixed assets—machinery, laboratory equipment, office equipment, and buildings).

### **Technological Development**

Activities completed to improve a firm's product and the processes used to manufacture it. Technological development takes many forms, such as process equipment, basic research and product design, and servicing procedures.

### **Human Resource Management**

Activities involved with recruiting, hiring, training, developing, and compensating all personnel.

### **Firm Infrastructure**

Firm infrastructure includes activities such as general management, planning, finance, accounting, legal support, and governmental relations that are required to support the work of the entire value chain. Through its infrastructure, the firm strives to effectively and consistently identify external opportunities and threats, identify resources and capabilities, and support core competencies.

**Each activity should be examined relative to competitors' abilities. Accordingly, firms rate each activity as *superior*, *equivalent*, or *inferior*.**

# The Value-Creating Potential of Primary Activities

- Inbound Logistics
  - Activities used to receive, store, and disseminate inputs to a product
- Operations
  - Activities necessary to convert the inputs provided by inbound logistics into final product form
- Outbound Logistics
  - Activities involved with collecting, storing, and physically distributing the product to customers

# The Value-Creating Potential of Primary Activities (cont'd)

- Marketing and Sales
  - Activities completed to provide the means through which customers can purchase products and to induce them to do so.
- Service
  - Activities designed to enhance or maintain a product's value
- Each activity should be examined relative to competitor's abilities and rated as superior, equivalent or inferior.

# The Value-Creating Potential of Primary Activities: Support

- Procurement
  - Activities completed to purchase the inputs needed to produce a firm's products.
- Technological Development
  - Activities completed to improve a firm's product and the processes used to manufacture it.
- Human Resource Management
  - Activities involved with recruiting, hiring, training, developing, and compensating all personnel.

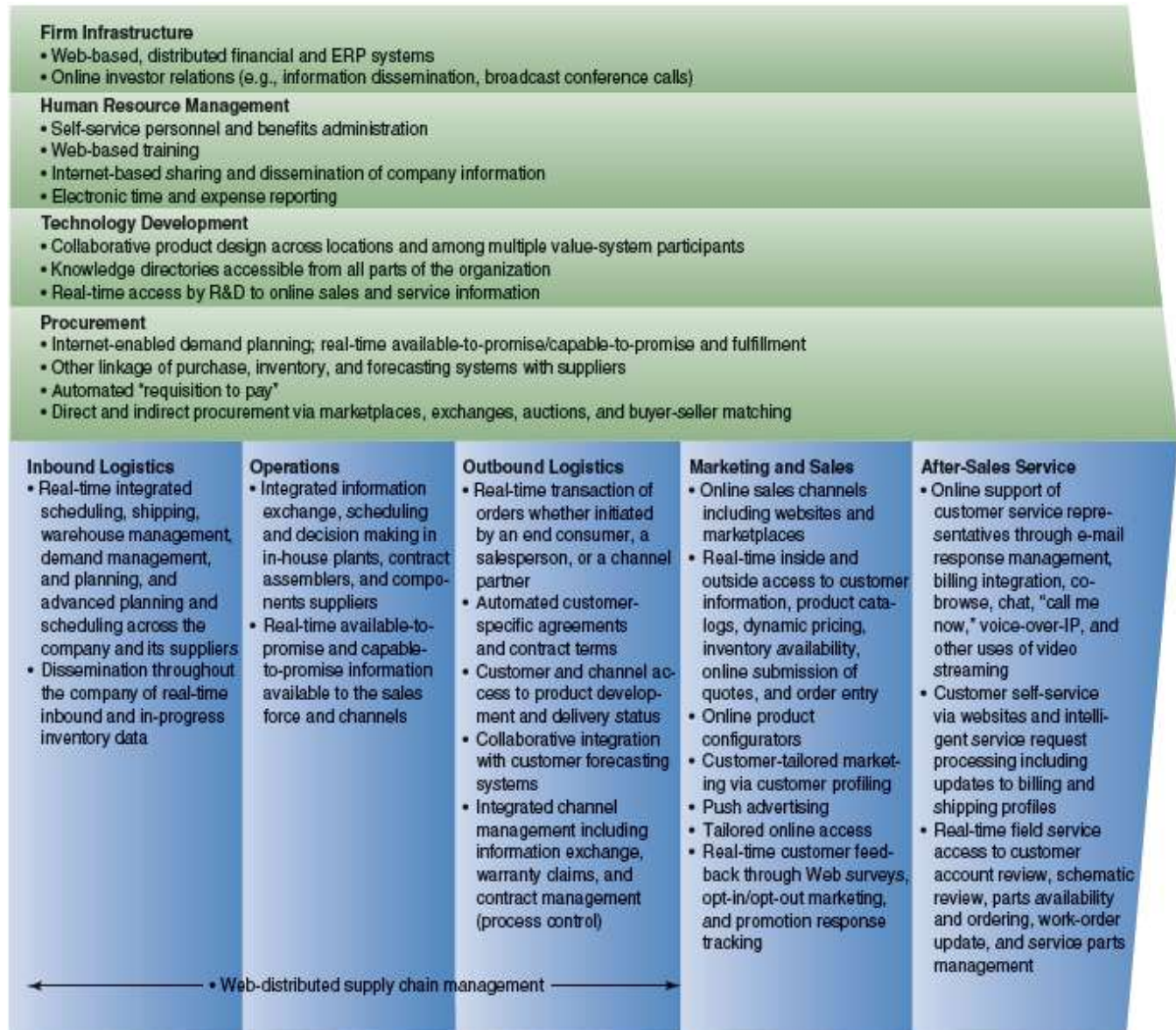
# The Value-Creating Potential of Primary Activities: Support (cont'd)

- Firm Infrastructure

- Activities that support the work of the entire value chain (general management, planning, finance, accounting, legal, government relations, etc.)
  - Effectively and consistently identify external opportunities and threats
  - Identify resources and capabilities
  - Support core competencies
- Each activity should be examined relative to competitor's abilities and rated as superior, equivalent or inferior.

Figure 3.4

## Prominent Applications of the Internet in the Value Chain



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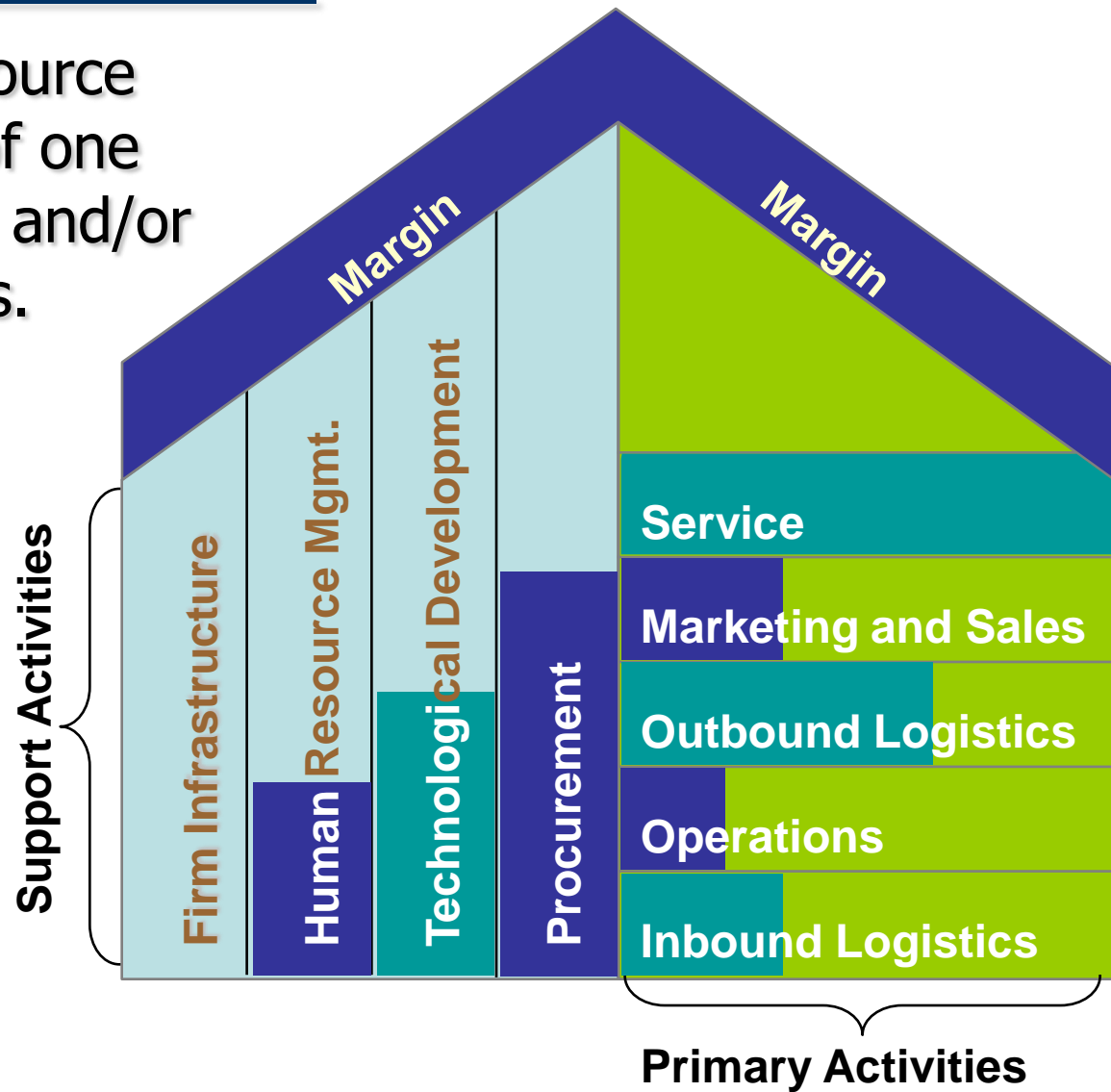


# Outsourcing

- The purchase of a value-creating activity from an external supplier
  - Few organizations possess the resources and capabilities required to achieve competitive superiority in all primary and support activities.
- By performing fewer capabilities:
  - A firm can concentrate on those areas in which it can create value.
  - Specialty suppliers can perform outsourced capabilities more efficiently.

# Outsourcing Decisions

A firm may outsource all or only part of one or more primary and/or support activities.



# Strategic Rationales for Outsourcing

- Improving business focus
  - Helps a company focus on broader business issues by having outside experts handle various operational details.
- Providing access to world-class capabilities
  - The specialized resources of outsourcing providers makes world-class capabilities available to firms in a wide range of applications.

# Strategic Rationales for Outsourcing (cont'd)

- Accelerating re-engineering benefits
  - Achieves re-engineering benefits more quickly by having outsiders—who have already achieved world-class standards—take over process.
- Sharing risks
  - Reduces investment requirements and makes firm more flexible, dynamic and better able to adapt to changing opportunities.
- Freeing resources for other purposes
  - Redirects efforts from non-core activities toward those that serve customers more effectively.

# Outsourcing Issues

- Seeking greatest value
  - Outsource only to firms possessing a core competence in terms of performing the primary or supporting the outsourced activity.
- Evaluating resources and capabilities
  - **Do not** outsource activities in which the firm itself can create and capture value.
- Environmental threats and ongoing tasks
  - **Do not** outsource primary and support activities that are used to neutralize environmental threats or to complete necessary ongoing organizational tasks.

# Outsourcing Issues (cont'd)

- Nonstrategic team resources
  - **Do not** outsource capabilities critical to the firm's success, even though the capabilities are not actual sources of competitive advantage.
- Firm's knowledge base
  - **Do not** outsource activities that stimulate the development of new capabilities and competencies.

# Cautions and Reminders

- Never take for granted that core competencies will continue to provide a source of competitive advantage.
- All core competencies have the potential to become **core rigidities**—former core competencies that now generate inertia and stifle innovation.
- Determining what the firm can do through continuous and effective analyses of its internal environment will increase the likelihood of long-term competitive success.