chapter 4

Evaluating a Company's Resources, Capabilities, and Competitiveness

LEARNING OBJECTIVES

LO1 Learn how to assess how well a company's strategy is working.

LO2 Understand why a company's resources and capabilities are central to its strategic approach and how to evaluate their potential for giving the company a competitive edge over rivals.

LO3 Grasp how a company's value chain activities can affect the company's cost structure and customer value proposition.

LO4 Learn how to evaluate a company's competitive strength relative to key rivals.

LO5 Understand how a comprehensive evaluation of a company's external and internal situations can assist managers in making critical decisions about their next strategic moves.

Chapter 3 described how to use the tools of industry and competitive analysis to assess a company's external environment and lay the groundwork for matching a company's strategy to its external situation. This chapter discusses the techniques of evaluating a company's internal situation, including its collection of resources and capabilities, its cost structure and customer value proposition, and its competitive strength versus that of its rivals. The analytical spotlight will be trained on five questions:

1. How well is the company's strategy working?
2. What are the company's competitively important resources and capabilities?
3. Are the company's cost structure and customer value proposition competitive?
4. Is the company competitively stronger or weaker than key rivals?
5. What strategic issues and problems merit front-burner managerial attention?

The answers to these five questions complete management's understanding of the company's overall situation and position the company for a good strategy-situation fit required by the "The Three Tests of a Winning Strategy" (see Chapter 1).

LO1 Learn how to assess how well a company's strategy is working.

Question 1: How Well Is the Company's Strategy Working?

The two best indicators of how well a company's strategy is working are (1) whether the company is recording gains in financial strength and profitability, and (2) whether the company's competitive strength and market standing are improving. Persistent shortfalls in meeting company financial performance targets and weak performance relative to rivals are reliable warning signs that the company suffers from poor strategy making, less-than-competent strategy execution, or both. Other indicators of how well a company's strategy is working include:

- Trends in the company's sales and earnings growth.
- Trends in the company's stock price.
- The company's overall financial strength.
- The company's customer retention rate.
- The rate at which new customers are acquired.
- Changes in the company's image and reputation with customers.
- Evidence of improvement in internal processes such as defect rate, order fulfillment, delivery times, days of inventory, and employee productivity.

The stronger a company's current overall performance, the less likely the need for radical changes in strategy. The weaker a company's financial performance and market standing, the more its current strategy must be questioned. (A compilation of financial ratios most commonly used to evaluate a company's financial performance and balance sheet strength is presented in the Appendix.)

Question 2: What Are the Company's Competitively Important Resources and Capabilities?

LO2 Understand why a company's resources and capabilities are central to its strategic approach and how to evaluate their potential for giving the company a competitive edge over rivals.

As discussed in Chapter 1, a company's business model and strategy must be well matched to its collection of resources and capabilities. An attempt to create and deliver customer value in a manner that depends on resources or capabilities that are deficient and cannot be readily acquired or developed is unwise and positions the company for failure. A company's competitive approach requires a tight fit with a company's internal situation and is strengthened when it exploits resources that are competitively valuable, rare, hard to copy, and not easily trumped by rivals' substitute resources. In addition, long-term competitive advantage requires the ongoing development and expansion of resources and capabilities to pursue emerging market opportunities and defend against future threats to its market standing and profitability.[1]

Sizing up the company's collection of resources and capabilities and determining whether they can provide the foundation for competitive success can be achieved through **resource and capability analysis.** This is a two-step process: (1) identify the company's resources and capabilities, and (2) examine them more closely to ascertain which are the most competitively important and whether they can support a sustainable competitive advantage over rival firms.[2] This second step involves applying the *four tests of a resource's competitive power.*

Identifying Competitively Important Resources and Capabilities

A company's **resources** are competitive assets that are owned or controlled by the company and may either be *tangible resources* such as plants, distribution centers, manufacturing equipment, patents, information systems, and capital reserves or creditworthiness, or *intangible assets* such as a well-known brand or a results-oriented organizational culture. Table 4.1 lists the common types of tangible and intangible resources that a company may possess.

CORE CONCEPT

A **resource** is a competitive asset that is owned or controlled by a company; a **capability** is the capacity of a company to competently perform some internal activity. Capabilities are developed and enabled through the deployment of a company's resources.

A **capability** is the capacity of a firm to competently perform some internal activity. A capability may also be referred to as a **competence.** Capabilities or competences also vary in form, quality, and competitive importance, with some being more competitively valuable than others. *Organizational capabilities are developed and enabled through the deployment of a company's resources or some combination of its resources.*[3] Some capabilities rely heavily on a company's intangible resources such as human assets and intellectual capital. For example, Nestlé's brand management capabilities for its 2,000+ food, beverage, and pet care brands draw upon the knowledge of the company's brand managers, the expertise of its marketing department, and the company's relationships with retailers in nearly 200 countries. W. L. Gore's product innovation capabilities in its fabrics, medical, and industrial products businesses result from the personal initiative, creative talents, and technological expertise of its associates and the company's culture that encourages accountability and creative thinking.

TABLE 4.1

Common Types of Tangible and Intangible Resources

Tangible Resources

- *Physical resources*—state-of-the-art manufacturing plants and equipment, efficient distribution facilities, attractive real estate locations, or ownership of valuable natural resource deposits
- *Financial resources*—cash and cash equivalents, marketable securities, and other financial assets such as a company's credit rating and borrowing capacity
- *Technological assets*—patents, copyrights, superior production technology, and technologies that enable activities
- *Organizational resources*—information and communication systems (servers, workstations, etc.), proven quality control systems, and a strong network of distributors or retail dealers

Intangible Resources

- *Human assets and intellectual capital*—an experienced and capable workforce, talented employees in key areas, collective learning embedded in the organization, or proven managerial know-how
- *Brand, image, and reputational assets*—brand names, trademarks, product or company image, buyer loyalty, and reputation for quality, superior service
- *Relationships*—alliances or joint ventures that provide access to technologies, specialized know-how, or geographic markets, and trust established with various partners
- *Company culture*—the norms of behavior, business principles, and ingrained beliefs within the company

Determining the Competitive Power of a Company's Resources and Capabilities

What is most telling about a company's aggregation of resources and capabilities is how powerful they are in the marketplace. The competitive power of a resource or capability is measured by how many of four tests for sustainable competitive advantage it can pass.[4]

CORE CONCEPT

The **VRIN tests for sustainable competitive advantage** ask if a resource or capability is *valuable, rare, inimitable,* and *nonsubstitutable.*

The tests are often referred to as the **VRIN tests for sustainable competitive advantage**—an acronym for *valuable, rare, inimitable,* and *nonsubstitutable.* The first two tests determine whether the resource or capability may contribute to a competitive advantage. The last two determine the degree to which the competitive advantage potential can be sustained.

1. *Is the resource or capability competitively* ***valuable?*** All companies possess a collection of resources and capabilities—some have the potential to contribute to a competitive advantage, while others may not. Google has failed in converting its technological resources and software innovation capabilities into success for Google Wallet, which has incurred losses of more than $300 million. While these resources and capabilities have made Google the world's number-one search engine, they have proven to be less valuable in the mobile payments industry.

2. *Is the resource or capability **rare**—is it something rivals lack?* Resources and capabilities that are common among firms and widely available cannot be a source of competitive advantage. All makers of branded cookies and sweet snacks have valuable marketing capabilities and brands. Therefore, these skills are not rare or unique in the industry. However, the brand strength of Oreo is uncommon and has provided Kraft Foods with greater market share as well as the opportunity to benefit from brand extensions such as Reese's Peanut Butter Cup Oreo cookies and Mini Oreo cookies.
3. *Is the resource or capability **inimitable** or hard to copy?* The more difficult and more expensive it is to imitate a company's resource or capability, the more likely that it can also provide a *sustainable* competitive advantage. Resources tend to be difficult to copy when they are unique (a fantastic real estate location, patent protection), when they must be built over time (a brand name, a strategy-supportive organizational culture), and when they carry big capital requirements (a cost-effective plant to manufacture cutting-edge microprocessors). Imitation by rivals is most challenging when capabilities reflect a high level of *social complexity* (for example, a stellar team-oriented culture or unique trust-based relationships with employees, suppliers, or customers) and *causal ambiguity,* a term that signifies the hard-to-disentangle nature of complex processes such as the web of intricate activities enabling a new drug discovery.
4. *Is the resource or capability **nonsubstitutable** or is it vulnerable to the threat of substitution from different types of resources and capabilities?* Resources that are competitively valuable, rare, and costly to imitate may lose much of their ability to offer competitive advantage if rivals possess equivalent substitute resources. For example, manufacturers relying on automation to gain a cost-based advantage in production activities may find their technology-based advantage nullified by rivals' use of low-wage offshore manufacturing. Resources can contribute to a competitive advantage only when resource substitutes don't exist.

Very few firms have resources and capabilities that can pass all four tests, but those that do enjoy a sustainable competitive advantage with far greater profit potential. Walmart is a notable example, with capabilities in logistics and supply chain management that have surpassed those of its competitors for over 40 years. Lincoln Electric Company, less well known but no less notable in its achievements, has been the world leader in welding products for over 100 years as a result of its unique piecework incentive system for compensating production workers and the unsurpassed worker productivity and product quality that this system has fostered.[5]

If management determines that the company doesn't possess a resource that independently passes all four tests with high marks, it may have a **bundle of resources** that can pass the tests. Although Nike's resources dedicated to research and development, marketing research, and product design are matched relatively well by rival Adidas, its cross-functional design process allows it to set the pace for innovation in athletic apparel and footwear and consistently outperform Adidas and other rivals in the marketplace. Nike's footwear designers get ideas for new performance features from the professional athletes who endorse its products and then work alongside footwear materials researchers, consumer trend analysts, color designers, and marketers to design new models that are presented to a review committee. Nike's review committee is made up of hundreds of individuals who evaluate prototype details such

CORE CONCEPT
Companies that lack a stand-alone resource that is competitively powerful may nonetheless develop a competitive advantage through **resource bundles** that enable the superior performance of important cross-functional capabilities.

as shoe proportions and color designs, the size of the swoosh, stitching patterns, sole color and tread pattern, and insole design. About 400 models are approved by the committee each year, which are sourced from contract manufacturers and marketed in more than 180 countries. The bundling of Nike's professional endorsements, R&D activities, marketing research efforts, styling expertise, and managerial know-how has become an important source of the company's competitive advantage and has allowed it to remain number one in the athletic footwear and apparel industry for more than 20 years.

Companies lacking certain resources needed for competitive success in an industry may be able to adopt strategies directed at eroding or at least neutralizing the competitive potency of a particular rival's resources and capabilities by identifying and developing **substitute resources** to accomplish the same purpose. For example, Amazon.com lacked a big network of retail stores such as that operated by rival Barnes & Noble, but its much larger, readily accessible, and searchable book inventory—coupled with its short delivery times and free shipping on orders over $35—has proven to be more attractive to many busy consumers than visiting a big-box bookstore. In other words, Amazon carefully and consciously developed a set of competitively valuable resources that were effective substitutes for the superior tangible resources of Barnes & Noble dedicated to its 1,400 brick-and-mortar retail stores and college book stores.[6]

Rather than try to match the resources possessed by a rival company, a company may develop entirely different resources that substitute for the strengths of the rival.

The Importance of Dynamic Capabilities in Sustaining Competitive Advantage

Resources and capabilities must be continually strengthened and nurtured to sustain their competitive power and, at times, may need to be broadened and deepened to allow the company to position itself to pursue emerging market opportunities.[7] Organizational resources and capabilities that grow stale can impair competitiveness unless they are refreshed, modified, or even phased out and replaced in response to ongoing market changes and shifts in company strategy. In addition, disruptive environmental change may destroy the value of key strategic assets, turning *static* resources and capabilities "from diamonds to rust."[8] Management's organization-building challenge has two elements: (1) attending to ongoing recalibration of existing capabilities and resources, and (2) casting a watchful eye for opportunities to develop totally new capabilities for delivering better customer value and/or outcompeting rivals. Companies that know the importance of recalibrating and upgrading resources and capabilities make it a routine management function to build new resource configurations and capabilities. Such a managerial approach allows a company to prepare for market changes and pursue emerging opportunities. This ability to build and integrate new competitive assets becomes a capability in itself—a **dynamic capability.** A dynamic capability is the ability to modify, deepen, or reconfigure the company's existing resources and capabilities in response to its changing environment or market opportunities.[9]

Management at Toyota has aggressively upgraded the company's capabilities in fuel-efficient hybrid engine technology and constantly fine-tuned the famed Toyota Production System to enhance the company's already proficient capabilities in manufacturing top-quality vehicles at relatively low costs. Likewise, management at BMW developed new organizational capabilities in hybrid engine design that allowed the company to launch its highly touted i3 and i8 plug-in hybrids. Resources and capabilities can also be built and augmented through alliances and acquisitions.[10] Cisco Systems has greatly expanded its engineering capabilities and its ability to enter new product categories through frequent acquisitions. Strategic alliances are a commonly used approach to developing and reconfiguring capabilities in the biotech and pharmaceutical industries.

CORE CONCEPT
A **dynamic capability** is the ability to modify, deepen, or reconfigure the company's existing resources and capabilities in response to its changing environment or market opportunities.

A company requires a dynamically evolving portfolio of resources and capabilities in order to sustain its competitiveness and position itself to pursue future market opportunities.

Is the Company Able to Seize Market Opportunities and Nullify External Threats?

An essential element in evaluating a company's overall situation entails examining the company's resources and competitive capabilities in terms of the degree to which they enable it to pursue its best market opportunities and defend against the external threats to its future well-being. The simplest and most easily applied tool for conducting this examination is widely known as **SWOT analysis,** so named because it zeros in on a company's internal **S**trengths and **W**eaknesses, market **O**pportunities, and external **T**hreats. *A company's internal strengths should always serve as the basis of its strategy—placing heavy reliance on a company's best competitive assets is the soundest route to attracting customers and competing successfully against rivals.*[11] As a rule, strategies that place heavy demands on areas where the company is weakest or has unproven competencies should be avoided. Plainly, managers must look toward correcting competitive weaknesses that make the company vulnerable, hold down profitability, or disqualify it from pursuing an attractive opportunity. Furthermore, a company's strategy should be aimed squarely at capturing those market opportunities that are most attractive and suited to the company's collection of capabilities. How much attention to devote to defending against external threats to the company's future performance hinges on how vulnerable the company is, whether defensive moves can be taken to lessen their impact, and whether the costs of undertaking such moves represent the best use of company resources. A first-rate SWOT analysis provides the basis for crafting a strategy that capitalizes on the company's strengths, aims squarely at capturing the company's best opportunities, and defends against the threats to its well-being. Table 4.2 lists the kinds of factors to consider in compiling a company's resource strengths and weaknesses.

CORE CONCEPT
SWOT analysis is a simple but powerful tool for sizing up a company's internal strengths and competitive deficiencies, its market opportunities, and the external threats to its future well-being.

Basing a company's strategy on its strengths resulting from most competitively valuable resources and capabilities gives the company its best chance for market success.

TABLE 4.2

Factors to Consider When Identifying a Company's Strengths, Weaknesses, Opportunities, and Threats

Potential Internal Strengths and Competitive Capabilities

- Core competencies in _____
- A strong financial condition; ample financial resources to grow the business
- Strong brand-name image/company reputation
- Economies of scale and/or learning and experience curve advantages over rivals
- Proprietary technology/superior technological skills/important patents
- Cost advantages over rivals
- Product innovation capabilities
- Proven capabilities in improving production processes
- Good supply chain management capabilities
- Good customer service capabilities
- Better product quality relative to rivals
- Wide geographic coverage and/or strong global distribution capability
- Alliances/joint ventures with other firms that provide access to valuable technology, competencies, and/or attractive geographic markets

Potential Internal Weaknesses and Competitive Deficiencies

- No clear strategic direction
- No well-developed or proven core competencies
- A weak balance sheet; burdened with too much debt
- Higher overall unit costs relative to key competitors
- A product/service with features and attributes that are inferior to those of rivals
- Too narrow a product line relative to rivals
- Weak brand image or reputation
- Weaker dealer network than key rivals
- Behind on product quality, R&D, and/or technological know-how
- Lack of management depth
- Short on financial resources to grow the business and pursue promising initiatives

Potential Market Opportunities

- Serving additional customer groups or market segments
- Expanding into new geographic markets
- Expanding the company's product line to meet a broader range of customer needs
- Utilizing existing company skills or technological know-how to enter new product lines or new businesses
- Falling trade barriers in attractive foreign markets
- Acquiring rival firms or companies with attractive technological expertise or capabilities

Potential External Threats to a Company's Future Prospects

- Increasing intensity of competition among industry rivals—may squeeze profit margins
- Slowdowns in market growth
- Likely entry of potent new competitors
- Growing bargaining power of customers or suppliers
- A shift in buyer needs and tastes away from the industry's product
- Adverse demographic changes that threaten to curtail demand for the industry's product
- Vulnerability to unfavorable industry driving forces
- Restrictive trade policies on the part of foreign governments
- Costly new regulatory requirements

The Value of a SWOT Analysis A SWOT analysis involves more than making four lists. The most important parts of SWOT analysis are:

1. Drawing conclusions from the SWOT listings about the company's overall situation.
2. Translating these conclusions into strategic actions to better match the company's strategy to its strengths and market opportunities, correcting problematic weaknesses, and defending against worrisome external threats.

Simply listing a company's strengths, weaknesses, opportunities, and threats is not enough; the payoff from SWOT analysis comes from the conclusions about a company's situation and the implications for strategy improvement that flow from the four lists.

Question 3: Are the Company's Cost Structure and Customer Value Proposition Competitive?

LO3 Grasp how a company's value chain activities can affect the company's cost structure and customer value proposition.

Company managers are often stunned when a competitor cuts its prices to "unbelievably low" levels or when a new market entrant comes on strong with a great new product offered at a surprisingly low price. Such competitors may not, however, be buying market positions with prices that are below costs. They may simply have substantially lower costs and therefore are able to offer prices that result in more appealing customer value propositions. One of the most telling signs of whether a company's business position is strong or precarious is whether its cost structure and customer value proposition are competitive with those of industry rivals.

Cost comparisons are especially critical in industries where price competition is typically the ruling market force. But even in industries where products are differentiated, rival companies have to keep their costs in line with rivals offering value propositions based upon a similar mix of differentiating features. But a company must also remain competitive in terms of its customer value proposition. Tiffany's value proposition, for example, remains attractive to people who want customer service, the assurance of quality, and a high-status brand despite the availability of cut-rate diamond jewelry online. Target's customer value proposition has withstood the Walmart low-price juggernaut by attention to product design, image, and attractive store layouts in addition to efficiency. The key for managers is to keep close track of how *cost effectively* the company can deliver value to customers relative to its competitors. *If the company can deliver the same amount of value with lower expenditures (or more value at a similar cost), it will maintain a competitive edge.* Two analytical tools are particularly useful in determining whether a company's value proposition and costs are competitive: value chain analysis and benchmarking.

Competitive advantage hinges on how cost effectively a company can execute its customer value proposition.

Company Value Chains

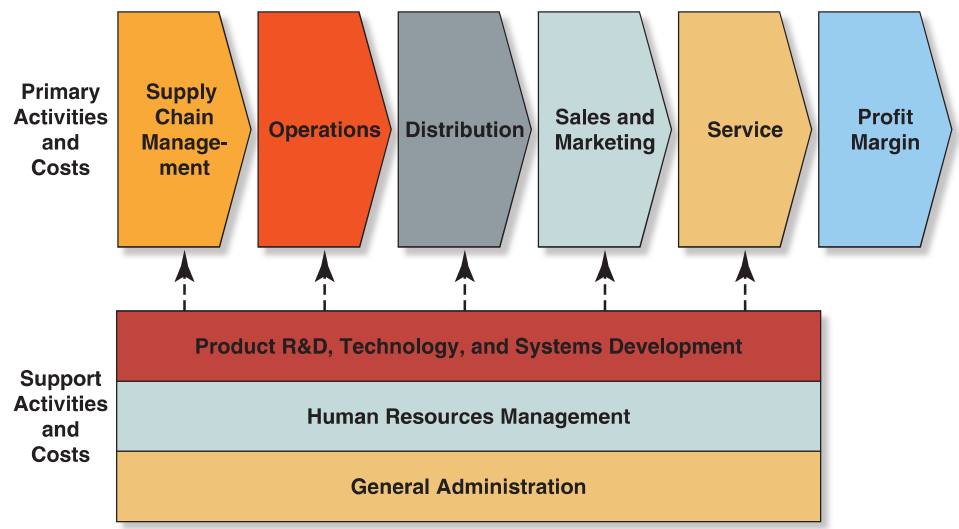
Every company's business consists of a collection of activities undertaken in the course of designing, producing, marketing, delivering, and supporting its product or service. All of the various activities that a company performs internally combine to form a **value chain,** so called because the underlying intent of a company's activities is to do things that ultimately *create value for buyers.*

CORE CONCEPT

A company's **value chain** identifies the primary activities that create customer value and related support activities.

As shown in Figure 4.1, a company's value chain consists of two broad categories of activities that drive costs and create customer value: the *primary activities* that are foremost in creating value for customers and the requisite *support activities* that facilitate and enhance the performance of the primary activities.[12] For example, the primary

FIGURE 4.1 **A Representative Company Value Chain**



PRIMARY ACTIVITIES

- **Supply Chain Management—**Activities, costs, and assets associated with purchasing fuel, energy, raw materials, parts and components, merchandise, and consumable items from vendors; receiving, storing, and disseminating inputs from suppliers; inspection; and inventory management.
- **Operations—**Activities, costs, and assets associated with converting inputs into final product form (production, assembly, packaging, equipment maintenance, facilities, operations, quality assurance, environmental protection).
- **Distribution—**Activities, costs, and assets dealing with physically distributing the product to buyers (finished goods warehousing, order processing, order picking and packing, shipping, delivery vehicle operations, establishing and maintaining a network of dealers and distributors).
- **Sales and Marketing—**Activities, costs, and assets related to sales force efforts, advertising and promotion, market research and planning, and dealer/distributor support.
- **Service—**Activities, costs, and assets associated with providing assistance to buyers, such as installation, spare parts delivery, maintenance and repair, technical assistance, buyer inquiries, and complaints.

SUPPORT ACTIVITIES

- **Product R&D, Technology, and Systems Development—**Activities, costs, and assets relating to product R&D, process R&D, process design improvement, equipment design, computer software development, telecommunications systems, computer-assisted design and engineering, database capabilities, and development of computerized support systems.
- **Human Resources Management—**Activities, costs, and assets associated with the recruitment, hiring, training, development, and compensation of all types of personnel; labor relations activities; and development of knowledge-based skills and core competencies.
- **General Administration—**Activities, costs, and assets relating to general management, accounting and finance, legal and regulatory affairs, safety and security, management information systems, forming strategic alliances and collaborating with strategic partners, and other "overhead" functions.

Source: Based on the discussion in Michael E. Porter, *Competitive Advantage* (New York: Free Press, 1985), pp. 37–43.

activities and cost drivers for a big-box retailer such as Target include merchandise selection and buying, store layout and product display, advertising, and customer service; its support activities that affect customer value and costs include site selection, hiring and training, store maintenance, plus the usual assortment of administrative activities. A hotel chain's primary activities and costs are mainly comprised of reservations and hotel operations (check-in and check-out, maintenance and housekeeping, dining and room service, and conventions and meetings); principal support activities that drive costs and impact customer value include accounting, hiring and training hotel staff, and general administration. Supply chain management is a crucial activity for Kroger or Amazon.com but is not a value chain component at LinkedIn or DirectTV. Sales and marketing are dominant activities at Procter & Gamble and GAP but have minor roles at oil-drilling companies and natural gas pipeline companies. With its focus on value-creating activities, the value chain is an ideal tool for examining how a company delivers on its customer value proposition. It permits a deep look at the company's cost structure and ability to offer low prices. It reveals the emphasis that a company places on activities that enhance differentiation and support higher prices, such as service and marketing.

The value chain also includes a profit margin component; profits are necessary to compensate the company's owners/shareholders and investors, who bear risks and provide capital. Tracking the profit margin along with the value-creating activities is critical because unless an enterprise succeeds in delivering customer value profitably (with a sufficient return on invested capital), it can't survive for long. Attention to a company's profit formula in addition to its customer value proposition is the essence of a sound business model, as described in Chapter 1. Concepts & Connections 4.1 shows representative costs for various activities performed by American Giant, a maker of high-quality sweatshirts, in its U.S. plants versus the various costs incurred by sweatshirt producers in Asia.

Benchmarking: A Tool for Assessing Whether a Company's Value Chain Activities Are Competitive

Benchmarking entails comparing how different companies perform various value chain activities—how materials are purchased, how inventories are managed, how products are assembled, how customer orders are filled and shipped, and how maintenance is performed—and then making cross-company comparisons of the costs and effectiveness of these activities.[13] The objectives of benchmarking are to identify the best practices in performing an activity and to emulate those best practices when they are possessed by others.

> **CORE CONCEPT**
> **Benchmarking** is a potent tool for learning which companies are best at performing particular activities and then using their techniques (or "best practices") to improve the cost and effectiveness of a company's own internal activities.

Xerox led the way in the use of benchmarking to become more cost-competitive by deciding not to restrict its benchmarking efforts to its office equipment rivals, but by comparing itself to *any company* regarded as "world class" in performing activities relevant to Xerox's business. Other companies quickly picked up on Xerox's approach. Toyota managers got their idea for just-in-time inventory deliveries by studying how U.S. supermarkets replenished their shelves. Southwest Airlines reduced the turnaround time of its aircraft at each scheduled stop by studying pit crews on the

Concepts & Connections 4.1

AMERICAN GIANT: USING THE VALUE CHAIN TO COMPARE COSTS OF PRODUCING A HOODIE IN THE UNITED STATES AND ASIA

American Giant Clothing Company claims to make the world's best hooded sweatshirt, and it makes them in American plants, despite the higher cost of U.S production, as shown in the accompanying table. Why is this a good choice for the company? Because costs are not the only thing that matters. American Giant's proximity to its factories allows for better communication and control, better quality monitoring, and faster production cycles. This in turn has led to a much higher-quality product—so much higher that the company is selling far more hoodies than it could if it produced lower-cost, lower-quality products overseas. Demand has soared for its hoodies, and American Giant's reputation has soared along with it, giving the company a strong competitive advantage in the hoodie market.

AMERICAN GIANT'S VALUE CHAIN ACTIVITIES AND COSTS IN PRODUCING AND SELLING A HOODIE SWEATSHIRT: U.S. VERSUS ASIAN PRODUCTION

	U.S.	Asia
1. Fabric (Highly automated plants make the spinning, knitting, and dyeing of cotton cheaper for American Giant's U.S. suppliers.)	$17.40	$18.40
2. Trim and hardware	3.20	2.30
3. Labor (Without highly automated sweatshirt manufacture, U.S. labor costs would be even higher.)	17.00	5.50
4. Duty	0.00	3.50
5. Shipping (Shipping from overseas is more expensive and takes longer.)	0.50	1.70
6. Total company costs	$38.10	$31.40
7. Wholesale markup over company costs (company operating profit)	41.90	48.60
8. Retail price (American Giant sells online to keep the price lower by avoiding middlemen and their markups.)	$80.00	$80.00

Source: Stephanie Clifford, "U.S. Textile Plants Return, with Floors Largely Empty of People," *New York Times,* Business Day, September 19, 2013, www.nytimes.com/2013/09/20/business/us-textile-factories-return.html?emc=eta1&_r=0 (accessed February 14, 2014).

auto-racing circuit. More than 80 percent of Fortune 500 companies reportedly use benchmarking for comparing themselves against rivals on cost and other competitively important measures.

The tough part of benchmarking is not whether to do it, but rather how to gain access to information about other companies' practices and costs. Sometimes benchmarking can be accomplished by collecting information from published reports, trade groups, and industry research firms and by talking to knowledgeable industry analysts, customers, and suppliers. Sometimes field trips to the facilities of competing or noncompeting companies can be arranged to observe how things are done, compare practices and processes, and perhaps exchange data on productivity and other cost components. However, such companies, even if they agree to host facilities tours and answer questions, are unlikely to share competitively sensitive cost information. Furthermore, comparing two companies' costs may not involve comparing apples to apples if the two companies employ different cost accounting principles to calculate the costs of particular activities.

However, a fairly reliable source of benchmarking information has emerged. The explosive interest of companies in benchmarking costs and identifying best practices has prompted consulting organizations (e.g., Accenture, A. T. Kearney, Benchnet—The Benchmarking Exchange, Towers Watson, and Best Practices, LLC) and several councils and associations (e.g., the APQC, the Qualserve Benchmarking Clearinghouse, and the Strategic Planning Institute's Council on Benchmarking) to gather benchmarking data, distribute information about best practices, and provide comparative cost data without identifying the names of particular companies. Having an independent group gather the information and report it in a manner that disguises the names of individual companies avoids the disclosure of competitively sensitive data and lessens the potential for unethical behavior on the part of company personnel in gathering their own data about competitors.

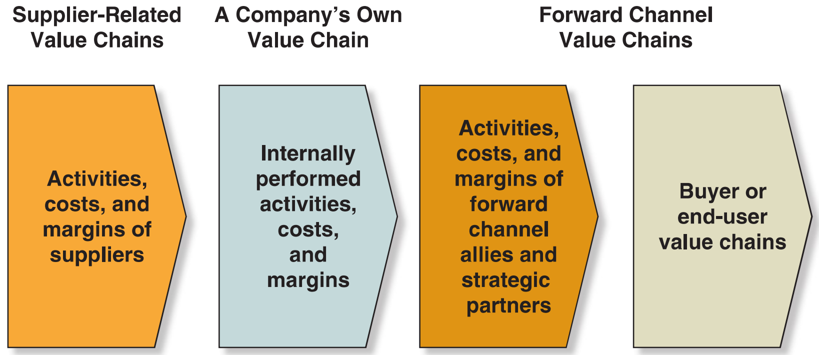
The Value Chain System for an Entire Industry

A company's value chain is embedded in a larger system of activities that includes the value chains of its suppliers and the value chains of whatever distribution channel allies it utilizes in getting its product or service to end users. The value chains of forward channel partners are relevant because (1) the costs and margins of a company's distributors and retail dealers are part of the price the consumer ultimately pays, and (2) the activities that distribution allies perform affect the company's customer value proposition. For these reasons, companies normally work closely with their suppliers and forward channel allies to perform value chain activities in mutually beneficial ways. For instance, motor vehicle manufacturers work closely with their forward channel allies (local automobile dealers) to ensure that owners are satisfied with dealers' repair and maintenance services.[14] Also, many automotive parts suppliers have built plants near the auto assembly plants they supply to facilitate just-in-time deliveries, reduce warehousing and shipping costs, and promote close collaboration on parts design and production scheduling. Irrigation equipment companies, suppliers of grape-harvesting and winemaking equipment, and firms making barrels, wine bottles, caps, corks, and labels all have facilities in the California wine country to be close to the nearly 700 winemakers they supply.[15] The lesson here is that a company's value chain activities are often closely linked to the value chains of its suppliers and the forward allies.

A company's customer value proposition and cost competitiveness depend not only on internally performed activities (its own company value chain), but also on the value chain activities of its suppliers and forward channel allies.

As a consequence, *accurately assessing the competitiveness of a company's cost structure and customer value proposition requires that company managers understand an industry's entire value chain system for delivering a product or service to customers, not just the company's own value chain.* A typical industry value chain that incorporates the value-creating activities, costs, and margins of suppliers and forward channel allies, if any, is shown in Figure 4.2. However, industry value chains vary significantly by industry. For example, the primary value chain activities in the bottled water industry (spring operation or water purification, processing of basic ingredients used in flavored or vitamin-enhanced water, bottling, wholesale distribution, advertising, and retail merchandising) differ from those for the coffee industry (farming, harvesting, exporting, roasting, packaging, marketing, wholesale distribution, and, in some cases, retail store operation). Producers of bathroom and kitchen faucets depend heavily on

FIGURE 4.2 **Representative Value Chain for an Entire Industry**



Source: Based in part on the single-industry value chain displayed in Michael E. Porter, *Competitive Advantage* (New York: Free Press, 1985), p. 35.

the activities of wholesale distributors and building supply retailers in winning sales to home builders and do-it-yourselfers, but producers of papermaking machines internalize their distribution activities by selling directly to the operators of paper plants.

Strategic Options for Remedying a Cost or Value Disadvantage

The results of value chain analysis and benchmarking may disclose cost or value disadvantages relative to key rivals. These competitive disadvantages are likely to lower a company's relative profit margin or weaken its customer value proposition. In such instances, actions to improve a company's value chain are called for to boost profitability or to allow for the addition of new features that drive customer value. There are three main areas in a company's overall value chain where important differences between firms in costs and value can occur: a company's own internal activities, the suppliers' part of the industry value chain, and the forward channel portion of the industry chain.

Improving Internally Performed Value Chain Activities Managers can pursue any of several strategic approaches to reduce the costs of internally performed value chain activities and improve a company's cost competitiveness.

1. *Implement the use of best practices* throughout the company, particularly for high-cost activities.
2. *Try to eliminate some cost-producing activities* by revamping the value chain. Many retailers have found that donating returned items to charitable organizations and taking the appropriate tax deduction results in a smaller loss than incurring the costs of the value chain activities involved in reverse logistics.
3. *Relocate high-cost activities* (such as manufacturing) to geographic areas such as China, Latin America, or Eastern Europe where they can be performed more cheaply.
4. *Outsource certain internally performed activities* to vendors or contractors if they can perform them more cheaply than can be done in-house.
5. *Invest in productivity-enhancing, cost-saving technological improvements* (robotics, flexible manufacturing techniques, state-of-the-art electronic networking).

6. *Find ways to detour around the activities or items where costs are high.* Computer chip makers regularly design around the patents held by others to avoid paying royalties; automakers have substituted lower-cost plastic for metal at many exterior body locations.
7. *Redesign the product* and/or some of its components to facilitate speedier and more economical manufacture or assembly.
8. *Try to make up the internal cost disadvantage* by reducing costs in the supplier or forward channel portions of the industry value chain—usually a last resort.

Rectifying a weakness in a company's customer value proposition can be accomplished by applying one or more of the following approaches:

1. Implement the use of best practices throughout the company, particularly for activities that are important for creating customer value—product design, product quality, or customer service.
2. Adopt best practices for marketing, brand management, and customer relationship management to improve brand image and customer loyalty.
3. Reallocate resources to activities having a significant impact on value delivered to customers—larger R&D budgets, new state-of-the-art production facilities, new distribution centers, modernized service centers, or enhanced budgets for marketing campaigns.

Additional approaches to managing value chain activities that drive costs, uniqueness, and value are discussed in Chapter 5.

Improving Supplier-Related Value Chain Activities Supplier-related cost disadvantages can be attacked by pressuring suppliers for lower prices, switching to lower-priced substitute inputs, and collaborating closely with suppliers to identify mutual cost-saving opportunities.[16] For example, just-in-time deliveries from suppliers can lower a company's inventory and internal logistics costs, eliminate capital expenditures for additional warehouse space, and improve cash flow and financial ratios by reducing accounts payable. In a few instances, companies may find that it is cheaper to integrate backward into the business of high-cost suppliers and make the item in-house instead of buying it from outsiders.

Similarly, a company can enhance its customer value proposition through its supplier relationships. Some approaches include selecting and retaining suppliers that meet higher-quality standards, providing quality-based incentives to suppliers, and integrating suppliers into the design process. When fewer defects exist in components provided by suppliers, this not only improves product quality and reliability, but it can also lower costs because there is less disruption to production processes and lower warranty expenses.

Improving Value Chain Activities of Forward Channel Allies There are three main ways to combat a cost disadvantage in the forward portion of the industry value chain: (1) Pressure dealers-distributors and other forward channel allies to reduce their costs and markups; (2) work closely with forward channel allies to identify win-win opportunities to reduce costs—for example, a chocolate manufacturer learned that by shipping its bulk chocolate in liquid form in tank cars instead of 10-pound molded bars, it could not only save its candy bar manufacturing customers the costs associated with unpacking and melting but also eliminate its own costs of molding bars and packing them; and (3) change to a more economical distribution strategy or perhaps integrate forward into company-owned retail outlets. Dell Computer's direct sales model eliminated all activities, costs, and margins of distributors, dealers, and retailers by allowing buyers to purchase customized PCs directly from Dell.

A company can improve its customer value proposition through the activities of forward channel partners by the use of (1) cooperative advertising and promotions with forward channel allies; (2) training programs for dealers, distributors, or retailers to improve the purchasing experience or customer service; and (3) creating and enforcing operating standards for resellers or franchisees to ensure consistent store operations. Papa John's International, for example, is consistently rated highly by customers for its pizza quality, convenient ordering systems, and responsive customer service across its 4,500 company-owned and franchised units. The company's marketing campaigns and extensive employee training and development programs enhance its value proposition and the unit sales and operating profit for its franchisees in all 50 states and 34 countries.

How Value Chain Activities Relate to Resources and Capabilities

A close relationship exists between the value-creating activities that a company performs and its resources and capabilities. When companies engage in a value-creating activity, they do so by drawing on specific company resources and capabilities that underlie and enable the activity. For example, brand-building activities that enhance a company's customer value proposition can depend on human resources, such as experienced brand managers, as well as organizational capabilities related to developing and executing effective marketing campaigns. Distribution activities that lower costs may derive from organizational capabilities in inventory management and resources such as cutting-edge inventory tracking systems.

Because of the linkage between activities and enabling resources and capabilities, value chain analysis complements resource and capability analysis as another tool for assessing a company's competitive advantage. Resources and capabilities that are *both valuable and rare* provide a company with the *necessary preconditions* for competitive advantage. When these assets are deployed in the form of a value-creating activity, *that potential is realized.* Resource analysis is a valuable tool for assessing the competitive advantage potential of resources and capabilities. But the actual competitive benefit provided by resources and capabilities can only be assessed objectively after they are deployed in the form of activities.

LO4 Learn how to evaluate a company's competitive strength relative to key rivals.

Question 4: What Is the Company's Competitive Strength Relative to Key Rivals?

An additional component of evaluating a company's situation is developing a comprehensive assessment of the company's overall competitive strength. Making this determination requires answers to two questions:

1. How does the company rank relative to competitors on each of the important factors that determine market success?

2. All things considered, does the company have a net competitive advantage or disadvantage versus major competitors?

Step 1 in doing a competitive strength assessment is to list the industry's key success factors and other telling measures of competitive strength or weakness (6 to 10 measures usually suffice). Step 2 is to assign a weight to each measure of competitive strength based on its perceived importance in shaping competitive success. (The sum of the weights for each measure must add up to 1.0.) Step 3 is to calculate weighted strength ratings by scoring each competitor on each strength measure (using a 1-to-10 rating scale where 1 is very weak and 10 is very strong) and multiplying the assigned rating by the assigned weight. Step 4 is to sum the weighted strength ratings on each factor to get an overall measure of competitive strength for each company being rated. Step 5 is to use the overall strength ratings to draw conclusions about the size and extent of the company's net competitive advantage or disadvantage and to take specific note of areas of strength and weakness. Table 4.3 provides an example of a competitive strength assessment using the hypothetical ABC Company against four rivals. ABC's total score of 5.95 signals a net competitive advantage over Rival 3 (with a score of 2.10) and Rival 4 (with a score of 3.70) but indicates a net competitive disadvantage against Rival 1 (with a score of 7. 70) and Rival 2 (with an overall score of 6.85).

Interpreting the Competitive Strength Assessments

Competitive strength assessments provide useful conclusions about a company's competitive situation. The ratings show how a company compares against rivals, factor by factor or capability by capability, thus revealing where it is strongest and weakest. Moreover, the overall competitive strength scores indicate whether the company is at a net competitive advantage or disadvantage against each rival.

> A company's competitive strength scores pinpoint its strengths and weaknesses against rivals and point to offensive and defensive strategies capable of producing first-rate results.

In addition, the strength ratings provide guidelines for designing wise offensive and defensive strategies. For example, consider the ratings and weighted scores in Table 4.3. If ABC Co. wants to go on the offensive to win additional sales and market share, such an offensive probably needs to be aimed directly at winning customers away from Rivals 3 and 4 (which have lower overall strength scores) rather than Rivals 1 and 2 (which have higher overall strength scores). ABC's advantages over Rival 4 tend to be in areas that are moderately important to competitive success in the industry, but ABC outclasses Rival 3 on the two most heavily weighted strength factors—relative cost position and customer service capabilities. Therefore, Rival 3 should be viewed as the primary target of ABC's offensive strategies, with Rival 4 being a secondary target.

A competitively astute company should utilize the strength scores in deciding what strategic moves to make. When a company has important competitive strengths in areas where one or more rivals are weak, it makes sense to consider offensive moves to exploit rivals' competitive weaknesses. When a company has competitive weaknesses in important areas where one or more rivals are strong, it makes sense to consider defensive moves to curtail its vulnerability.

TABLE 4.3

Illustration of a Competitive Strength Assessment

Key Success Factor/ Strength Measure	Importance Weight	ABC CO. Strength Rating	ABC CO. Score	RIVAL 1 Strength Rating	RIVAL 1 Score	RIVAL 2 Strength Rating	RIVAL 2 Score	RIVAL 3 Strength Rating	RIVAL 3 Score	RIVAL 4 Strength Rating	RIVAL 4 Score
Quality/product performance	0.10	8	0.80	5	0.50	10	1.00	1	0.10	6	0.60
Reputation/image	0.10	8	0.80	7	0.70	10	1.00	1	0.10	6	0.60
Manufacturing capability	0.10	2	0.20	10	1.00	4	0.40	5	0.50	1	0.10
Technological skills	0.05	10	0.50	1	0.05	7	0.35	3	0.15	8	0.40
Dealer network/distribution capability	0.05	9	0.45	4	0.20	10	0.50	5	0.25	1	0.05
New-product innovation capability	0.05	9	0.45	4	0.20	10	0.50	5	0.25	1	0.05
Financial resources	0.10	5	0.50	10	1.00	7	0.70	3	0.30	1	0.10
Relative cost position	0.30	5	1.50	10	3.00	3	0.95	1	0.30	4	1.20
Customer service capabilities	0.15	5	0.75	7	1.05	10	1.50	1	0.15	4	0.60
Sum of importance weights	**1.00**										
Weighted overall strength rating			**5.95**		**7.70**		**6.85**		**2.10**		**3.70**

(Rating scale: 1 = very weak; 10 = very strong)

Question 5: What Strategic Issues and Problems Must Be Addressed by Management?

LO5 Understand how a comprehensive evaluation of a company's external and internal situations can assist managers in making critical decisions about their next strategic moves.

The final and most important analytical step is to zero in on exactly what strategic issues company managers need to address. This step involves drawing on the results of both industry and competitive analysis and the evaluations of the company's internal situation. The task here is to get a clear fix on exactly what industry and competitive challenges confront the company, which of the company's internal weaknesses need fixing, and what specific problems merit front-burner attention by company managers. *Pinpointing the precise things that management needs to worry about sets the agenda for deciding what actions to take next to improve the company's performance and business outlook.*

If the items on management's "worry list" are relatively minor, which suggests the company's strategy is mostly on track and reasonably well matched to the company's overall situation, company managers seldom need to go much beyond fine-tuning the present strategy. If, however, the issues and problems confronting the company are serious and indicate the present strategy is not well suited for the road ahead, the task of crafting a better strategy has got to go to the top of management's action agenda.

Compiling a "worry list" of problems and issues creates an agenda for managerial strategy making.

KEY POINTS

In analyzing a company's own particular competitive circumstances and its competitive position vis-à-vis key rivals, consider five key questions:

1. *How well is the present strategy working?* This involves evaluating the strategy in terms of the company's financial performance and competitive strength and market standing. The stronger a company's current overall performance, the less likely the need for radical strategy changes. The weaker a company's performance and/or the faster the changes in its external situation (which can be gleaned from industry and competitive analysis), the more its current strategy must be questioned.
2. *Do the company's resources and capabilities have sufficient competitive power to give it a sustainable advantage over competitors?* The answer to this question comes from conducting the four tests of a resource's competitive power—the VRIN tests. If a company has resources and capabilities that are competitively *valuable* and *rare,* the firm will have the potential for a competitive advantage over market rivals. If its resources and capabilities are also hard to copy (*inimitable*) with no good substitutes (*nonsubstitutable*), then the firm may be able to sustain this advantage even in the face of active efforts by rivals to overcome it.

   SWOT analysis can be used to assess if a company's resources and capabilities are sufficient to seize market opportunities and overcome external threats to its future well-being. The two most important parts of SWOT analysis are (1) drawing conclusions about what story the compilation of strengths, weaknesses, opportunities, and threats tells about the company's overall situation, and (2) acting on the conclusions to better match the company's strategy to its internal strengths and market opportunities, to correct the important internal weaknesses, and to defend against external threats. A company's strengths and competitive assets are strategically relevant because they are the most logical and appealing building blocks for strategy; internal weaknesses are important because they may represent vulnerabilities that need correction. External opportunities and threats come into play because a good strategy necessarily aims at capturing a company's most attractive opportunities and at defending against threats to its well-being.

3. *Are the company's cost structure and customer value proposition competitive?* One telling sign of whether a company's situation is strong or precarious is whether its costs are competitive with those of industry rivals. Another sign is how it compares with rivals in terms of its customer value proposition. Value chain analysis and benchmarking are essential tools in determining whether the company is performing particular functions and activities well, whether its costs are in line with competitors, whether it is able to offer an attractive value proposition to customers, and whether particular internal activities and business processes need improvement. Value chain analysis complements resource and capability analysis because of the tight linkage between activities and enabling resources and capabilities.
4. *Is the company competitively stronger or weaker than key rivals?* The key appraisals here involve how the company matches up against key rivals on industry key success factors and other chief determinants of competitive success and whether and why the company has a competitive advantage or disadvantage. Quantitative competitive strength assessments, using the method presented in Table 4.3, indicate where a company is competitively strong and weak and provide insight into the company's ability to defend or enhance its market position. As a rule, a company's competitive strategy should be built around its competitive strengths and should aim at shoring up areas where it is competitively vulnerable. When a company has important competitive strengths in areas where one or more rivals are weak, it makes sense to consider offensive moves to exploit rivals' competitive weaknesses. When a company has important competitive weaknesses in areas where one or more rivals are strong, it makes sense to consider defensive moves to curtail its vulnerability.
5. *What strategic issues and problems merit front-burner managerial attention?* This analytical step zeros in on the strategic issues and problems that stand in the way of the company's success. It involves using the results of both industry and competitive analysis and company situation analysis to identify a "worry list" of issues to be resolved for the company to be financially and competitively successful in the years ahead. Actually deciding upon a strategy and what specific actions to take comes after the list of strategic issues and problems that merit front-burner management attention has been developed.

Good company situation analysis, like good industry and competitive analysis, is a valuable precondition for good strategy making.

ASSURANCE OF LEARNING EXERCISES

connect

LO1

1. Using the financial ratios provided in the Appendix and the financial statement information for Costco Wholesale Corporation, Inc., below, calculate the following ratios for Costco for both 2013 and 2014.
   1. Gross profit margin
   2. Operating profit margin
   3. Net profit margin
   4. Times interest earned coverage

5. Return on shareholders' equity
6. Return on assets
7. Debt-to-equity ratio
8. Days of inventory
9. Inventory turnover ratio
10. Average collection period

Based on these ratios, did Costco's financial performance improve, weaken, or remain about the same from 2013 to 2014?

Consolidated Statements of Income for Costco Wholesale Corporation, Inc., 2013–2014 (in millions, except per share data)

	2014	2013
Net sales	$110,212	$102,870
Membership fees	2,428	2,286
Total revenue	112,640	105,156
Operating Expenses		
Merchandise costs	98,458	91,948
Selling, general and administrative	10,899	10,104
Operating income	3,220	3,053
Other Income (Expense)		
Interest expense	(113)	(99)
Interest income and other, net	90	97
Income before income taxes	3,197	3,051
Provision for income taxes	1,109	990
Net income including noncontrolling interests	2,088	2,061
Net income attributable to noncontrolling interests	(30)	(22)
Net income	$2,058	$2,039
Basic earnings per share	$ 4.69	$ 4.68
Diluted earnings per share	$ 4.65	$ 4.63

Consolidated Balance Sheets for Costco Wholesale Corporation, 2013–2014 (in millions, except per share data)

ASSETS	AUGUST 31, 2014	SEPTEMBER 1, 2014
Current Assets		
Cash and cash equivalents	$ 5,738	$ 4,644
Short-term investments	1,577	1,480
Receivables, net	1,148	1,201
Merchandise inventories	8,456	7,894
Deferred income taxes and other current assets	669	621
Total current assets	17,588	15,7840
Property and Equipment		
Land	4,716	4,409
Buildings and improvements	12,522	11,556
Equipment and fixtures	4,845	4,472
Construction in progress	592	585
Less accumulated depreciation and amortization	(7,845)	(7,141)
Net property and equipment	14,830	13,881

gam46985_ch04_065-088.indd 85 12/18/15 01:31 AM

Consolidated Balance Sheets for Costco Wholesale Corporation, 2013–2014 (in millions, except per share data)

ASSETS	AUGUST 31, 2014	SEPTEMBER 1, 2014
Other assets	606	562
Total assets	$ 33,024	$ 30,283
Liabilities and Equity		
Current Liabilities		
Accounts payable	$8,491	$7,872
Accrued salaries and benefits	2,231	2,037
Accrued member rewards	773	710
Accrued sales and other taxes	442	382
Deferred membership fees	1,254	1,167
Other current liabilities	1,221	1,089
Total current liabilities	14,412	13,257
Long-term debt	5,093	4,998
Deferred income taxes and other liabilities	1,004	1,016
Total liabilities	20,509	19,271
Equity		
Preferred stock $.005 par value; 100,000,000 shares authorized; no shares issued and outstanding	0	0
Common stock $.005 par value; 900,000,000 shares authorized; 437,683,000 and 436,839,000 shares issued and outstanding	2	2
Additional paid-in capital	4,919	4,670
Accumulated other comprehensive loss	(76)	(122)
Retained earnings	7,458	6,283
Total Costco stockholders' equity	12,303	10,833
Noncontrolling interests	212	179
Total equity	12,515	11,012
Total liabilities and equity	$ 33,024	$30,283

Source: Costco Wholesale Corporation, 2014 10-K.

LO2 2. REI operates more than 130 sporting goods and outdoor recreation stores in 34 states. How many of the four tests of the competitive power of a resource does the retail store network pass? Explain your answer.

connect

LO3 3. Review the information in Concepts & Connections 4.1 concerning American Giant's average costs of producing and selling a hoodie sweatshirt and compare this with the representative value chain depicted in Figure 4.1. Then answer the following questions:

(a) Which of the company's costs correspond to the primary value chain activities depicted in Figure 4.1?

(b) Which of the company's costs correspond to the support activities described in Figure 4.1?

(c) How would its various costs and activities differ if the company chose to produce its hoodies in Asia?

(d) What value chain activities might be important in securing or maintaining American Giant's competitive advantage?

LO4 4. Using the methodology illustrated in Table 4.3 and your knowledge as an automobile owner, prepare a competitive strength assessment for General Motors and its rivals Ford, Chrysler, Toyota, and Honda. Each of the five automobile manufacturers should be evaluated on the key success factors/strength measures of cost competitiveness, product-line breadth, product quality and reliability, financial resources and profitability, and customer service. What does your competitive strength assessment disclose about the overall competitiveness of each automobile manufacturer? What factors account most for Toyota's competitive success? Does Toyota have competitive weaknesses that were disclosed by your analysis? Explain.

EXERCISES FOR SIMULATION PARTICIPANTS

1. Using the formulas in the Appendix and the data in your company's latest financial statements, calculate the following measures of financial performance for your company: **LO1**
    1. Operating profit margin
    2. Return on total assets
    3. Current ratio
    4. Working capital
    5. Long-term debt-to-capital ratio
    6. Price-earnings ratio
2. Based on your company's latest financial statements and all of the other available data regarding your company's performance that appear in the Industry Report, list the three measures of financial performance on which your company did "best" and the three measures on which your company's financial performance was "worst." **LO1**
3. What hard evidence can you cite that indicates your company's strategy is working fairly well (or perhaps not working so well, if your company's performance is lagging that of rival companies)? **LO1**
4. What internal strengths and weaknesses does your company have? What external market opportunities for growth and increased profitability exist for your company? What external threats to your company's future well-being and profitability do you and your co-managers see? What does the preceding SWOT analysis indicate about your company's present situation and future prospects—where on the scale from "exceptionally strong" to "alarmingly weak" does the attractiveness of your company's situation rank? **LO2**
5. Does your company have any core competencies? If so, what are they? **LO2**
6. What are the key elements of your company's value chain? Refer to Figure 4.1 in developing your answer. **LO3**
7. Using the methodology illustrated in Table 4.3, do a weighted competitive strength assessment for your company and two other companies that you and your co-managers consider to be very close competitors. **LO4**

ENDNOTES

1. Birger Wernerfelt, "A Resource-Based View of the Firm," *Strategic Management Journal* 5, no. 5 (September– October 1984); Jay Barney, "Firm Resources and Sustained Competitive Advantage," *Journal of Management* 17, no. 1 (1991); Margaret A. Peteraf, "The Cornerstones of Competitive Advantage: A Resource-Based View," *Strategic Management Journal* 14, no. 3 (March 1993).
2. Birger Wernerfelt, "A Resource-Based View of the Firm," *Strategic Management Journal* 5, no. 5 (September–October 1984), pp. 171–80; Jay Barney, "Firm Resources and Sustained Competitive Advantage," *Journal of Management* 17, no. 1 (1991); Margaret A. Peteraf, "The Cornerstones of Competitive Advantage: A Resource-Based View," *Strategic Management Journal* 14, no. 3 (March 1993).

3. R. Amit and P. Schoemaker, "Strategic Assets and Organizational Rent," *Strategic Management Journal* 14, no. 1 (1993).
4. David J. Collis and Cynthia A. Montgomery, "Competing on Resources: Strategy in the 1990s," *Harvard Business Review* 73, no. 4 (July–August 1995).
5. Margaret A. Peteraf and Mark E. Bergen, "Scanning Dynamic Competitive Landscapes: A Market-Based and Resource-Based Framework," *Strategic Management Journal* 24 (2003), pp. 1027–42.
6. George Stalk, Philip Evans, and Lawrence E. Schulman, "Competing on Capabilities: The New Rules of Corporate Strategy," *Harvard Business Review* 70, no. 2 (March–April 1992).
7. David J. Teece, Gary Pisano, and Amy Shuen, "Dynamic Capabilities and Strategic Management," *Strategic Management Journal* 18, no. 7 (1997); Constance E. Helfat and Margaret A. Peteraf, "The Dynamic Resource-Based View: Capability Lifecycles," *Strategic Management Journal* 24, no. 10 (2003).
8. C. Montgomery, "Of Diamonds and Rust: A New Look at Resources," in *Resource-Based and Evolutionary Theories of the Firm,* ed. C. Montgomery (Boston: Kluwer Academic Publishers, 1995), pp. 251–68.
9. D. Teece, G. Pisano, and A. Shuen, "Dynamic Capabilities and Strategic Management," *Strategic Management Journal* 18, no. 7 (1997); K. Eisenhardt and J. Martin, "Dynamic Capabilities: What Are They?" *Strategic Management Journal* 21, nos. 10–11 (2000); M. Zollo and S. Winter, "Deliberate Learning and the Evolution of Dynamic Capabilities," *Organization Science* 13 (2002); C. Helfat et al., *Dynamic Capabilities: Understanding Strategic Change in Organizations* (Malden, MA: Blackwell, 2007).
10. W. Powell, K. Koput, and L. Smith-Doerr, "Interorganizational Collaboration and the Locus of Innovation," *Administrative Science Quarterly* 41, no. 1 (1996).
11. M. Peteraf, "The Cornerstones of Competitive Advantage: A Resource-Based View," *Strategic Management Journal,* March 1993, pp. 179–91.
12. Michael E. Porter, *Competitive Advantage* (New York: Free Press, 1985).
13. Gregory H. Watson, *Strategic Benchmarking: How to Rate Your Company's Performance Against the World's Best* (New York: John Wiley & Sons, 1993); Robert C. Camp, *Benchmarking: The Search for Industry Best Practices That Lead to Superior Performance* (Milwaukee: ASQC Quality Press, 1989); Christopher E. Bogan and Michael J. English, *Benchmarking for Best Practices: Winning Through Innovative Adaptation* (New York: McGraw-Hill, 1994); Dawn Iacobucci and Christie Nordhielm, "Creative Benchmarking," *Harvard Business Review* 78, no. 6 (November–December 2000).
14. M. Hegert and D. Morris, "Accounting Data for Value Chain Analysis," *Strategic Management Journal* 10 (1989); Robin Cooper and Robert S. Kaplan, "Measure Costs Right: Make the Right Decisions," *Harvard Business Review* 66, no. 5 (September–October 1988); John K. Shank and Vijay Govindarajan, *Strategic Cost Management* (New York: Free Press, 1993).
15. Michael E. Porter, "Clusters and the New Economics of Competition," *Harvard Business Review* 76, no. 6 (November–December 1998).
16. Reuben E. Stone, "Leading a Supply Chain Turnaround," *Harvard Business Review* 82, no. 10 (October 2004).