THE COMPETITIVE ADVANTAGE THEORY AS A GROWTH STRATEGY

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Abstract: To do well in any business you must develop a long-term strategy. Making consistent decisions in all aspects of a firm's operations is difficult without a well-defined and clearly integrated strategy. By far the most widely pursued corporate directional strategies are those designed to achieve growth in sales, assets, profits or some combination. Companies that do business in expanding industries must grow to survive. Continuing growth means increasing sales and a chance to take advantage of the experience curve to reduce the per-unit cost of products sold, thereby increasing profits. This cost reduction becomes extremely important if a corporation's industry is growing quickly and competitors are engaging in price wars in attempts to increase their shares of the market. Firms that have not reached "critical mass" (that is, gained the necessary economy of large scale production) will face large losses unless they can find and fill a small but profitable niche where higher prices can be offset by special product or service features.

Keywords: competitive advantage, growth strategy, growth resources, core competencies, explicit knowledge, tacit knowledge

Michael Porter in his book The Competitive Advantage of Nations, has developed a model that allows to analyze why some nations are more competitive than others and also why some industries within nations are more competitive than others.

This model of determining factors of national advantage has become known as Porters Diamond. It suggests that the national home base of an organization plays an important role in shaping the extent to which it is likely to achieve advantage on a global scale. This home base provides basic factors, which support or hinder organizations from building advantages in global competition.

Porter's Five Forces Analysis is a tool for analyzing the attractiveness of an industry. It has 5 components -customer, competitor, suppliers, barriers to entry, threat of substitutes. The tool allows you to consider each of these areas and to determine whether this is going to be profitable or not for companies in that industry. Porter identifies many elements that can be considered in each of these areas. These factors can be scored, the higher the score the better the industry. A simple way to do this is to score each factor out of four: 1: weak; 4: strong.

Threat of New Entrants

New entrants to an industry typically bring to it new capacity, a desire to gain market share, and substantial resources. They are, therefore, threats to an established corporation. The threat of entry depends on the presence of entry barriers and the reaction that can be expected from existing competitors.

An entry barrier is an obstruction that makes it difficult for a company to enter an industry. Some of the possible barriers of entry are:

- Economies of scale: scale economies in the production and sales of some products give to the manufacturing company a significant cost advantage over any new rival
- Product differentiation: some big corporations create high entry barriers through their high level of advertising and promotion
- Capital requirements: the need to invest huge financial resources in manufacturing facilities creates a significant barrier to entry to any competitor
- Switching costs: for example for a new software which training costs are very high
- Access to distribution channels: small entrepreneur often have difficulty in obtaining supermarket shelf space for their goods because large retailers charge for space and give priority to the firms who can pay for the advertising needed to generate high customer demand
- Cost disadvantages independent of size: once a new product earns sufficient market share to be accepted as the standard for that type of product, the maker has a key advantage
- Government policy: governments can limit entry into an industry through licensing requirements by restricting access to raw materials such as oil-drilling protected areas.

Rivalry Among Existing Firms

In most industries, corporations are mutually dependent. A competitive move by one firm can be expected to have a noticeable effect on its competitors and thus may cause retaliation or counterefforts. According to Porter, intense rivalry is related to the presence of several factors, including:

- Number of competitors – when the competitors are few and roughly equal in size, they wath each other carefully to make sure that any move by another firm is matched by an equal countermove.
- Rate of industry growth – anythe only path to growth is to take sales away from a competitor
- Product or service characteristics - many people choose a product based on location, variety of selection and pricing
- Amount of fixed costs – special offers for customers
- Capacity – if the only way a manufacturer can increase capacity is in a large increment by building a new plant, it will run that new plan at full capacity to keep unit costs as low as possible -thus producing so much that the selling price falls through industry
- Height of exit barriers – exit barriers keep a company from leaving an industry ; the brewing industry, for example, has a low percentage of companies that voluntarily leave the industry because breweries are specialized assets with few uses except for making beer
- Diversity of rivals - rivals that are very different ideas of how to compete are likely to cross paths often and unknowingly challenge each other's position. This happens often in the retail clothing industry when a number of retailers open outlets in the same location, thus taking sales away from each other.

Threat of Substitute Products or Services

Substitute products are those products that appear to be different but can satisfy the same need as another product (for example, Nutrasweet is a substitute for sugar).

According to Porter, "substitutes limit the potential returns of an industry by placing a ceiling on the prices firms in the industry can profitably charge." To the extent that switching costs are low, substitutes may have a strong effect on an industry. Tea can be considered a substitute for coffee. If the price of coffee goes up high enough, coffee drinkers will slowly begin switching for tea. The price of tea thus puts a price ceiling on the price of coffee. Identifying possible substitute products or services is sometimes a difficult task. It means searching for products or services that can perform the same function, even though they have a different appearance and may not appear to be easily substitutable.

Bargaining Power of Buyers

Buyers affect an industry through their ability to force down prices, bargain for higher quality or more services, and play competitors against each other. A buyer or a group of buyers is powerful if some of the following factors hold true:

- A buyer purchases a large proportion of the seller's product or service (for example, oil filters purchased by a major auto maker)
- A buyer has the potential to integrate backward by producing the product itself (for example a newspaper chain could make its own paper)
- Alternative suppliers are plentiful because the product is standard or undifferentiated (for example, motorists can choose among many gas stations)
- Changing suppliers costs very little (for example, office supplies are easy to find)
- The purchased product represents a high percentage of a buyer's costs, thus providing an incentive to shop around for a lower price (for example, gasoline purchased for resale by convenience stores makes up half their total costs)
- A buyer earns low profits and is thus very sensitive to costs and service differences (for example, grocery stores have very small margins)
- The purchased product is unimportant to the final quality or price of a buyer's products or services and thus can be easily substituted without affecting the final product adversely (for example, electric wire bought for use in lamps)

Bargaining Power of Suppliers

Suppliers can affect an industry through their ability to raise prices or reduce the quality of purchased goods and services. A supplier or supplier group is powerful if some of the following factors apply:

- The supplier industry is dominated by a few companies, but it sells to many
- Its product or service is unique and/or it has built up switching costs
- Substitutes are not readily available
- Suppliers are able to integrate forward and compete directly with their present customers
- A purchasing industry buys only a small portion of the supplier group's goods and services and is thus unimportant to the supplier

Relative Power of Other Stakeholders

A sixth force should be added to porter's list to include a variety of stakeholder groups from the task environment. Some of these groups are governments (if not explicitly included elsewhere), local communities, creditors (if not included with suppliers), trade associations, special interests groups, unions (if not included with suppliers), shareholders, and complementors.

A complementor is a company or an industry whose product works well with another industry's or a firm's product and without which the product would lose much of its value.

Michael Porter proposes two "generic" competitive strategies for outperforming other corporations in a particular industry: lower cost and differentiation.

These strategies are called generic because they can be pursued by any type of size of business firm, even by non-profit organizations.

- Lower cost strategy is the ability of a company or a business unit to design, produce and market a comparable product more efficiently than its competitors
- Differentiation strategy is the ability to provide unique and superior value to the buyer in terms of product quality, special features or after-sales service.

Cost leadership is a low-cost competitive strategy that aims at the broad mass market and requires "aggressive construction of efficient scale facilities, vigorous pursuit of cost reductions from experience, tight cost and overhead control, avoidance of marginal customer accounts and cost minimization in areas like R&D, service, sales force, advertising, etc. Because of its lower costs, the cost leader is able to charge a lower price for its products than its competitors and still make a satisfactory profit. Having a low-cost position also gives a company or business unit a defense against rivals. Its lower costs allow it to continue to earn profits during times of heavy competition. Its high market share means that it will have high bargaining power relative to its suppliers (because it buys in large quantities). Its low price will also serve as a barrier to entry because few new entrants will be able to match the leader's cost advantage. As a result, cost leaders are likely to earn above-average returns on investment.

Differentiation is aimed at the broad mass market and involves the creation of a product or service that is perceived throughout its industry as unique. The company or business unit may then charge a premium for its product. This specialty can be associated with design or brand image, technology, features, dealer network or customer service. Differentiation is a viable strategy for earning above-average returns in a specific business because the resulting brand loyalty lowers customers' sensitivity to price. Increased costs can usually be passed on to the buyers. Buyer loyalty also serves as an entry barrier - new firms must develop their own distinctive competence to differentiate their products in some way in order to compete successfully. Research does suggest that a differentiation strategy is more likely to generate higher profits than is a low-cost strategy because differentiation creates a better entry barrier. A low cost strategy is more likely, however, to generate increases in market share.

Porter further purposes that a firm's competitive advantage in an industry is determined by its competitive scope, that is, the breadth of the company's or business unit's target market.

Before using one of the two generic competitive strategies (lower cost or differentiation), the firm or unit must choose the range of product varieties it will produce, the distribution channels it will employ, the types of buyers it will serve, the geographic areas in which it will sell and the array of related industries in which it will also compete. This should reflect an understanding of the firm's unique resources.

Evaluate the importance of the resources to ascertain if they are internal strategic factors – those particular strength and weaknesses that will help determine the future of the company. To the extent that a resource (such as a firm's financial situation) is significantly different from the firm's own past, its key competitors, or the industry average, the resource is likely to be a strategic factor and should be considered in strategic decisions. A resource is an asset, competency, process, skill, or knowledge controlled by a corporation. A resource is a strength if it provides a company with a competitive advantage. It is something the firm does or has the potential to do particularly swell relative to the abilities of existing or potential competitors. A resource is a weakness if it is something the corporation does poorly or doesn't have the capacity to do although its competitors have the capacity.

Just because a firm is able to use its resources and capabilities to develop a competitive advantage does not mean it will be able to sustain it. Two characteristics determine the sustainability of a firm's distinctive competencies: durability and imitability.

Durability is the rate at which a firm's underlying resources and capabilities (core competencies) depreciate or become obsolete. New technology can make a company's core competency obsolete or irrelevant.

Imitability is the rate at which a firm's underlying resources and capabilities (core competencies) can be duplicated by others. To the extent that a firm's distinctive competency gives it competitive advantage in the market place, competitors will do what they can to learn and imitate that set of skills and capabilities. Competitors' efforts may range from reverse engineering (taking apart a competitor's product in order to find out how it works, to hiring employees from the competitor, to outright patent infringement. A core competency can be easily imitated to the extent that it is transparent, transferable and replicable.

- Transparency is the speed with which other firms can understand the relationship of resources and capabilities supporting a successful firm's strategy.
- Transferability is the ability of competitors to gather the resources and capabilities necessary to support a competitive challenge.
- Replicability is the ability of competitors to use duplicated resources and capabilities to imitate the other firm's success.

It is relatively easy to learn and imitate another company's core competency or capability if it comes from explicit knowledge, that is, knowledge that can be easily articulated and communicated. This is the type of knowledge that competitive intelligence activities can quickly identify and communicate. Tacit knowledge, in contrast, is knowledge that is not easily communicate because it is deeply rooted in employees experience or in a corporation's culture. Tacit knowledge is more valuable and more likely to lead to a sustainable competitive advantage than is explicit knowledge because it is much harder for competitors to imitate.

Porters Diamond has been used in various ways. Organizations may use the model to identify the extent to which they can build on home based advantages to create competitive advantage in relation to others on a global front. On national level, governments can (and should) consider the policies that they should follow to establish national advantages, which enable industries in their country to develop a strong competitive position globally.

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