

Competitive Advantage

What makes a firm profitable?

Where do firm profits come from?

- Think back to Pi Economics
- Profits are the area between the demand curve and the cost curve
 - Demand curve often called consumers **willingness-to-pay (WTP)**
 - Cost curve includes opportunity costs

Value Creation and Value Capture

- The first principle is that your product has to have value
 - There has to be a Pi to begin with!
- The second principle is that you have to be able to turn that value into profits
 - You want to get a good slice of the Pi you baked
- The main threat is competition
 - Similar to Industry Analysis, you want it to be difficult for other firms to copy you
 - Similar to having a firm-level BTE
 - Rule of thumb: be unique!

Enterprise Example

- Creation: Mostly created by WTP
 - Serves a different customer segment (not just business travelers)

Everybody wants to throw us in the same pot with the other rental car companies, but our businesses are different. We have no plans to be in the airports. We're sticking to our niche.

- Capture: Complementary strategic decisions
 - Referral relationships with mechanics, dealers, insurers
 - Local **economies of scale (EOS)** with dense network of locations
 - Competitive and affable **human resource management (HRM)**

A highly decentralized network of company-owned branches -- "a confederation of small businesses," in Andrew Taylor's description -- fuels Enterprise's growth on the strength of referral relationships with auto dealers, insurance agents and adjusters and body shops. Competition among the branches is notorious, with managers encouraged by the home office to place bets with each other on staff performance. (The losers might pay for dinner or work extra hours at the winning branch.)

So How Do You Get There?

- First, decide on your position
 - 3 Questions from lecture are basically What, Where, How
- Next, plan out why you'll succeed (if you can!)
 - Sometimes just as important to discover why you shouldn't do something
 - Plenty of profitable opportunities, but which are the best fit for you?
- Common organizing tool you'll see for strategy evaluation
 - Scope
 - Approach
 - Internal Logic
 - External Logic

Takeaways

1. Firm profits come from creating value, and capturing it (in the form of profits)
2. Need to do both, often boils down to positioning

Closing Thought for Next Week

It may not be enough to play a game well -- you must also be sure you are playing the right game.