

Chapter 4 Internal Analysis

WPC 480

Learning Objectives (1 of 2)

- LO 4-1 Differentiate among a firm's core competencies, resources, capabilities, and activities.
 - LO 4-2 Compare and contrast tangible and intangible resources.
 - LO 4-3 Evaluate the two critical assumptions behind the resource-based view.
 - LO 4-4 Apply the VRIO framework to assess the competitive implications of a firm's resources.
 - LO 4-5 Evaluate different conditions that allow a firm to sustain a competitive advantage.
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Learning Objectives (2 of 2)

- LO 4-6 Outline how dynamic capabilities can enable a firm to sustain a competitive advantage.
 - LO 4-7 Apply a value chain analysis to understand which of the firm's activities in the process of transforming inputs into outputs generate differentiation and which drive costs.
 - LO 4-8 Identify competitive advantage as residing in a network of distinct activities.
 - LO 4-9 Conduct a SWOT analysis to generate insights from external and internal analysis and derive strategic implications.
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What Are Core Competencies?

Unique strengths

Embedded deep within a firm

Allows differentiation of products and services from rivals

Results in:

- Creating higher value for the customer or
 - Offering products and services at lower cost
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Examples of Core Competencies

IKEA

- Designing modern functional home furnishings at low cost

Beats Electronics

- Marketing: perception of coolness

Facebook

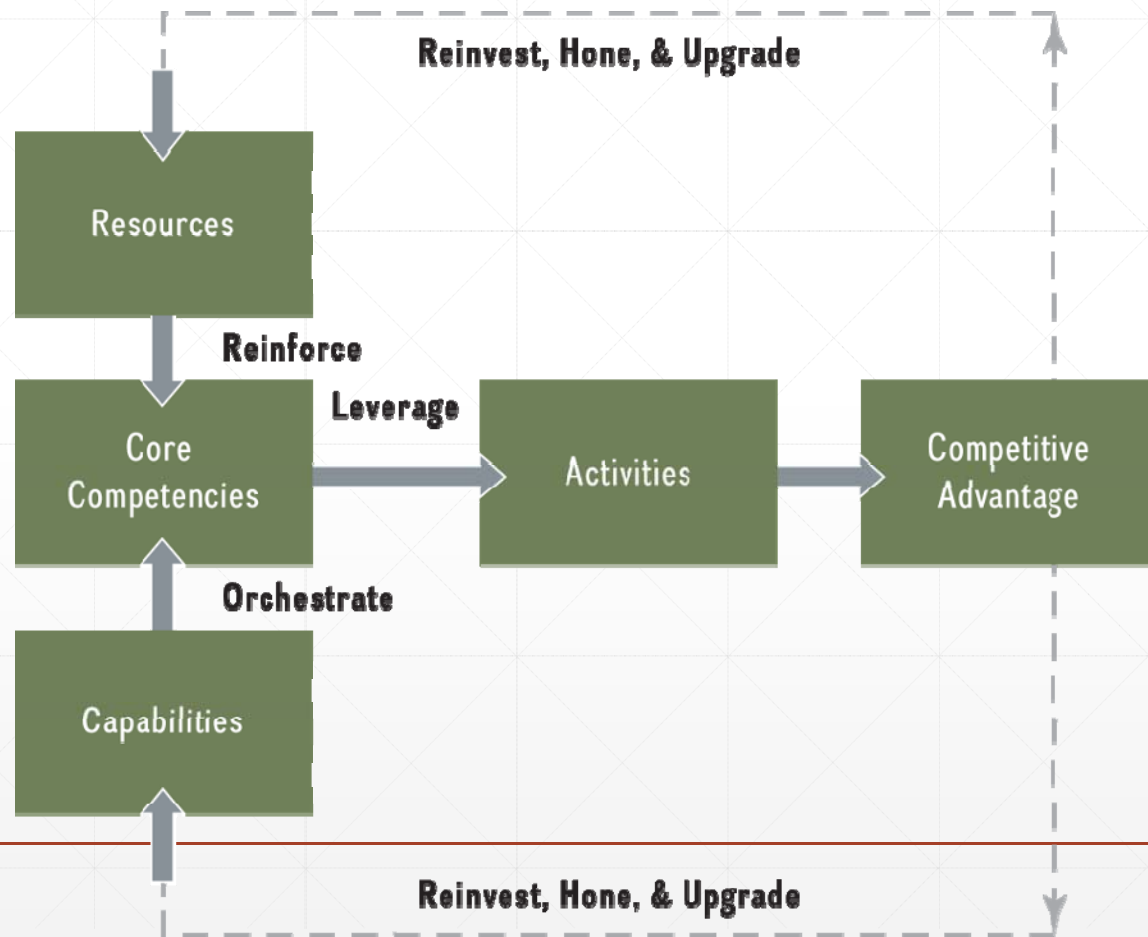
- IT capabilities to provide reliable social network services globally on a large scale.

Netflix

- ~~• Creating proprietary algorithms-based on individual customer preferences.~~

Links to Competitive Advantage and Superior Firm Performance

Exhibit 4.3



[Jump to Appendix 2 long image description](#)

Resources, Capabilities and Activities

Help deliver core competencies

Resources:

- Any assets that a firm can draw on

Capabilities:

- Organizational and managerial skills

Activities:

- Distinct and fine-grained business processes
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The Resource Based View

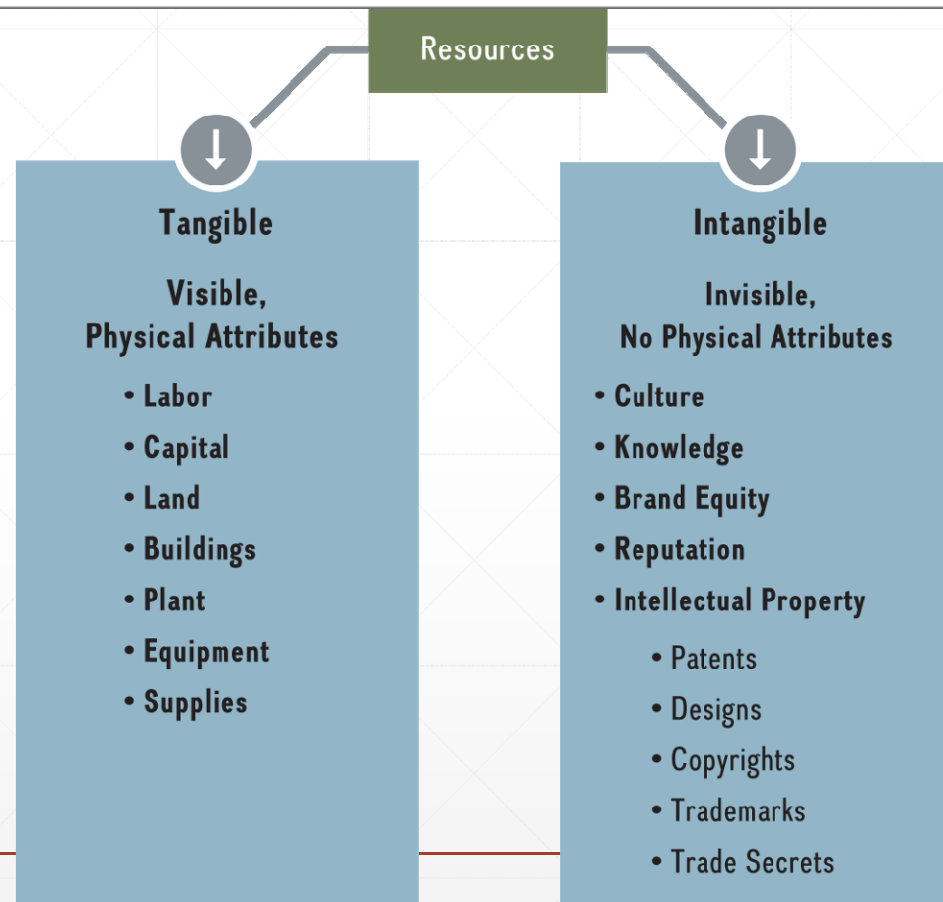
Resources are key to superior firm performance

- Aids in identifying core competencies

Resources fall into two categories:

- Tangible
 - Resources that have physical attributes
 - Visible
 - Intangible
 - Resources that do not have physical attributes
 - Invisible
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Tangible and Intangible Resources



[Jump to Appendix 3 long image description](#)

Exhibit 4.4

Two Critical Assumptions of the RBV

Resource Heterogeneity

- A firm is a unique bundle of resources and capabilities
- These bundles differ across firms

Resource Immobility

- Resources don't move easily from firm to firm
 - Resources are difficult to replicate
 - Resources can last for a long time
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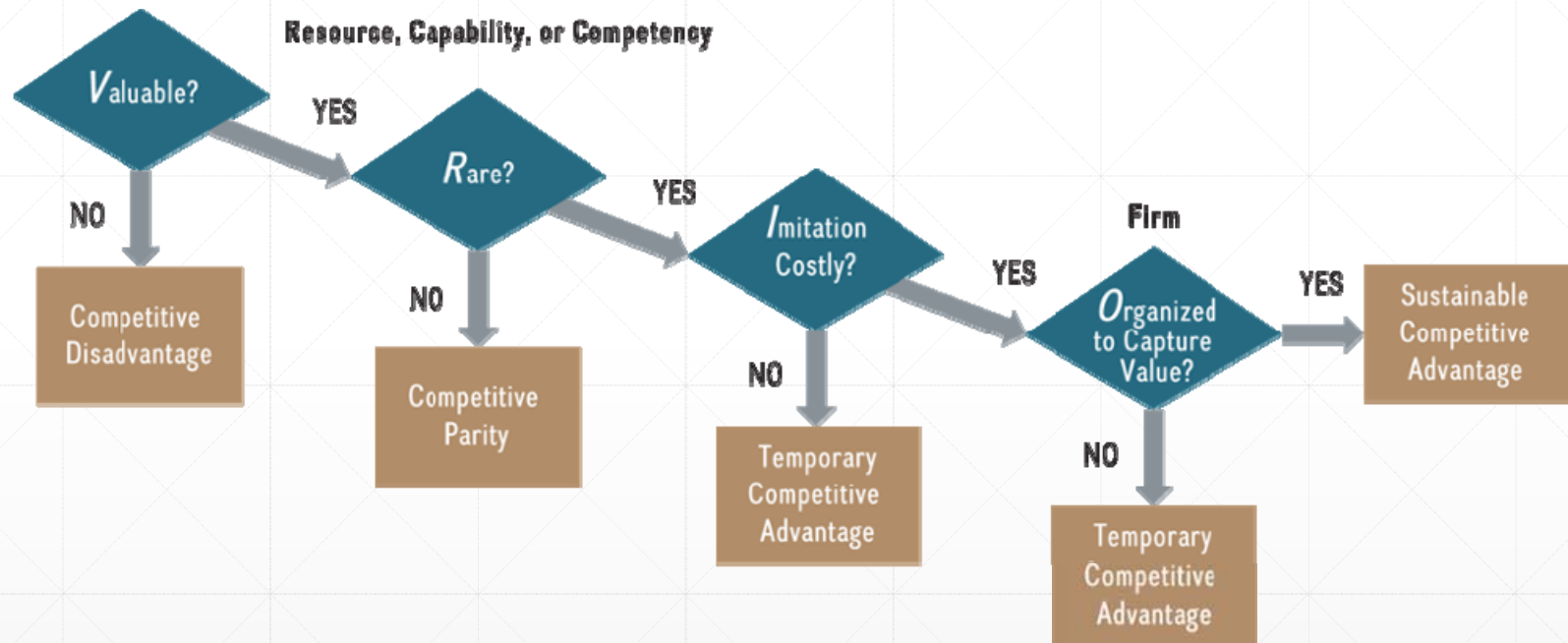
The VRIO Framework

Tool for evaluating firm resource endowments

To be the basis of a competitive advantage, resources must be:

- Valuable,
 - Rare,
 - Costly to Imitate, and the firm must be
 - Organized to capture the value of the resource
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The VRIO Decision Tree



A Resource Is...

Valuable if:

- Helps exploit an opportunity or offset a threat

Rare if:

- Only one or a few firms possess it

Costly to Imitate if:

- Competitors can't develop the resource for a reasonable price

The firm is organized to capture value through:

- Effective organizational structure and coordinating systems
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Isolating Mechanisms

Barriers to imitation

Prevents rivals from competing away firm advantage

- Better expectations of future resource value
 - Path dependence
 - Causal ambiguity
 - Social complexity
 - Intellectual property (IP) protection
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Core Rigidity

A former core competency

- Turned into a liability
- Result of an environment change
- No longer fits in the external environment

Turns a resource from an asset to a liability

Dynamic Capabilities

A firm's ability to:

- Adapt resources over time
 - Create, deploy, modify, reconfigure, upgrade, leverage
 - In consideration of the external environment

The goal:

- Develop resources, capabilities, and competencies
 - Create a strategic fit with the firm's environment
 - Change in a dynamic fashion
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The Dynamic Capabilities Perspective

A model that emphasizes a firm's ability to:

- Modify and leverage its resource base
- Gain and sustain competitive advantage in a constantly changing environment

Dynamic markets are due to:

- Technological change
 - Deregulation
 - Globalization
 - Demographic shifts
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Resource Stocks and Flows

Resource stocks

- The firm's current level of intangible resources
 - New product development
 - Engineering expertise
 - Innovation capability
 - Reputation for quality

Resource flows

- The firm's level of investments to maintain or build a resource
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The Bathtub Metaphor

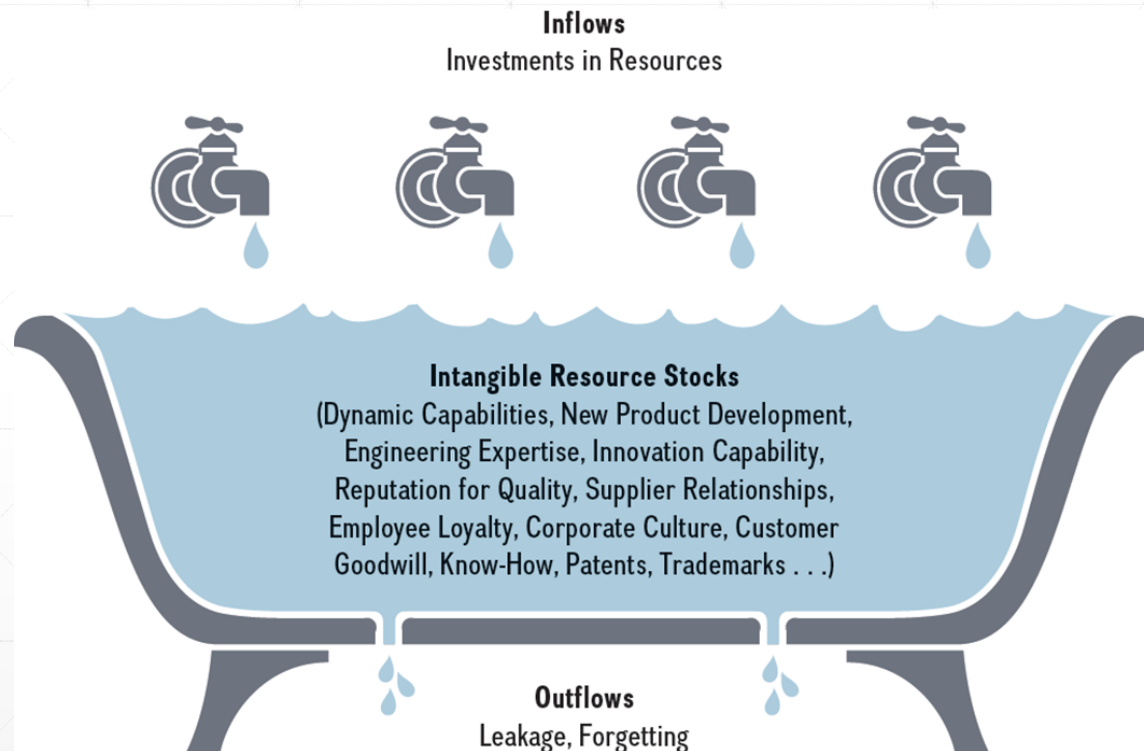


Exhibit 4.6

SOURCE: Figure based on metaphor used in I. Dierickx and K. Cool (1989), "Asset stock accumulation and sustainability of competitive advantage," *Management Science* 35: 1504–1513.

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The Value Chain

Internal activities a firm engages in when transforming inputs into outputs

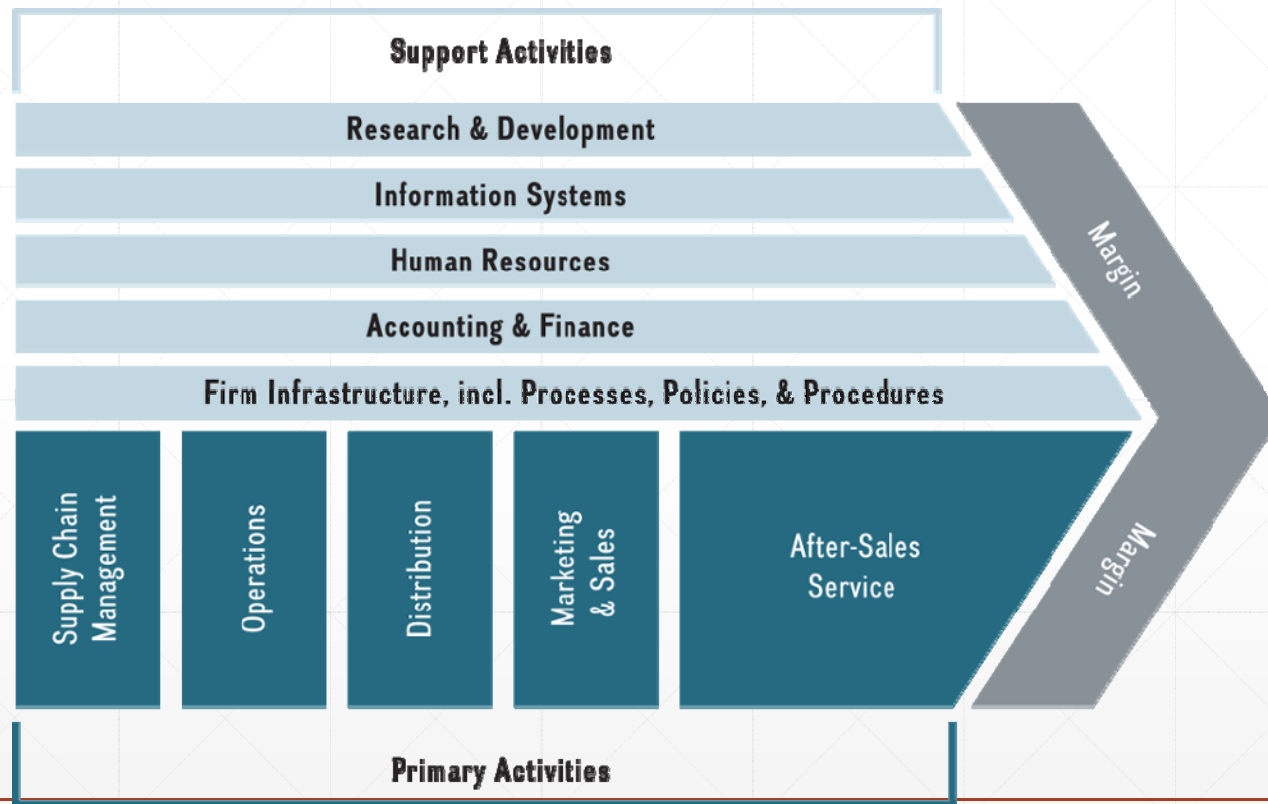
- Through primary and support activities

Each activity adds incremental value

- Raw materials → components → products

Each activity adds incremental costs

A Generic Value Chain



[Jump to Appendix 6 long image description](#)

Exhibit 4.7

Primary Activities

Firm activities that add value directly

Transform inputs into outputs as the firm moves a product or service horizontally along the internal value chain.

- Supply chain management
 - Operations
 - Distribution
 - Marketing and sales
 - After-sales service
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Support Activities

Firm activities that add value indirectly

Necessary to sustain primary activities

- Research and development (R&D)
 - Information systems
 - Human resources
 - Accounting and finance
 - Firm infrastructure
 - Processes, policies, and procedures
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Strategic Activity Systems

A network of interconnected activities

- Socially complex and causally ambiguous
- Enhance likelihood of sustained competitive advantage

Characteristics:

- Elements can be easily observed
 - How activities are managed is not easily observed
 - Difficult to imitate
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Strategic Activity Systems Must Evolve

External environment changes

Competitors develop their activity systems

How activity systems are updated:

- Add new activities
 - Remove activities that are no longer relevant
 - Upgrade activities that have become stale
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How to Generate Additional Insights

SWOT analysis combines external and internal analysis:

- External analysis: Covered in Chapter 3
- Internal analysis: Covered in Chapter 4

Purpose:

- Leverage internal strengths to exploit external opportunities
 - Mitigate internal weaknesses and external threats
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SWOT Analysis

A framework that allows managers to synthesize insights obtained from an internal and external analysis to derive strategic implications

Internal Analysis

- Strengths
- Weaknesses

External Analysis

- Opportunities
 - Threats
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Strategic SWOT Questions

How can the firm use strengths to take advantage of opportunities?

How can the firm eliminate or minimize an internal weakness to mitigate an external threat?

How can the firm use strengths to reduce the likelihood and impact of threats?

How can the firm overcome weaknesses to improve its ability to take advantage of an external opportunity?

The Final Step...

Evaluate the pros and cons of each strategic alternative.

Select one or more alternatives to implement.

Carefully explain decision rationale.

- Including why other strategic alternatives were rejected
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A Word of Caution

A strength can simultaneously be a weakness

An opportunity can simultaneously be a threat

Example:

- Google is located in Silicon Valley.
 - Strength: near Universities
 - Weakness: high cost of living
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