DIVING DEEP TO IDENTIFY CORE COMPETENCES

A key question we often raise with our Strategy Explorer clients when they are thinking about their strategy is: what should that strategy be built on ?

Should it be built on market opportunity or the strategic capabilities of the organization ?

In Exploring Corporate Strategy, we show how the identification of competences can be linked to an analysis of the competitive position of an organization. Separately, there is a white paper on competitor analysis on this website. What follows are edited extracts from chapter 3 of Exploring Corporate Strategy on competence analysis.

Unique resources and core competences

Having or creating a basis competitive advantage in a market is likely to be the basis of superior performance. Competitive advantage is dependent on an organisation having distinctive or unique capabilities that competitors will find difficult to imitate. This could be because the organisation has unique resources that underpin competitive advantage and that others cannot imitate or obtain – a long established brand, for example. It is, however, more likely that an organisation achieves competitive advantage because it has distinctive, or core, competences.

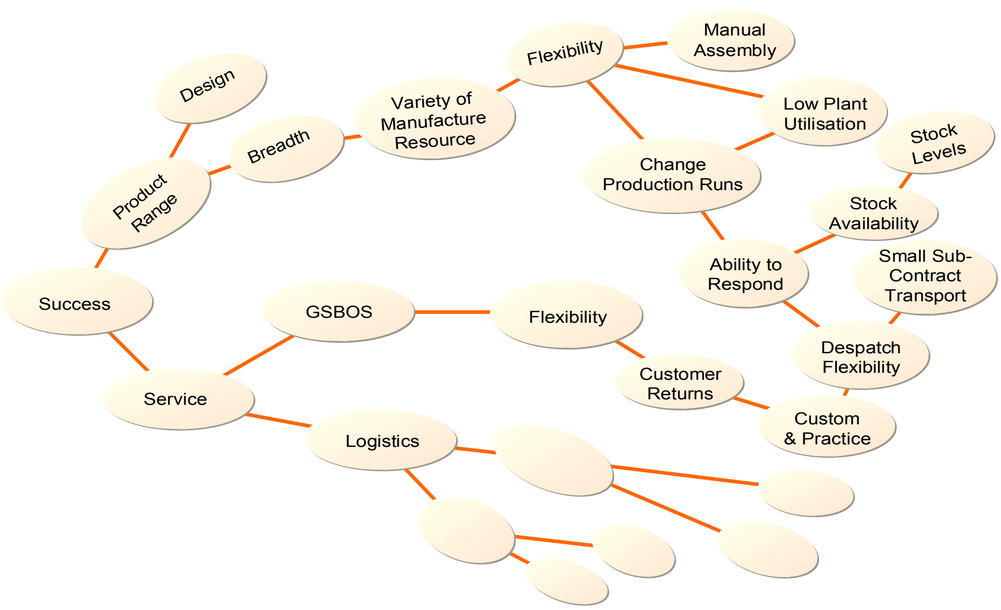
The concept of core competences was developed, most notably by Gary Hamel and C.K. Prahalad. While various definitions exist, here *core competences*[i] are taken to mean the skills and abilities by which resources are deployed through an organisations's activities and processes such as to achieve competitive advantage in ways that others cannot imitate or obtain. For example, a supplier that achieves competitive advantage in a retail market might have done so on the basis of a unique resource such as a powerful brand, or by finding ways of providing service or building relationships with that retailer in ways that its competitors find difficult to imitate – a core competence. But how can executives identify such competences?

Activity maps

Managers often find it difficult to identify with any clarity the strategic capability of their organisation. Too often they highlight capabilities not valued by customers but seen as important within the organisation, perhaps because they were valuable in the past. Or they highlight what are, in fact, critical success factors (product features particularly valued by customers) like 'good service' or 'reliable delivery', whereas strategic capability is about the resources, processes and activities that underpin the ability to meet such critical success factors. Or they identify capabilities at too generic a level. This is not surprising given that strategic capability may well be embedded in a complex set of linked activities. But if they are to be managed proactively, finding a way of identifying and understanding capabilities and the linkages that are likely to characterise competences is important.

One way of undertaking such diagnosis is by means of an activity map that tries to show how the different activities of an organisation are linked together. In chapter 3 of Exploring Corporate Strategy we use the example of a plastics manufacturer we refer to as Plasco. There are computer programs in existence that can be used for activity mapping; or it can be done more basically, for example by drawing network diagrams, as shown in Exhibit 1. This map was generated by groups of managers from within the organisation, working with a facilitator, mapping the activities of their organisation on a large blank wall initially by using Post-its®.

Exhibit 1:An Activity Systems Map (extract)



They began by undertaking a competitor analysis (search the Strategy Explorers Web site for a White Paper on Competitor Analysis). The aim here was to identify a) the critical success factors (CSFs) in relation to their customers and b) on which of these their business outperformed competitors. They identified the CSFs of brand reputation, product range, innovation, excellence of service and reliability of delivery and that Plasco was seen as particularly successful in relation to competitors in terms of its level of service and its product range. Managers were relatively easily able to identify what Michael Porter refers to as *higher order strategic themes*:[ii] that the main benefits it offered were to do with flexibility and rapid response. But the reasons why Plasco outperformed competitors did not emerge until these themes themselves were 'unpacked' by identifying the resources and competences that underpinned them. To do this managers kept asking themselves more and more specifically what activities 'delivered' the customer benefits. Exhibit 1 is only a selection of these activities. The eventual map consisted of hundreds of Post-its®, each representing an activity in some way contributing to strategic capability. The activity-based competences summarised in Exhibit 3.8 emerged from this diagnostic process.

When they analysed the bases of reliable delivery, they could not find reasons why they were outperforming competitors. The logistics of the company were no different from other companies. They were essential but not unique – threshold resources and competences.

When they examined the activities that gave rise to the good service they provided, however, they found other explanations. They were readily able to identify that much was down to their having a more flexible approach than their competitors, the main one of which was a major US multinational. But the explanations for this flexibility were less obvious. The flexibility took form, for example, in the ability to amend the requirements of the retailers' orders at short notice; or when the buyers in the retailers had made an error, to `bale them out' by taking back stock that had been delivered. What was much less obvious were the activities underpinning this flexibility. The mapping surfaced some explanations:

- The junior manager and staff within the firm were `bending the rules' to take back goods from the major retailers when, strictly speaking, the policies and systems of the business did not allow it.
- Plant utilisation was relatively lower and less automated than competitors, so it was easier to change production runs at short notice. Company policy, on the other hand, was to improve productivity through increased utilisation and to begin to automate the plans. Lower levels of production management were not anxious to do this, knowing that if they did, it would reduce the flexibility and therefore diminish their ability to provide the service customers wanted.

Much of this was down to the knowledge of quite junior managers, sales representatives and staff in the factory as to `how to work the system' and how to work together to solve the retailers' problems. This was not a matter of company policy or formal training; but it was custom and practice that had built up over the years. The result was a relationship between sales personnel and retail buyers in which buyers were encouraged to `ask the impossible' of the company when difficulties arose.

Sound logistics and good quality products were vital, but the core competences which underpinned their success were the result of linked sets of activities built up over the years which it was difficult, not only for competitors but also for people in the organisation, to clearly identify.

General lessons that can be drawn from such maps about how competitive advantage is achieved and the relationship between competences and competitive advantage include:

- *Consistency and reinforcement*. The different activities that create value to customers are likely to be pulling in the same direction and supporting rather than opposing each other (e.g. in Plasco an open management style facilitated rule bending and in turn flexibility).
- *Difficulties of imitation*. It is more difficult for a competitor to imitate a mix of linked activities than to imitate any given one. In Plasco such linked activities had been built up over years, culturally embedded, were complex and causally ambiguous – the lessons of section 3.4.3. If the multinational competitor of Plasco decided to try to compete on the same basis of flexibility it would have no comparable experience to draw on to do this.
- *Trade-offs*. Even if imitation were possible it could pose another problem for competitors. For example, Plasco's international competitor might place in jeopardy its current position with its existing customers that it is satisfying through more standardised mass production.

Developing strategic capabilities

There are different ways in which managers might develop strategic capabilities:

- *Adding and changing capabilities.* Could capabilities be added, or changed so that they become more reinforcing of outcomes that deliver against critical success factors? For example, in Plasco, could even faster internal ways of responding to customer needs be found?
- *Extending capabilities.* Managers might identify strategic capabilities in one area of the business, perhaps customer service in one geographic business unit of a multinational, that are not present in other business units. They might then seek to extend this throughout all the business units. Whilst this seems straightforward, studies find it is not. The capabilities of one part of an organisation might not be

easily transferred to another because of the problems of managing change (search the Strategy Explorers web site for a white paper on the Culture Web).

- *Stretching capabilities.* Managers may see the opportunity to build new products or services out of existing capabilities. Indeed, building new businesses in this way is the basis of related diversification.
- *Entrepreneurial bricolage*: There is evidence that strategic capabilities may be built by exploiting resources, skills and knowledge that have been ignored or rejected by others; indeed that this is often what entrepreneurs who develop new business models do.
- *Ceasing activities.* Could current activities not central to the delivery of value to customers be done away with, outsourced or reduced in cost? This is what new industry entrants, such as Ryanair or easyJet in the airline industry, did to create new business models for low cost airlines.
- *External capability development.* There may be ways of developing capabilities by looking externally For example, managers may seek to develop or learn new capabilities by, by acquisition or entering into alliances and joint ventures.

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[i] Gary Hamel and C.K. Prahalad were the academics who promoted the idea of core competences. For example: G. Hamel and C.K. Prahalad, 'The core competence of the corporation', *Harvard Business Review*, vol. 68 (1990), no. 3, pp. 79–91. The idea of driving

strategy development from the resources and competences of an organisation is discussed in G. Hamel and C.K. Prahalad, 'Strategic intent', *Harvard Business Review*, vol. 67 (1989), no. 3, pp. 63–76 and G. Hamel and C.K. Prahalad, 'Strategy as stretch and leverage', *Harvard Business Review*, vol. 71 (1993), no. 2, pp. 75–84. Also see G. Hamel and A. Heene (eds), *Competence-based Competition*, Wiley, 1994.

[ii] Michael Porter explains how mapping what he calls "activity systems" can be important in considering competitive strategy in his article 'What is strategy?' (*Harvard Business Review*, vol. 74, no. 6, Nov-Dec 1996, pp. 61-78).