

Session 3

Competitive Advantage in Economic Competition

In this session you will learn:

1. How superior value creation as the objective of marketplace exchange rules economic competition.
2. How your business can create more value
3. How your business can capture its share of that value to create value for the firm
4. How to analyze an industry value chain and your firm's place in that chain
5. How to use the five forces model to analyze industries and markets for their profit potential
6. How to focus firm resources on attractive segments of an industry to gain competitive advantage
7. How to identify a firm's sources of competitive advantage

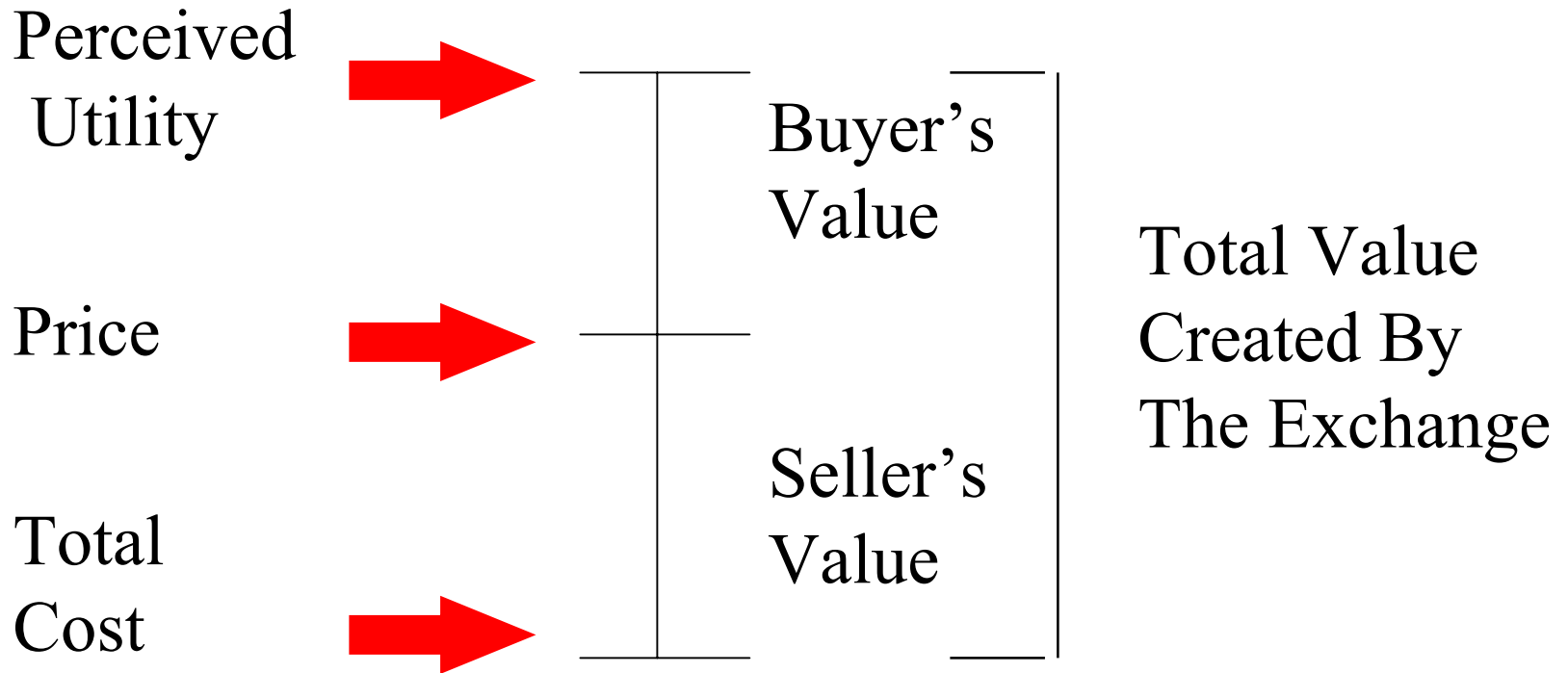
Strategy is the Route to Competitive Advantage

- GOALS
- OBJECTIVES
- STRATEGY
- TACTICS

The Game of Economic Competition

- Exchange creates value
- Competitive position determines who gets to exchange
- Power determines how value is allocated

Exchange Creates Value for Buyers and Sellers



To Win You Must...

- Create More value
- Capture More Value

Winners Increase Value By Delivering Higher Utility

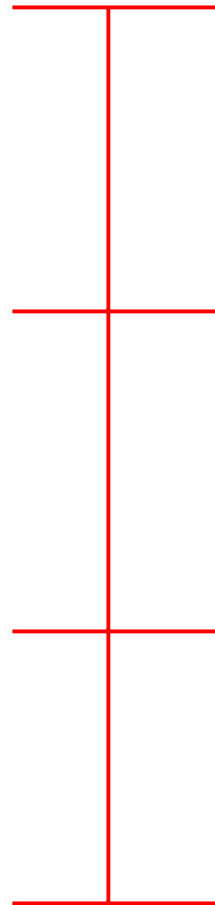
Advantaged Firm's
Perceived Utility

Product Patent
Knowledge of Customers
Locational Advantage

Competitor's
Perceived Utility

Price

Cost



Winners Increase Value By Delivering Higher Utility

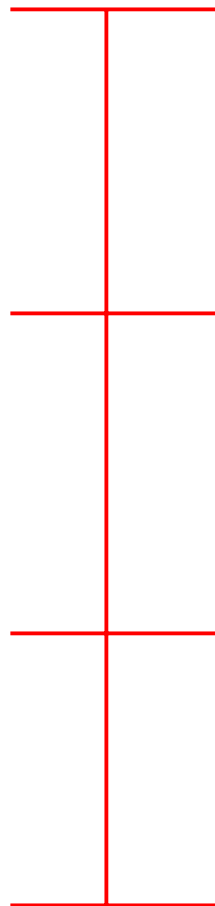
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**BUT CAPTURING VALUE
IS A DIFFERENT GAME**

The Players in the Game Share the Total Value That is Created



RAW MATERIALS

COMPONENTS

ASSEMBLED PARTS

ASSORTMENT OF PRODUCTS

DELIVERED SYSTEM

FOCAL PRODUCT

CUSTOMER / USER

Rules of the Game (1-3)

- Customer value sets ceiling on value available to chain
- Bargaining power determines allocation of value
- In the long run players in the game can only get the value they create

Competition Determines Ability to Capture Value

RAW MATERIALS

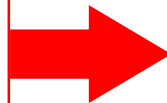
COMPONENTS

ASSEMBLED PARTS

ASSORTMENT OF PRODUCTS

DELIVERED SYSTEM

POTENTIAL
ENTRANTS



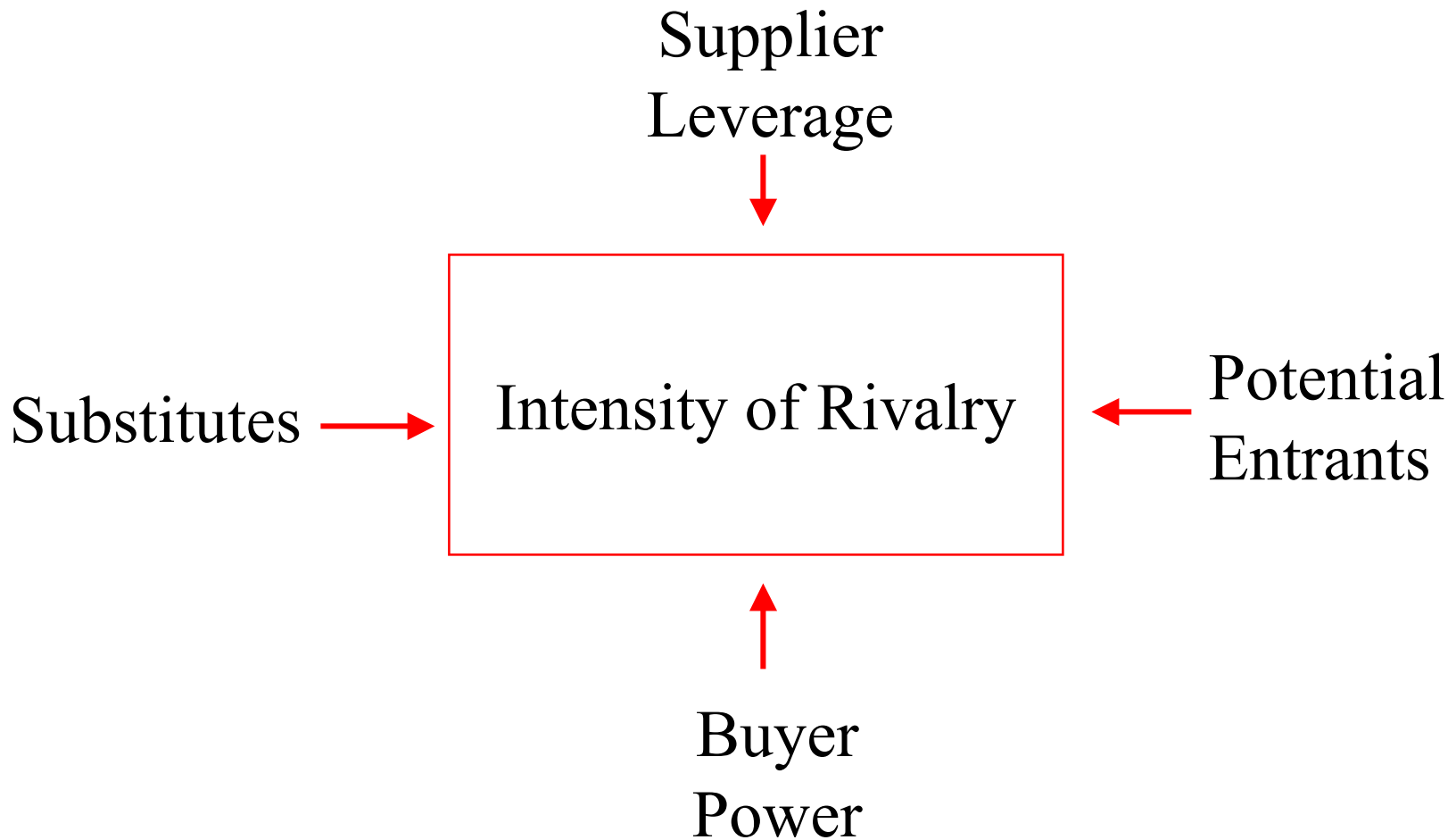
FOCAL PRODUCT



SUBSTITUTE
PRODUCTS

CUSTOMER / USER

Ability to Capture Value is Affected by Five Forces



The Customers Capture Value When...

- Product has little differentiation
- Low switching costs
- Few buyers buy large volume
- Product performance is not premium need
- Buyers have full information
- Backward integration is credible threat
- Buyers earn low profits

The Suppliers Capture Value When...

- Supplier's product has few substitutes
- High switching costs
- Supplier's product performance is important
- Few suppliers serve many customers
- Credible threat of forward integration

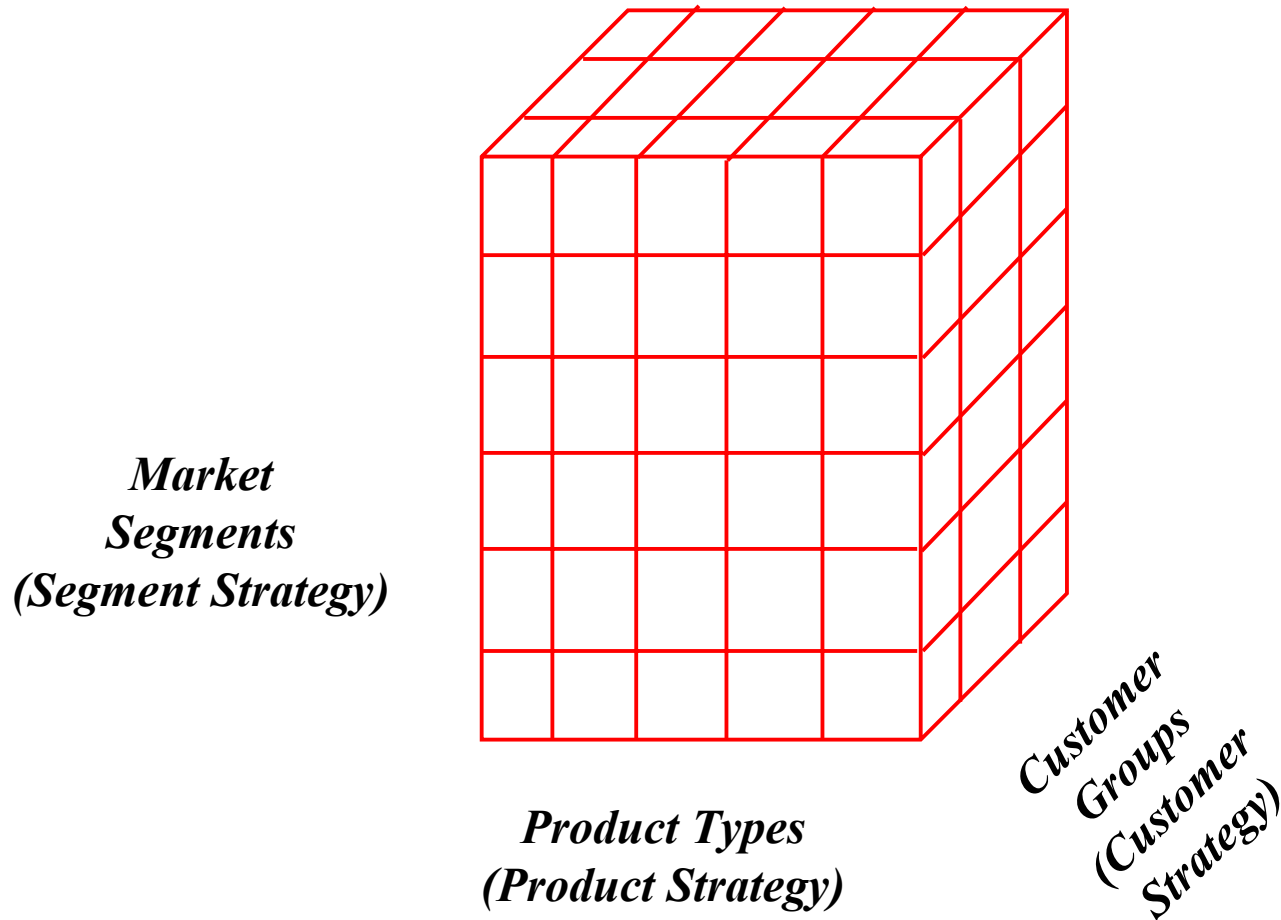
Industry Rivalry Determines Ability to Capture Value

- Intensity of competition within industry determines value captured by that industry
- Firm's competitive advantage determines its share of industry value

Rivalry is Intense When...

- Numerous, equally balanced competitors
- Slow industry growth
- High fixed costs
- Competitors have diverse goals
- High exit barriers
- There are high strategic stakes

The Ability to Create and Capture Value Varies Across the Industry



Winners Apply More Resources to Attractive Combinations

The Law of Competition

- Competition reduces profits to risk adjusted rate of return
- Supranormal profits are available only to firms with sustainable competitive advantage

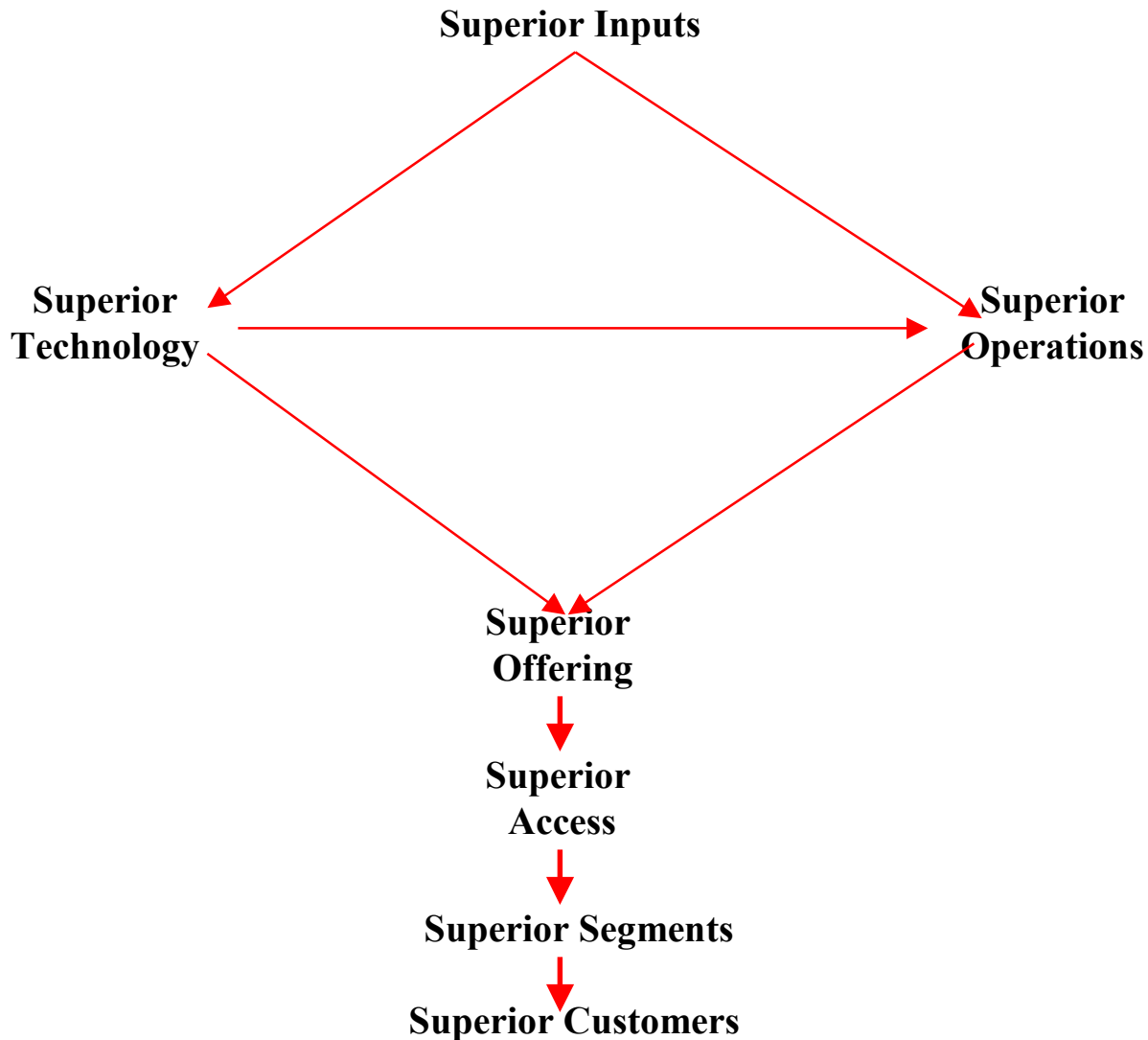
Final Rules of the Game (4-5)

- Existence of substitute products limits price industry can charge
- Threat of new entry limits supranormal profits

Good Strategies...

**ENABLE THE BUSINESS
TO SUSTAINABLY DELIVER
SUPERIOR VALUE
TO CHOSEN MARKET AND
TO KEEP ITS SHARE (OR MORE)
OF THE VALUE CREATED**

These are the Seven Sources of Competitive Advantage



Winning Strategies...

- Radically change the value equation
- Push the boundaries of the product market
- Increase accessibility--reduce distribution cost
- Compress the supply chain
- Anticipates and acts on shifts in the environment before rivals