Building Core Competencies

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Building core competencies using Four Criteria of Sustainable competitive advantage

Four Criteria are:

- Valuable capabilities
- Rare Capabilities
- Costly-to-imitate capabilities
- Non-substitutable capabilities

Core Competencies

- Core competencies are sources of competitive advantage for the firm over its rivals. Capabilities failing to satisfy the four criteria of sustainable competitive advantage are not core competencies, meaning that although every core competence is a capability, not every capability is a core competence.
- In slightly different words, for a capability to be a core competence, it must be valuable and unique from a customers point of view.
- For a competitive advantage to be sustainable, the core competence must be un-imitable and non-substitutable by competitors.

Sustained competitive advantage

- A sustained competitive advantage is achieved only when competitors cannot duplicate the benefits of a firms strategy or when they lack the resources to attempt imitation.
- For some period of time, the firm may earn a competitive advantage by using capabilities that are, for example, valuable and rare, but imitable.
- For example, Walmart initiated a major sustainability program that helped to reduce the use of containers, saving approximately 1000 barrels of oil and thousands of trees while simultaneously saving $2 million.
- GE’s ecomanagement system, through which it has developed an introduced new, “greener” products to meet growing demand, is another example.
- Sustainable competitive advantage results only when all four criteria are satisfied.

Criteria 1: Valuable

- Valuable capabilities allow a firm to exploit opportunities or neutralise threat in its external environment.
- By effectively using capabilities to exploit opportunities, a firm creates value for customers.
- Example: Under former CEO Jack Welch's leadership, GE built a valuable competence in financial services.
- It built this powerful competence largely through acquisitions and its core competence in integrating newly acquired businesses.

Criteria 2: Rare

- Rare capabilities are capabilities that few, if any, competitors posses.
- A key question to be answered when evaluating this criterion is, “How many rival firms posses these valuable capabilities?”.
- Capabilities possessed by many rivals are unlikely to be sources of competitive advantage for anyone of them.
- Instead, valuable but common resources and capabilities are sources of competitive parity.
- Competitive advantage results only when firms develop and exploit valuable capabilities that differ from those shared with competitors.

Criteria 3: Costly to imitate

- Costly to imitate capabilities are capabilities that other firms cannot easily develop. Capabilities that are costly to imitate are created because of one reason or a combination of three reasons:
- **Unique historical conditions**: A firm with a unique and valuable organizational culture that emerged in the early stages of the company's history 'may have an imperfectly imitable advantage over firms founded in another historical period'. Example: Arvind eye care derives its high effectiveness in eye care through a service oriented culture, where even the poorest patients are treated with respect.
- **Causally ambiguous**: Competitors cant clearly understand how a firm uses its capabilities as the foundation for competitive advantage. As a result, firms are uncertain about the capabilities they should develop so duplicate the benefit of a competitors value creating strategy. Example: For years, firms tried to imitate Southwest Airlines low cost strategy but most have been unable to do so, primarily because they cant replicate Southwests unique culture.
- **Social complexity**: Social complexity means that atleast some, and frequently many, of the firms capabilities are the product of complex social phenomena. Interpersonal relationships, trust, friendships among managers and between managers are employees, and a firms reputation with suppliers and customers are examples of social complex capabilities.

Criteria 4: Non-substitutable

- Non-substitutable capabilities are capabilities that do not have strategic equivalents. This final criterion for a capability to be a source of competitive advantage is that there must be no strategically equivalent valuable resources that are themselves either not rare or imitable.
- In general, the strategic value of capabilities increases as they become more difficult to substitute. The more invisible the capabilities are, the more difficult it is for firms to find substitutes and the greater the challenge is to competitors trying to imitate a firms value creating strategy.
- Firm specific knowledge and trust based working relationships between managers and nonmanagerial personnel, such as existed for years at Southwest Airlines, are examples of capabilities that are difficult to identify and for which finding a substitute is challenging.

Outcomes from combinations of the criteria for sustainable competitive advantage

Is the resource or capability valuable?	Is the Resource or Capability rare?	Is the Resource or Capability costly to imitate?	Is the resource or capability Non-substitutable?	Competitive consequences
No	No	No	No	Competitive Disadvantage
Yes	No	No	Yes/No	Competitive parity
Yes	Yes	No	Yes/No	Temporary competitive advantage
Yes	Yes	Yes	Yes/No	Sustainable competitive advantage

- References: Strategic Management, Michael A.Hit. et all, 2012, Cenage Learning.