Chapter 3 – The internal environment: Resources, capabilities, core competencies and competitive advantages

TRUE/FALSE

1. A firm should try to obtain a sustainable competitive advantage by implementing strategies based on its particular resources, capabilities and core competencies.

   ANS: T PTS: 1 DIF: Moderate REF: Introduction

2. Competitive advantages that firms possess are permanent.

   ANS: F PTS: 1 DIF: Moderate REF: Introduction

3. A global mind-set is the ability to study an internal environment in ways that depend on the assumptions of a single country, culture and context.

   ANS: F PTS: 1 DIF: Moderate REF: The context of internal analysis

4. The analysis of a firm's internal environment requires evaluators to examine the firm's portfolio of strategies and the bundles of homogenous resources and capabilities managers have created.

   ANS: F PTS: 1 DIF: Moderate REF: The context of internal analysis

5. Increasingly customers perceive higher value in global rather than domestic brands.

   ANS: T PTS: 1 DIF: Moderate REF: Creating value

6. Firms create value by innovatively bundling and leveraging their resources and capabilities.

   ANS: T PTS: 1 DIF: Moderate REF: Creating value

7. Sometimes mistakes are made as the firm analyses conditions in its internal organisation.

   ANS: T PTS: 1 DIF: Easy REF: The challenge analysing the internal organisation

8. We can often locate information about a firm's sources of competitive advantage in its corporate financial information.

   ANS: F PTS: 1 DIF: Hard REF: Tangible resources

9. Value-creating reputation is a quick way for firms to win the hearts of stakeholders.

   ANS: F PTS: 1 DIF: Hard REF: Intangible resources

10. Capabilities of an organisation emerge over time through complex interactions between and among tangible and intangible resources.

    ANS: T PTS: 1 DIF: Moderate REF: Capabilities

11. All resources and capabilities are core competencies.

    ANS: F PTS: 1 DIF: Moderate REF: Core competencies

12. Every core competence is a capability and every capability is a core competence.

ANS: F PTS: 1 DIF: Moderate REF: Core competencies

13. While valuable capabilities decrease competitive rivalry, rare capabilities increase it.

ANS: F PTS: 1 DIF: Hard REF: The four criteria of sustainable competitive advantage

14. Capabilities may be easy to imitate if they are causally ambiguous or socially complex.

ANS: F PTS: 1 DIF: Moderate REF: Costly to imitate

15. For capabilities to be a source of competitive advantage, they must allow a firm to perform value-creating activities in a manner that provides value similar to that provided by competitors.

ANS: F PTS: 1 DIF: Moderate REF: Non-substitutable

16. A value chain analysis examines how a firm's external activities are aligned with its primary activities.

ANS: F PTS: 1 DIF: Easy REF: Value chain analysis

17. Outsourcing is a way of adding value to a business that converts an external value-creating activity into an internal supplier.

ANS: F PTS: 1 DIF: Hard REF: Outsourcing

18. Partnership management and operational skills are essential skills that managers need to possess in order to carry out outsourcing programs.

ANS: F PTS: 1 DIF: Hard REF: Outsourcing

19. Once a firm has developed core competencies that can create value, it can use these core competencies as a permanent competitive advantage.

ANS: F PTS: 1 DIF: Moderate REF: Competencies, strengths, weaknesses and strategic decisions

20. Changes in the external environment cause core competencies to become core rigidities.

ANS: F PTS: 1 DIF: Moderate REF: Competencies, strengths, weaknesses and strategic decisions

MULTIPLE CHOICE

1. Which of the following is *not* a factor that determines the sustainability of a competitive advantage?
   A. The rate of core competence obsolescence because of environmental changes
   B. The availability of substitutes for the core competence
   C. The inimitability of the core competence
   D. The extent of a core competence's effect on a firm's operations

   ANS: D PTS: 1 DIF: Moderate REF: Introduction

2. The term a *global mind-set* refers to the ability:
   A. to study an external environment in ways that are dependent on the assumptions of a single firm
   B. to study an internal environment in ways that are dependent on the assumptions of a single country
   C. to develop a competitive advantage in multiple markets
   D. to develop human resources policies in culturally diverse markets

   ANS: C PTS: 1 DIF: Hard REF: The context of internal analysis

3. Evidence has suggested that ________ of organisational decisions fail.
   A. 70 per cent
   B. 60 per cent
   C. 50 per cent
   D. 40 per cent

   ANS: C PTS: 1 DIF: Hard REF: The challenge of analysing the internal organisation

4. The three conditions that characterise difficult managerial decisions concerning resources, capabilities and core competencies are:
   A. imitability, complexity and interorganisational conflicts
   B. uncertainty, value and availability of resources
   C. uncertainty, complexity and interorganisational conflicts
   D. complexity, rarity and capacity

   ANS: C PTS: 1 DIF: Hard REF: The challenge of analysing the internal organisation

5. The condition of uncertainty in managerial decision making occurs when:
   A. it is difficult to determine which core competency to nurture
   B. a wide range of internal issues must be examined
   C. there are changes in technologies, economic and political trends, and societal values
   D. managers are unable to determine the best course of action to take

   ANS: C PTS: 1 DIF: Hard REF: The challenge of analysing the internal organisation

6. Competitive advantage typically comes from:
   A. individual resources
   B. one very outstanding resource
   C. several outstanding resources acting independently
   D. the unique bundling of several resources

   ANS: D PTS: 1 DIF: Moderate REF: Resources

7. Intangible resources include:
   A. a firm’s reputation for its goods and services
   B. a firm’s borrowing capacity
   C. depreciated capital assets
   D. manufacturing facilities

   ANS: A PTS: 1 DIF: Moderate REF: Intangible resources

8. A firm's reputation for its goods and services is:
   A. not an issue of principle concern for a firm
   B. an example of an intangible resource that can provide a competitive advantage
   C. a resource for the firm against which funds can easily be borrowed
   D. an example of a tangible resource

   ANS: B PTS: 1 DIF: Moderate REF: Intangible resources

9. Relative to tangible resources, intangible resources are:
   A. of less value to the firm
   B. not the focus of strategic analysis
   C. more difficult for competitors to imitate
   D. more likely to be reflected on the firm's balance sheet

   ANS: C PTS: 1 DIF: Hard REF: Intangible resources

10. Which of the following is a true statement about capabilities?
    A. Capabilities derive from a firm's capacity to deploy resources that have been integrated to achieve a desired end state.
    B. Capabilities emerge quickly when resources interact.
    C. Human capital is not a capability.
    D. Capabilities become weaker and less valuable through repetition and practice.

    ANS: A PTS: 1 DIF: Hard REF: Capabilities

11. The primary basis for a firm's capabilities is:
    A. its ability to increase capacity as demand warrants
    B. the amount of capital resources readily available
    C. the good reputation it has built throughout its customer base
    D. the skills and knowledge of its employees

    ANS: D PTS: 1 DIF: Moderate REF: Capabilities

12. Which of the following tools can help identify and build core competencies?
    A. Porter's five forces model and value chain analysis
    B. Scanning and the four criteria of sustainable competitive advantage
    C. Value chain analysis and the four criteria of sustainable competitive advantage
    D. Porter's five forces model and internal analysis

    ANS: C PTS: 1 DIF: Hard REF: Building core competencies

13. A firm's resources and capabilities:
    A. are inherited, not created
    B. are always core competencies
    C. may be a source of incompetence
    D. are all a firm needs to focus on

    ANS: C PTS: 1 DIF: Hard REF: Value chain analysis

14. Resources and capabilities are core competencies only when their use:
    A. leads to a competitive advantage for a firm
    B. permits the diffusion of threats in the external environment
    C. provides opportunities to defeat competitors
    D. encourages quick responses to changes in the global economy

    ANS: A PTS: 1 DIF: Moderate REF: Building core competencies

15. From the customer's point of view, a capability can be a core competence if it is:
    A. easily accessible to workers
    B. supported by the top management team
    C. valuable and non-substitutable
    D. a stable feature of the firm's environment

    ANS: C PTS: 1 DIF: Hard REF: The four criteria of sustainable competitive advantage

16. Capabilities that other firms cannot develop easily are classified as:
    A. rare
    B. valuable
    C. non-substitutable
    D. costly to imitate

    ANS: D PTS: 1 DIF: Moderate REF: Costly to imitate

17. Which of the following is *not* a condition of costly to imitate capability?
    A. Social complexity
    B. Causally ambiguous
    C. Human skills
    D. Unique historical conditions

    ANS: C PTS: 1 DIF: Moderate REF: Costly to imitate

18. Causally ambiguous means that:
    A. the connection between cause and effect of capital is unclear in a firm
    B. rivals find it difficult to understand the link between a firm's competencies and its competitive advantage
    C. the connection between industry and firm performance is unclear
    D. the effect of a firm's resources are unclear to the firm itself

    ANS: B PTS: 1 DIF: Hard REF: Costly to imitate

19. A firm's inability to understand how a competitor uses its competencies to gain competitive advantage is an example of:
    A. social complexity
    B. causal ambiguity
    C. the rarity of a capability
    D. the non-substitutability of a capability

    ANS: B PTS: 1 DIF: Hard REF: Costly to imitate

20. Value chain analysis is a tool used to:
    A. analyse a firm's external environment
    B. concentrate on a firm's internal environment without addressing concerns about the actions of competing firms
    C. examine a firm's resources and capabilities to identify its core competencies
    D. determine the expected duration of an opportunity in a firm's external environment

    ANS: C PTS: 1 DIF: Hard REF: Value chain analysis

21. Value chain activities can be:
   A. analysed only in for-profit organisations
   B. segmented into primary and support activities
   C. segmented into resources and capabilities
   D. analysed, but are of little use in building a competitive advantage for a firm

   ANS: B PTS: 1 DIF: Easy REF: Value chain analysis

22. Value-creating primary activities include:
   A. purchasing raw materials and supplies
   B. developing an appropriate corporate structure
   C. selecting appropriate distribution channels
   D. planning corporate strategy and setting goals

   ANS: C PTS: 1 DIF: Hard REF: Value chain analysis

23. Value chain support activities include:
   A. converting inputs into product
   B. developing advertising and promotional campaigns
   C. distributing the product to customers
   D. recruiting, hiring and training personnel

   ANS: D PTS: 1 DIF: Hard REF: Value chain analysis

24. Outsourcing involves:
   A. selling a value-creating activity to other firms in an industry
   B. selling a value-creating activity to other firms, regardless of their industry
   C. purchasing a value-creating activity from an external supplier
   D. using computers to obtain data from the internet

   ANS: C PTS: 1 DIF: Moderate REF: Outsourcing

25. Outsourcing does not work effectively without:
   A. having value-creating support activities outsourced
   B. building networks with outsourcing partners
   C. extensive internal capabilities to coordinate external sourcing
   D. having value-creating primary activities outsourced

   ANS: C PTS: 1 DIF: Hard REF: Outsourcing

26. Which of the following is *not* an essential skill that a manager needs to possess to manage outsourcing programs?
   A. Change management
   B. Extended diversification
   C. Strategic thinking
   D. Partnership governance

   ANS: B PTS: 1 DIF: Moderate REF: Outsourcing

27. When selecting activities to outsource, firms should select activities that:
   A. capture and create value
   B. neutralise external threats
   C. are critical to their success
   D. are non-strategic capabilities

   ANS: D PTS: 1 DIF: Hard REF: Outsourcing

28. What causes core capabilities to become core rigidities?
    A. Changes in the external and internal environment
    B. Inertia and competition
    C. Strategic myopia and inertia
    D. Lack of knowledge and poor use of assets

    ANS: C PTS: 1 DIF: Hard REF: Competencies, strengths, weaknesses and strategic decisions

ESSAY

1. Do competitive advantages last forever? Explain your answer.

   ANS:
   No, competitive advantage does not last forever. Over time, rivals use their own unique resources, capabilities and core competencies to form different value-creating propositions that duplicate the focal firm's ability to create value for customers. Because competitive advantages are not permanently sustainable, firms must exploit their current advantages while simultaneously using their resources and capabilities to form new advantages that can lead to future competitive success.

   PTS: 1 DIF: Easy REF: Introduction

2. Explain the role of innovation in a firm's competitive advantage.

   ANS:
   Innovation has historically been important for economic development and company profitability, but, currently, it is particularly crucial in terms of intensity, speed and scale of development, and diffusion of knowledge and technologies. Enhanced competition has made innovation increasingly important in all types of markets. Incremental improvements in products and processes are no longer enough to sustain a competitive advantage in many industries. Innovative capabilities have become unavoidable in order to remain competitive.

   PTS: 1 DIF: Moderate REF: Introduction

3. Describe the importance of internal analysis to the strategic success of a firm.

   ANS:
   In today's global competition, the traditional sources of competitive advantage (e.g. labour costs, capital costs and raw materials) are much less effective. Rather, modern firms should see themselves as a bundle of heterogeneous resources, capabilities and core competencies that can be used to create an exclusive market position. Therefore, a firm must understand its capabilities and how they lead to core competencies, and it must have a similar understanding of competitors' capabilities. This understanding is generated through an internal analysis.

   PTS: 1 DIF: Moderate REF: The context of internal analysis

4. How do firms create value? How is value measured?

   ANS:
   Firms use their resources as the foundation for producing goods or services that will create value for customers. Value is measured by a product's performance characteristics and by its attributes for which customers are willing to pay. Firms create value by innovatively bundling and leveraging their resources to form capabilities and core competencies.

   PTS: 1 DIF: Easy REF: Creating value

5. How can managers deal with conditions affecting decisions about resources, capabilities and core competencies?

   ANS:
   Judgement is required when making decisions related to these conditions. Judgement is the capability of making successful decisions when there is no obviously correct model or rule or when relevant data are unreliable or incomplete. In this type of situation, decision makers must be aware of possible cognitive biases. For example, overconfidence can often lower value when a correct decision is not obvious, such as when determining whether an internal resource is a strength or weakness.

   When exercising judgement, decision makers often take intelligent risks. In the current competitive landscape, executive judgement can be a particularly important source of competitive advantage. One reason is that, over time, effective judgement allows a firm to build a strong reputation and retain the loyalty of stakeholders whose support is linked to above-average returns.

   Significant changes in the value-creating potential of a firm’s resources and capabilities can occur in a rapidly changing global economy. Because these changes affect a company’s power and social structure, inertia or resistance to change may surface. Even though these reactions may happen, decision makers should not deny the changes needed to assure the firm’s strategic competitiveness. If the need for change is ignored, difficult experiences can be avoided in the short run. However, in the long run, the failure to change when needed leads to performance declines and, in the worst-case scenario, to failure.

   PTS: 1 DIF: Moderate REF: The challenge of analysing the internal organisation

6. Describe the various types of resources.

   ANS:
   Resources are either tangible or intangible. Tangible resources are those assets that can be seen and quantified. There are four types of tangible resources: financial resources (borrowing capacity, ability to generate internal funds); physical resources (plant and equipment, access to raw materials); technological resources (patents, trademarks and copyrights); and organisational resources (formal reporting structure, controlling and coordinating systems). Intangible resources are those assets in the firm that cannot be seen. There are three types of intangible resources: human resources (knowledge, trust, management capabilities and organisational routines); resources for innovation (ideas, scientific capability and innovation potential); and reputation (brand name, perceptions of product quality and supplier relations).

   PTS: 1 DIF: Hard REF: Resources

7. Discuss the relationship between capabilities and core competencies.

   ANS:
   Not all of a firm’s resources and capabilities are strategic assets – that is, assets that have competitive value and the potential to serve as a source of competitive advantage. Some resources and capabilities may result in incompetence because they represent competitive areas in which the firm is weaker than its competitors. Thus, some resources or capabilities may stifle or prevent the development of a core competence. Of course, not all capabilities are core competencies, and some firms can have weaknesses in important capabilities that detract from their core competencies.

   PTS: 1 DIF: Moderate REF: Core competencies

8. Describe the four specific criteria that managers can use to decide which of their firm’s capabilities have the potential to create a sustainable competitive advantage.

   ANS:

Core competencies are capabilities that are valuable, rare, costly to imitate and non-substitutable as well as a source of sustainable competitive advantage. For a capability to be valuable means that it helps a firm exploit opportunities and/or neutralise threats in the external environment. Rare means that a capability is possessed by few if any potential competitors. Costly to imitate means that a capability cannot be easily developed by other firms. Finally, non-substitutable capabilities do not have strategic equivalents.

PTS: 1 DIF: Easy REF: The four criteria of sustainable competitive advantage

9. Describe value chain analysis.

ANS:
Value chain analysis allows a firm to evaluate its resources and capabilities by understanding the activities that create value for the firm. There are two central types of activities in a value chain, primary activities and support activities. Primary activities are those that are involved in a product's physical creation, its sale and distribution to buyers and its service after the sale. Support activities are those activities necessary for the primary activities to occur.

To conduct a value chain analysis, people should study and identify all activities of a firm and evaluate how they impact efforts to create value for the customer. Analysis should be conducted in conjunction with an assessment of the competitor's capabilities in the same areas.

PTS: 1 DIF: Moderate REF: Value chain analysis

10. Discuss the risks of outsourcing.

ANS:
There are concerns about the consequences of outsourcing. For the most part, these concerns revolve around firms potentially risking the ability to innovate as well as job loss when work is outsourced to other companies. This may lead to social and political difficulties. Additionally, outsourcing does not always deliver the value expected, and there is the risk that an outsourcing partner could learn the technology and become a competitor.

PTS: 1 DIF: Moderate REF: Outsourcing