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THE IMPORTANCE OF BUILDING A SUSTAINABLE COMPETITIVE ADVANTAGE AND HOW IT DIRECTLY COORELATES WITH AN ORGANIZATIONS' LONG-TERM SUCCESS

by

TRENTON MCNAIRY

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THE UNIVERSITY OF TEXAS AT ARLINGTON

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April 10, 2019

ABSTRACT

THE IMPORTANCE OF BUILDING A SUSTAINABLE COMPETITIVE ADVANTAGE AND HOW IT DIRECTLY COORELATES WITH AN ORGANIZATIONS' LONG-TERM SUCCESS

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The University of Texas at Arlington, 2019

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This research focuses on the importance of building a sustainable, competitive advantage within an organization, and highlights how the imitability of an organization's competitive advantage directly correlates with the long-term success of that organization. Additionally, this project touches on the hardships some organizations in the retail industry are facing in today's market and how the organizations who are not performing well are potentially being affected by the inflexibility and unsustainability of their firm's founding competitive advantage(s).

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CHAPTER 1

INTRODUCTION

Building a competitive advantage is the most important aspect of creating any business or organization but developing one that is sustainable is even more challenging. Perhaps this is why entrepreneurs and business investors argue the first step in creating a business is to conduct a feasibility analysis. By conducting a feasibility analysis, the entrepreneur is forced to consider whether or not they can imbed a sustainable competitive advantage into their business model or product/service. The failure to create a competitive advantage that is not sustainable is the reason many brick-and-mortar retailers are closing their doors for good. Available research on competitive advantages sheds light on the importance of imbedding this factor into any business. This research can explain why many retailers are facing hardships today. Through this research, the importance of an inimitable competitive advantage and how it directly correlates with the long-term success of an organization is highlighted. Today’s retailers, successful and failing, will provide insight on how some organizations are excelling and why some firms are continuing to face closure despite their attempts to remain afloat. After analyzing these organizations, current findings can explain why such organizations are in the position they are in. This research can provide insight to organizations of all sizes in regard to the sustainability and long-term success of their business model.

The primary questions include; what is a sustainable competitive advantage? How is it implemented? Why is it so important? How can it affect my organization? All of these

important questions can be answered through research and findings. Beginning with thefirst, a sustainable competitive advantage is a long-term competitive advantage that is not easily replicated by another rival. Easy, right? In essence, it is what creates value for any business, and differentiates them from their competitors. It is also a factor that hopefully creates a high barrier to entry, preventing others from entering your market. But this challenge can be a huge step ahead of other organizations and is possibly the most challenging aspect to achieve. While an excellent competitive advantage embodies several of these aspects, it is difficult to implement one that benefits from all mentioned characteristics. Throughout several chapters, this paper will address multiple models and frameworks created by scholars, businesspeople, and experienced entrepreneurs who have summarized ways in which a firm can remain competitive in such a challenging market.

CHAPTER 2

STRATEGIC MANAGEMENT

Jay Barney, the father of the resource-based view, states there are four components to the sustainable competitive advantage: "Value, rareness, inimitability, and sustainability." While delving further into detail on these characteristics, keep in mind that according to Barney, an excellent long-term advantage for an organization will embody these four characteristics.

Barney is best known for his contributions to the resource-based view of a competitive advantage in the 90s. While his work builds on Michael Porter's Five Forces Model, Barney's work focuses more within the realms of intra-industry competition. To simplify, intra-industry competition is when two firms who are in the same industry are competing. An example of intra-industry competition would be Target and Wal-Mart as they are both full-line discount retailers who typically target the same customer base. Barney's resource-based view attempts to explain why some firms in one industry do better than another. This view focuses on how an existing firm can use their current resources to create a sustainable competitive advantage; again, tying this back to the importance of a firm's competitive advantage. Most importantly, the resource-based theory signifies the four components mentioned earlier and how they come together to create a sustainable competitive advantage rather than just competitive parity.

Research conducted by Jay Barney creates a framework distinguishing four different levels of performance among firms. The framework establishes competitive

disadvantage, competitive parity, temporary competitive advantage, and sustained competitive advantage all as a different level of firm performance. Beginning with the first of four, competitive disadvantage describes a firm with resources, which do not increase its revenues or decrease its costs. This firm's resources are not seen as valuable and are a source of competitive disadvantage. An example of a firm designated as suffering from competitive disadvantage would be one who pays for unnecessary things not resulting in a return on their investment. Competitive parity describes a firm with resources that are valuable but not rare. This resource would be necessary to satisfy a customer, but something they could also get elsewhere. An example could be a high-end retailer who offers free alterations. If a customer's favorite retailer did not offer this service, they might go down the street to another high-end retailer that does. While this is necessary to keep customers, it is a service that is also offered by many other retailers and, therefore, is only a source of competitive parity. The third level is temporary competitive advantage. A firm at this level would have resources, which are valuable and rare. The problem with this level is new entrants to the market can arrive at any time and steal valuable customers. A temporary competitive advantage is just as simple as a new firm entering the market that is able to do business in a way, which outperforms existing firms. Because the existing firm was not able to create a competitive advantage that is valuable, another firm is able to enter the market. This is why it is imperative to protect these resources by making them costly to imitate, thus achieving the fourth level of performance; sustained competitive advantage. This level is the most highly regarded and is the level all organizations strive to achieve.

The resource-based model assumes the unique collection of capabilities and resources possessed by an organization is what helps the organization determine its strategy

to compete against other rival firms; this also defines strategic management. As Jay Barney notes, strategic management is a firm's source of competitive advantage. The theory suggests how a firm can capitalize on its existing capabilities or opportunities in order to gain a long-term competitive advantage. There are many companies who neglect certain resources belonging to their firm and fail to realize how those resources could actually be a source of competitive advantage. Being aware of those opportunities is the basis of strategic management and also describes several components of a Strengths, Weaknesses, Opportunities, and Threats (SWOT) analysis. Similarly, from a strategic management point of view, it is important for managers to think outside of the box and find new uses for current resources or realize how economies of scale can potentially give a firm a leg up on their competitors.

CHAPTER 3

STRATEGIC MANGEMENT ANALYSES

A great example of a firm who analyzed their current market for new opportunities using their existing resources is Gap Inc. In 2011, Gap publicly acquired a small catalog-based athleisurewear brand called Athleta. At the time, Gap Inc. was trying to diversify their portfolio. Athleta, a retailer of clothing in a market Gap Inc. had currently not ventured into before was an optimistic opportunity. Not only would Gap Inc. be able to diversify their portfolio of brands by jumping into the quickly growing athleisurewear market, but they would be able to use their current resources to gain a leg up on other retailers who were currently in the market. Gap Inc. was smart to acquire a brand that already had a loyal following rather than starting from scratch and creating an entirely new brand, which would entail attracting an entirely new market and focusing on market expansion as their only option to gain new loyal customers. This was a strategic move on Gap's part because the only other major retailer thriving in this segment at the time of acquisition was Lululemon Athletica. While this is not the case anymore, Athleta and Lululemon now hold most of the market share for the upscale athleisurewear market.

Gap Inc. took a small catalog-based company and utilized their company's resources to scale their new acquisition quickly. By tapping into a pool of qualified candidates from their existing brands, Athleta was able to create a stellar management team. Athleta was also able to use Gap Inc.'s knowledge on scaling stores to develop their own store models. The brand used existing store formats previously used by Gap and

Banana Republic to cut down on entirely new expansion and store design costs. They also benefited from using similar technology as Gap Inc.'s other brands in order to continue contracting with companies who Gap Inc. already had an established relationship with. By taking advantage of all of these opportunities, Athleta was able to strategically grow in size rapidly. The first brick-and-mortar store was opened within the first year of acquisition and numerous other successful stores were opened within the following years. Today, Athleta has over 180 stores across the nation with less than eight years of growth under its belt. This is an enormous accomplishment that Athleta was able to complete through the opportunities their sister brands created for them.

The acquisition of Athleta by Gap Inc. was a strategic move because the organization saw a growing market for athleisurewear and knew they possessed the knowledge and experience to develop a new brand that could potentially be a source of competitive advantage for the newly acquired subsidiary. This has proven to be a sustainable competitive advantage because of Athleta's enormous success and its ability to take a hold of the market share, forcing other athleisure brands out of the market. Using the firm's current resources, whether they are tangible or intangible, was an excellent way for Gap Inc. to practice strategic management.

An example of a company who did not analyze their organization for potential opportunities is Wal-Mart. Wal-Mart now competes directly with Amazon as an etailer (online retailer), but still relies heavily on their physical locations to bring in most of their revenue. Wal-Mart had the resources and capabilities to scale as quickly as Amazon did. In fact, Wal-Mart had a better opportunity because of their ginormous fleet of physical locations, loyal customers, brand name recognition, and connection of warehouses and

distribution centers across the US. Amazon did not benefit from any of these advantages, but they had analyzed the market for opportunities and knew the direction retailers were heading: etailing. By the time Wal-Mart realized the opportunities their resources could have developed, Amazon was already dominating the online sales market and had created their own sustainable competitive advantages that Wal-Mart could not as easily penetrate. Now, Wal-Mart still directly competes with Amazon, but they continue having to rely on their physical store locations as a primary revenue source. Had Wal-Mart continuously been analyzing their organization for opportunities and thought about using its resources in a way which might be more efficient or generate more revenue, the organization might have been the one dominating the online sales market today.

This is a current example of how Wal-Mart was not practicing strategic management to zero in on the organization's unique collection of resources and capabilities, and why Amazon is still able to outperform Wal-Mart as an etailer today. This example breaks strategic management down to its core ideology: to determine why some firms (within competing industries) outperform other firms. It all boils down to the use of an organization's resources and how these resources can be a source of competitive advantage for the firm, whether it is a temporary advantage or a more long-term, sustainable opportunity for the company. The acknowledgement and use of strategic management practices is essential for a firm who wants to make the best use of their resources.

CHAPTER 4

SWOT ANALYSIS

Strategic Management is tied back to SWOT analyses in research conducted by Jay Barney. One of the most commonly known models, a SWOT analysis, is broken into four components; strengths, weaknesses, opportunities, and threats. While there are four components, they are divided into two groups of two components each. The first group being internal phenomena and the second being external phenomena. The first grouping includes a firm's strengths and weaknesses. These are both internal factors of the firm; aspects the firm controls directly and chooses to act or not act upon. A strength for the firm is any characteristic of the organization that gives them a leg up against their competitors. A weakness is any characteristic that disables the firm from outperforming intra-industry competition. Alternatively, there are the external factors of a firm. These external factors include the last two letters of the acronym, opportunities and threats. Opportunities are a positive, external factor that a company can take advantage of. Gap Inc. acquiring Athleta was an opportunity the firm recognized and proceeded to utilize their strengths to take advantage of the opportunity. Threats can be defined as a negative, external factor a firm might face. A threat can come in many forms, but typically retailers suffer from threats such as changing market landscapes, government regulations, or other competitors increasing their market share.

Many entrepreneurs will lump a SWOT analysis in with their feasibility analysis or use a SWOT analysis as a tool for strategic management practices. This entails a manager

or an employee who uses this model to determine opportunities in competing markets or industries, or even uses it to identify strengths within the organization that could lead to new opportunities to gain a leg up on current competitors. Analyzing these aspects of a company defines how to use strategic management as a tool to gain a competitive advantage.

Strategic management is a great way to improve the profitability of a business by looking at ways an organization can take advantage of underutilized resources, but there are other frameworks which can help those within a firm to understand what determines the competitive positioning of that firm within their industry. While profitability is important to focus on, understanding what factors affect the firm's positioning among others can lead to greater results and even better opportunities for strategic managers to exploit.

CHAPTER 5

PORTER'S FIVE FORCES MODEL

The well-known model that analyzes a company's individual competitive positioning within an industry is known as Porter's Five Forces model. Similar to the SWOT analysis, this framework is broken up into parts which can help explain the "forces" affecting the positioning of a firm. The five segments of this theory are further categorized into horizontal and vertical competition. Vertical and horizontal competition can be compared to the external and internal forces affecting a firm we mentioned earlier. Horizontal competition includes three of the five forces in the framework, and those forces are the threat of substitute products or services, the threat of established rivals, and the threats of new entrants. These horizontal factors go into determining where the firm lies in the competitive landscape. These three threats can make any organization fall below the desired positioning, and because of this, it is increasingly important to watch these threats within the industry and how they are performing. The ability to stay on top of competition means observing what your competitors are offering to their customers as well as keeping an eye out for new companies entering the industry. If a company can manage these threats and keep ahead of them by introducing rival products or increasing their own market share, they will have an easier time managing their positioning within the competitive landscape. Not only do all companies need to observe potential threats, but they need to be cognizant of the remaining two vertical factors; the bargaining power of suppliers and the bargaining power of customers. These two factors are equally as important to controlling the

positioning of a firm. To acknowledge the bargaining power of the suppliers, a firm needs to ensure the suppliers of their products are not the sole producer; if so, the supplier can then take advantage of the firm's inability to procure the product elsewhere. A firm in this situation faces a threat to profitability and efficiency, which directly affects their competitive positioning. Additionally, the firm needs to focus on the bargaining power of their customer, too. The most effective way to control the customer's bargaining power is to lower the buyer's ability to substitute the product or service. In a perfect scenario, a firm would find a supplier and a buyer who both rely on the firm to be the only link between the producer and the customer. Organizations who are not the only seller of the product face a higher bargaining power of the customer because they have the option to purchase the product elsewhere if the organization's condition are not satisfying. Department stores suffer from this threat because their competitors generally sell the same items and have the capability to put competing items on promotion to steal customers. This firm rivalry is a huge factor that plays into the growing profitability of specialty stores and decline of department stores. Because specialty stores are the lone seller of their own products, they face little to no competition from other retailers, providing them with more bargaining power than their customers.

So, what makes every one of these frameworks relevant to the topic at hand? They all focus on the significance of competitors and how they affect firm rivalry and performance. In Jay Barney's research, he focuses on the four aspects that help a firm to distinguish itself from its competitors. In his related strategic management framework, the focus is on how to outperform competitors while being as efficient as possible. SWOT analyses aid an organization in zeroing in on external and internal factors that drive

competition. And, lastly, Porter's Five Forces model uses this analysis to determine an organization's positioning within a competitive landscape. Frameworks and models such as these, and many more existing theories, are proof of the significance educators and researchers have put on sustainable competitive advantages and how firms rely on them to keep their competitive positioning high. By creating a competitive advantage that is inimitable, rare, valuable, and sustainable from the start, an organization is able to position themselves to enter the market successfully while avoiding the external and internal threats all competing organization's face within their industries.

CHAPTER 6

EVALUATING COMPETITIVE ADVANTAGES

In order to put this proposition into context, it is imperative to look inside other companies who have positioned themselves well and determine how strong the barriers to their competitive advantages are. Alternatively, we can take a look at poorly performing companies and evaluate how their failure to create a long-lasting competitive advantage or inability to build strong barriers to entry have prohibited them from being successful within their industry.

Recent year-end reports are showing signs of hard times at Nike. The well-known athleticwear retail giant is facing intense competition as the athleisurewear market is rapidly growing. Nike is suffering a loss of sales as a result of new market entrants, even in a time when the market is growing in size. In Porter's Five Forces model, one of the horizontal factors described is a threat of new entrants into the market. While Nike has been a household name for decades, they are relying too heavily on their brand name recognition and failing to recognize its weak spots in terms of long-term sustainability. Nike's biggest problem at hand is that other athleisurewear retailers are finding ways to produce workout apparel that is just as great of quality, if not better, while offering it at a discounted price. Specialty retailers such as Athleta and Lululemon Athletica are also benefiting from the exclusivity of their product. Nike operates their own stores, but they also contract with other department and sporting goods stores to sell their product. While this tactic helps Nike to saturate the market, it also gives them less control over how, where

and at what cost their products are being sold. Nike has for so long doubted the rise of other market entrants when they should have been focusing on how they can raise the barriers to entry and protect their competitive advantage. If the organization wants to remain successful in this growing market, they will need to find new ways to differentiate themselves from competitors, essentially protecting any advantages they enjoy. In a time where a customer's perception of a brand is the contributing factor to that company's sustainable competitive advantage, they need to focus less on brand name recognition and instead on how they can evaluate the importance of differentiation among their market. Nike still benefits from the global recognition they have created, but it is not enough. Customers are becoming loyal to companies which they have an emotional connection with. Nike sees this and has been pouring marketing dollars into campaigns and athlete sponsorships that can resonate with customers and pull at their heartstrings, driving that emotional connection. However, Nike's struggle in this industry is due to their inability to create products which are not substitutable by other retailers, thus connecting their slowed growth with the company's low importance of cementing a sustainable competitive advantage into every aspect of the company.

Target is an excellent example of a company who is addressing the drawbacks of their competitive advantages. The national corporation evaluated their current offerings and has adapted to the way retail is changing. Adapting is the key to a sustainable competitive advantage. Organizations who cannot be flexible or adapt to the changing retail landscape are ultimately going to fail, as many have already gone bankrupt. Instead of waiting for the inevitable, Target changed their direction and faced expansion issues they were suffering from head on. Being a big box store, Target struggles to find adequate retail

space in small, densely-packed urban areas. To overcome this problem, Target introduced a new format of stores that is much smaller and closer in size to a CVS Health or Walgreens Pharmacy. This allows the company to expand in its ideal markets much more easily and at a quicker pace. This is not the only benefit to Target's new concept, though. The company knew that today's customers were looking for convenience, which is why smaller drugstores are frequented by shoppers several times a week, more often than typical full-line discount stores or supermarkets. If Target could introduce a smaller format store that is convenient and encourages customers to stop by more frequently, they could grow their sales astronomically. This is a wonderful example of a strategic management focused attitude, but also of the flexibility Target has instilled into their competitive advantage. The ability to adapt is offering Target a growth opportunity when many big box retailers are closing their doors. This shift in store formats was strategic in the fact that it avoids cannibalization of its traditional full-line stores though differentiation of product assortment, but it also penetrates the current market at a much higher percentage than Target was already operating. The corporation's quick response to a new opportunity that presented itself is the main driver for Target's major success in the United States. This quick response meant strategic planning as well as the willingness to accept changes to their founding principles. Without this flexibility, Target would not have been able to penetrate an entirely new market of customers they had not been targeting.

Nike and Target are just a few of countless examples to be mentioned. These well-known organizations are further demonstrating my proposition that the long-term success of an organization boils down to the retailer's sustainable competitive advantage. In order to remain competitive among other firms in the industry, retailers need to develop a strategy

that creates value and conveys to their customers why they are different from the others. Organizations do this by focusing on four aspects of a competitive advantage; rareness, value, inimitability, and sustainability. If a firm can nail these four characteristics and remain to be innovative and flexible when it comes to the changing retail landscape, their chances for long-term success are much more achievable.

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BIOGRAPHICAL INFORMATION

Trenton McNairy was born and raised in Denton, TX. He moved to Arlington after his high school graduation to pursue his undergraduate of business management at the University of Texas at Arlington. While attending UTA, he joined the Honors College, became a PAL through the Department of Student Success, and was a Scholar of the Goolsby Leadership Academy Cohort 14. Alongside Cohort 14 of the Goolsby Leadership Academy, Trenton also studied abroad in South America for three weeks during his undergraduate studies. While attending school, he worked for Athleta doing several different roles, including an internship in his final undergraduate semester. After graduation, he will pursue a career in the apparel industry in New York City. His interests are product design and development, as well as researching and analyzing current market trends within the apparel industry.