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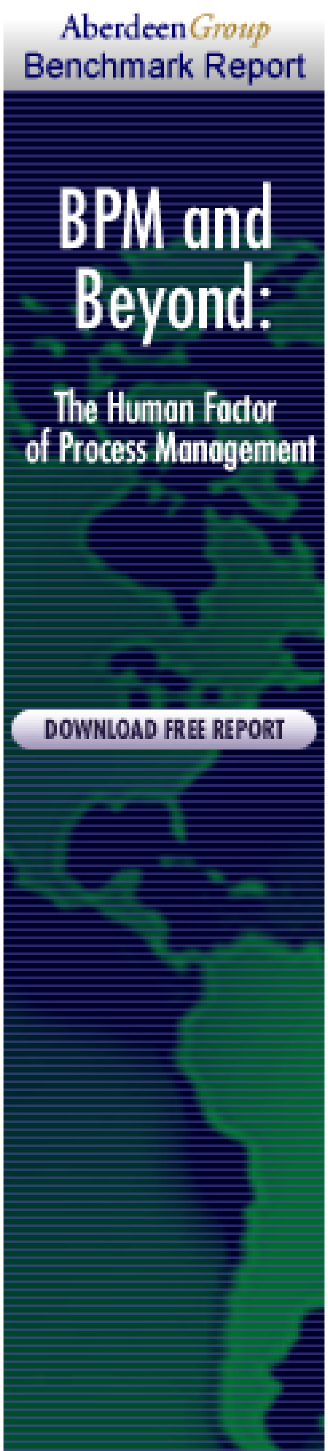
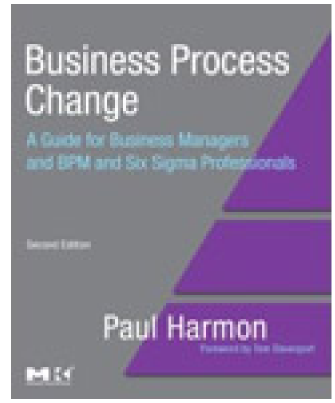


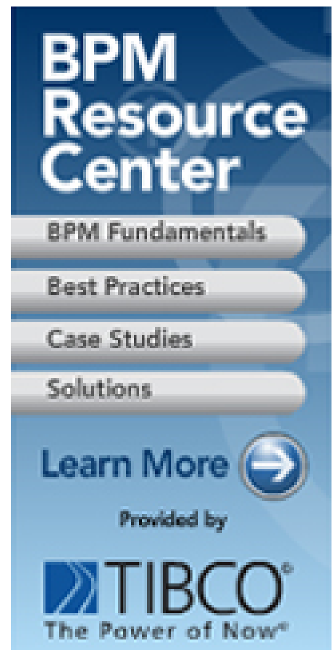
Porter, ERP and BPMS

I recently reviewed the book, *Business Process Management: The SAP Roadmap* by Snabe, Rosenberg, Moller, Scavillo and others. It had me thinking about where SAP is today and where they are trying to go, and how it all ties back to some basic ideas that Michael Porter first described in his book, *Competitive Advantage*, which he published in 1985.

Porter argues that "competitive advantage" refers to a situation in which one company manages to dominate an industry for a sustained period of time. An obvious example, in our time, is Wal-Mart, a company that completely dominates retail sales in the US and seems likely to continue to do so for the foreseeable future.

Achieving a competitive advantage should be the goal of every leading company. Having defined the goal, Porter next considers how a company might gain competitive advantage. In other words, he asks how we can distinguish between the losers, the winners, and those rare winners that achieve real dominance. "Ultimately," Porter concludes, "all differences between companies in cost or price derive from the hundreds of activities required to create, produce, sell, and deliver their products or services such as calling on customers, assembling final products, and training employees." In other words, "activities are the basic units of competitive advantage." This conclusion is closely related to Porter's analysis of a value chain. A value chain





consists of all the activities necessary to produce and sell a product or service. Today, we would probably use the word "processes" rather than "activity," but the point remains the same. Companies succeed because they understand what their customers will buy and proceed to generate the product or service their customers want by means of a set of activities that create, produce, sell and deliver the product or service.

So far, the conclusion seems like a rather obvious conclusion, but Porter goes further. He suggests that companies rely on one of two approaches when they seek to organize and improve their activities or processes. They either rely on an approach which Porter terms "operational effectiveness" or they rely on "strategic positioning."

Operational Effectiveness. As Porter uses the term, operational effectiveness means performing similar activities better than rivals perform them. In essence, this is the "best practices" approach we hear so much about. Every company looks about, determines what appears to be the best way of accomplishing a given task and then seeks to implement that process in their organization. Unfortunately, according to Porter, it isn't an effective strategy. The problem is that everyone else is also trying to implement the same best practices. Thus, everyone involved in this approach gets stuck on a treadmill, moving faster all the time, while barely managing to keep up with their competitors. Best practices don't give a company a competitive edge - they are too easy to copy. Everyone who has observed companies investing in software systems that don't improve productivity or price but just maintain parity with one's competitors understands this. Worse, this approach drives profits down because more and more money is consumed in the effort to copy the best practices of competitors. If every company is relying on the same processes then no individual company is in a position to offer customers something special for which they can charge a premium. Everyone is simply engaged in an increasingly desperate struggle to be the market leader and everyone is trying to get there by copying each other's best practices while their margins continue to shrink. As Porter sums it up: "Few companies have competed successfully on the basis of operational effectiveness over an extended period, and staying ahead of rivals gets harder every day."

Strategic Positioning. The alternative is to focus on evolving a unique strategic position and then tailoring the company's value chain to execute that unique strategy. "Strategic positioning," Porter explains, "means performing different activities from rivals' or performing similar activities in different ways." He goes on to say that, "While operational effectiveness is about achieving excellence in individual activities or functions, strategy is about combining activities." Indeed, Porter goes on to say that those who take strategy seriously need to have lots of discipline because they have to reject all kinds of options to stay focused on their strategy.

Rounding out his argument, Porter concludes, "Competitive advantage grows out of the entire system of activities. The fit among activities substantially reduces cost or increases differentiation." He goes on to warn that, "Achieving fit is difficult because it requires the integration of decisions and actions across many independent subunits." Obviously, I'm just providing the barest summary of Porter's argument. In essence, however, it is a very strong argument for defining a goal and then shaping and integrating a value chain to assure that all the processes in the value chain work together to achieve the goal.

The importance of this approach, according to Porter, is derived from the fact that "Positions built on systems of activities are far more sustainable than those built on individual activities." In other words, while rivals can usually see when you have improved a specific activity, and duplicate it, they will have a much harder time figuring out exactly how you have integrated all your processes. They will have an even harder time duplicating the management discipline required to keep the integrated whole functioning smoothly.

The Business Process Reengineering movement that dominated the early and mid-Nineties understood what Porter meant. BPR enthusiasts may have done many things wrong, but they had the big picture. They wanted companies to begin by defining their strategic goals and business models. Then, they wanted companies to creating a value chain that used IT systems to tightly integrate all their business processes to achieve their strategic goals.

In the reaction to BPR, and concerned about the growing costs of software development and the possibility of computer systems failing when they tried to process post-2000 dates, most large companies ended the Nineties by embracing off-the-shelf ERP software. The software was relatively inexpensive, it was Y2K conformant, and it offered most companies an immediate upgrade to client-server applications that were linked together and relied on a common, relational database.

Unfortunately, although ERP applications solved many IT problems that companies were struggling with in the late Nineties, they failed to address the concerns that Porter had highlighted. In essence, ERP applications are best practice applications. They improved operational effectiveness at the expense of both a unique strategy and a tightly integrated value chain. Most companies tried to ameliorate this problem by tailoring the various ERP applications for their particular needs, but this significantly reduced the value of the ERP applications, making them difficult and costly to maintain or to upgrade.

This situation was dramatically emphasized in the early years of this decade when a number of "dot.com" companies began to challenge leading companies in industries they had dominated for years. Suddenly, customers were willing to go online to identify companies offering the products they wanted and to order products they found there. Many of the "dot.com" companies were poorly conceptualized and failed, but others went on to revolutionize their industries. Today, 80% of the business and textbooks sold, worldwide, are purchased from Amazon.com. and by the end of this decade the publishing industry will probably be completely changed.. Similar revolutions have happened in the music industry, the telco industry and the newspaper industry, to name a few.

A company wired together by its Internet systems is integrated in exactly the way that Porter recommended. It's hard for another company to quickly duplicate what Amazon.com is doing. On the other hand, a company that depends on ERP applications is in exactly the opposite position. It is executing processes that depend on best practice software applications that can be easily duplicated by any rival. Moreover, the company depending on ERP finds itself locked into a system of applications that are difficult to change - and thus, the company is limited in its ability to either innovate or quickly change its business model.

Business Process Management Suites

(BPMS) are being used for several different purposes. Many IT groups are simply using BPMS tools to create new workflow applications. This use may save IT time and money, but it is hardly a break through of any kind. Leading edge companies are using BPMS tools as a way of managing and controlling their ERP applications. In essence, BPMS tools rely on Internet protocols that enable companies to link all their processes together into a single value chain. By programming inside the BPMS environment, developers are also able to tailor the ERP modules without making any changes in the actual ERP applications. Thus, in effect, the BPMS software gives the company much greater integration and significantly improved flexibility, while simultaneously avoiding the necessity to tailor the ERP modules, themselves. The company's ERP investment is preserved while the company's ability to make radical changes in order to deal with competitive challenges is much improved.

It is obvious that SAP recognizes the value of BPMS and is working hard to develop its own BPMS tools (e.g. NetWeaver) that will assure that SAP can offer its customers the kind of flexibility that other BPMS vendors have already begun to demonstrate. The SAP roadmap described in *Business Process Management: The SAP Roadmap* describes just such a path.

In essence, using BPMS tools, a company can focus on achieving the tight integration that Porter urges, while simultaneously becoming more agile. Integrating and embedding ERP applications within a larger BPMS system provides the tailoring and the seamless integration that can become the basis for a sustained competitive advantage. Then, the only thing the organization will need is a winning strategy - and that's up to the executive team.

Till next time,

Paul Harmon

If you haven't read *Competitive Advantage*, you should download Porter's July 2005 *Harvard Business Review* article "What is Strategy," which provides a very nice summary and is available from Amazon.com

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