Once More: Porter on Competitive Advantage

By Paul Harmon

I usually date the beginning of the modern business process management movement to Michael Porter's book *Competitive Advantage*, published in the mid-Eighties. I certainly realize that others had been advocating business process improvement before then -- Geary Rummler was active well before Porter -- but I give Porter special credit because he was able to discuss processes in a way that led senior executives to began to take process management seriously. Porter formulated ideas, like the "value chain" and "competitive advantage," that have remained key elements in our discussions ever since.

Given the speed with which the business world is changing, it seems like a term can hardly hold unto its meaning for 3 years, let along 20 years. The modern tendency is to use a term for 3-4 years, then invent a new term and launch a new media campaign to promote the latest new thing. Thus, we have watched "components' replace "business objects," and, recently seen "services" replace "components" in a succession that had a lot more to do with marketing than with technology.

Every business speaker, today, feels free to use the term "competitive advantage" to mean what ever he or she wants it to mean. There's nothing wrong with this. After all, it is in the nature of language that words, as T.S.Elliot explained, "strain, crack and sometimes break, under the burden, under the tension, slip, slide, perish, decay with imprecision...." The underlying concerns that Porter originally raised in *Competitive Advantage*, and discussed more powerfully and succinctly in his Nov-Dec 1996 *Harvard Business Review* article, "What Is Strategy?," are so fundamental to really understanding what Business Process Management is all about, however, that it's worth returning to Porter's original use of the term and recalling his argument.

Porter begins by defining "competitive advantage." In his writing, 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, 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 low cost producer, and everyone is trying to get there by copying each others 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."

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.

Geary Rummler has often made this same point using slightly different language. Rummler argues that the goal should be to optimize the value delivered by a value chain. He warns against sub-optimizing a value chain. In other words, Rummler emphasizes how companies fail to maintain an integrated positioning strategy. Rummler describes that most companies delegate responsibility to departments and provide incentives that encourage the department head to maximize departmental efficiency. By focusing on departments companies ignore the "white space in the organization chart" that only a value chain strategy can organize and coordinate. Typically, each department works to improve the processes within its own domain. Too often departments make changes in their departmental processes that create problems for other departments. In other words, one department's best practice may make things better for that department, while it simultaneously makes processes in other departments function less effectively, resulting in the sub-optimization of the value chain as a whole. In many cases IT applications are introduced that improve departmental activities while, as a side effect, making the data resulting from those activities less available to those in other departments. All too often -process redesign groups and Six Sigma teams, with the best intentions, undertake projects that improve a specific process without considering the impact of their effort on other processes in other departments.

The problem with Porter's analysis is, of course, that it assumes that senior management thinks about processes, weighs Porter's advice, and elects to pursue a positioning strategy. It assumes that managers know about the value chain their specific processes support and can determine how a change in one process will impact other processes in the same value chain. It assumes that there is a management team that is constantly focused on integrating processes into a whole and that the team is empowered to restrain anyone that seeks to sub-optimize the value chain.

Most companies have not embraced Porter's strategic positioning approach. Most senior managers, if asked, would say that they were pursuing a more or less well defined "best practices" strategy and, without knowing it, probably encourage silo thinking on the part of their departmental managers, who are encouraged to improve their departmental processes without any clear integrative vision .

Everyone admires Wal-Mart for its business accomplishments. Wal-Mart clearly defines what it means for a company to achieve competitive advantage in an industry. Clearly Wal-Mart executives have embraced strategic positioning – they intend to be the low-cost producers and are doing everything they can to integrate all their activities to achieve that strategy. Most companies lack the both the vision and the discipline to achieve a competitive advantage.

As process practitioners and consultants, we need to be sure that we understand what is involved in corporate success. Every time we redesign, improve, or automate a process without a clear understanding of how the resulting process will contribute to a better integrated, more effective value chain, as a whole, we risk reducing the organization’s completive advantage and bringing the organization a little closer to oblivion.