



北京大学中国经济研究中心
研究系列

■ Hao Ma

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Anatomy and Constellation



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图书在版编目(CIP)数据

竞争优势:解剖与集合(Competitive Advantage: Anatomy and Constellation)/马浩著. —北京:北京大学出版社,2004.9

(北京大学中国经济研究中心研究系列)

ISBN 7-301-07774-2

I. 竞… II. 马… III. 企业-市场竞争-研究-英文 IV. F270

中国版本图书馆 CIP 数据核字(2004)第 087135 号

书 名: 竞争优势:解剖与集合(Competitive Advantage: Anatomy and Constellation)

著作责任者: 马 浩 著

责任编辑: 张 燕

标准书号: ISBN 7-301-07774-2/F·0919

出版发行: 北京大学出版社

地 址: 北京市海淀区中关村北京大学校内 100871

网 址: <http://cbs.pku.edu.cn> 电子信箱: em@pup.pku.edu.cn

电 话: 邮购部 62752015 发行部 62750672 编辑部 62752926

排 版 者: 北京高新特打字服务社 51736661

印 刷 者: 三河市新世纪印刷厂

经 销 者: 新华书店

650 毫米×980 毫米 16 开本 19.75 印张 252 千字

2004 年 9 月第 1 版 2004 年 9 月第 1 次印刷

国内定价: 30.00 元

International Price: US \$ 30.00

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First Edition 2004

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ISBN 7-301-07774-2/F·0919

Competitive Advantage: Anatomy and Constellation

by Hao Ma


Published by

Peking University Press

Peking University, Beijing

100871, China

Printed in the People's Republic of China



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Introduction

This book is an integrative account of the nature and causes of competitive advantage based on solid scholarly research in mainstream Strategic Management and related academic fields, illustrated with extensive contemporary business examples. It is intended to assist general managers in their strategizing for sustainable competitive advantage and persistent superior performance.

This book can also be used as an MBA or EMBA text in Strategic Management and as source materials for executive training programs and consulting practice.

**Preface to the Research Series of
Peking University
China Center for Economic Research**

The publication of Adam Smith's seminal treatise on *The Wealth of Nations* in 1776 witnessed the separation of economics from philosophy and its inception as an independent field of scholarly inquiry among social sciences. Ever since, economics has attracted many students and gained tremendous impact, and has become a shining star in the crown jewel of all social sciences. Economic theory is a simplified logical system that is advanced to explain human behavior and social phenomena. Like any theories in social sciences, economic theories arise from the observation, interpretation, and conceptualization of social economic phenomena, and have to be constantly re-invented with the evolution of the human society. Economic theories also have to constantly subject themselves to the verification and refutation by actual economic events and phenomena, old and new, so as to tell the wheat from the chaff and inform on what could be temporarily accepted and what should be suspected and abandoned.

From this perspective, China's economic reform and open door practice since the 1970s provide many a challenge to the modern day mainstream economic theories: from household responsibility system



in the rural area to the privatization of previously state-owned enterprises, from the un-ambiguity of property rights and transition to modern corporation system to the dual track systems in resource allocation and product distribution. Such are the achievements of the reform effort and the ensuing problems, and many of them were unexpected by existing economic theories and hence could not be appropriately explained. However, underlying any economic phenomenon, there must be a certain logic or rationale. When existing theories cannot explain an economic phenomenon, new theories are called for. As such, China's reform and open door policies promise to be a goldmine for economic inquiries, rendering a great opportunity for innovation in economic theories.

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Since the reform and opening up, with the incremental establishment and refinement of the market economic system, modern economics also has found its increasing impact in China. Whether international or domestic, the purposes of economic inquiries are to better understand social economic phenomena, and promote the progress of human society through the applications of economic theories and policy formulations. With the advancement and deepening of the market-oriented reform, many interests conflict each other, contradictions abound, making economic phenomena increasingly more complex. Facing a specific problem, what are the causes, what are the effects? Contemplating on a particular reform policy, what could be the impact it will exert, in part or in whole, on the incentive mechanism, resource allocation, and income distribution? Absent appropriate theoretical and methodological guidance, an economic problem could be difficult to dissect and a hasty policy could trigger even more new problems. Therefore, innovative effort in theory-building based on the new phenomena observed during the

course of China's economic reform will not only contribute to the development of modern economic theories, but also further help provide impetus to the smooth sailing of China's reform cause. Such effort should be honorable duty mighty unavoidable to every serious Chinese economist.

Ten years ago, several young scholars and I, all fully trained overseas in modern economics, founded China Center for Economic Research (CCER) at Peking University, under the auspices of the Peking University administration and support of various circles of society. Although the research environment, working conditions, and financial reward were much more superior overseas than they were in China then, the opportunity of witnessing and participating in history-making proved to be fascinating and the opportunity of making monumental contributions to modern economic theories irresistible. We hoped that, with CCER's new organizing system, and through conglomeration of a critical mass of aspiring, passionate, dedicated, and well-trained economic experts, we could make our contribution to China's economic education, its economic theories, and policy formulation, and, eventually its modernization.

In the first ten years of CCER, research faculty has increased to 24 from its original 6. CCER has become an important base for theoretical research and policy study in China. During the 10 years, many CCER faculty members have gone to the frontline and grass-roots, conducting field research in rural areas and urban enterprises, and some have also participated in high-ranking policy consultation and decision process. Such efforts helped generate research publications and policy reports that boast penetrating analysis, unique insights, and convincing impact. They also offered practical help to the reform efforts of rural areas, state-owned enterprises, financial



sector, fiscal policy, foreign trade, and telecommunications, etc. During the last 10 years, CCER has taken good advantage of its frequent communications and exchanges with leading economic research institutions in the world, hosting leading economists, many Nobel Laureats included, through conferences and short visits. These conferences and visits helped generate valuable discussions and research articles, reports, and briefings on China's financial system and its reform, the mobility of the rural labor force, income inequality between urban and urban areas, land policy, social security systems, and a host of other important issues encountered during China's reform. Now, in celebrating the 10 year anniversary of CCER, Peking University Press takes the initiative and offers to publish a CCER research series showcasing the research results and achievement of the CCER faculty that include the above mentioned research output as well as output from other scholarly endeavors. On the one hand, this series provides a report card to all the leaders in various circles who have supported CCER in the past 10 years. On the other hand, it begs for the attention of experts and scholars, domestic and abroad, and hopes to generate further discussions and debates and induce more research effort on China's reform and development.

In the long history of China, 10 years are but a fleeting and transient moment; in terms of the research opportunity furnished by China's economic reform and the many theoretical questions that have to be addressed, the effort of CCER in the last 10 years is also but a straw in a haystack. Looking into the future, the CCER scholars will honor the initial charge of the original founding members, and, together with all concerned economic researchers and friends worldwide, attempt their very best in advancing China's economic education, theoretical development, and policy studies. I

believe, with our collective effort, we will soon embrace the renaissance of China in the 21st century and witness the parade of grand masters in economic science sailing from the great land of China.

Justin Yifu Lin, Ph D
Professor and Director
China Center for Economic Research
Peking University
September 2004

Preface

Business firms are important economic and social agents in the modern society. If the game of business can be construed as the competition for limited resources in business eco-sphere and in society at large, then winners of the game, by definition, are able to command a large share of the scarce social and economic resources and exert their impact on society. For any firms, winners in particular, their existence then can be justified by their competitive advantages over other firms or other types of social or economic agents. That is, they exist because they are in a better position to deliver customer value and contribute to the needs of society. And for that, they are duly rewarded through their superior performance. In one word, to win the game and to even survive, a firm needs competitive advantage.

This book attempts to advance an integrative and systematic framework on the nature and causes of competitive advantage. In order to enjoy persistent superior performance, a firm has to gain, enhance, and renew its competitive advantages over other firms on a constant basis. Where does competitive advantage come from? How do we detect them? How long can an advantage sustain? How do a firm's advantages interact and effect through time? Addressing these questions is of paramount importance for strategy research and



practice, as the ultimate goal of strategy is indeed to achieve persistent superior performance. The framework offered in this book is advanced precisely for this purpose.

I shall emphasize that this book is written primarily for practitioners. For pure research purpose, one has to work in more narrowly defined areas using specific and often discipline-based tools or approaches so as to gain deeper understanding of a particular strategic issue. Business reality, however, is not necessarily organized around elegant theoretical lines. As such, strategy practitioners need multiple weapons in their tool-kit to tackle different strategy issues and situations. A strategist is necessarily a generalist, seeking practical help and guidance from a whole range of theories and frameworks. For this reason, this book is an eclectic endeavor. Taking a holistic approach, it does not work within any extant perspectives or research paradigms. Rather, it is issue-driven. And the issue here is competitive advantage.

To better understand competitive advantage, this book draws on all the resources hitherto available (any prior theories, models, frameworks, and evidence on competitive advantage) in the strategy and related fields. It attempts to embrace the strategy literature on competitive advantage in its totality. Using the *SELECT* framework (Substance, Expression, Locale, Effect, Cause, and Time-horizon of competitive advantage) and the *ARTS* framework (Amplification, Renewal, Trade-Off, and Sustaining of competitive advantages), it coalesces major research streams in strategy and presents them in a comprehensive and coherent way, more readily accessible to strategic management practitioners. So my role will be the architect, now let's review some of the major building blocks.

In the past four decades or so, we have witnessed a parade of important treatises on strategy. In the groundbreaking work on *The Concept of Corporate Strategy* (1971), Kenneth Andrews established the strategy concept as the cornerstone of the field, then known as Business Policy. He and his colleagues at Harvard championed the idea of fit between internal working of the organization and the external requirement of the environment, an idea that is central to the now famous SWOT framework.

Richard Rumelt, in 1974, published his work on *Strategy, Structure, and Economic Performance*, calling our attention to the advantage of firms pursuing related diversification that exploited synergy across businesses, and also the advantage of matching organizational structure with strategy, a theme first explored by Alfred Chandler, Jr. in *Strategy and Structure* (1962).

Charles Hofer and Dan Schendel's book *Strategy Formulation: Analytical Concepts* (1978) helped formalize the conceptual framework and advance the discipline status of *Strategic Management*, that guided research in the field for almost two decades. Their treatment of levels of strategy has been of particular value in understanding firm's pursuit of advantage at various levels of the diversified firm in contemporary business.

Raymond Miles and Charles Snow, in *Organizational Strategy, Structure, and Process* (1978), popularized their typology of generic strategies, emphasizing the notions of configuration, ideal type, and equi-finality in firm's search for competitive advantage and superior performance.

In the 1980s, Michael Porter's *Competitive Strategy* (1980) and *Competitive Advantage* (1985) propelled to prominence the in-



dustry positioning or structural approach. The five-force model, three generic strategies, and the value chain became standard language for strategy researchers, consultants, and practitioners alike.

Richard Nelson and Sydney Winter's work on *An Evolutionary Theory of Economic Change* (1982) helped us understand how organizational routine form and change as well as its implication for organizational learning, adaptation, and firm's search for advantage.

Pankaj Ghemawat's book on *Commitment* (1991) articulated the importance of persistence in strategy for sustainable advantage, which could arise out of a series of investment decisions that require irrevocable commitment of resources.

The great economist Joseph Schumpeter's seminal work on the process of capitalist economy has found its tremendous impact in the strategy field. Inspired largely by Schumpeter's theory of innovation, C. K Prahalad and Gary Hamel advocate *Competing for the Future* (1994), making strategic intent and core competence a staple in daily business conversation.

Schumpeter would also find its influence in Richard D'Avani, who brings to our attention the phenomenon of *Hypercompetition* (1994), where archrivals engage in cutthroat battle through four escalating arenas; where only the paranoid survive; and where no sustainable advantage is possible.

In the mean time, we've also received the coroner's report, *The Death of Competition* (1996), in which James Moore convincingly argues that the traditional way of competition as we know it, i. e., product or market based bilateral competition, is no longer of much relevance. Instead, the focus of competition, which is indeed

more intense than ever before, has been placed on leadership in business ecosystems rather than on product dominance or even industry dominance. So the competitive landscape is changing.

From game theory with a newly invented word, comes *Co-opetition* (1996), where Brandenburger and Nalebuff demonstrate the power of pursuing a strategy that explores the benefits of both competition and cooperation, a strategy that is mean to change the game.

Recently, Jay Barney's *Gaining and Sustaining Competitive Advantage* (2002) systematically expounds the resource-based view of the firm, a perspective emerged in the mid-1980s which is currently gaining the strongest momentum. He advises strategists to base a firm's strategy on its valuable, rare, and inimitable resources, providing a valuable approach for understanding sustainable competitive advantage.

Why do we need another book in strategy? What is this book about? My mission in this book is to cut across the important milestones in the field and integrate the various research streams in strategy into an integrative whole. The organizing theme of this book is competitive advantage. And the integrative whole is the proposed *SELECT ARTS* framework. My inspiration for undertaking such a work can be found in Schumpeter that an innovation is often a creative combination of existing ideas, approaches, or materials. I intend to make the *SELECT ARTS* framework more complete than its building blocks but will in no way claim to replace them.

One simply has to know when to use these extant theories and in what context. This framework helps strategy practitioners better apply them. True to the spirit of strategic decisions that depend on



the quality of managerial choice, it's the general managers' task to *select from the tool-kit what is needed for a particular strategic task*. My mission will be complete if this book helps you gain some value-added understanding of the whole range of options when it comes to the art of creating and sustaining competitive advantage. Treating the firm as an evolving constellation of competitive advantage, this book offers a first cut on an advantage-based view of the firm.