

COMPETITIVE ADVANTAGE

A competitive advantage exists when a firm has a product or service that is perceived by its target market customers as better than that of its competitors. Unfortunately, entrepreneurs are often confronted with two myths surrounding the creation of a competitive advantage. One is that most good business opportunities are already gone. The other is that small firms cannot compete well with big companies. Both of these ideas are erroneous! Nevertheless, existing companies, large and small, do not typically welcome competitors. As one well-respected author, Karl H. Vesper, puts it:

Established companies do their best to maintain proprietary shields... to ward off prospective as well as existing competitors. Consequently, the entrepreneur who would create a new competitor to attack them needs some sort of "entry wedge," or strategic competitive advantage for breaking into the established pattern of commercial activity.

Before choosing such an entry wedge, the entrepreneur needs to understand the basic nature of the competition he or she faces in the marketplace. Only then can a competitive advantage be developed properly.

The Basic Nature of Competition

The following strategies of three entrepreneurs show the simplicity of many successful competitive advantages:

- Dale Dunning and his two partners started Wall Street Custom Clothiers in 1986, with suits selling for \$700 to \$2,000. Dunning targets upscale consumers by traveling to their offices, instead of waiting for customers in a retail shop.
- Ron Sanculi spent two years developing the perfect salsa recipe before packaging it in an ordinary mason jar with a generic label and seeking shelf space along with many other brands. Since 1991, Sanculi has sold nearly 500,000 bottles of Mad Butcher's Salsa.
- Allen Conway, Sr., is the founder of Discount Labels, a company launched in 1980 to meet the needs of customers who require small quantities of printed labels quickly- a market of little interest to established companies. Because of its ability to fill orders within 24 hours, the company is the nation's largest short-run manufacturer of custom labels.

These entrepreneurs compete successfully within their respective industries. Each understands the nature of competition and follows a simple but sound strategy. But what are the basic factors in a competitive market?

A number of factors determine the level of competition within an industry. Several typologies have been developed to categorize these competitive forces. For example, Michael Porter, in his book *Competitive Advantage*, identifies five factors that determine the nature and degree of competition in an industry:

1. Bargaining power of buyers
2. Threat of substitutes
3. Bargaining power of suppliers

4. Rivalry among existing competitors
5. Threat of new competitors

To a large degree, these five market forces collectively determine the ability of a firm, whether large or small, to be successful. Obviously, all industries are not alike; therefore, each force has varying impact from one situation to the next. Porter identifies numerous elements of industry structure that influence these five factors. Detailed explanation of them is, however, beyond the scope of this discussion. Briefly stated, these factors influence the creation of a competitive advantage as follows:

Buyer power influences the prices that firms can charge, for example, as does the threat of substitution. The power of buyers can also influence cost and investment, because powerful buyers demand costly service. The bargaining power of suppliers determines the cost of raw materials and other inputs. The intensity of rivalry influences prices as well as the costs of competing in areas such as plant, product development, advertising, and sales force. The threat of entry places a limit on prices and shapes the investment required to deter entrants.

The more completely entrepreneurs understand the underlying forces of competitive pressure, the better they will be able to assess market opportunities or threats facing their venture. Obviously, which forces dominate industry competition depend on the particular circumstances. Therefore, the challenge to the entrepreneur is to recognize and understand these forces so that the venture is positioned best to cope with the industry environment.

Porter has identified several fatal flaws that plague entrepreneurs' strategic thinking regarding their competitive situation. Three of these flaws are

1. Possessing no true competitive advantage. Imitation of rivals is both hard and risky and reflects a lack of any competitive advantage.
2. Pursuing a competitive advantage that is not sustainable. The entrepreneur must make sure that the competitive advantage cannot be quickly imitated.
3. Misreading industry attractiveness. The most attractive industry may not be the fastest-growing or the most glamorous.

Dess, Gregory G., G.T. Lumpkin and Marilyn L. Taylor. Strategic Management. 2 ed. New York: McGraw-Hill Irwin, 2005.