Chapter 2
Competitive Advantage

ABSTRACT

This chapter defines what competitive advantage means to a company and describes the traditional types of competitive advantage that a company may possess. For cost advantage, the major drivers of cost are explained to provide an understanding of how they, either individually or in combination, cause the cost of a company's activity. Similarly, for differentiation, the principal drivers of uniqueness are explained, including how they interact to create sustainability of differentiation. The chapter also looks at how advances in Information Technology (IT) affect competition and discusses the sources of competitive advantage. In addition, it covers the strategies that a company needs to pursue to exploit the technology so as to gain an advantage and protect it from rivals. In particular, the attention is shifted to neo-classic competitive advantages, which are generated from business strategies that avoid the classic trade-offs between mass production and invention models, where IT plays a key role by allowing a company to implement improvements more quickly. On the need to sustain a competitive advantage, the chapter reviews Porter's concept of sustainability and explains the main factors involved. In a construction context, the nature of competition is described. The key sources of competitive advantage for international contractors are reviewed with respect to their distinct abilities to operate in the global markets. It is followed by illustrating how the sources can potentially be converted into critical success factors for the companies using the five cases presented in chapter 1. The chapter concludes with a summary of the main points covered on competitive advantage.

TRADITIONAL COMPETITIVE ADVANTAGES

The two classic competitive advantages are described and they are directly related to their respective business strategies described in Chapter 1. In essence, when a company chooses to lead others by adopting cost leadership or product differentiation strategies, they are taking steps or actions to gain advantages in respect to cost or differentiation of its products or services.

Cost Advantage

Cost advantage is a traditional type of competitive advantage a company may possess. Managers recognize the importance of cost, and many strategic plans target cost leadership or cost reduction as their goal. Porter (1985) explains that a company's cost position is determined by the cost behavior of its value activities and that cost advantage results if the company achieves a lower cumulative cost of performing value activities than its competitors.

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Defining the company's value chain would be a necessary first step before a cost analysis of its value activities can be performed more effectively. Thereafter, the analysis is carried out to disaggregate the generic value chain into individual value activities to reflect:

1. Size and growth of the cost represented by the activity;
2. Cost behavior of the activity; and
3. Competitor differences in performing the activity.

On cost behavior, Porter (1985) mentions there are ten structural factors or 'cost drivers'. They are:

1. Economies of scale;
2. Learning;
3. The pattern of capacity utilization;
4. Linkages;
5. Interrelationships;
6. Integration;
7. Timing;
8. Discretionary policies;
9. Location; and
10. Institutional factors.

He explains that cost drivers are the structural causes of the cost of an activity and the company can more or less control them. Several cost drivers can combine to determine the cost of a given activity within a company and the cost drivers can vary among companies, even in the same industry, if they adopt different value chains. More often, the cost drivers interact with one another to determine the cost behavior of a particular activity. Seldom would one cost driver be the sole determinant of a company's cost position. However, Walker (2009) argues that influencing market position involves looking at 'cost drivers' – those factors that determine the company's costs, and 'value drivers' – those factors that determine customer value. He explains that any factor that raises value to the customer or lowers cost and leads to a net improvement in the company's market position is important. The drivers of value and cost that can have direct influence on a company's market position are listed in Table 1.

Clearly, cost advantage arises only if a company's cumulative cost of performing all the value activities is lower than competitors' costs. And, cost advantage is only valuable to a company, in strategic terms, if this advantage is sustainable. Porter (1985) explains that sustainability will be present if the sources of a company's cost advantage are difficult for competitors to replicate or imitate. It can lead to superior performance if the company is able to charge a price that is not lower than competitors when, at the same time, provides an acceptable level of value to the customer. It is common for competitors to have value chains that are different from the company's. Therefore, a company needs to evaluate its relative cost position against its competitors in relation to:

1. Composition of its value chain; and
2. Cost drivers of each activity.

Generally, the inherent efficiency of the value chains of a company and competitors, if they are different, will determine the relative cost position. Usually, the value chains of companies differ only in some value activities. A company will only

Table 1. List of value drivers and cost drivers

Value Driver	Cost Driver
Technology Quality Delivery Breadth of Line Service Customization Geography Risk Assumption Brand/Reputation Network Externalities Environmental Policy Complements	Economies of Scale Economies of Scope Learning Curve Low Input Costs Organizational Practices Vertical Integration

(Source: Walker, 2009)