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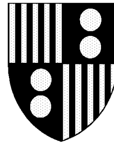

University of Navarra

ARE YOU MAKING THE MOST OF YOUR STRATEGIC ASSETS?

Carlos García Pont*
Alfredo Enrione**

RESEARCH PAPER Nº 251 BIS
June, 1993

* Professor of Business Policy, IESE
** Doctoral Candidate, IESE

Research Division
IESE
University of Navarra
Av. Pearson, 21
08034 Barcelona - Spain

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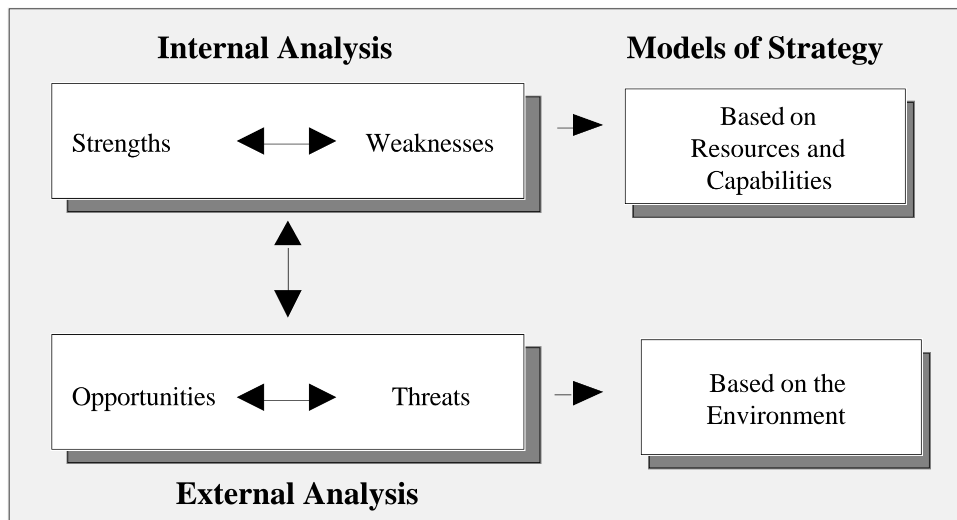
In what way are we different from our competitors? Why don't we have access to certain market segments? Why, in the same industry, do we see such large differences in performance? When faced with these questions, most managers respond along the lines: "We know the needs of our clients better", "We have our own technology", "We're more flexible", etc. The common thread running through these responses is that they all stress the importance, in order to be competitive, of certain proprietary "strategic assets". This paper offers a framework for identifying such assets and explains how the essence of management lies in identifying, maintaining and developing these assets, which are the foundation upon which competitive advantage is built.

Understanding the sources of competitive advantage has always been one of management's most important tasks. Since the 1960s, the dominant model for analyzing a company's strategic situation (see Figure 1) has been based on finding coherence between the external analysis, or analysis of the environment, and the internal analysis, or analysis of the company's characteristics. External analysis consists in identifying the opportunities and threats that the environment presents to the company. Internal analysis, on the other hand, seeks to identify the strengths and weaknesses of the company itself. According to this model, the task of management is to secure competitive advantage by using the company's strengths to exploit the opportunities offered by the environment, neutralize the threats and avoid the company's weaknesses (Andrews, 1971; Ansoff, 1965; Hofer & Schendel. 1978).

Figure 1. Focus of Analysis and the Models of Strategy



Strategy Models based on the Environment

Although both sides of the coin -internal analysis and external analysis- have been studied, in the last two decades there has been greater emphasis on developing the external analysis, that is, the analysis of the industry environment and the positioning of the company relative to its competitors (Grant, 1992). This diagnosis of the company's competitive position has been based on an analysis of the industry's structure. The industry in which a company chooses to compete and its positioning within that industry –the specific segments in which it participates– determine its scope for growth and profit (Porter, 1981; Rumelt, 1984; Scherer, 1980). The entry barriers to certain industries and the barriers to mobility between market segments preserve the profitability of the companies that operate in them.

That is why this model stresses the choice of industry and segment in which to compete as the most important of management decisions. Strategic decisions of this sort largely determine the profitability of the company.

However, observation of reality shows us that in all industries there are companies that do well and companies that do badly, companies that grow and companies that see their market share decline, despite the fact that they are all competing directly in the same market segments. In fact, it has been found that the differences in profitability between firms operating in the same industry are significantly greater than the differences in average profitability between industries (Rumelt, 1990). This forces us to reconsider the importance of the choice of industry and segment as a determinant of a company's profitability.

Why then does one company do better than another? What is it that enables it to achieve consistently better results? What makes some companies capable of maintaining their competitive advantage? What is the source of these differences in performance? The most obvious answer is that companies are not all the same, that successful companies *have something* that the others do not and are capable of *developing and doing business* in ways that their competitors cannot.

We shall therefore have to look at companies' internal characteristics to find the differences, or at the way these characteristics fit with the environment in which the companies compete. That is why, in the last decade, there has been a resurgence of interest in the internal strengths of the company as the key to competitive success. There is a new, asset-based view of the firm (1) that conceives the company as possessing a stock of resources and capabilities of different kinds, which are the true source of competitive advantage.

Strategy Models based on Resources and Capabilities: Strategic Assets

An organization's chances of survival –in the last analysis, the long-term goal of any organization is survival– are determined by its ability to do specific things, to perform actions that meet the needs of the environment or market in which it competes.

This potential to «do things» is determined by the capabilities and/or resources that it possesses. **Resources** are the inventory of assets, both tangible and intangible, that the company has at its disposal and that give it a potential for action. **Capabilities** are the ability to deploy these resources, to realise this potential. The combination of resources and capabilities, acquired over the history of the organization, is transformed into the products and services that the organization delivers to the market .

Resources and capabilities become **Strategic Assets** when they are determinants of the organization's competitive advantage (Amit & Shoemaker, 1993). Not all resources or capabilities are equally important for the functioning of all companies, and the importance of a particular asset for any given company can also vary over time. Identifying strategic assets in order to strengthen and develop them is the subject of the following section.

Characteristics of Strategic Assets

In order to identify a company's strategic assets, we first have to know what the characteristics of such assets are. Various authors have defined the following characteristics:

1. Strategic assets must be valuable. The company must be able to obtain competitive advantages by using them. In assigning resources to building up strategic assets, the company has to be able to give priority to those that give it competitive advantage. There have been numerous cases where companies have tried to develop assets that were not really important and have sunk a large part of their resources in doing so.

   For many years, size was considered a source of competitive advantage because it brought economies of scale. The North American division of General Motors based its strategy on achieving economies of scale and sought to maintain its supremacy by making large investments in developing its North American plants. However, the globalization of competition in the automobile industry has cast doubt on the importance of economies of scale as a source of competitive advantage. Modern automobile production technology has made them considerably less important. Under pressure from foreign competition, General Motors created a joint venture with Toyota in California that showed it

that the capabilities that it was trying to develop in its other plants were not relevant in the automobile market.

2. Strategic assets should set the company apart from its competitors. A company's resources will only be a source of competitive advantage if they are not shared by all of its actual or potential competitors. If all of the companies in an industry have the same assets, these assets will not afford any of them a relative advantage. This does not imply that they cannot be valuable in themselves or even indispensable. The assets that any company needs in order to compete in an industry form the basis of the entry barriers to that industry; however, for this same reason, once the company has entered the industry, these assets no longer serve to differentiate it from its competitors. Within the industry, strategic assets are distributed in a heterogeneous fashion, which means that each company can be unique.

   A company can only maintain a competitive advantage if it makes the most of relevant assets that differentiate it from its competitors, especially in the eyes of consumers. Heavy investment in brands is merely a way of obtaining an asset that sets a company apart from its competitors.

3. Strategic assets must be difficult to imitate. It is of little use to a company to have an important and unique asset in an industry if its competitors can develop it immediately and so neutralize the advantage in the short term. Identifying the importance of an asset does not imply being able to acquire it immediately and make it part of the company's resources and capabilities. The competitive advantage provided by specific resources can only be sustained if a company's competitors cannot develop the same resources in the short term. A large part of the success of some of the Japanese automobile manufacturers has been based on a mastery of specific production technologies. Attempts by American and European manufacturers to incorporate these technologies into their production processes have not produced immediate results. General Motors has taken more than 10 years to introduce them in one of its divisions - Saturn- and industry experts acknowledge that it would be difficult to apply them to other divisions of the company. Seat, the Spanish subsidiary of Volkswagen, has invested nearly 200,000 million pesetas in developing a totally new plant that operates with these technologies. It will not be easy, however, to apply the same changes to the company's factory in Zona Franca, Barcelona, or to export it to other units of the group. Applying such technologies is not simply an engineering project; it requires a change in the concept of production that is very difficult to introduce at all levels of the organization.

4. Strategic Assets are a product of the company's history. They are developed and acquired over a long period as a result of a series of strategic and operational decisions. Even if it were possible to understand the causal relationship between certain strategic decisions and the acquisition of specific capabilities, which might be extremely difficult (Reed & Defillippi, 1990), we would have to reproduce an identical sequence of decisions in order to obtain those capabilities. Porter (1990) indicates that the competitive strength of particular industrial sectors within a nation is a consequence of the competitive conditions that each sector has had to cope with.

One of the explanations given for the development of Japanese production technologies is the scarcity of resources that Japanese companies were faced with after the Second World War; for example, the lack of space, which led to a specific type of demand in factories. Other companies that were not subjected to this sort of scarcity developed production techniques based on mass production and specialization.

5. Strategic assets cannot be bought in a market for resources. If they could be bought in a market, all the companies in any given sector would have access to them, so long as they could afford to pay. Therefore, no company would be able to obtain a competitive advantage by the mere fact of possessing strategic assets.

   Previously, the ability to design automobiles was an internal capability and resource of most of the companies in the automobile industry. The relative design capacity differentiated companies. However, the tendency to subcontract automobile design to outside companies has made design capacity something common to all companies in the industry. The design companies «rent» their strategic assets and, therefore, any competitor has access to them. This is a clear example of an asset that is no longer «strategic» because there is a market for it. However, the creation of this market heightens the importance of other assets, such as the ability to integrate work done in-house with the technical staff of the company itself.

   Strategic assets are frequently assimilated in organizational routines (Nelson and Winter, 1982) or in the sum of the capacities of teams of people that are difficult to separate. This makes them non-transferrable goods in themselves. When we speak of «time-to-market» as a source of competitive advantage, we are talking about a series of organizational processes that make it possible for the company to develop and market its products in a short space of time. A company is unlikely to be able to buy this asset unless it can acquire the entire group of people who make up the process, together with the systems that make it possible. Process engineers, product engineers, plant staff, etc. would be needed in order to really «acquire» this asset. When we talk about «acquiring» this whole group of people, what we are really talking about is acquiring a new mentality, a new way of defining tasks –and this is obviously not something that can be achieved overnight.

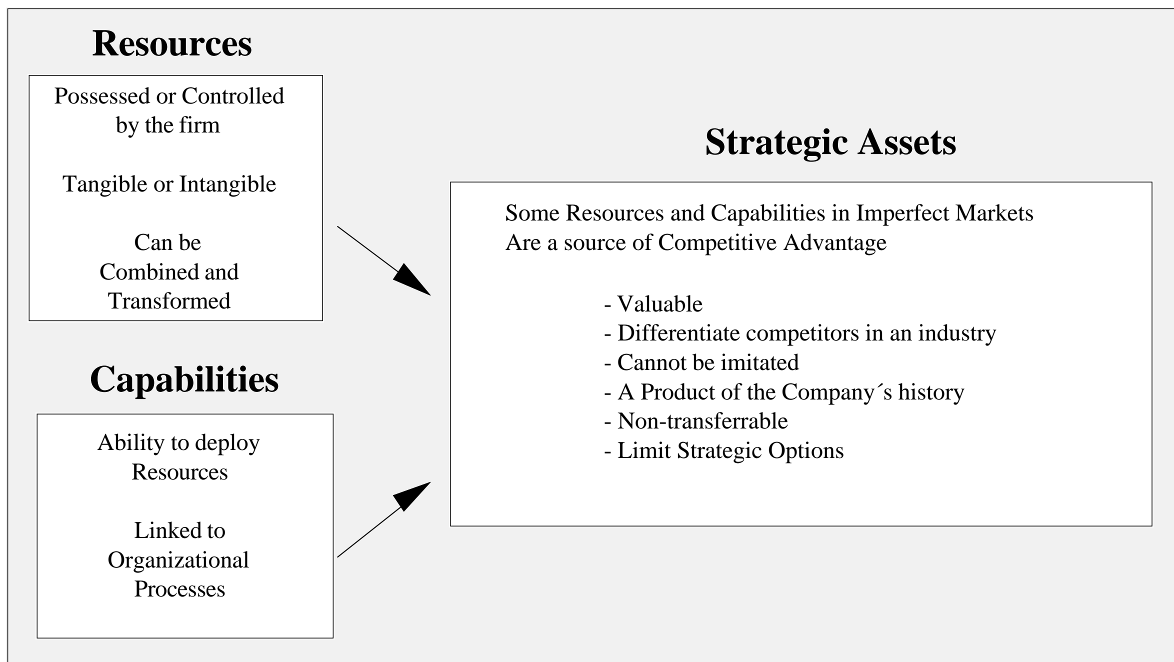
6. Strategic assets limit the company's scope for competitive action. Just as a company's strategic assets are not easily imitated or acquired, the composition of this stock of resources and capabilities is difficult to change in the short term. Therefore, companies that compete in the same sector will find their strategic options limited to those that they can take on with their current stock of strategic assets. That is why one of the key aspects of strategy is to develop these assets.

   This would explain why, when companies diversify or even when they enter into agreements or alliances, they tend to do so in related areas of business. This is what Dosi (1991) describes as «corporate coherence». Where there is no restriction on the range of strategic possibilities, holding companies or conglomerates would achieve results as good as or better than companies that have diversified into related businesses, given that they would naturally

diversify their operational risk. However, companies generally look for areas that allow them to exploit the resources and capabilities that they have acquired in the past.

The characteristics of strategic assets are summarized in Figure 2.

Figure 2. Characteristics of Strategic Assets



Where should we look for our Strategic Assets?

Having analyzed the characteristics of strategic assets in general, it is time to identify the specific strategic assets that the company has at its disposal. To do this it is helpful to look at each of the company's activities in turn, considering each of the following five categories of asset:

Technological

Technological assets can be of two types: the stock of technologies and the flow of technologies. The former refers to the technology upon which the actual and immediate products of the company are based. The stock of technologies is the product of the company's technological history and shapes its future possibilities. The distinguishing capabilities, especially the ability to coordinate different production skills and integrate different fields of technology, represent the collective learning of company (Hamel and Prahalad, 1990). Equally important is the flow of new ideas, the rate at which the company is able to add new technologies to its «tool box».

In high-tech industries, a company's technological position relative to its competitors will be determined in the long term by its capacity to invent or absorb new technology. In less sophisticated companies, competitive advantage will come from adopting new technologies or assimilating technologies developed in other industries; the strategic asset will therefore lie, not in having a team of in-house researchers, but in the ability to scan the environment for new developments.

Positional

This type of asset can be defined in terms of a company's position relative to the competition in various respects. The most obvious is physical location, which may enable the company to exploit the opportunities peculiar to its territory, or, as in the case of large supermarkets and department stores, prevent competitors from locating nearby. Another less tangible, although no less important, positional asset is the company's relative position within a network of contacts that go beyond its marketing relationships (Kogut, Shan & Walker, 1991; Hall, 1992). In highly complex sectors, contacts with government agencies, research centers and even competitors become essential in order to monitor the environment in which the organization operates. It could also be said that, in the context of a «mental map», a company's reputation or prestige is a positional asset (Itami, 1988; Aaker, 1989; Grant, 1992). This will be closely related to customer loyalty to the brand, which is a valuable asset in itself when it translates into a price differential compared with the competition, which is why it is sometimes called «Brand Equity» (Joachimsthaler, 1993). Obviously, the company will also have a certain reputation among its suppliers of resources –financial institutions, the labour market, raw material suppliers, shareholders, etc.– which will depend on other factors, such as financial management, human resources management, etc. (Hall, 1992). One final resource that can also be considered a positional asset is access to competitive information, i.e. a store of valuable information about the business, the clients, the suppliers, etc. that has been built up in the course of the company's history (Hall, 1992). However, the valuable thing is not the store of information in itself, but the organization's ability to manage it and use it effectively in making decisions (Andreu, 1993).

Know-how

One of the most important assets in any organization is know-how: the sum of the unwritten knowledge stored in each of its members, which is the key to the company's daily activities. This know-how can be specific to certain areas of the company, such as the experience of *skilled craftsmen* in making specially designed parts, or the sales force's intimate knowledge of its customers. The importance of knowing how to do things extends to all of the company's activities, from purchasing to accounting or logistics, including all those activities that make up the company's infrastructure. For example, the knowledge that the people in charge of Purchasing or Logistics share with their suppliers, and the closeness of the relationship between them, will directly affect the performance of the rest of the firm. The mastery of production processes can also bring advantages when it comes to developing and implementing innovations in products and processes. As for the characteristics described above, it is obvious that people's know-how is valuable; it is the result of years of experience; it is asymmetrically distributed in relation to competitors; and in most instances it is not directly transferrable to competitors because certain key skills manifest themselves only within a team of people and in the particular environment in which that team works. Many of these skills are skills of the team and are intimately associated with the combination of individual capabilities and the pattern of integration that exists in the organization where they operate.

Finally, we should not regard this attribute as being restricted to the inside of the organization; we must also recognize that, for a company, the know-how of its clients and suppliers is fundamentally important (Hall, 1992), as well as that of its «partners» in the different types of alliance that have proliferated during the 1980s and 1990s. For example, it is a well-known fact that it is often the more sophisticated clients that prompt the technological development of their suppliers. In this respect, for example, it could be said that the close relationship between Motorola and Apple has contributed to Apple's ability to differentiate itself in the personal computer industry. However, it is important to note that the usual way of doing things inside a company can also become an obstacle to implementing change in the organization.

Regulatory

The regulatory system within which a company operates can be a source of assets for that company. What in Spain has been referred to as «the challenge of '92» is the disappearance of one of the assets that contributed to the development of Spain's industrial base. Tariff protection created an artificial environment that allowed the country to maintain internal competitiveness while holding potential foreign competitors at bay. The disappearance of this barrier has exposed the weaknesses of companies whose most important asset was precisely this protection. We are currently witnessing another clear example of this with the deregulation of the airline industry in Europe, whereby any EC company can offer domestic flights in countries other than its own as long as they are extensions of flights that started in the company's home country. These two examples demonstrate the risk of basing a competitive position on existing regulations. The automobile industry, on the other hand, shows how regulation can provide a temporary advantage that helps companies to reposition themselves. The countries of the European Community have no choice but to protect their automobile industry because of its relative importance to the economy. However, the progressive deregulation of the market obliges these companies to develop or acquire the assets required to cope with foreign competition. The Seat factory in Martorell, where innovative production methods previously unprecedented within the Volkswagen group have been introduced, is an example of the effort that European manufacturers are making to renew their inventory of strategic assets.

In other cases, the existence of regulations can be essential to the development of an industry. Without regulations governing patents and intellectual property, sectors such as software development or the pharmaceutical industry would see their incentive for product innovation seriously threatened.

Organizational

All of the assets developed in any of the groups mentioned above are developed by the people who make up the organization. For this reason, organizational capabilities are essential to the development of competitive advantage. Organizational capabilities are of two fundamental kinds. The first is combinative capability. Most organizations do not base their success on the application of isolated resources or specific capabilities, such as a superior technological capacity, a special relationship with regulatory bodies, an excellent purchasing policy, or an automation process. Organizations combine all of their activities, and thus also the strategic assets involved in each activity, in organizational processes that result in the overall successful functioning of the company (Kogut, 1992; Lado, Boyd & Right, 1992).

The second fundamental organizational capacity is innovation. Innovation, not in terms of exploiting the results of research and development, but in terms of integrating the organization for the purpose of developing new tasks, knowing how to identify and develop new strategic assets that build on those the company already possesses and that offer a challenge to the company's present way of doing things. What we are talking about here is the company's ability to change, to take on new ways of operating, to identify within itself the capabilities and resources with the potential to become strategic assets.

The keys to strategy in the long term are not products and markets, but the processes whereby the former are produced and the latter are served. Competitive success depends on transforming a company's key processes into strategic assets that improve the value added to the client. Companies create these assets by making strategic investments that link and transcend the company's business units and functions. The responsibility for supporting the transformation of a company's processes into strategic assets lies with management (Stalk et al., 1992).

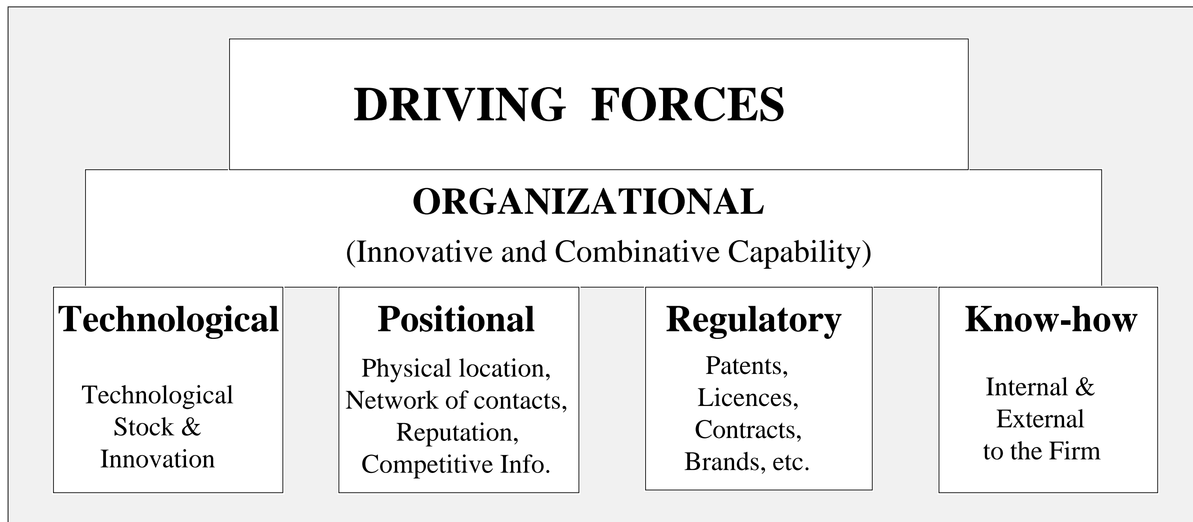
A Method for Identifying Strategic Assets

As we pointed out at the beginning of this article, the usual response of managers when asked to define the basis of their company's competitive advantage is to cite general company issues: «We have the best products», «Our distribution is unbeatable», «We've won the loyalty of our clients», etc. Managers must ask themselves what really lies behind these statements. There are a great number of different strategic assets that give support to customer service or lead to improvement in products, among other things. In order to identify these assets it is helpful to start with what the top management of a company defines as its «driving forces», those that drive the activities of the company or represent its main competitive advantage.

The next step is to identify what supports the driving force, how each of the company's activities supports it through specific strategic assets. This allows us to identify a pyramid of support and helps us to see the key interrelationships between these different activities. From there we can proceed to the third step of the process.

Identifying these interrelationships allows us to study what the organizational processes are that allow these relationships to be fluid. These processes will be organizational strategic assets. They are the most relevant processes within the functioning of the company, those that allow the different strategic assets of the different activities to combine to form a higher-order asset. For example, a company cannot be client-oriented without coordinating the efforts of Marketing and Logistics, or without there being a close and efficient relationship between product design and customers or the sales force (see Figure 3).

Figure 3. The Pyramid of Strategic Assets

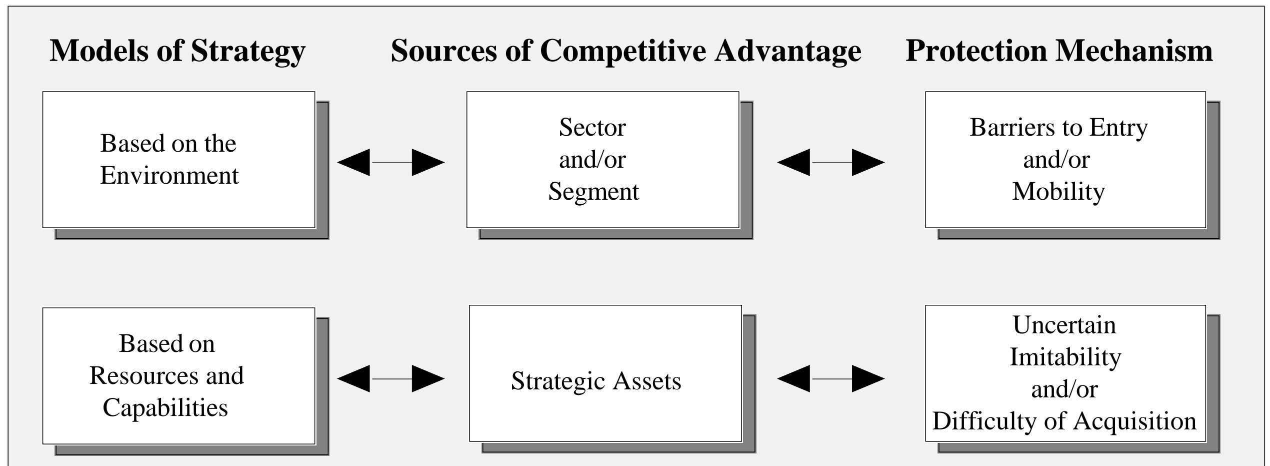


It is important to emphasize that it is impossible for an outside observer to clearly distinguish the firm's driving forces and the way they interrelate with its other strategic assets. This is a task for the managers themselves. Who else could identify and weigh up the most important variables in the functioning of the organization? It is not always easy to carry out this analysis systematically and to understand its strategic implications in a global way. One of the main aims of this paper is precisely to provide a tool that will enable managers first of all to know what they are looking for and where they are most likely to find it, and secondly to put these essential assets in the context of the strategic management of the organization.

Now what? Strategic Assets and Management

Highlighting the importance of strategic assets as sources of competitive advantage in no way means forgetting about traditional analysis. Whereas, before, we talked about choosing sectors and market segments, now we seek to identify strategic assets. Thus, the assets owned by the participants in a given segment are the reason for the barriers to mobility, while the fact that strategic assets are difficult to develop or acquire explains why competitive advantage is sustainable over time (see Figure 4).

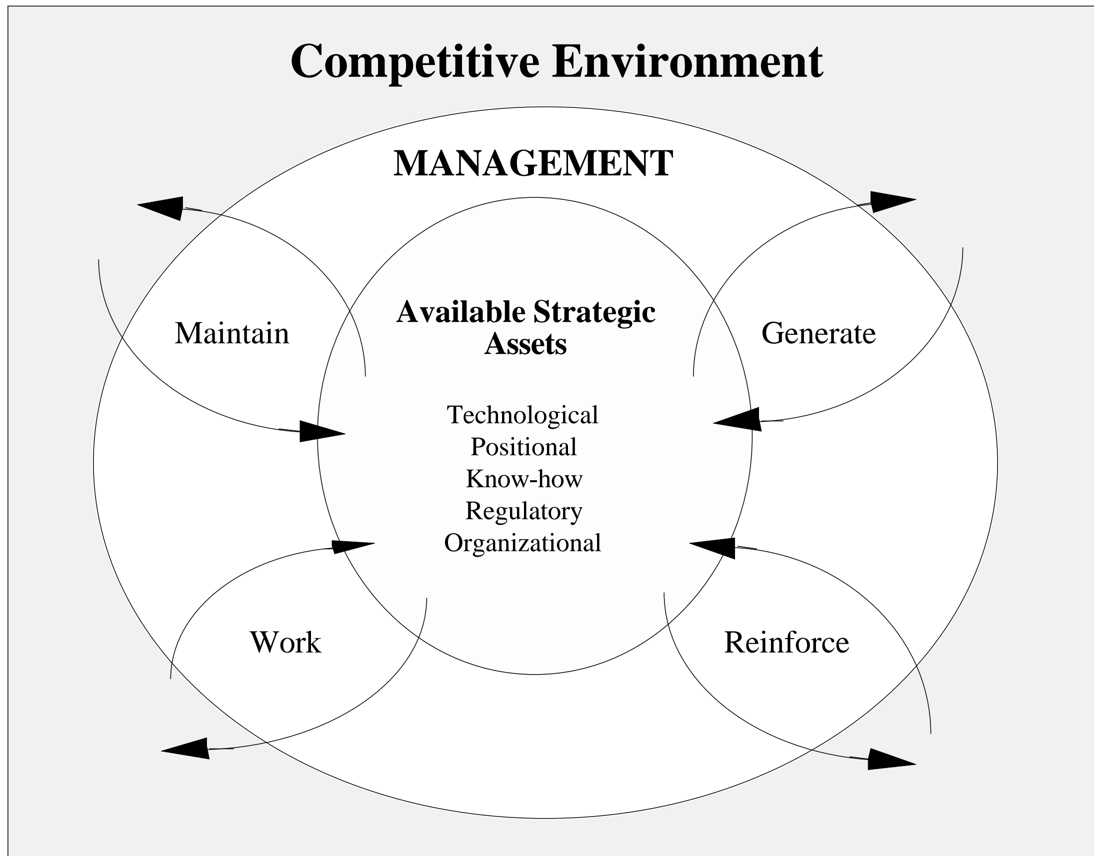
Figure 4. Mechanisms for Preserving Competitive Advantage



The more traditional approach to strategic planning is to start at corporate level, moving on to the level of the business unit and finishing by defining functional strategies. If we consider this procedure from the point of view of strategic assets, we see that it effectively ignores the company's resources and capabilities until the very end of the process. We believe that this practice leads to two common mistakes: First, the action plans are derived from the external analysis, from the demands of the environment, from the fact of having identified certain market openings or positioning possibilities. What the organization knows how to do is not taken into account until the process is almost completed. Traditional strategic planning fails to take account of resource management as the foundation of the company's competitive advantage.

Considering the company as a set of strategic assets shifts the focus of management's attention. Whereas before we chose a strategy on the basis of a choice of products and/or markets, we now take an action-oriented view based on the potential of our assets. The assets we have are strategic to the extent that we can obtain profit from them, to the extent that they enable us to do things better than our competitors or in a different way. Managing strategic assets therefore becomes a key aspect of management. The basic components of strategic asset management are: Generating, Reinforcing, Maintaining and Putting them to Work. It is through these four management tasks that the company controls its position in the competitive environment (see Figure 5).

Figure 5. Managing Strategic Assets



Generate

Management has to consider what resources and capabilities are needed within its strategy and determine the flow of assets in the company. The stock of strategic assets is like the filling of a tank. In the short term, you can regulate the flow of liquid into the tank but not the level of liquid in the tank. In the long term, this level will be determined by the history of the flow. Management has to maintain a flow of strategic assets that is sufficient to ensure that the level matches the company's present and future needs.

Once the internal and external sources of resources and capabilities have been identified, the manager's task is to capture and develop them. The difficulty of finding managers who fit the needs of the company illustrates this situation. Developing the right managers is a long and costly process that requires great care.

Reinforce

Once the company has the basic resources and capabilities it needs in order to compete, it must focus its attention on reinforcing them. This means, first of all, strengthening the ties between these assets and the organization. The quest for employee

commitment is a clear example of how companies strive to keep some of their key skills and knowledge out of the hands of their competitors.

Secondly, reinforcing strategic assets means making incentive systems consistent with the development and use of the organization's key resources and capabilities. There is no doubt that this also means having control systems that enable the company to assess its competitive position in terms of these same assets. Although it is not always easy to design such systems, as they are highly complex, the company must at least ensure that its incentive and control systems do not run counter to the development and use of its strategic assets.

Maintain

Strategic assets have to be sustained and maintained within the company. There are two key elements in maintaining resources and capabilities: organizational design and communication (Ulrich & Lake, 1990). We have to recognize that the design of the organization sends very clear signals to its members in terms of what the priorities are, the desired degree of flexibility, and also more subtle elements such as the style of work that is sought. In this sense, the structure adopted must be consistent with the commitment assumed in terms of strategic assets. Prahalad and Hamel (1990) have highlighted the fact that the key to the success of Cannon was its ability to structure itself around a group of core competences.

For example, a structure with a large number of hierarchic levels does not seem the most appropiate if the company's goal is to be flexible in responding to the demands of consumers.

On the other hand, the most obvious counterpart to organizational structure are communication systems. In order to achieve synergies among the company's activities, the relevant information must be made available to the people who carry out these activities. It is surprising the way some companies that make the needs of the client their number one priority nevertheless hold back a lot of supposedly confidential information from all employees below a certain hierarchical level.

Work

Strategic assets are only useful when they are put to work for the company. Management must find ways to obtain the greatest possible yield from these assets. Developing a stock of strategic assets is a long and costly process. The make-up of this stock cannot be altered in the short term. That is why management's efforts must be oriented toward maximizing the potential profit from the company's relevant assets. Just as the return on assets is regarded as a key parameter from a financial point of view, company managers should consider the return on strategic assets as one of the key measures of performance.

Conclusion

A company's strategic assets are what differentiate it and make it unique, allowing it to develop different strategies and set itself apart from its competitors. Competitiveness comes not only from anticipating market trends or responding rapidly to changes in demand,

but also –and sometimes crucially– from developing the capabilities that allow companies to react successfully to these changes. We believe that this paper will help distinguish the assets that really contribute to a sustainable competitive advantage from those that are less valuable. For example, the brilliance of our Marketing Director may be a unique and valuable resource, but if we do not make sure that he has strong ties with the company, he may decide to go and work for a competitor, in which case we would lose our source of competitive advantage. In assessing human resources we should ask ourselves whether productivity depends on specific individuals or on group skills that are more difficult to imitate. This conceptual framework is also useful when it comes to deciding whether to buy in a technology or to develop it in-house, depending on how easy or difficult it is to protect this asset from competitors. Thus, the innovations in a company will be relevant only when they incorporate elements or combinations of elements that cannot be imitated by other companies. Finally, at the corporate level, an approach based on strategic assets will shed light on the depth and scope of a diversification strategy, since this strategy will be worthwhile only insofar as it contributes to generating strategic assets through new combinations, maintaining or strengthening the existing stock of assets and making the most of the resources and capabilities that the company has at its disposal. □

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(1) Selznick (1949) pointed out that organizations have «distinctive capabilities» that allow them to **sustain a position outperforming their competitors**. Andrews (1971) highlighted the analysis of a company's strengths and weaknesses as a basis for confronting the opportunites and threats of the environment. Penrose (1959) emphasized the role of strategic capabilities in the development of the organization.

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