

# Analyzing Your Company

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Understanding your company is essential if you are to Maximize Value Creation in your business. Even legendary companies can fail when they stray from their strengths. Wal-Mart failed when they tried to use their low-cost skills to sell high-end clothing, Dell failed when they strayed from their mail order business into department stores, and high-volume Pepsi failed when they bought boutique drink maker Snapple. Different businesses require different competencies. It doesn't matter how much money you have, how many employees you have, or how successful you have been in the past if you venture outside your company's strengths.

## The Analysis

The first step to understanding your company is to list your resources. Begin with your balance sheet: How much cash do you have? What are your physical assets? Then look at your people: What are the skills of the people you employ? Resources are the most basic building blocks a company can use to create value and thus create a profit.

Second, list your strengths and weaknesses. Include competencies, extensive (or lack of) experience, access (or lack thereof) to additional capital, good (or bad) location, etc.

The goal is not to make lists, but to analyze your company to:

- Understand where you are vulnerable so you can position yourself accordingly
- Determine your core competencies so you can leverage them
- Develop a competitive advantage on which you can focus

To do this I suggest using the VRIN framework, commonly called the Resource Based View of the firm (RBV).

Whereas it is easy to classify each capability of a firm as a “core competence” or even a “competitive advantage,” the RBV framework forces you to look at each resource and strength and ask if it is:

- Valuable
- Rare
- Inimitable
- Non-substitutable

Competencies that pass all of these tests are considered “Competitive Advantages.”



When testing if a resource is *Valuable*, we ask if the resource is in demand and if some of that demand can be appropriated by the company as profit. For example, the capability to grow corn is valuable because corn is used in everything from food to plastics. Whether a farmer can profit from that capability is limited because commodity prices are often very low. This leads us to the second test. A resource or capability that is not *Rare* is not a competitive advantage precisely because it is not an “advantage.” Instead of the corn-growing example let’s consider the ability to grow wine grapes, otherwise known as viticulture. Is it Valuable? Yes. Is it Rare? For this example we will assume that it is.

When a resource or capability is Valuable and Rare, the owner will make a profit—at least in the very short term. But as microeconomics shows, where there is a profit to be made there is a competitor ready to be born. This is why you should ask if a capability or resource is *Inimitable*.

Returning to our grapes, we must note that the ability to raise wine grapes can be taught (<http://wineserver.ucdavis.edu/index.php>), so competitors will enter the viticulture market if there is an attractive profit to be made. Viticulture is imitable. Wine grape vines do take relatively unique land and many fruitless years until they are mature enough to produce. Plus the grapes require more tender loving care and perhaps more skill than mechanized grain farming. Therefore we would say that the ability to grow wine grapes is “moderately inimitable.”

Grape-growers could potentially earn a profit because grapes are Valuable and their cultivation is Rare and moderately Inimitable. High prices will encourage users to substitute other goods, however, so next you must look at your competency and learn if it is *Non-substitutable*.

There are substitutes for wine grapes. You can make wine from most fruits. Buyers can substitute other alcoholic drinks such as beer, spirits, or even mead for wine. In fact, in the modern world wine can be substituted by Coke, tea, Kool-Aid—even water! Obviously wine grapes are not Non-substitutable in the overall market, which is partially why decent wine can be purchased for less than \$10/ bottle—people can drink many things, keeping demand for wine relatively low.

Altogether, you would say that the ability to grow wine grapes is not a competitive advantage. Although there is demand for them, it is a controlled demand and there is plenty of supply. But don't lose heart future viticulturists!

If a person or company can grow premium wine grapes due to ownership of a unique hillside in Oregon's Willamette valley, or can grow grapes cheaper than competitors due to a unique hybrid grapevine, they will have a competitive advantage. The reason is that there is no imitation or substitute for premium grapes that come from ideal micro-cultures (i.e. hillsides). Similarly, a low cost position allows you to profit even when market prices have lowered to the competitive price.

Competitive advantages tend to have limited life spans. But competitive advantages that have maintained or are expected to maintain their advantage over the long term are considered "Sustainable Competitive Advantages." For example, the unique hillside in Oregon would be a

**Core Competency:**

Something a company does especially well. Often requires years of experience to develop.

**Competitive Advantage:**

Something a company does that allows it to either maintain lower costs than competitors, or else differentiate its product/service. A competitive advantage must be Valuable, Rare, Inimitable, and Non-substitutable.

**Sustainable Competitive Advantage:**

A competitive advantage that can be maintained over a long period of time.

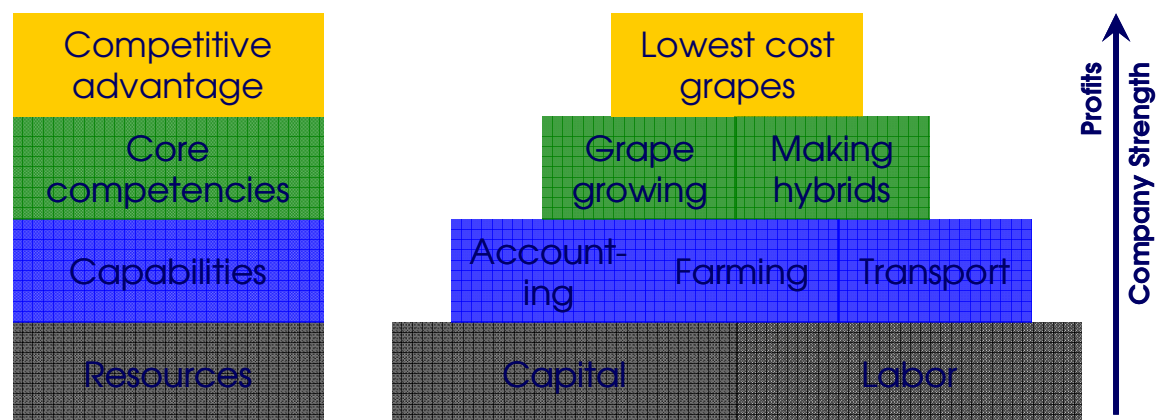
**Competitive Price:**

In microeconomics, the price where the highest-cost competitor makes neither a profit nor a loss.

Sustainable Competitive Advantage. The unique vines may not be a sustainable competitive advantage because imitators could acquire the vines or devise other low-cost strategies. Companies with sustainable competitive advantages are fortunate and should be especially careful to focus their efforts accordingly.

Hopefully you will find that you have a competitive advantage as you analyze your own company. If not, you are not alone. Many companies, perhaps most, do not have a true competitive advantage. Measured on the “Company Attractiveness Hierarchy,” these companies run their business at the *Capabilities* level. Reactors rather than leaders, they work hard—chasing every trend, fighting competitors directly, and blaming “the tough market” for their lack of profitability. These companies are mediocre, and are at risk if a competitor develops a competitive advantage.

### Company Attractiveness Hierarchy



As you continue managing your business, be sure to focus your attention on the competitive advantage you have or the competitive advantage you would like to develop. Move your business to the *Competitive Advantage* level. Soon, as Michael Porter the master of strategic management says, you will find your business in a position of leadership. This is Maximizing Value Creation through Good Business Run Wisely! Δ

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## For more information

To learn more about other components of strategic management, including analyzing your business, visit [\*\*www.McKinneyStrategicManagement.com\*\*](http://www.McKinneyStrategicManagement.com).

The McKinney Group, LLC was founded by Robert A. McKinney, a business strategist and classical entrepreneur, to focus on Maximizing Value Creation through Good Business Run Wisely. With his keen eye for excellence, proven business results and belief in the free market, Robert created The McKinney Group, LLC out of passion for entrepreneurship.

All functions of The McKinney Group, LLC are focused on businesses from startup to \$50MM because this is where the great businesses of tomorrow are found. It's also where businesses are run on a tight budgets and lean resources. We specialize in helping these businesses through analysis, planning, strategizing and finding solutions that develop competitive advantage.

We work with businesses we believe in. And we get results. Contact the McKinney Group, LLC and tell us your story.

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