Core competence

A company's most valuable resource

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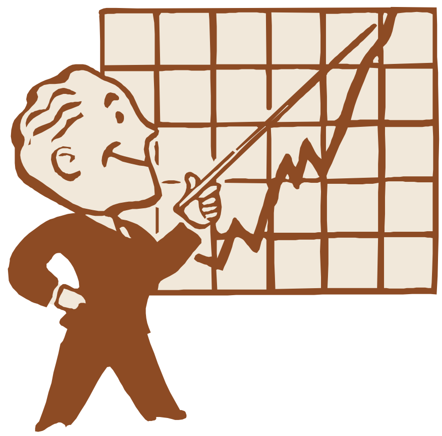
Core competencies are the capabilities that underlie leadership in any range of products or services, and enable a company to deliver a fundamental customer benefit. Besides defining business development priorities, regular core competence reviews also help in focussing on levels of investment, plans to strengthen skills and technologies, outsourcing decisions, alliances, internal deployment and developing a strategic architecture, among others. Read on to get an expert perspective on this critical driver of growth.

What makes British Airways, Singapore Airlines, Wall Mart, Toyota or Dell different from the crowd? When many companies make similar products, or offer similar services, what differentiates one from another? Core competencies are the capabilities that underlie leadership in any range of products or services. Have you ever thought, what makes a small scale SPM builder like Bombay Machines, different? They have built their core competence around strong fundamental design processes, and their value proposition to their customers lies in providing them with those small yet vital details that most would like to cut corners. That is why customers keep coming back to them again and again.



What did Microsoft, Dell, Toyota, Matsushita, Sharp, Sony or Toshiba do differently yesterday that has put them in leadership positions today? A firm can capture a disproportionate share of profits from future markets by building competencies today that will make a disproportionate contribution to future customer values. It has taken Toyota decades to get to their present position, although, much of its accelerated growth seems to have come in the last two decades. The length of time it takes to build competencies to build world-class leadership depends on the culture & learning ability within the organisation. It also depends on the size and resilience, but could take five, ten or even more years in building global leadership.

Leading examples

Some companies that have been market leaders continue to do so while others do not, why? The answer is, these companies have built strong core competencies, and view it as their most valuable resource. Core competencies are also skills that enable a company to deliver a fundamental customer benefit. Honda's core competence is in combustion engines and gear trains. For Toyota, it is in its culture and unique production system. For Toshiba and Sharp it is flat screens. For Sony and Matsushita, it is miniaturisation. HP's competencies are in measurement, computing and communications. 3M's core competencies lie in adhesives, substrates and advanced materials across thousands of products. FedEx developed core competencies in logistics and bar coding. Wal-Mart's ability to provide benefits of choice, availability and value to its customers has made it a leader. Motorola's competencies are in wireless communications and Goldman Sachs in financial engineering.

What is core competence?

Hamel and Prahalad define competence as a bundle of skills and technologies, and, core competence as a sum of learning across individual skill sets and individual organisational units. Any bundle of skills that yield a significant cost advantage in the delivery of a particular benefit is also core competence. Therefore, core competence must also make a disproportionate contribution to customer value.

Core competencies are also the skills that enable a firm deliver benefits to the customer. Ace Designers too has developed competencies in strong fundamental design processes, and its value proposition of low cost pricing comes from volume production. Its focus is built around developing skill sets and technology based product centres.

When MKL in Hubli developed new competencies around implementing lean manufacturing system and the JIT culture, enormous cost savings had accrued from eliminating wastages and rationalisation. These were passed on to the customers in the form of price reductions. The company then went on to develop cost effective CNC lathes and co-developed a range of milling, drilling and surface grinding machines, besides large size CNC machining centres. This made a huge contribution to its customer value. Competition between companies, today, is as much for competencies as it is for market power and position.

If one had to produce a list of capabilities that were important to the success of one's business, one will probably come up with a long list. It is not possible for the management to pay equal attention to all of them. The senior management will have to then concentrate on those capabilities that lie at the centre called 'core', rather than those on the periphery. How do you consider a competence as 'core'?

Zeroing in on the 'core'

Firstly, when the competence makes a disproportionate contribution to a customer perceived value, try asking what are the value elements in the product or service. Find out what the customer is really paying for. Find out which value elements are most important to the customer. Use this to make the biggest contribution to price realisation. Competing for air space, Air Deccan the first low cost airline model in India has developed its core competencies around a customer-friendly 24/7/365-reservation model, managing a high aircraft utilisation rate and sustaining a low cost air-travel business model. Its unique value proposition to a customer is not only literally bringing the convenience of ticketing to the latter's drawing rooms but also in offering affordable, reliable and safe air travel. Providing its customer with ticket costs that are almost half that of the other airlines is by far its biggest value proposition to the customer. By developing competencies to constantly lower fares and provide value-added services, it can stay ahead of any future competition. In case of MKL, the price reductions passed on to their customers made a huge contribution to customer perceived value.

Secondly, the capability must be competitively unique. If a capability is easily duplicatable by a competitor it is difficult to call it 'core'. Although all cars have power trains, at Honda it has been its core competence. A core competence is truly core when it forms the basis of entry into new product markets. When you drive a Honda you will experience superior fuel economy, zippy acceleration, less noise and vibration. Honda has leveraged this competence to enter the aerospace industry. Its entry vehicle is the HF 118 turbofan jet engine for small business planes. Honda jet is now being tested in Japan. Through a strategic competence partnership with GE, it will enter the American market and compete with Pratt and Whitney PW 600 engines, which are presently outside of GE's manufacturing range. GE is acquiring Honda's competencies through this alliance for affordability, reliability and fuel efficiency.

At MKL, its competencies with different materials, short product development cycles and in precision engineering led to extension of product markets, and its competencies in processes led to the development of new products and markets. Hence, extendibility is the third ingredient to considering a competence as 'core'.

Is it same as competitive advantage?

Although core competence is an asset, it is not in the accounting sense. Skills are often mistaken for competence. HLL's millions of retail outlets is not its core competence. Wal-Marts logistics is its core competence. An aptitude to manage a factory, how much big, is not core competence. Toyota's lean manufacturing is its core competence.

Competencies do not wear out. Core competence may lose value over time. But the more it is used the more refined it gets becoming more valuable (eg, lean manufacturing). Competitive advantage is not a core competence, but a core competence is a competitive advantage. Similarly, a critical success factor is not a core competence, but a core competence can be a critical success factor.

Core competence is a developed aptitude. It is often heard, 'ability to make good castings is our core competence' or 'our backward integration - having our own foundry is our core competence' or 'to provide manufacturing solutions is our core competence'. It is important to distinguish between core competence and other forms of competitive advantage. Core competence is not a vertical integration. Nobody has made a suggestion that in core competence you have to do everything in-house.

Risks to avoid

One must view a company as a portfolio of competencies as much as one views it with its products and services. There are many risks of ignoring core competencies.

- The opportunities for growth will needlessly get reduced
- In a machine manufacturing company, one unit developed a new product that had new value proposition to its customers. It needed competencies in technology areas that existed in the other unit. There was no way the unit could depend on borrowing those competencies and had to rapidly develop its own. In case of multiple units company, when an opportunity is sighted, if the required competencies to respond are in another unit, there may be no way to redeploy people to another unit if unit managers are 'protective' about their people
- As companies fragment into smaller business units, the business-unit boundaries may make it difficult to apply competencies across borders
- Lack of core competence can desensitise a company in many different ways. If you hurry to maximise brand share, you may succumb to rent a competitor's competencies rather than invest in building your own - a dangerous shortcut
- Typically in India, CNC machine manufacturers have heavily focussed on the end product. Consequently, they have not invested adequately in acquiring new core competencies such as developing the electronics that will

control the machine or its software. The competency supplier can supply this borrowed competence to any competitor
- Investment in new core competencies provides the seeds for tomorrow's product harvest. If you fail to understand the core competence basis for competition in your industry, new entrants may surprise you in your business
- Companies that are insensitive to the issue of core competencies may relinquish valuable skills and thereby the markets by selling or closing part businesses. A leading machinery manufacturer, inspite of and in stark contrast to an exemplary and successful BPR & turnaround display, later probably chose to restructure the re-engineered business. Its decision to close and relocate a profit-making unit that had grown in sales by almost 500% in recent years, resulted in relinquishing valuable skills, skills that did not exist in the new location. Insensitiveness to the issue of core competencies resulted in losing it business

Getting it right

Managing core competencies in a firm should be the aim of the general management. It should not be entirely left to the technical guys, because the concept must not be jeopardised in building new businesses. Core competencies can best be defined for a firm, if teams work on identifying the competencies. It must be the result of a series of meetings, debates (heated is OK), disagreements, unexpected insights, an excitement about future potential and new opportunities. The process is aimed at a wide and deeper understanding of the skills that currently make the firm successful, and go beyond the served markets to new businesses. It also becomes sensitive to the existence of competition for competencies. Competence is the company's most valuable resource.

Key factors

Stability of the senior management teams and its strategic agenda are key factors in building new competencies. Consistent efforts and a consensus agenda will also play an important role. In a multi-unit machine building business, there was competence in one of the units to build consistent high quality machines on a fast flow rate matching the demand behaviour. When it tried to do this in the other units without borrowing the competence across the units, it failed to succeed. Although it had people with skills, the competence velocity was very low to redeploy those behind new market opportunities.

The mobility of competency is aided when frequent meets to exchange ideas take place. The Kirloskar Group had the unique concept of functional committees across companies in various disciplines such as exports, manufacturing, and foundry etc, to ensure there was mobility of competencies between group companies. When minds are closed and not open to accepting ideas, the

advantages that can be gained by sharing competencies will be lost. Core competencies must be leveraged across business units as and when required. The companies that are good at this get greater effective use of their competencies.

Implementation issues

Many companies wrongly give their chief financial officer more raw powers than the heads of their divisions or human resources department, while it should be the other way round. Competition for competence is the highest order of competitive rivalry; therefore access to competencies is a more critical driver of growth than access to cash. Core competence can be lost in many ways - wrongly divesting a performing unit, fragmented through divisionalisation, lack of funding, incompetent stewardship, etc. Core competencies need to be protected from erosion with vigour.

Regular core competence reviews will help in focussing on levels of investment, plans to strengthen skills and technologies, outsourcing decisions, alliances, internal deployment, developing a strategic architecture, competence acquisition goals, defining business development priorities, allocation of core competence resources, benchmarking competence building efforts against rivals and building a corporate community who view themselves as carriers of corporate core competencies.

Strategic repositioning

In the quest for competitiveness, restructuring the portfolio and downsizing the head count will make the company smaller, re-engineering processes and continuous improvement will make it better. However, regenerating the strategies and reinventing the industry will make the company different. MKL's unit at Hubli was a market leader and India's largest exporter of machine tools for many long years to first world countries. But its leadership was not permanent; it learned that compelling forces required the company to change radically in the ways it dealt with its customers, competition and change. And the last decade saw it demonstrate how an industry can rise to a leadership position by regenerating core strategies, competing, building new core competencies, and going beyond re-engineering (refer 'X-Engineering' - Modern Machine Tools, July 2004). It was a classic example of reinventing the industry. Hence, it can be said that there is no such thing as permanent leadership; it simply has to be reinvented again and again.

Toyota's consistency with its core competence in lean manufacturing has steadily made it a leader. For decades, it has stayed focussed on developing the competency and improving it continuously. What's your core competence? Would you rather build than downsize? Do you want organic growth or are happy with deal making? Do you want to re-engineer your processes or would you rather have an industry definition? Do you dream of the long-term possibility or the short-term feasibility? Would you like to be leveraging resources or allocating them? The answer lies in adopting the core competence route. ✦

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