THE END OF COMPETITIVE ADVANTAGE

HOW TO KEEP YOUR STRATEGY MOVING AS FAST AS YOUR BUSINESS

FOREWORD BY
ALEX GOURLAY
ALLIANCE BOOTS

Rita Gunther McGrath

HARVARD BUSINESS REVIEW PRESS

Praise for *The End of Competitive Advantage*

"*The End of Competitive Advantage* is an incredibly practical playbook for competing in today's dynamic world. Rita McGrath's compelling book provides clear guidance for leaders searching for the competitive edges that seem to grow more elusive by the day. A must-read."

—Scott Anthony, Managing Partner, Innosight; author, *The Little Black Book of Innovation*

"Rita Gunther McGrath cements her status as one of the top business gurus in the world with *The End of Competitive Advantage*. She asserts that sustainable competitive advantage is obsolete and offers a thoroughly compelling argument that successfully managing waves of transient advantage is the future of business success."

—John Caddell, author, *The Mistake Bank* (forthcoming)

"In today's economy, committing to achieve sustainable competitive advantage is like building the Maginot Line: It locks you into a position from which it is hard to move, and it does not keep the bad guys out. Better instead to adopt Rita McGrath's playbook for exploiting transient competitive advantages and get your organization to embrace the fact that the only constant is change."

—Geoffrey Moore, author, *Crossing the Chasm* and *Escape Velocity*

"How do you strategize when sustainable competitive advantages are gone? You need a playbook for strategy that fits today's fast and uncertain world. You need new methods for organizing and acting to deliver continuous growth and profits over decades. You need a new competitive advantage—this book."

—Alex Osterwalder, entrepreneur and cofounder, Strategyzer.com

"McGrath's central insight is authentic, empirical, and profound. Too many organizations unicorn-hunt for 'sustainable' competitive advantage at the expense of investing in agile—and anticipatory—strategic opportunities. This book will provoke useful arguments around creating versus exploiting innovation opportunism."

—Michael Schrage, Research Fellow, MIT Sloan's Center for Digital Business; author, *Who Do You Want Your Customers to Become?*

"If competitive advantage was *ever* sustainable, that time has passed. McGrath's book not only captures the shortcomings of traditional, static models, but lays out the tools that fuel leading performance. *The End of Competitive Advantage* will give you an entirely new perspective on how to think about strategy."

—Francisco D'Souza, CEO, Cognizant

"This smart, readable book addresses today's most significant strategy reality: that we are living in an era of transient advantage. Rita McGrath provides a playbook for this new landscape, showing how you can identify opportunities fast, execute against them at scale, and be unafraid to move on when the situation changes."

—William D. Green, former Chairman, Accenture

"The urge to hold on to one's established competitive advantage is a vicious trap. McGrath clearly establishes the factors central to building a dynamic competitive edge for an enterprise of tomorrow. Refreshing, insightful, and a must-read."

—Sanjay Purohit, Senior Vice President, Infosys Ltd.

"McGrath's groundbreaking work is aptly timed for today's dynamic markets, where winning requires continuous reconfiguration."

—Nancy McKinstry, CEO and Chairman, Executive Board, Wolters Kluwer nv

"*The End of Competitive Advantage* makes clear that high-performance teams have to stay vigilant. Are your leaders seizing new opportunities or just trying to optimize an outdated strategy? Keep your head up and stay alert, or a transient advantage might pass you by."

—Klaus C. Kleinfeld, Chairman and CEO, Alcoa

"As a long-time member of the Rita McGrath fan club, I was delighted to see this book. Her approach to strategy is fresh and practical, and is exactly what managers need today. It acknowledges competitive realities but shows a clear path forward. It is one of the most illuminating takes on how to deal with disruption that I have ever read."

—Clayton M. Christensen, Kim B. Clark Professor of Business Administration, Harvard Business School

THE END OF COMPETITIVE ADVANTAGE

HOW TO KEEP YOUR STRATEGY MOVING AS FAST AS YOUR BUSINESS

Rita Gunther McGrath

Harvard Business Review Press
Boston, Massachusetts

Printed in the United States of America
10 9 8 7 6 5 4 3 2 1

Library of Congress Cataloging-in-Publication Data

McGrath, Rita Gunther.
The end of competitive advantage: how to keep your strategy moving as fast as your business/Rita McGrath.
pages cm
Includes bibliographical references.
ISBN 978-1-4221-7281-0 (alk. paper)
1. Strategic planning. 2. Competition. I. Title.
HD30.28.M38378 2013
658.4'012–dc23
2012051721

ISBN13: 9781422172810
eISBN: 9781422191415

You jolted me from complacency in my nice little bureaucratic job.

Said that if it were a “top five” school the PhD would be worth doing—otherwise not.

We started a family, left the city we both loved, moved away from our friends, and got a mortgage.

I was miserable. Transitions are hard.

But we went on to build something quite remarkable—together.

For John, and discovering what our next chapter holds.

Contents

Foreword

This book could not be more timely. Any leader seeking to understand what it takes to win in the ruthlessly competitive markets most of us are faced with today will benefit from reading it. In my thirty-two years as a retailer (beginning as a “Saturday boy” at Boots in Glasgow), I have personally witnessed a dramatic acceleration of the pace of change and the upending of assumptions we used to take for granted. Shopping behavior is changing dramatically. We are witnessing the end of advantages that made our 163-year-old Boots brand iconic. Consumers give businesses less permission to be wrong than ever before, and the Boots brand is not immune to this shift.

We were first introduced to Rita’s ideas when Boots Group merged with Alliance UniChem in 2006 to form Alliance Boots, and the breathing room that followed allowed us to take this newly formed company private in 2007. At that time we decided to transform the organization in a way that would enable us to operate very differently—by putting our customers first. Working with Rita, who is a gifted and original strategic thinker, we sought to embed many of the principles presented in this book into the leadership mind-set of our new organization. And we continue to do that today. We seek to be quicker and more decisive. We seek to be more candid, so that pending news—even negative news—travels fast and is immediately addressed. We seek to spend more time thinking about the future than we ever have before. We seek to break down silos so that our organization is appropriately structured to capture opportunities and act as one unified entity. Most of all, we seek to create courageous leaders—leaders who regard the fast pace of competitive exchange as exciting and who are fully engaged in creating an organization that can boldly capture opportunities and just as boldly move away from strategies and business practices that no longer represent opportunities.

When we started our evolution, many observers were skeptical. The Boots brand was tired and undervalued, they said, and the strategy poorly explained and not all that well executed. Moreover, our new business model, which combined a business-to-business wholesale operation with a customer-focused retail business, had seldom proved to be successful. But our results have proven our critics wrong. Measures assessing the recognition of our brand, satisfaction of our customers, and engagement of our employees are at record levels, and the profitability of Alliance Boots has been increasing by at least 10 percent every year since its privatization. And all this was achieved despite the global recession.

Our evolution, like yours, is far from over. We believe, however, that the concept of strategy presented in this book is invaluable. Strategy needs to change because customers and markets are changing faster than ever. The ideas in these pages provide a much-needed guide to a world of transient competitive advantage.

—Alex Gourlay
Chief Executive, Health & Beauty Division, Alliance Boots
Nottingham, United Kingdom, January 2013

Preface

Strategy is stuck. If you dropped into a boardroom discussion or an executive team meeting, chances are you'd hear a lot of strategic thinking based on ideas and frameworks designed in, and for, a different era. The biggies—such as Michael Porter's five forces analysis, BCG's growth-share matrix for analyzing corporate portfolios, and Hamel and Prahalad's core competence of the firm—are all tremendously important ideas.[1] Many strategies today are still informed by them. But virtually all strategy frameworks and tools in use today are based on a single dominant idea: that the purpose of strategy is to achieve a sustainable competitive advantage. This idea is strategy's most fundamental concept. It's every company's holy grail. And it's no longer relevant for more and more companies.

In this book, I take on the idea of sustainable competitive advantage and argue that executives need to stop basing their strategies on it. In its place, I offer a perspective on strategy that is based on the idea of transient competitive advantage: that to win in volatile and uncertain environments, executives need to learn how to exploit short-lived opportunities with speed and decisiveness. I argue that the deeply ingrained structures and systems that executives rely on to extract maximum value from a competitive advantage are liabilities—outdated and even dangerous—in a fast-moving competitive environment.

This much at least seems to be well understood. But then why hasn't basic strategy practice changed? Most executives, even when they realize that competitive advantages are going to be ephemeral, are still using strategy frameworks and tools designed for achieving a sustainable competitive advantage, not for quickly exploiting and moving in and out of advantages.

This book addresses that problem. It offers a new set of practices based on the notion of transient, not sustainable, competitive advantage. With this book, you'll get a new playbook for strategy—one that is based on a new set of assumptions about how the world works—and learn how some of the most successful companies in the world use the new playbook to compete and win when competitive advantages are transient.

The Evolution of Strategy

How did the idea of sustainable competitive advantage get so entrenched in the first place? Let me retrace how this concept evolved and, in parallel, show how my own work—both in academia and in the world of management practice—has led up to this book.

Sustainable Competitive Advantage

Historically, strategy and innovation have been thought of as two separate disciplines, in both research and practice. Strategy was all about finding a favorable position in a well-defined industry and then exploiting a long-term competitive advantage. Innovation was about creating new businesses and was seen as something separate from the business's core set of activities. Initially, I studied the corporate innovation process, much of which is laid out in my previous coauthored books.[2] At the time, relatively few serious scholars were studying "corporate venturing," with a few exceptions such as Bob Burgelman; Kathy Eisenhardt; and, of course, my coauthor, mentor, and colleague Ian C. MacMillan.[3] Instead, most of my PhD colleagues were busy studying positional dynamics within industries (with the goal of understanding how to achieve sustainable competitive advantages).

My academic work at that time had mostly to do with fostering entrepreneurial behavior within large firms. A major insight from those days was that when you're trying to enter fields in which you don't have a broad-based platform of experience—in other words, areas in which the ratio of assumptions you have to make relative to knowledge that you possess is high—a different set of disciplines needs to be employed. Ian MacMillan and I wrote a suggested approach to tackling this dilemma in "Discovery-Driven Planning," a best-selling article in *Harvard Business Review* that has since become a staple of entrepreneurship and innovation courses.[4] We didn't realize it at the time, but we were laying the foundations for a new approach to strategy, in which sustainable competitive advantage wasn't really the point.

The Growing Gap between Traditional Approaches to Strategy and the Real World

I had the opportunity to apply many of these ideas with consulting clients as we sought to help them develop an innovation proficiency. But this is when it started becoming obvious to us that most companies we were working with were really having trouble with their basic strategy for competing in their core businesses. Diverse clients such as DuPont, 3M, Nokia, Intel, and IBM were all beginning to recognize that traditional approaches to strategy and innovation weren't keeping pace with the speed of the markets in which they were competing.

But even as management tools to supposedly help cope with the pace of competition proliferated, executives didn't use them. Executives reported to the consultancy Bain "that the speed of the new economy has caused people and firms to believe they don't have time to implement tools," and firms, particularly in North America, were feeling "understaffed," with the consequence that they were sticking increasingly to tools they had already had experience with. Ironically, at the time, despite a lot of innovation in management tools and approaches, firms were increasing their reliance on strategy tools that they had inherited from the past.[5] So although they talked about using increasingly sophisticated approaches, if you looked at what they were really working with you would still find SWOT analyses, industry analyses, and rather conventional competitive analysis.[6] Although executives realized the need for new approaches to strategy, they were still using old ones—or none at all.

Along with this growing gap in practice, some scholars in academia started to question the idea of sustainable competitive advantage. Ian MacMillan was one of the first to tease out its specific implications for strategy. Competitive advantage, he reasoned, could best be thought of in waves, with the job of the strategist being to seize strategic initiative by launching ever-new waves.[7] He and Rich D'Aveni coined the term "hypercompetition" to characterize markets in which a firm's competitive advantage would be quickly competed away.[8]

In both business and academia there was an increasing sense that existing frameworks were not doing a great job helping leaders cope with the faster pace of competition. And then, with the advent of the internet and the knowledge-based economy in general, decreases in protective trade regulations, and technological advances, things seemed to move ever faster, and for some reason companies that you would think would be able to cope lost their edge. Max Boisot, a dear and now departed friend, summed up the implications for unstable advantage in knowledge-intensive industries, basically concluding that the most profitable point in the evolution of an advantage was also its most fragile.[9] By the late 1990s, the connection between innovation and strategy went mainstream with the publication of Clay Christensen's *The Innovator's Dilemma*,[10] which cited discovery-driven planning as a useful element of the strategists' toolkit while trying to do innovative things.[11]

Transient Competitive Advantage

What was starting to happen was that the disparate fields of competitive strategy, innovation, and organizational change were all coming together. This in turn meant we needed to add new frameworks and tools for practicing strategy to the well-entrenched ones such as five forces analysis and the growth-share matrix. In my previous books, *Harvard Business Review* and journal articles, talks, and consulting, I've tried over the years to sketch out what a new way of practicing strategy might look like. Options reasoning, for instance, is a way of making investments in the future without having to risk massive losses.[12] Intelligent failures can be helpful in facilitating learning.[13] Opportunity recognition is a skill that can be enhanced and developed in a systematic way.[14] The resource allocation process is perhaps the most significant way to influence what gets done in an organization and who does it.[15] You need to think of customer "jobs to be done," rather than rigid markets influenced by supply and demand.[16] Business model innovation was every bit as important as R&D or product innovation.[17] And different leadership behaviors need to be deployed in businesses with different levels of maturity.[18]

The implications of all these ideas came together in what I'm calling in this book a new playbook for strategy. The new playbook is based on a new set of assumptions about how the world works—a different set of assumptions from those that gave us the useful frameworks and tools we've been using for the past several decades. The strategy playbook today needs to be based on the idea of transient competitive advantage—that is, where you compete, how you compete, and how you win is very different when competitive advantage is no longer sustainable.

Basing your strategies on a new set of assumptions can seem daunting, even if you know it’s the right thing to do. Even more challenging is shifting the ultimate goal of your strategy from a sustainable competitive advantage to a transient one—you can no longer plan to squeeze as much as you can out of any existing competitive advantage unless you are already well into exploring a new one. But as you’ll see from the stories in this book from companies and leaders all over the world who are competing on transient advantages, once you start working with the new strategic playbook, changes in the configuration of your advantages don’t have to be intimidating at all. Some of the executives I interviewed actually seemed to be having fun—rather than being defensive and debilitated, they used the pursuit of transient competitive advantages to represent a compelling and engaging call to action for their people and a spur to innovation.

Fast-moving strategies have implications for managerial careers as well. A friend of mine working for a Brazilian company suggested a somewhat counterintuitive idea: “In Brazil,” he said, “we’ve been through it all—inflation, corruption, unpredictable governmental regulation, you name it. And you know, you get good at it.” He pointed out that managers whose only experience is with more tame types of competition would be flummoxed if they had to confront some of the challenges his generation of leaders in Brazil had to overcome on a routine basis.

Although it’s easy to see the devastation wreaked on companies whose leaders were not prepared to be dynamically competitive, I think it’s important to recognize the benefits, too. Sclerotic and inefficient industries get better when faced with genuine competitive threats. Would anyone want to go back to the days in which the government-owned telephone company dictated pricing and choices, for instance? In their quest to find the next opportunity, companies are getting better at figuring out what people really need and will pay for, at designing better experiences, and at wresting new efficiencies from existing assets. In a lot of cases, the value an average person gets for the same dollar, yen, or euro is vastly greater than it was even a decade or two ago. And there are more opportunities for new ideas and for young companies to thrive than ever before.

Before closing this preface, I’d like to acknowledge some of the people who have been instrumental in making this book a reality. Jill S. Dailey, of Accenture, proved invaluable as an intellectual sparring partner, a source of new ideas, and a resource for figuring out how these ideas could work in practice. The idea of arenas and of industries competing with industries is an idea we’ve worked on pretty intensively together. Ian MacMillan was a sounding board and an unapologetic critic of those ideas he didn’t feel made sense. I appreciated the suggestions and comments of the many people I interviewed for the book. Alison Norman, Xi Zhang, and Sooreen Lee provided invaluable research assistance. Melinda Merino and the team at Harvard Business Review Press have been true partners in crafting and shaping the ideas presented here.

I hope you enjoy this introduction to people and companies that I believe represent some of the best new strategic thinking and behavior for winning even when competitive advantages don’t last. They don’t always get it right—in fact, if my ideas about temporary advantage and learning from failure apply, it's almost impossible for a company to call it correctly every time. What matters, though, when you have been taken by surprise or something negative occurs, is what you do next. The best firms look candidly at what happened, figure out how to do it better the next time, and move on. It's a bit like surfing a wave—you might fall off and find yourself embarrassedly paddling back to shore, but great surfers get back on that board. So too with great companies. They move from wave to wave of competitive advantages, trying not to stay with one too long because it will become exhausted, and always looking for the next one. It has been fun getting to know them.

—Rita Gunther McGrath
Princeton Junction, New Jersey

1

The End of Competitive Advantage

Fuji Photo Film Company had an inauspicious beginning. It was divested from Japan's first cinematic film manufacturer in the 1930s because it was a chronic underperformer. Over the years, it improved its poor reputation for quality, became a significant global firm, and began to take on giants such as Eastman Kodak in film and film processing. The market for amateur and professional chemical-based photographic processes hadn't really changed in over a hundred years, meaning that competition tended to devolve around distribution rather than products, and Fuji struggled to break into markets in which Kodak was entrenched. There were many innovations, to be sure—including roll film, 35-millimeter film, easy-to-load cartridges, and even disposable cameras—but the basic position of film at the center of the photography industry's competitive universe hadn't changed for decades.

In the 1970s, however, an event that subsequently proved seminal to the evolution of the photography business took place. Two members of one of America's wealthiest families, Nelson Bunker Hunt and William Herbert Hunt, made a play to corner the silver market. They were interested in using silver as a hedge against inflation (a big issue at the time) and also as a diversifying asset class given that they had large holdings in oil. They began to make investments in silver in 1973, at which point the price of an ounce of silver was just under $2. In early 1979, the price had risen to about $5. By the time their plans were publicly exposed at the end of 1979, they had amassed more than 100 million ounces (6.25 million pounds) of silver, which observers guessed was about half the world's supply. Their actions caused the price of silver to jump to a mind-boggling number of over $50 per ounce.[1]

The consternation among manufacturers was palpable—what would happen if silver, a key ingredient in film processing, proved far more expensive than their economic models had predicted? Further, what if the investors in silver had such a lock on the market that there would not be enough of the material to go around? Their anxiety didn't last long, however, because in March of 1980 the price of silver collapsed precipitously, bringing with it collateral damage in the form of one of the sharpest declines in the Dow Jones Industrial Average ever experienced.[2] With the crisis over, most photography companies, Kodak among them, settled back into doing business as usual.

Minoru Ohnishi, who became CEO of Fuji Photo Film in 1980, remained deeply uneasy about the experience, however. He sensed that a fundamental change was potentially afoot in the photography business. The introduction of Sony's first digital camera, the Mavica, in 1984 created the reality of photography that could do without film. He said later, "That's when I realized film-less technology was possible."[3] He wasted no time moving on this insight. He invested heavily in building up expertise in digital technologies to prepare for the next round of competition in the photography business. His determination for the company to make this transition was described as "single-minded" by a writer for *BusinessWeek*, who observed that if one were to tally up Fuji's investments by 1999 in research and technology dedicated to digital products, it would easily top $2 billion. The article went on to note a "mystical" belief among the company employees in the correctness of this strategy. This attitude was reflected by chief scientist and senior advisor Hirozo Ueda, who told the reporter, "We're not going to quit, and we're not going to lose this battle."[4] By 2003, Fujifilm had nearly five thousand digital processing labs in chain stores throughout the United States; at the time, Kodak had less than a hundred.[5]

Ohnishi was determined not only to keep his company relevant in digital technologies for photography, but also to extend its reach to opportunities outside the photography business. He pushed the company to establish a sales channel for new products such as magnetic tape optics and hybrid electronic systems. It became the first non-US company to produce videotape. Later diversification efforts took the firm into biotechnology and office automation. It entered floppy disk manufacturing. Ohnishi was an innovator in business processes at Fuji as well. In a Japanese context famous for its long-tenured "salarymen," Ohnishi championed a lean headquarters staff, even going to great lengths to benchmark how well Fuji compared with forty other Japanese companies with respect to how many staff were involved in overhead functions. Although Fuji came in at 9 percent (and the average of the rest was 16.7 percent), Ohnishi was determined to bring this ratio down to 7 percent by asking the organization to cut its workload significantly and to eliminate 50 percent of the time-consuming consensus building and documentation that were standard business practice at the time.[6]

The reconfiguration of the company continued after Ohnishi was replaced by Shigetaka Komori, with sometimes-painful transitions as jobs were lost and facilities closed. The firm aggressively pulled resources from the photographic film business, reportedly cutting more than $2.5 billion in costs in order to invest those resources in new businesses.[7] Today, Fujifilm has significant health care and electronics operations and obtains some 45 percent of its revenue from document solutions and office printers.[8] All this was accomplished during several decades in which Japan's domestic industries were moribund and the country seemed unable to escape stagnation. In 2011, Fujifilm generated $25 billion in revenue, employed more than 78,000 people, and ranked 377th on *Fortune*'s Global 500 list. Kodak has gone bankrupt.

Fuji's story suggests that simply managing well, developing quality products, and building up well-recognized brands is insufficient to remain on top in increasingly heated global competition. The stakes for the company were huge—it risked undermining its existing advantages, and had to make a bet on a highly uncertain future. Yet, ultimately, it was Fuji's approach—investing in new advantages and pulling resources from declining ones—that proved to be more robust in the face of change. It didn't get it right every time, and sometimes the transitions were painful. But the company didn't get trapped by its past.

When competitive advantages don't last, or last for a much shorter time than they used to, the strategy playbook needs to change. Leaders have inherited a lot of ideas that may have made sense at one point but aren't keeping up with the pace of strategic change today. Although executives realize that rapid change is the norm, the strategies they use to compete still draw on frameworks and practices that were most effective decades ago. Executives need a new set of strategy frameworks and practices for winning over the long haul, even as sustainable competitive advantages have become a thing of the past.

This book is about the dynamics of transient, rather than sustainable, competitive advantage. It shows the new strategic logic—where to compete, how to compete, and how to win—when competitive advantages are temporary, and shows what we can learn from companies that have learned to ride the wave from one transient advantage to another.

Your Strategy Is Based on Old Assumptions

Sony. Research In Motion (RIM). Blockbuster. Circuit City. Even the New York Stock Exchange. The list of once-storied organizations that are either gone or are no longer relevant is a long one. Their downfall is a predictable outcome of practices that are designed around the concept of sustainable competitive advantage. The fundamental problem is that deeply ingrained structures and systems designed to extract maximum value from a competitive advantage become a liability when the environment requires instead the capacity to surf through waves of short-lived opportunities. To compete in these more volatile and uncertain environments, you need to do things differently.

When I got my start in the strategy field, there were two foundational assumptions we took practically as gospel. The first was that *industry matters most*. We were taught that industries consist of relatively enduring and stable competitive forces—take the time and effort to deeply understand these forces, and voilà, you can create a road map for your other decisions that is likely to last for some time. The emphasis in strategy was therefore analytical: because industries were assumed to be relatively stable, you could get a decent payoff by investing in analytical capabilities to spot industry trends and design your strategy accordingly. Those were the days of the five-year plan. A major assumption was that the world of five years from now was to some extent comprehensible today.

For instance, the traditional network television model in the United States was successful for many decades because the limited and expensive broadcast spectrum meant that a few players (in this case the major networks) dominated the few channels to customers. Constraints having to do with geography, syndication rights, and ratings all kept the model in place for years. For advertisers, this meant that television stations offered the promise of extremely large mass markets. Over the last thirty years, the constraints that held this model in place have eroded. Cable television eliminated the constraint of limited channels, fragmenting the mass market. Video rentals allowed viewers to watch content at their own convenience. The ability to record programs and skip the commercials was later embraced by a public weary of intrusive advertisements. More recently, the internet has facilitated an explosion of "channels" that viewers might look to for entertainment. This relaxation of constraints has fundamentally undermined the networks' business model. Indeed, the most important dynamic wasn't network-to-network competition but an invasion from other industries.

The second assumption was that *once achieved, advantages are sustainable*. Having achieved a solid position within an industry, companies were encouraged to optimize their people, assets, and systems around these advantages. In a world of lasting advantage, it made sense to promote people who were good at running big businesses, operated with greater efficiency, wrung costs out of the system, and otherwise preserved the advantage. Management structures that directed resources and talent to strong core businesses, often called "strategic business units," were associated with high performance. The core assumption here was that you could optimize your systems and processes around a set of sustainable advantages.

There are indeed examples of advantages that can be sustained, even today. Capitalizing on deep customer relationships, making highly complicated machines such as airplanes, running a mine, and selling daily necessities such as food are all situations in which some companies have been able to exploit an advantage for some time. But in more and more sectors, and for more and more businesses, this is not what the world looks like any more. Music, high technology, travel, communication, consumer electronics, the automobile business, and even education are facing situations in which advantages are copied quickly, technology changes, or customers seek other alternatives and things move on.

The New Logic of Strategy

The assumption of sustainable advantage creates a bias toward stability that can be deadly. My research suggests that rather than stability being the normal state of things and change being the abnormal thing, it is actually the other way around. Stability, not change, is the state that is most dangerous in highly dynamic competitive environments.

Think about it: the presumption of stability creates all the wrong reflexes. It allows for inertia and power to build up along the lines of an existing business model. It allows people to fall into routines and habits of mind. It creates the conditions for turf wars and organizational rigidity. It inhibits innovation. It tends to foster the denial reaction rather than proactive design of a strategic next step. And yet "change management" is seen as an other-than-normal activity, requiring special attention, training, and resources. A Google search on the phrase "change management" turns up 21,600,000 results—that's twenty-one *million* citations.

A preference for equilibrium and stability means that many shifts in the marketplace are met by business leaders denying that these shifts mean anything negative for them. Consider the reaction of executives from Research In Motion (the parent company of BlackBerry devices) to the 2007 introduction of the iPhone. Jim Balsillie, the company's co-CEO, told a Reuters reporter that the launch of Apple's iPhone wasn't a major threat, simply the entry of yet another competitor into the smartphone market.[9] Five years later, the company is at risk for its very survival, facing a slew of disappointing product launches, subscriber defection, continuing service outages, and shareholders in open revolt. Its former leaders have been replaced. Yet this company's products were so beloved by its corporate users that asking them to put away their BlackBerries was like asking them to amputate a limb. What happened? A long track record of relatively stable success caused the ambition to hungrily search for new opportunities to atrophy. Once that's gone, it's hard to regain quickly in the face of fast competitive onslaughts.

It's typical for leaders to deny there is an issue until far too late, at which point there is an "all hands on deck" full-blown crisis. As one of my interview respondents from a major medical device manufacturer observed, "We had seen it coming, and decided to ignore it and put our fingers into our ears until it became so obvious that we could no longer ignore it." Only then are resources mobilized, teams formed, and a sense of urgency created. Unfortunately, by that time it is often too late. Strategy today instead needs to be based on a new set of assumptions and practices.

Where to Compete: Arenas, Not Industries

One of the biggest changes we need to make in our assumptions is that within-industry competition is the most significant competitive threat. Companies define their most important competitors as other companies within the same industry, meaning those firms offering products that are a close substitute for one another. This is a rather dangerous way to think about competition. In more and more markets, we are seeing industries competing with other industries, business models competing with business models even in the same industry, and entirely new categories emerging out of whole cloth. This is most obvious in those markets that have embraced the digital revolution —just look at the shrinking CD section of your local bookstore (if, of course, your local bookstore is still around) and you'll see what I mean. Indeed, a reporter for the *Wall Street Journal* recently observed that if you look at categories of purchases for the average American family, vehicle purchases, apparel and services, entertainment, and food away from home are all shrinking, some at double-digit rates. What's growing? Spending on telephone services, up by 11 percent since the 2007 introduction of the iPhone.[10]

It isn't that industries have stopped being relevant; it's just that using industry as a level of analysis is often not fine-grained enough to determine what is really going on at the level at which decisions need to be made. A new level of analysis that reflects the connection between market segment, offer, and geographic location at a granular level is needed. I call this an *arena*. Arenas are characterized by particular connections between customers and solutions, not by the conventional description of offerings that are near substitutes for one another.

To use a military analogy, battles are fought in particular geographic locations, with particular equipment, to beat particular rivals. Increasingly, business strategies need to be formulated with that level of precision. The driver of categorization will in all likelihood be the outcomes that particular customers seek ("jobs to be done") and the alternative ways those outcomes might be met. This is vital, because the most substantial threats to a given advantage are likely to arise from a peripheral or nonobvious location.

This further raises the issue that a firm may not have a single approach that holds for all the arenas in which it participates. Instead, the approach may be adapted to the particular arena and competitors it is facing. For example, consider the strategy of language-teaching firm Berlitz. As Marcos Justus, their former Brazilian president, told me, in Brazil, competition for the mass market was fierce, but competition for customers in the upper income brackets was less so. There, a strategy of focusing on the upper echelons and positioning the brand as an elite product made sense. In the United States, where the majority of customers are somewhere in the middle, a different positioning featuring convenience and flexibility made sense. These are two different strategies, responding to the exigencies of the two different arenas. Both of these strategies, however, drive Berlitz's evolution toward the cultural consultancy it aspires to become.

The arena concept also suggests that conventional ideas about what creates a long-lived advantage will change. Product features, new technologies, and the "better mousetrap" sorts of sources of advantage are proving to be less durable than we once thought. Instead, companies are learning to leverage more ephemeral things such as deep customer relationships and the ability to design irreplaceable experiences across multiple arenas. They will be focused on creating capabilities and skills that will be relevant to whatever arenas they happen to find themselves operating in. And they may even be more relaxed about traditional protections and barriers to entry, because competition will devolve around highly intangible and emotional factors.

There is a big difference between thinking about strategy in terms of arenas as opposed to industries. In industry analysis, the goal is often to determine one's relative position with respect to other players in the same industry. It's good to have a large market share. And competitive threats are of the traditional kind—moves regarding product introductions, pricing, promotions, and so on. It's very easy to be blindsided. In the 1980s, for instance, no money-center bank even saw the threat of Merrill Lynch's cash management account offering because it wasn't offered by a bank; millions in deposits flew out the door before anybody realized what was going on. More recently, Google's moves into telephone operating systems and online video have created consternation in traditional phone businesses; retailers such as Walmart are edging into health care; and the entire activity of making payments is being contested by players from a bunch of different industries, including mobile phone operators, internet credit providers, swipe card makers, and, of course, traditional credit and debit card providers.

Although this is oversimplifying things a bit, you can think of traditional strategic analysis as being somewhat like the game of chess, which is quite sophisticated and nuanced but in which the goal is to achieve a powerful competitive advantage in a major market, akin to checkmating one's opponent. Arena-based strategy is much more akin to the Japanese game of Go, in which the goal is to capture as much territory as possible—the winner in Go lays the strategic groundwork by adroit placement of pieces on a board, eventually capturing enough territory to overwhelm