

## The Knowledge-based View of Strategy Formulation

### *Introduction*

Over the past two decades, business firms and organizations have increasingly focused on intangible resources as a means of generating a competitive advantage. Examples of intangible resources include industry knowledge, vendor relationships, and customer services.

Prior to the mid-1990s, businesses and organizations focused on the development of traditional tangible products and resources in order to devise strategies for gaining and maintaining a competitive advantage in the marketplace. In this traditional model, a firm would identify its valuable resources in order to create a product that was needed or wanted in the marketplace. For example, British Petroleum's (BP) original strategy was centered on its main tangible resource, petroleum. Consumers' gas-guzzling cars and highly itinerant lifestyles drove the need for the petroleum resource that BP had become expert in refining. However, in recent years, BP's view of strategy formulation has proved to be inadequate. Along with navigating the rising scarcity of petroleum resources, BP has learned how damaging its oil-refining practices can be when devastating mistakes – such as the massive 2010 Gulf of Mexico oil spill – occur. In addition, as cars have become more gas-efficient, BP has been forced to re-evaluate its resource-intensive strategy and instead use its energy expertise to move toward a more renewable energy strategy. As a result, BP has partnered with numerous wind, solar, and bio-fuel organizations worldwide in order to drive its new energy strategy forward. BP's organizational boundaries have become less clear as the company has engaged in more partnerships with other businesses and as the services industry has experienced exponential growth. The changes implemented by BP indicate a wider shift in the marketplace that has provided a foundation for a more knowledge-based view of strategy formulation within companies and organizations.

To strengthen our understanding of the growing knowledge-based view of strategy formulation, we will next take a closer look at how important knowledge is identified within an organization.

### *The Foundation: Identifying Knowledge within Organizations*

According to the 2013 *Merriam-Webster* online dictionary, knowledge is defined as “the fact or condition of knowing something with familiarity gained through experience or association” (*Merriam-Webster*, 2013). In organizations and businesses, most people correlate this definition with the capability and “know-how” of the organization's employees. The knowledge possessed by an organization's employees, in areas such as performing a specific production technique or informing the workplace understanding of a specific business concept, makes up an intangible resource known

as *employee competence*. As such, an organization's knowledge can be partly determined by, and defined as, the competency of its employees.

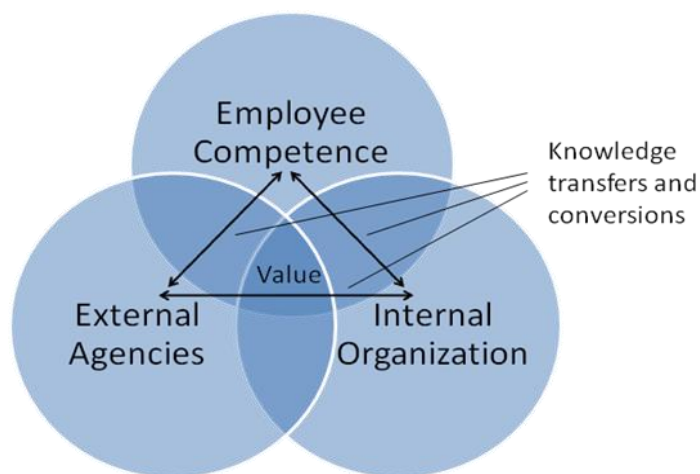
To create value for their organization, employees can use their competency to transfer or convert knowledge both internally, within an organization, and externally, via partnerships with other organizations. When transferring or converting knowledge internally within an organization, employees can improve areas such as workflow processes, product designs, budget structures, training programs, and organizational efficiencies. When transferring or converting knowledge externally to other organizations, employees can create and enhance customer relationships, vendor alliances, reputation attentiveness, brand identity, and market awareness.

As employees continue to develop workplace skills and master business concepts, their actions develop value for their organization. Employees become agents for their organization, building both tangible and intangible resources by exhibiting and utilizing their expertise. Due to its foundational importance to an organization, employee competence is the primary building block in the knowledge-based view of strategy formulation.

Next, we will examine the two other intangible resources – internal organization and external agencies – that work in accordance with employee competence to create a complete knowledge-based view of strategy formulation within organizations.

### *Completing the Knowledge-based View of Strategy Formulation*

Along with employee competence, the knowledge components known as *internal organizations* and *external agencies* also generate valuable information and create a competitive advantage for an organization.



## Figure 1: The Knowledge-based View of Workplace Organization

*Internal organization* refers to the internal structures of an organization that are created by its managers and employees. Examples of internal structures include product patents, computer programs, proprietary branding, project templates, design models, operating processes, and training programs. While the employees create these valuable structures within the organization, the components and organization of these structures are “owned” by the company itself. In addition to the more formal structures that lie under the umbrella of internal organization, other informal processes – such as workplace politics, culture, spirit, and networks – also are included within the internal organization resource.

*External agencies* refer to the relationships between an organization’s employees and external organizations, such the relationship between a company supplier of a product and a consumer who buys that product. These relationships are created and maintained by a company’s employees. Sometimes, these relationships can be converted into formal legal assets for the organization – for example, through the creation of trademarks or partnerships. Other external relationships are dynamic and uncertain in nature, changing (in both good and bad ways) over time. Such informal relationships might include customer services, vendor partnerships, and charity alliances. For example, the NFL is a well-known supporter of the American Cancer Society’s goal to end breast cancer. In support of this cause, NFL players are encouraged to wear the color pink in games during the month of October. In addition, post-game auctions of pink merchandise worn by players are sold to the public, with all proceeds going toward the charity. The NFL’s positive reputation for “having heart” can be contributed to its public display of supporting the breast cancer charity.

As displayed in Figure 1, above, all three intangible resources discussed in this reading – employee competence, internal organization, and external agencies – are critical in creating the knowledge-based view of strategy formulation. As knowledge is transferred and converted among these resources, areas of value are developed for the organization. The overall value to the organization is depicted as the center area in the figure, in which all three resources overlap one another. This overall value translates into a competitive advantage – and tangible profits – for the organization.

In the last section of this reading, we will investigate how an organization’s use of knowledge serves as a basis for developing a competitive advantage strategy.

### *Developing a Competitive Advantage Strategy*

Organizations that use knowledge as a means for gaining a competitive advantage create a strategy focused on how well information flows among the three intangible resources: employee competence, internal organization, and external

agencies. This strategy centers on the effectiveness of a two-way flow of knowledge. That is, the more frequently and smoothly the knowledge transfer process occurs between and among resources, the more value this process creates for the organization.

A well-developed strategy leverages the knowledge-transfer process and reduces blockages that hinder knowledge from being shared. All knowledge flows are viewed as important, regardless of the organization's boundaries. This awareness challenges the way people view the organization and the importance of the value chain as a whole. Whether information is flowing among employees, suppliers, customers, or contractors, the relationships surrounding information exchange are extremely valuable to the competitiveness of the organization.

One example of a company that has embraced the knowledge-transfer process, and thus transformed its business, is Holcim, one of the world's largest cement, gravel, and concrete suppliers (Zack, 2003). In essence, Holcim has sold the same product for over 100 years (ibid). In the early-to-mid 2000's, in order to stay profitable in a hypercompetitive market, Holcim decided to transition away from a resource-based strategy toward a knowledge-based strategy (ibid). Holcim has embraced the idea of knowledge as a fundamental resource, and thus has become highly efficient in transferring knowledge among its employees, internal organization, and external agencies in order to improve inefficiencies and grow more innovative. For example, after deeming its energy costs the most expensive part of its cement manufacturing process, Holcim worked with another company in Switzerland to invent production machinery that utilized alternate fuel sources such as dried sewerage sludge, plastic waste, and used tires (ibid). During this process, Holcim employees have learned more about alternative fuel sources and efficiencies, while customers have benefited from a more efficient and cost-effective product. In addition, supplier partnerships have formed during this process that have strengthened Holcim's network resources and product options, in addition to improving the innovation process for all parties involved (ibid).

### Summary

- The shift in the marketplace toward blurred organizational boundaries and exponential growth in the services industry has provided the foundation for the knowledge-based view of strategy formulation in organizations.
- By *Merriam-Webster's* definition, knowledge is "the fact or condition of knowing something with familiarity gained through experience or association."
- Knowledge-based strategy formulation is based on three intangible resources: employee competence, internal organization, and external agencies.
- The knowledge possessed by employees in order to perform a specific technique or inform the understanding of a concept creates the intangible resource known as *employee competence*.

- The intangible structures of an organization created by employees, such as patents, computer programs, designs, and processes, are referred to as the company's *internal organization*.
- The dynamic and often-uncertain relationships created by employees with external organizations, such those between suppliers and customers, are known as *external agencies*.
- As knowledge is transferred and converted between and among intangible resources, an area of value is created for the organization, giving rise to a competitive advantage.
- A well-developed knowledge-based strategy leverages the knowledge transfer process and reduces blockages that hinder knowledge from being transferred and shared throughout the value chain.

### *References*

*Merriam-Webster Dictionary Online*, s.v. "knowledge," accessed June 9, 2013, <http://www.merriam-webster.com/dictionary/knowledge>.

Zack, Michael. "What Is a Knowledge-based Organization?" Paper presented at the Organizational Learning & Knowledge 5<sup>th</sup> International Conference, Lancaster University Management School, Lancaster, UK, May 30 – June 2, 2003.