

# Organizational Culture: Can It Be a Source of Sustained Competitive Advantage?

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*Three attributes that a firm's culture must have to generate sustained competitive advantages are isolated. Previous findings suggest that the cultures of some firms have these attributes; thus, these cultures are a source of such advantages. The normative implications of the analysis are discussed. Firms that do not have the required cultures cannot engage in activities that will modify their cultures and generate sustained superior financial performance because their modified cultures typically will be neither rare nor imperfectly imitable. Firms that have cultures with the required attributes can obtain sustained superior financial performance from their cultures.*

Recent attempts to explain the sustained superior financial performance of firms like IBM, Hewlett-Packard, Proctor and Gamble, and McDonald's have focused on the managerial values and beliefs embodied in these firms' organizational cultures ("Corporate Culture," 1980; Deal & Kennedy, 1982; Peters & Waterman, 1982; Tichy, 1983). These explanations suggest that firms with sustained superior financial performance typically are characterized by a strong set of core managerial values that define the

ways they conduct business. It is these core values (about how to treat employees, customers, suppliers, and others) that foster innovativeness and flexibility in firms; when they are linked with management control, they are thought to lead to sustained superior financial performance.

Many of these explanations have a strong normative orientation. Firms with strong cultures are pointed out as examples of excellent management (Peters & Waterman, 1982); mechanisms for modifying the cultures of other firms to approximate closely the cultures of successful firms have been widely discussed and applied ("Corporate Culture," 1980; Tichy, 1983; Quinn, 1980). These efforts are seen not only as ways of improving employee morale or quality of work life, but also as vital for improving a firm's financial performance. Recall that Peters and Waterman (1982) chose firms for their sample that not only had an excellent reputation for management, but also were superior financial performers over the last two decades (Peters & Waterman, 1982, pp. 22-23).

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This paper examines the relationship between organizational culture and sustained superior financial performance. The conditions under which a firm's culture can be a source of sustained competitive advantage, and thus by implication, a source of sustained superior financial performance are examined (Hirshleifer, 1980). It is concluded that, under a relatively narrow set of conditions, a firm's culture can be the source of such sustained advantages. However, arguments suggest that the normative implications of studies on organizational cultures are limited significantly. While some firms may obtain sustained superior financial performance from their organizational cultures, firms without such cultures cannot expect to engage in managerial activities which will develop cultures that, in turn, will generate such performance. Thus, the normative implications of studies on organizational cultures are limited to describing how firms enjoying sustained superior financial performance can maintain their success, and how less successful firms can obtain average, or normal, performance. Studies of cultures cannot be used to describe how less successful firms, by modifying their cultures, can come to enjoy sustained superior performance.

First, some of the key concepts used in this analysis are defined. Second, the attributes that a firm's culture must have in order to be a source of sustained superior performance are discussed. Third, the organizational cultures of at least some firms are examined to see if they meet these criteria. Finally, whether or not firms that do not currently have organizational cultures that are a source of this level of performance can engage in managerial actions to develop such cultures is considered.

### **Culture and Performance**

Few concepts in organizational theory have as many different and competing definitions as "organizational culture." Smircich (1983), for example, has cited five classes of such definitions in her review of the literature on organizational cultures. Rather than attempt to resolve

these numerous and subtle definitional conflicts, a definition that is consistent with most of the research about organizational culture and a firm's performance is used here (e.g., Deal & Kennedy, 1982; Peters & Waterman, 1982). In this work, organizational culture typically is defined as a complex set of values, beliefs, assumptions, and symbols that define the way in which a firm conducts its business. In this sense, culture has pervasive effects on a firm because a firm's culture not only defines who its relevant employees, customers, suppliers, and competitors are, but it also defines how a firm will interact with these key actors (Louis, 1983). This conception of organizational culture blurs classical distinctions between an organization's culture and its structure and strategy (Tichy, 1983) because these attributes of a firm are direct manifestations of cultural assumptions about what business a firm is in and how it conducts that business.

While there is little consensus concerning the definition of organizational culture, there is broader agreement about sustained superior financial performance. In microeconomics, the financial performance of firms is divided into three categories: normal performance, superior performance, and below normal performance. Normal economic performance is that rate of return on a firm's investments just large enough to keep a firm's assets engaged in their current activities (Hirshleifer, 1980). Using language from organization theory (McKelvey, 1982), a normal return is a return just large enough to ensure a firm's survival. Technically, a normal return is the expected rate of return of a firm in perfectly competitive markets (Copeland & Weston, 1979). Superior financial performance is a rate of return greater than a normal return and indicates that a firm is prospering. Below normal financial performance is a rate of return insufficient to keep a firm's assets engaged in their current activities. Firms that obtain this level of return for a relatively long period of time typically do not survive (McKelvey, 1982).

Superior financial performance can be either temporary or sustained. Temporary superior per-

formance is the result of competitive dynamics widely described in microeconomics (Hirshleifer, 1980). Suppose a particular firm is able, for any of a variety of reasons, to obtain superior financial performance. Other firms, observing this, typically will seek to obtain this same level of performance by duplicating whatever makes a successful firm successful (Hirshleifer, 1980). Imitation increases the competition facing the initially successful firm, reduces margins, and decreases the level of financial performance. Increased competition through imitation will continue until no firms are obtaining superior financial performance (i.e., until all firms obtain approximately normal economic returns).

Certain firms may enjoy competitive advantages that are not subject to imitation, and thus these can be the source of *sustained* superior performance. In these settings, firms may enjoy superior financial performance even after imitative attempts by other firms cease (Lippman & Rumelt, 1982). Of course, sustained superior financial performance cannot be expected to last forever (Hirshleifer, 1980). Firms may invent new ways of competing that do not imitate, but replace, old ways (Barney, 1985b; Schumpeter, 1950). Also, natural business cycles sometimes can jeopardize a firm's sustained superior financial performance. Many of the firms studied by Peters and Waterman (1982), for example, currently are facing some financial difficulties ("Who's excellent," 1984). However, in the context of microeconomic definitions of a firm's performance, if these firms are still earning a greater than normal economic return, and if this return is not eroded through entry and imitation, then they are still enjoying sustained superior financial performance (although it may be at a reduced level).

### **Culture and Sustained Superior Financial Performance**

In order for a firm's culture to provide sustained competitive advantages, and thus, by implication, be a source of sustained superior financial performance, three conditions must be met

(Barney, 1985a). First, the culture must be valuable; it must enable a firm to do things and behave in ways that lead to high sales, low costs, high margins, or in other ways add financial value to the firm. Because superior financial performance is an economic concept, culture, to generate such performance, must have positive economic consequences. Second, the culture must be rare; it must have attributes and characteristics that are not common to the cultures of a large number of other firms. Finally, such a culture must be imperfectly imitable; firms without these cultures cannot engage in activities that will change their cultures to include the required characteristics, and if they try to imitate these cultures, they will be at some disadvantage (reputational, experience, etc.) compared to the firm they are trying to imitate.

These three characteristics result from the definition of sustained superior financial performance and research on competition by strategists (Porter, 1980) and economists (Hirshleifer, 1980). The first requirement, that a firm's culture must enable it to do things and behave in ways that add economic value to the firm, is clearly a prerequisite for generating even normal economic performance. If a firm's culture enables it to behave in ways that are inconsistent with a firm's competitive situation, then that culture cannot be a source of superior financial performance, sustained or otherwise.

The requirement that valuable cultures must be rare to generate sustained superior performance reflects the dynamics of competition discussed earlier. If many firms have similar cultures that allow them to behave and compete in approximately the same way, none will possess a culturally-based competitive advantage, and above normal economic performance cannot be expected (Hirshleifer, 1980).

Finally, even if the above conditions are met, it is still necessary for a firm's culture to be imperfectly imitable for it to generate sustained superior financial performance. Perfectly imitable cultures, even if they are valuable, and even if they are currently rare, are subject to imitation that dissipates any competitive advantages they

may provide. The culture-driven success of one firm creates an incentive for other firms to modify their cultures to duplicate that success. If the culture is perfectly imitable, it cannot give any one firm a sustained competitive advantage and the margin reducing dynamics discussed earlier are likely to emerge. Thus, for example, if the cultural attributes isolated by Peters and Waterman (1982) are, in fact, easily transferable, as is suggested on the cover of the paperback edition of their book, then these cultural attributes cannot be a source of sustained competitive advantage, and their existence in a firm cannot be an explanation of sustained superior financial performance.

A firm that has a valuable, rare, and imperfectly imitable culture enjoys a sustained competitive advantage that reflects that culture. Such a firm will enjoy the positive economic consequences of its culture. Relatively few other firms will be able to obtain these same benefits, and those firms that currently do not enjoy them cannot engage in activities that will make it possible to obtain them. However, the overall financial performance of a firm with such advantages can be reduced to normal, or even below normal levels, if a firm fails to manage other strategically relevant functions successfully (Peters & Waterman, 1982). These other functions might include both the financial and analytical characteristics of a firm's business. In addition, while a firm with a valuable, rare, and imperfectly imitable culture can obtain sustained superior financial performance, other attributes of a firm, including, perhaps, unique geographical advantages and luck, also can lead to such performance (Barney, 1985a).

This analysis does not imply that firms currently enjoying culturally-based advantages will always enjoy these advantages, because a valuable culture today could, in different economic or competitive conditions, become an economic liability. Moreover, because other attributes of a firm also can generate sustained above normal performance, it is possible that several firms in an industry all can obtain sustained superior

financial performance based on different competitive advantages (Lippman & Rumelt, 1982). However, it will not be possible for a large number of firms to obtain such performance on the basis of a single type of organizational culture.

### **Economic Profit from Organizational Culture**

If a firm's culture, in order to be the source of sustained competitive advantages, must be valuable, rare, and imperfectly imitable, then the possibility that organizational cultures with these characteristics exist must be evaluated. Previous research on organizational cultures suggests that at least some cultures of some firms have these characteristics, and thus can be a source of sustained competitive advantage. This research also suggests that not all firms have cultures with these three attributes (Martin, Feldman, Hatch, & Sitkin, 1983; Tichy, 1983), and thus organizational culture is not a source of competitive advantage for all firms.

### **The Economic Value of Culture**

Much of the literature on organizational culture and the performance of a firm can be interpreted as suggesting that culture can have significant positive economic value for a firm. Certain organizational cultures apparently enable firms to do and be things for employees, customers, suppliers, and others that could not be done, or could not be done as well, by firms without these cultures (Deal & Kennedy, 1982; Ouchi, 1981). Many of these activities have shown a positive economic impact on firms.

Peters and Waterman (1982) give perhaps the broadest description of the economic value of certain organizational cultures. Each of their eight characteristics of an excellent company reflects strong values and beliefs in organizational cultures. Thus, for example, firms that are simultaneously loosely- and tightly-coupled typically have an organizational culture with a strong set of core values [one of which encourages creativity and innovativeness (Peters &

Waterman, 1982, p. 319)]. Firms without such a culture may attempt to develop the attributes of a tight-loose system, but such attempts generally are not as successful because the culture of the organization neither supports nor values such behavior. In a similar vein, firms that are successful at obtaining productivity through their people generally have an organizational culture that supports and values the worth of the employee. Firms without such a supportive culture generally do not succeed in maximizing their productivity through their people. Firms that stay close to their customers typically are obsessed with customer service and satisfaction. This obsession, once again, reflects some of the core values of an organization's culture.

Each of these cultural traits can result in positive economic gains for firms. Both Peters and Waterman (1982) and Porter (1980) note that staying close to one's customer can result in timely market information, joint product development activities, and intense brand loyalties. These benefits result in high sales and increased margins, and thus have a direct positive financial impact on a firm. Innovativeness, productivity through people, and the other cultural factors cited by Peters and Waterman (1982) also have positive economic consequences.

Simply because the cultures of certain firms enable them to engage in activities with positive economic impact does not imply that all organizational cultures have such effects. Indeed, implicit in much of the organization cultures literature is the notion that an organization's culture can significantly reduce a firm's effectiveness, disabling the firm from perceiving all its competitive/operational options and preventing it from choosing options consistent with competitive/operational necessities (Crozier, 1964; Porter, 1980; Riley, 1983; Tichy, 1983).

### **Valuable and Rare Cultures**

That a firm's culture may enable it to behave in ways with positive economic impact does not necessarily imply that a firm can obtain sustain-

able competitive advantages from its culture. In addition, these cultural attributes must be rare.

The frequency with which valuable organizational cultures occur among firms is ultimately an empirical question. Previous research has indicated that some organizational cultures, far from being rare, are likely to be quite common among any given set of firms (DiMaggio & Powell, 1983; Spender, 1983). Indeed, some have argued that although cultures may appear to be unique or specific to a given firm, they sometimes actually reflect an underlying commonality and function, and thus are not rare at all (Martin et al., 1983).

Despite these findings, it must be admitted that some organizational cultures might exist in a relatively small number of firms, and thus hold the potential for generating sustained superior financial performance. Numerous authors have noted that firms are idiosyncratic social inventions, reflecting the unique personalities and experiences of those who work there (Barley, 1983; Polanyi, 1958). Firms are also historically bound, partially reflecting the unique circumstances of their founding (Pettigrew, 1979; Selznick, 1957), the unique personalities of their founders (Schein, 1983; Zucker, 1977), and the unique circumstances of their growth (Chamberlin, 1933; Clark, 1970, 1972). Often, these unique experiences of a firm are reflected in a firm's culture. Rare experiences can lead to a rare culture. If these cultures are also valuable, then they hold the potential for generating sustained competitive advantages.

The assertion that the unique personalities and history of a firm can lead to rare cultures is consistent with the contingency view of culture discussed by Smircich (1983). However, this does not necessarily imply that the cultures of these firms will be unique as well (Martin et al., 1983). Different organizational experiences may lead to similar cultural outcomes. Even among firms with unique histories, cultures may not be rare, and thus without potential for generating sustained superior financial performance.

## The Imitability of Culture

For a firm's culture to be a source of sustained competitive advantage, it must not only be valuable and rare, it also must be imperfectly imitable. Without imperfect imitability, any competitive advantage that a valuable and rare culture might give will create strong incentives for imitation.

There is significant evidence which suggests that valuable and rare organizational cultures often may be very difficult, if not impossible, to imitate. First, it may not be possible for individuals observing a culture (let alone those experiencing a culture) to describe what about a particular organization's culture adds value to a firm (Lippman & Rumelt, 1982). Values, symbols, beliefs, and the like are notoriously difficult to describe and categorize (Barley, 1983; Gregory, 1983). Moreover, the relationship between these highly subjective organizational characteristics and a firm's competitive advantages also defies rigorous description and inspection. The valuable and rare aspects of an organization's culture often become part of the unspoken, unperceived common sense of the firm. Many have argued that culture is a powerful force in explaining the behavior of individuals and groups within organizations precisely because it is unspoken and taken for granted (Berger & Luckman, 1967; Goffman, 1959; Polanyi, 1958). If those attempting to observe a culture to imitate it cannot describe what is valuable, those aspects of that culture cannot be consciously imitated [although firms might accidentally successfully imitate a culture they cannot describe (Lippman & Rumelt, 1982; McKelvey, 1982)].

Even if valuable and rare organizational cultures can be described by potential imitators, as is apparently sometimes possible (e.g., Ouchi, 1981; Peters & Waterman, 1982), it still may not be possible to imitate these cultures. The characteristics of organizational culture that may make it rare may also make it difficult to imitate. Valuable organizational cultures may be intrinsically bound up with a firm's unique history and heri-

tage—and history defies easy imitation. This conception of culture is explored in Clark's (1970, 1972) notion of an organizational saga, that is, the embodiment of the values, symbols, and beliefs of a firm as expressed through its unique history. Selznick (1957), Stinchcombe (1965), and Zucker (1977) observed that the constellation of persistent symbols, beliefs, and values that characterize a firm's culture at least partially reflect the unique early history of the firm, including the pattern-setting influence of company founders. A firm with a history significantly different from that of a firm whose culture it would like to imitate may find an unbridgeable barrier to imitation. If this firm's culture is also valuable and rare, then it may enjoy a sustainable competitive advantage.

Finally, even if the economically relevant aspects of a firm's culture can be described, and even if they are not historically specific in character, conscious and successful cultural imitation still may be imperfect. The components of organizational culture (including values, symbols, and beliefs) are as difficult to purposefully change as they are to describe (Smircich, 1983). The existence of multiple, possibly contradictory cultures within the same firm makes the management of culture all the more problematic (Gregory, 1983). Indeed, the data show that attempts to modify such subtle and interdependent aspects of organizations through organizational development methods have met with mixed results at best (Porras & Berg, 1978a, 1978b). While numerous authors have described ways in which an organization's culture can be managed (Peters, 1978; Quinn, 1980; Tichy, 1983), it must be admitted that at least some organizational cultures resist planned change. If a potential imitator cannot manage the change of its own culture to approximate the culture of a firm with a culturally-based strategic advantage, then the latter may be safe from imitation and its strategic advantage may be sustained.

It has been argued that the cultures of some firms may be immune from planned imitation. If these cultures are valuable and rare, then they



can be a source of sustained strategic advantage. This is not to suggest that a firm's culture stays the same since it certainly does evolve over time (Zucker, 1977; Selznick, 1957). This also does not suggest that all attributes of all organizational cultures are imperfectly imitable. Rather, previous findings indicate that some organizational cultures may be valuable, rare, and imperfectly imitable, and thus the source of sustained superior financial performance.

## Normative Implications of Culture Research

### Firms Without Valuable Cultures

For firms without valuable cultures, the normative implications of these analyses are somewhat limiting. Such firms cannot expect to obtain even temporary competitive advantages on the basis of their organizational culture. However, because a firm's culture can have such a significant impact on the ways a firm conducts its business, these firms often are forced to engage in activities that modify their culture to include at least some economically valuable attributes. Thus, a firm facing a competitive environment that requires low-cost production strategies with a culture that does not emphasize managerial efficiency often will engage in actions to try to develop the value of efficiency among its managers.

Suppose, through significant managerial efforts expended over time, a firm is able to modify its culture. Could this modified culture, then, be a source of sustained competitive advantage? Given our previous analysis, this seems unlikely for at least two reasons. First, if this firm is imitating the valuable culture of a competing firm, then even if this firm is successful at modifying its culture, that modified culture will only enable it to do the things that the firm it is imitating already does. Such successful *imitation* does not give a firm a competitive advantage, sustained or otherwise, in the area of organizational culture. Rather, it suggests that the valuable cul-

ture in question is less rare than it was before imitation, which in turn implies the likely development of the competitive dynamics suggested previously [i.e., reduced margins due to competitive entry (Hirshleifer, 1980)]. Thus, the best return that a firm can expect from imitating the valuable culture of a competing firm is an approximately normal return.

The second reason is that if one firm can consciously manage its culture to modify it to enhance its value, then other firms also are likely to modify their cultures in this manner. Returns to culture modifications depend not only on improving the economic value of a firm's culture, but also on the ability of other firms to make modifications in their cultures that result in similar cultures. If a large number of firms can successfully manage this change, then these culture changes will not result in any one firm enjoying a culture-based competitive advantage. But, if only a few firms are able to modify their cultures appropriately, then these firms can enjoy a sustainable competitive advantage.

There are at least two reasons why modifying a firm's culture in this manner might be possible for only a small number of firms. On the one hand, firms that are able to successfully modify the economic value of their cultures may enjoy a superior understanding of the skills necessary to accomplish this change. That is, they may have superior culture management skills. Such skills, if they are understood by only a few firms (i.e., if they are rare) and if those firms that do not have these skills cannot obtain them (i.e., if they are imperfectly imitable), can enable some firms to make culture changes while other firms cannot.

On the other hand, some organizational cultures may be more susceptible to change than others. Young and small firms, for example, often have more flexible organizational cultures than older and larger firms (Tichy, 1983). If these changeable cultures are characteristic of only a small number of competing firms (i.e., rare), and if firms without changeable cultures cannot develop change-facilitating attributes (i.e., these changeable cultures are imperfectly imitable),

then firms with these types of cultures can obtain sustainable advantages. However, if a large number of competing firms have equally flexible cultures, or if firms without such cultures can engage in activities to increase the changeability of their cultures, then these cultural traits cannot be a source of sustained competitive advantage.

There is a paradox central to this discussion. For an organization's culture to be the source of sustained superior performance, it must be valuable, rare, and imperfectly imitable. To obtain sustained superior performance from modifying its culture, a firm must have either valuable, rare, and imperfectly imitable culture management skills, or it must have a valuable, that is, flexible, rare, and imperfectly imitable culture. Firms either have these attributes, in which case they endow a firm with sustained superior performance, or they do not have them. If they do not have these attributes, but are successful in acquiring them, then these attributes are not imperfectly imitable, and thus cannot be the source of sustained superior performance. If it was possible to tell a large number of firms how to modify their cultures to include economically valuable attributes, then culture would cease to give any one firm a competitive advantage, and could not be the source of sustained superior performance. Thus, the normative implications of culture research are limited to assisting firms that already possess valuable, rare, and imperfectly imitable cultures and culture management skills in recognizing and nurturing these organizational characteristics to obtain sustained above normal performance. Such research, and the consulting it implies, cannot be used to help firms without valuable, rare, or imperfectly imitable cultures or culture management skills to obtain such performance, for such efforts are, in principle, imitable.

#### **Firms with Valuable Cultures**

From our brief review of findings on organizational culture, at least some firms have valuable, rare, and imperfectly imitable cultures. For such

firms, the normative implications of our arguments are clear. These firms should attempt to understand what it is about their cultures that gives them competitive advantages, and then to nurture and develop these cultural attributes, thereby increasing the likelihood that their competitive advantage will not be dissipated through mismanagement (Lenz, 1980; Stevenson, 1976).

From another point of view, the injunction that firms should study their culture to nurture its strengths is a reaffirmation of the now popular notion that firms should "stick to their knitting" (Peters & Waterman, 1982). The analysis suggests that this recommendation only applies to those firms that have valuable, rare, and imperfectly imitable cultures. For firms without valuable cultures, sticking to what they know best cannot generate even normal economic returns. Such activities will jeopardize a firm's survival. Even if firms have valuable cultures, if those cultures are not rare or imperfectly imitable, they cannot be expected to lead to sustained superior performance. Only if a firm's culture is valuable, rare, and imperfectly imitable will "sticking to one's knitting" generate sustained superior financial performance.

#### **Conclusion**

A firm's culture can be a source of sustainable competitive advantage if that culture is valuable, rare, and imperfectly imitable. The sustained superior performance of firms like IBM, Hewlett-Packard, Proctor and Gamble, and McDonald's may be, at least partly, a reflection of their organizational cultures (Peters & Waterman, 1982). Firms with valuable, rare, and imperfectly imitable cultures should nurture these cultures. Firms without valuable, rare, or imperfectly imitable cultures cannot expect their cultures to be the source of sustained competitive advantages. Nor can such firms expect that efforts to change their cultures, though they may successfully incorporate new valuable attributes, will generate sustained superior performance. For such efforts are typically imitable, and thus, at best, only the source of temporary superior perfor-



mance. These firms must look elsewhere if they are to find ways to generate expected sustained superior financial performance.

The analysis presented here has important implications for current debates concerning the ability to manage a firm's culture to improve financial performance (Smircich, 1983; Tichy, 1983). This reasoning suggests that if firms can modify their cultures to improve their financial performance, then such modifications can, in the long run, only generate normal economic returns. For if one firm is able to modify its culture, then it is likely that others can as well. In this case, the advantages associated with this culture are imitable, and thus only a source of normal economic performance. Only when it is not possible to manage a firm's culture in a planned way does that culture have the potential of generating expected sustained superior financial performance. Thus, those who argue that culture is simply another in a series of manipulatable tools available to managers for the implementation of

business strategies (Schwartz & Davis, 1981; Tichy, 1983) deny the possibility that culture can be a source of sustained superior performance, while those who argue that culture is not readily manipulatable (Smircich, 1983) uphold the possibility that culture can be a source of sustained superior financial performance for some firms.

A firm's culture is one of several attributes that differentiate firms one from another (Alchian, 1950; Alchian & Demsetz, 1972). It is in these sustainable differences between firms that explanations of sustained superior financial performance must be sought (Chamberlin, 1933). As Demsetz (1973, p. 2) once observed, it is often not easy to describe what it is about some firms that makes them more successful than others. Precisely because an organization's culture is hard to describe; because the common sense of managers is taken for granted; and because even if the culture can be described, it is difficult to change; a firm's culture can hold promise for sustained superior financial performance for some firms.

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