Journal of Business Research 67 (2014) 2106–2114

Contents lists available at ScienceDirect

Journal of Business Research

Technological advantage, alliances with customers, local knowledge and competitor identification

Jie Wu [a,b,1], Paul Olk [c,*]

[a] Leeds University Business School, University of Leeds, Leeds LS2 9JT, UK
[b] Faculty of Business Administration, University of Macau, Macau
[c] Department of Management, Daniels College of Business, University of Denver, 2101 S. University Blvd., Denver, CO 80208-8921, USA

ARTICLE INFO

Article history:
Received 1 March 2014
Received in revised form 1 April 2014
Accepted 30 April 2014
Available online 14 May 2014

Keywords:
Competitor identification
Customer ties
Firm capabilities
Local knowledge
Turbulent environment
China

ABSTRACT

Research typically studies competitor identification in stable markets and seldom considers possible antecedents in a dynamic context. To address this situation, this study combines a relational view, a capability-based approach, and a managerial cognition view to predict competitor identification. The hypotheses concern how a firm's customer ties, technological advantage, their interaction, and top manager's local knowledge influence competitor identification. Using a sample of 1348 firms across manufacturing and servicing sectors in China, we find that strong customer ties have a positive impact on competitor identification, firm-specific technological advantage has a negative impact, and the interaction of the two positively relates to competitor identification as does having greater local knowledge. These results suggest that a relational view, a capability-based view and a managerial cognition view complement one another in determining competitor identification in a dynamic environment.

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1. Introduction

Competitor identification occupies a central position in strategic management and marketing research. Bergen and Peteraf (2002) argue that before a company can engage in any offensive or defensive moves to enhance its position; before it can decide how to position itself or its product in the competitive landscape; and before it can attempt to exploit any competitive advantage, a company must first determine who are its rivals. Competitor identification is the important first task of numerous competitive processes, and several research streams in business, including marketing, economics and business law, directly or indirectly address the importance of competitor identification and its sources. Within the strategic management literature, competitor identification is fundamental to several important topics including competitive intelligence (e.g., Zahra & Chaples, 1993), strategic groups (e.g., McNamara, Deephouse, & Luce, 2003; Peteraf & Shanley, 1997), top management team cognition (e.g., Clark & Montgomery, 1999; Hodgkinson, 1997; Lant & Baum, 1997; Porac, Thomas, & Baden Fuller, 1989), and industrial organization economics (e.g., Porter, 1980), to name a few. While these research streams each recognize the importance of identifying competitors, less agreement exists among them in terms of how competitors are identified. An early effort takes an external approach, defining a company's competitors as those companies in the same industry or population. This operationalization makes it relatively easy to define competitors but often results in a large competitor set; typically too many for managers to keep track of when developing company strategy. Responding to this limitation, other researchers started to focus on the subset of companies (i.e., a strategic group) that managers consider to be direct competitors.

A second literature, which currently is attracting increasing attention, focuses internally on how managers create cognitive models of the industry by grouping together similar organizations. Researchers taking this approach map “stable, commonly similar beliefs regarding firm capability and patterns of competition within an industry” in moderately dynamic markets (Porac & Thomas, 1990; Thomas & Pollock, 1999, p. 136). Under dynamic conditions, however, these stable beliefs may not develop or persist. As environmental dynamism increases, market boundaries become blurred and a collective cognitive model deteriorates (Reger & Palmer, 1996). To address this problem, researchers have begun to recognize that companies have heterogeneous capabilities and that there may not be a collective cognitive model of competitors. Rather, each company may have its own set of competitors that differs from other companies' sets (Clark & Montgomery, 1999; Porac et al., 1989).

Although previous research has outlined both external and internal factors that affect competitor identification, these findings come from

* Corresponding author. Tel.: + 1 303 871 4531; fax: + 1 303 871 2294.
E-mail address: pmolk@du.edu (P. Olk).
[1] Tel.: +44 1133 3432636, +86 853 83978887.

http://dx.doi.org/10.1016/j.jbusres.2014.04.019
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studies of firms in stable environments. Few studies examine conditions where the market and environment are volatile. This lacuna is surprising because, as various scholars emphasize (Bergen & Peteraf, 2002; Peteraf & Bergen, 2003), managers in a dynamic environment may not easily perceive the market demands or capabilities and distinctive characteristics of other companies. Environmental dynamics can have important effects on competitor identification. Thus a fundamental question in competitor identification that remains unexplored is: How do companies in more turbulent conditions identify their competitors? To shed light on competitor identification in dynamic conditions, we combine a capabilities approach, a managerial cognition approach and a relational view to develop hypotheses regarding how a firm's strong customer ties influence its competitor identification. Two key insights from our study are that, in a volatile market, greater local knowledge and the combination of a company's technological advantage with stronger relational ties become important sources of information about competition. This additional information provides greater knowledge about competitors' activities and capabilities, and helps define the number of companies that managers consider similar and competitors.

2. Theoretical background

2.1. The external versus the internal perspectives

Competitor identification is the initial step in competitor analysis (Bergen & Peteraf, 2002; Chen, 1996) and the most fundamental problem in competitive sensemaking (Porac & Thomas, 1990). Researchers from several different perspectives have investigated competitor identification. Early studies generally viewed competitor identification as an external, objective concept. This approach implicitly assumes that every firm competes against every other firm within an industry (Hotelling, 1929). For most market structures, however, defining competitors so broadly might be unrealistic (and problematic) (Demsetz, 1981). Suffering from bounded rationality and imperfect information, decision makers cannot be expected to compare their firms with all the other industry participants, define their opportunity set and choose among alternative strategies (White & Eccles, 1987). To account for this, research has proposed alternatives. One is the concept of a strategic group, which is essentially an industry substructure. Hunt (1979), the originator of this term, bases his arguments on the observation that competitive rivalry takes place at an intermediate level between the aggregated industry-level and the disaggregated firm-level. According to strategic group literature, all firms within an industry may not compete with one another, but greater competition will exist among the groups of firms similar to one another on key structural or strategic dimensions (Dess & Davis, 1984; McGee & Thomas, 1986). Population ecologists, meanwhile, propose a localized competition hypothesis that argues that firms with similar resource requirements tend to compete more intensely with each other (Baum & Mezias, 1992; Hannan & Freeman, 1989).

While this research suggests an external and objective definition of competitors, recent research has explored competitor identification from the perspective of managerial cognition and perception (Lant & Baum, 1997; Porac, Thomas, Wilson, Paton, & Kanfer, 1995; Reger & Huff, 1993). In this approach, researchers recognize that decision makers simplify the competitive environment by using a mental model of competitive groups. The mental models of organizational strategists determine perceptions of competing organizations and the company's response to competitive conditions. Common to many of these initial approaches is the expectation that the set of companies share these perceptions. That is, over time, the companies' collective beliefs not only initially define but also sustain the market boundaries (Lant & Baum, 1997; Porac & Thomas, 1990; Porac et al., 1989; Porac et al., 1995; Reger & Huff, 1993). These inter-organizational perceptions remain fairly inert, resistant to change even during an economic recession (e.g., Hodgkinson, 1997).

While strong empirical evidence supports this expectation, questions about its generalizability arise because most of the studied firms operated in relatively stable environments. For instance, Porac et al.'s (1995) seminal paper uses data from an “old and institutionalized industry” — the Scottish knitwear industry, characterized by “small firms consisting of a single business unit” (Porac et al., 1995: 210). Research examining perceptions under changing environmental conditions has found greater diversity among managers' perceptions than in more stable conditions (Reger & Palmer, 1996). This has led other researchers to focus on a company's perceptions rather than the collective view for understanding competitive identification in dynamic markets. Peteraf and Bergen (2003), and Bergen and Peteraf (2002), build upon this emphasis on company perceptions to develop a framework of the antecedents of competitor identification in the ready-to-eat cereal industry in North America. Their study suggests that managers should engage in broad environmental scanning to avoid blindspots and to identify early on, any potential competitors or substitutes. Similarly, Few (2007) examines competitor identification by 15 financial services managers in the U.S. following a one-time deregulation. He finds that a manager's sense of the company's identity complements an economic (e.g., Peteraf & Bergen, 2003) and a categorization (e.g., Porac et al., 1995) approach in identifying competitors.

2.2. A relational perspective

While there are good arguments for believing that a mental model of competitors will extend to more turbulent contexts, there is reason to question whether firms in a quickly shifting environment will be able to form clear perceptions of customer needs and the degree of market commonality among firms. In a rapidly changing external environment, managers may not have the time or ability to scan the environment for possible competitors. Further, if changes occur quickly, the information may not be easily available for managers to scan. Instead, managers may have to rely upon additional mechanisms for identifying competitors. This has been the situation in many emerging markets such as China, where the general market conditions have greatly changed. For example, over the past three decades of reform policies, China has transitioned to a market-based economy and private enterprises now play a crucial role in China's market economy. The rise of private enterprises has changed the nature of competition and greatly shaped the competitive arena. The open market reform in many emerging market like China has enticed a tremendous surge in investment by multinational companies (MNCs). Accompanying this change in the number and types of competitors have been significant institutional changes from central planning to market economy. The ‘state-building’ of market reform inevitably results in influences from governments such as establishing the regulatory framework of property rights and modifying the forces of market. With these market transitions and institutional changes, managers tend to rely upon additional mechanisms for information about competitors (Chen & Wu, 2011). Since customers' needs are important in understanding competitor identification (Bergen & Peteraf, 2002), a good source of information in these contexts will be the relationships that companies develop with customers.

2.3. Local knowledge perspective

Numerous scholars address the importance of examining the characteristics of top management, or upper echelon, for understanding a company's strategic activities and performance (Finkelstein & Hambrick, 1990; Hambrick & Mason, 1984). This approach highlights the significance of a manager's perceptions of the context and willingness to change, and how these lead to a better or worse fit between the company's strategy and the demands in the environment. Of primary concern in this line of research is the accuracy over time of the manager to perceive the environment and to implement the change. Researchers argue that longer-tenured managers tend to become stale and not as

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