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Competitors' Strategic Heterogeneity and Firm Performance

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This paper explores intra-industry heterogeneity by proposing a new perspective. Whereas the strategic management literature tends to conceptualize strategic heterogeneity as the divergence between a focal firm and its rivals, we offer a complementary view in which we consider it to be the result of the differences among the strategic positions of the rivals of a firm. We argue that, when heterogeneity is examined from this perspective, vicarious learning and competitive alignment (instead of competition, collusion or legitimation) are the mechanisms that explain the impact of heterogeneity on performance. We also propose that the experience that firms accumulate by competing with the same rivals moderates this relationship. We test our hypotheses on the Spanish banking sector over the period 1999–2009. The results are consistent with them.

Introduction

The traditional concern of strategic management with the differences in performance among the firms that populate an industry has led researchers to focus on firm heterogeneity as a cornerstone in the analysis of competitive advantage (Barney, 1991; Peteraf, 1993; Scherer and Ross, 1990). From a strategic management perspective, heterogeneity tends to be conceptualized as a characteristic of the firm in relation to its rivals (i.e., how different a firm is compared to its direct competitors). In contrast, in this article we maintain that heterogeneity can be conceptualized in other ways. We propose that heterogeneity can also be understood as a property of the set of direct competitors of a focal firm (i.e., how different the competitors of a focal firm are from each other). Thus, while the traditional approach to heterogeneity conceives heterogeneity as the strategic distance between the focal firm and its direct rivals (Caves and Porter, 1977; McGee and Thomas, 1992; Peteraf, 1993), our conception focuses on the heterogeneity stemming from the strategic distances among the direct rivals of the focal firm.

Our contention is that the degree of strategic heterogeneity among rivals determines both the amount of information available from the observation of the strategies of rivals and the difficulties in designing effective competitive strategies. As a consequence, we propose vicarious learning and competitive alignment as the most appropriate mechanisms to clarify the impact of heterogeneity in the set of competitors on firm performance. We argue that both learning through observation and competitive alignment are conditioned by the plurality of strategies that the rivals adopt. On the one hand, the strategic heterogeneity in the set of competitors determines the quality and quantity of knowledge that can be learnt from them (Haunschild and Sullivan, 2002; Barnett, 2008). A high level of strategic heterogeneity in the group of rivals offers greater opportunities for acquiring knowledge through observation. On the other hand, heterogeneity also makes it more difficult for the firm to find a strategic configuration that aligns with the strategies of all its rivals (Ghemawat, 1991; Barnett and Hansen, 1996). The combination of these two effects results in an inverted U relationship between strategic heterogeneity in the set of competitors and focal firm performance.

This paper also analyzes how the experience accumulated with rivals conditions the impact of strategic heterogeneity among competitors on performance. Firms can gather information about the strategic options of their rivals by observing them or by retrieving past observations from the organizational memory (Huber, 1991). As firms accumulate competitive experience, they have greater knowledge about the strategic positions of the rivals and, as a result, the need to observe their rivals to obtain information about different strategic options decreases. We argue that, in these cases, competitive experience replaces strategic heterogeneity in the set of rivals as a source of learning for reasons based on information preference, information redundancy and information costs (Schwab, 2007). Consequently, basing our arguments on a learning perspective, we argue that competitive experience negatively moderates the link between the strategic heterogeneity of the set of rivals and firm performance.

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The addition of this approach to the analysis of strategic heterogeneity has two benefits. First, it complements the traditional perspective. By focusing on the position of the firm in relation to its competitors, the traditional approach said nothing about whether these rivals were a relatively homogeneous or heterogeneous group. This may be seen as a gap in the theory because, irrespective of the strategic position of a firm, rivals can show disparate levels of strategic heterogeneity. As we show in this article, this characteristic of rivals influences the results of the firm. Consequently, the proposed approach complements the traditional one and analyzes the consequences of strategic heterogeneity within an industry more comprehensively.

Second, the new approach incorporates theoretical mechanisms that help us to understand the effect of strategic diversity on firm performance. The traditional view argues in terms of legitimation, collusion and competitive behaviour to explain the consequences of the strategic distance between the firm and its rivals (Cool and Dierickx, 1993; Deephouse, 1999; Fiegenbaum and Thomas, 1990; Gimeno and Woo, 1996; Meyer and Rowan, 1977; Peteraf and Shanley, 1997). However, these arguments are not well suited to the analysis of the strategic heterogeneity among competitors, as they are based on the focal firm and its location in the strategic space. As we argue in this article, the mechanisms that explain the role of strategic heterogeneity as a characteristic of the set of rivals are vicarious learning and competitive alignment. Consequently, this new perspective not only complements, but also expands the analysis of strategic heterogeneity and its implications on firm performance.

We test our hypotheses in the Spanish retail banking sector between 1999 and 2009. Like many other banking sectors in the world, it underwent a deregulation process in the '80s and '90s of the past century which reduced the restrictions on the activities that each kind of bank (commercial banks, saving banks and credit unions) was allowed to perform. As a result, many different strategic orientations developed and the competitive patterns changed greatly. In the period analyzed, the Spanish banking sector is a context in which we can take advantage of varying levels of heterogeneity to test our model.

Our results confirm that strategic heterogeneity in the set of rivals influences focal firm performance in the form of an inverted U. This means that firms whose direct rivals show an intermediate level of strategic heterogeneity will perform better than firms operating in contexts of high or low levels of strategic heterogeneity. Our arguments, based on vicarious learning and competitive alignment, expand our knowledge about intra-industry heterogeneity. Our findings also suggest that competitive experience with the same rivals reduces the impact of strategic heterogeneity on firm performance. This is an important contribution to the organizational learning literature because it suggests that a firm's competitive experience and the strategic heterogeneity in its set of rivals can be considered alternative sources of information.

The rest of the paper is structured as follows. First, we offer a brief overview of the previous conceptualization of strategic heterogeneity and the mechanisms through which it influences firm performance. In addition, we explain the suitability of vicarious learning and competitive alignment to explore the impact of strategic heterogeneity in the set of rivals on firm performance. Then, we develop our hypotheses about heterogeneity in the set of rivals and competitive experience. The fourth Section describes the context in which we test these hypotheses, a representative sample of the Spanish retail banking sector, and the fifth Section presents the results. Finally, the last Section concludes and discusses the main implications.

Theoretical framework

Our theoretical framework briefly describes the traditional approximations to the study of strategic heterogeneity and the new perspective that is proposed in this paper. First, we review the main mechanisms used in strategic management to analyze the consequences of heterogeneity when it is conceptualized as the strategic distance between the focal firm and its rivals. Second, we present vicarious learning and competitive alignment as the mechanisms explaining the effect of heterogeneity when it is analyzed from our perspective: strategic distance among rivals.

The traditional approach: the analysis of similarity between a firm and its competitors

The strategic heterogeneity between a focal firm and its rivals has received a great deal of attention in strategic management (Deephouse, 1999; Porter, 1980). Many strategy scholars have tried to determine the value of being different and the value of being the same, given that this is important for managers as they try to achieve the right market position for their firms. In spite of the efforts of researchers, there is still no agreement on the balance between similarity and differentiation that firms should choose. The literature is divided between those who recommend occupying close positions to competitors and those who are in favor of occupying distant ones. This lack of agreement may be due to the plurality of arguments used to explain the effect of the strategic heterogeneity between a firm and its competitors on performance. Among these arguments, those based on competition, legitimation and collusion are the most popular in the strategic management field (Barney, 1991; Baum and Mezias, 1992; Caves and Porter, 1977; DiMaggio and Powell, 1983; Meyer and Rowan, 1977). These mechanisms use different suppositions and provide different predictions about the role of heterogeneity in competitive dynamics and performance.

According to the competition mechanism, the distance between market positions reduces competitive intensity and, therefore, improves firm performance. This mechanism considers that markets have finite resources that are divided among competing firms according to their positions. Firms occupying the same position in the market depend on similar resources to develop their activities and, as a consequence, compete more intensively among themselves (Audia and Kurkoski, 2012;