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# Scanning and updating failure: How AT & T turned its political capability into a core rigidity

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## 1. Introduction

One of the most influential theories in the management literature in recent years has been the resource-based view (RBV) of the firm. As part of the RBV, there has been an intense focus on capabilities as theory predicts that capabilities are at the heart of unlocking the value that give firms a competitive advantage over rivals. While it is intuitive that establishing a capability or capabilities in key areas should yield a net positive payout, *ex ante* allocation decisions at the firm level may not bear such payouts *ex post*. And while the overwhelming empirical evidence supports the general hypothesis that capability attainment is positively related to performance, there is a segment of empirical findings that calls this into question (Newbert, 2007).

One of the reasons that firm-level capabilities may not provide an advantage lies in managerial decision-making over time. For example, management may build a capability for some attribute that induces higher performance in one time period, but then may fail to adjust its decision in subsequent periods. The failure to adjust may result from a failure to appropriately scan the firm's environment, which leads to poor incremental updating. In failing to pick up important signals in the environment, or in failing to incorporate such signals, management becomes inertial and rigid. This paper is focused on managerial decision-making in the context of capability build-up and capability deployment over time. The central theme is in incorporating the theoretical notion of a corporate rigidity (Leonard-Barton, 1992) as the outcome of a former capability coupled with poor scanning and poor updating. In order to do this, I utilize an in-depth, historical case study to document managerial dysfunctions that result in a capability eventually becoming a rigidity. The setting for the case study is American Telephone and Telegraph (AT & T), primarily from 2000 to 2011. More specifically, I argue that AT & T's central capability was political, as success was often derived from good relations with government officials, both elected and appointed. However, after the 2008 U.S. elections, AT & T's management suffered inertia, as it failed to read clear signals from newly elected politicians and newly appointed regulators. This failure culminated in the failed takeover attempt of T-Mobile USA in 2011.

The paper, therefore, contributes to the literatures on capabilities theory and corporate political actions. However, at the same time, the paper contributes to the telecommunications literature. The telecommunications literature has a very robust archive of regulation-based studies (Chiang & Hauge 2013; DeVries, Simic, Achtzehn, Petrova, & Mahonen, 2014; Cheng, 2016). However,

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there is a dearth of research on corporate reactions to this regulation. Garcia-Murillo and MacInnes (2005) studied the lobbying efforts of telecommunications companies in and around the passage of the Telecommunications Act of 1996, using a public choice perspective. More recently, Sindik (2014) studied the lobbying activities of broadcast and wireless firms using institutional theory as an underpinning. However, in addition to an institutional logic, Sindik (2014) also incorporated the notion of strategic choice in the decisions to lobby and, more specifically, how and where to lobby. The current research follows these two papers in further developing the corporate political activity (CPA) literature as applied to the telecommunications industry, which is a second contribution of the work.

The paper is composed of the following sections. Section 2 contains the theoretical considerations and, more specifically, capabilities and rigidities theory. Section 3 explains the methods employed. Sections 4 through 7 are the sections of the case study (Case Study Parts I, II, III, and IV), which are aligned both topically and chronologically.

## 2. Theory

### 2.1. Capabilities

Capabilities have been defined as embedded firm-level processes that have an intended and specific purpose (Winter, 2003). Additionally, and following Winter (2000), capabilities are not *ad hoc*, meaning that they are repeated processes that the firm intentionally practices for two purposes. The first purpose is to improve the capability and the second purpose is to create firm value relative to its rivals (Drenevich & Kriauciunas, 2011). These repeated processes are considered organizational routines (Nelson and Winter 1982) that allow firms to operate and profit in their chosen markets. As part of the RBV, capabilities have had an increasingly important role in explaining heterogeneous outcomes as scholars have deemed resource stocks a necessary but insufficient condition for competitive advantage (Powell, 2002).

In order for a capability to lead to an advantage, resources must be effectively deployed. The explicit intent to compete along certain capabilities has been described as a top-down process within the firm and, therefore, managerial capabilities are crucial (Castianas & Helfat 2001; Adner & Helfat, 2003; Brown, 2017). Managerial capabilities include not only which strategies to follow but also how to execute these strategies. Therefore, while it may appear that competitors are competing along very similar dimensions, it is the firm-level processes that lead to advantage vis-à-vis rivals. Noda and Bower (1996) theorize that competitive advantage resides in the iterative choices made by management even if competitors appear to be operating along similar lines. These iterative choices are sometimes re-combinations of existing resources as new information is processed by management (Kogut & Zander, 1992). This recombination hypothesis is prevalent in dynamic capabilities theory (Teece, Pisano, & Shuen, 1997), which posits that sustained competitive advantage is earned only if firms learn through feedback loops; in other words, if firms have routines to improve their routines.

The ultimate goal for firms is to increase the probability of earning both competitive advantage and superior economic returns (Amit & Schoemaker, 1993; Barney, 1991). There are a number of papers which have provided evidence that capability development, deployment and proficiency lead to such goals. The mechanisms by which these are goals are realized through both the selection of key resources *ex ante* and the deployment of capabilities that optimize these resources *ex post* (Makadok, 2001). In essence, rent-seeking is the culmination of managerial capabilities in resource picking and capability deployment (Makadok, 2001).

### 2.2. Overconfidence and rigidities

While capabilities have been portrayed primarily as positively linked to firm-level performance. However, contrary evidence exists that depicts capabilities as potentially dangerous to corporate health in certain instances. Leonard-Barton (1992) proposed the concept of "core rigidity," which reflects a successful firm's myopic behavior. According to this view, managerial disability may lead to a non-linear relationship between capabilities and performance because of "…a gap between current environmental requirements and a corporation's core capabilities (Leonard-Barton, 1992: 118)." Too much success can blind management to alternative information or innovative techniques as an over-investment (in either time or money) in current capabilities fosters inertia at the expense of opportunity exploration (Henningsen, Henningsen, Eden, & Cruz, 2006; Miller, 2002; Park, 2000).

The mechanism for such decline is as follows. High levels of capabilities may also generate a commitment that drives strategic persistence to the point of diminishing firm performance (Grossman & Cannella, 2006; Lant, Milliken, & Batra, 1992). In some cases (i.e. stable environment), high levels of commitment may trigger firm-level success while in others (i.e. turbulent), market variability may diminish the value due to greater uncertainty. There is a second explanation, however, for a non-linear relationship between the value of capabilities and performance. Capabilities at very low levels as well as very high levels seem to be theoretically tied to weaker performance. The accumulation of pivotal capabilities will initially improve operational performance; however, the magnitude of this effect tends to diminish as the value delivered is outweighed by the costs of developing and maintaining the firm's capability. Ultimately, this relationship can turn negative as the external environment shifts the competitive parameters that lead to success. This overinvestment in previously needed capabilities may be indicative of poor resource allocation by management through the failure to iteratively change strategy (Noda & Bower, 1996).

The causes of the hypothesized performance decline reflect aspects of inertia and path dependence (Tripsas & Gavetti, 2000). As organizations learn how to accumulate capabilities, decision-makers within the firm become focused on those traits that yield high performance. However, as this benign focus becomes a more malignant myopia, inertial pressures constrain management, which further entrenches their current commitment. The initial capabilities become institutionalized and self-reinforcement then poses