

Forum on Economic Policymaking in Conditions of Uncertainty

Tuesday, 14 July 2020
2.00 pm - 4.00 pm

Competitive Advantage and Factor Shocks: The Role of Discretion in Asset-Based Strategies

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Resource-based view (RBV)

- A dominant theory in strategy that informs how companies develop competitive advantage (Barney 1991)
 - Counterpoint to economists (firm = profit maximizing function) and to Industrial organization thinkers (profitability ~industry structure)
- *Firms that have valuable, rare, hard-to-imitate, and non-substitutable resources are able to create a sustainable competitive advantage*

Own & Control

RBV has “a very simple view about how resources are connected to the strategies that the firm pursues” (Barney & Arikan 2001: 174)

Static worldview

- Differences in heterogeneously distributed resources are stable over time (Barney 1991)
- RBV “assumed stability in product markets” (Priem & Butler 2001: 22)

Focal issues

Although resources in the RBV are “tied semi-permanently to the firm” (Wernerfelt, 1984: 172), they can nonetheless reside in loci outside of firm boundaries (e.g. reputation, brand value, trust, supply and political networks)

→ Limited *structural discretion* over ‘external’ resources

The value of firm resources often hinges on the continued availability of external factors (Ellram et al 2013, Harris et al 2015)

→ What is the direction of expected *shocks* (positive or negative)?

→ Do firms have the *technical discretion* to deal with factor shocks (specific or generic complementarity)?

RBV: Configurational equifinality

- Resource heterogeneity is the de facto economic reality \leftrightarrow “environmental models of competitive advantage” (Barney 1991: 100)
- Firms follow idiosyncratic pathways to acquire, accumulate, and integrate their resource configurations (Costa et al 2013; Maritan & Peteraf 2011)
- Diverse resource configurations can lead to equifinal competitive advantage (Lippman & Rumelt 2003; Meyer et al 1993) BUT not every resource configuration has the same environmental exposure
 - E.g. firms “develop specialized assets to enhance profits at the price of **reduced flexibility** in the face of Schumpeterian shocks” (Amit & Schoemaker 1993: 39).

Distinct resources and resource configurations can underpin competitive advantage

1. Structural Discretion

Managerial Discretion	Internal Resources	External Resources	Sources
Residual rights to exercise control, including monitoring and sanctioning	<p>High</p> <p>IRs are subject to rules and routines and respond elastically to fiat power and inelastically to the environment</p> <p><u>Source:</u> ownership and employment contracts</p> <p>IRs can appropriate control rights (e.g. employee shirking) but monitoring is feasible</p>	<p>Low</p> <p>ERs respond inelastically to firm fiat power but elastically to the environment. ER is +/- autonomous</p> <p><u>Source:</u> Perceptions and attributions of stakeholders</p> <p>ERs can easily appropriate control rights as monitoring and measuring is hard</p>	<p>Foss & Foss, 1999; Grossman & Hart, 1986; Zander & Kogut, 1995</p>
Rights to residual income	<p>Typically belong to the firm but can be bargained away in the case of employees</p>	<p>Undetermined</p>	<p>Foss Foss 1999, Jensen Meckling 1976, Coff 1999</p>
Value Pattern	<p>Despite Principal-Agent problems and possible mutiny, generally aligned with firm objectives</p>	<p>Aligned with individual objectives or objectives of partner firm</p>	<p>Parsons, 1956</p>
Transaction costs	<p>Reduced (which is why firms exist)</p>	<p>Higher ~ opportunism risk and monitoring difficulties</p>	<p>Williamson, 1975, 1985</p>

2. Shock sensitivity & uncertainty

- Two types of sensitivity
 - Positive: a factor shock leads to more abundance and lower prices
 - Negative: a factor shock leads to more scarcity and higher prices
- For simplicity, we presume firms in the same industry have the same sensitivity direction (I.e. a shock is objectively positive or negative from an industry perspective)
- Counterexample
 - Tightening of CO2 emission regulation for car manufacturers has different effects for Tesla or Range Rover

3. Technical Discretion

Superior complementarity drives competitive advantage (Adegbesan 2009)

$$V(F \cup RB) = V(F) + V(RB) + V(S) \text{ and } S > 0$$

F = Factor, RB = Resource Base, S = complementarity

- Two types
 - *Specific*: requires factor-specific investment (Dierickx & Cool, 1989), increases bilateral dependency, facilitates returns to scale & scope → low technical discretion
 - *Generic*: utilization of a 'general purpose technology' enables greater rent extraction from any resource → high technical discretion because can be "redeployed to alternative uses" (Williamson, 1991: 281)

Competitive advantage can be rooted in specific and/or generic complementarity with an external factor

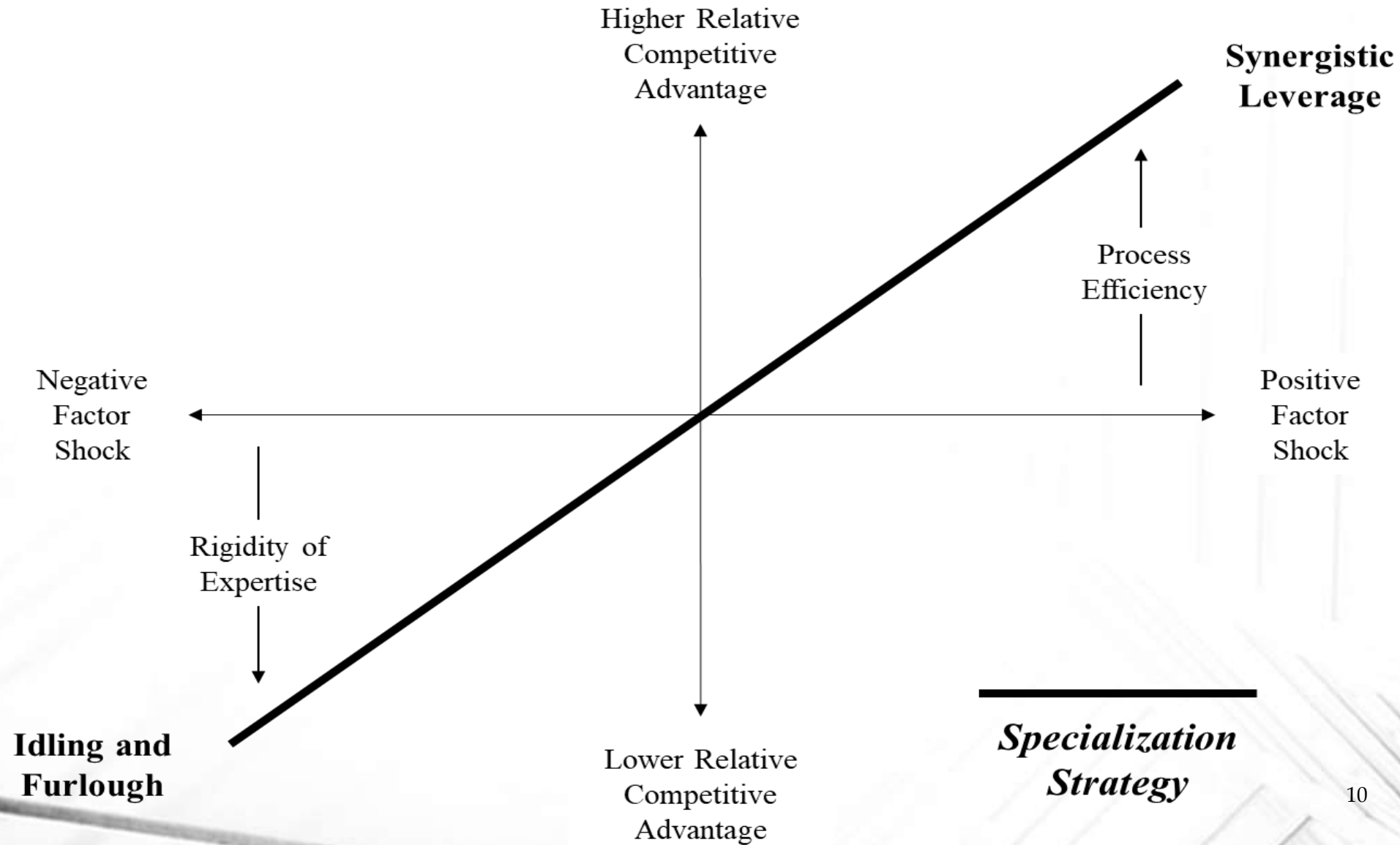
Congruent insights

- 1) Distinct resource configurations can underpin competitive advantage
- 2) A resource's ability to create competitive advantage is susceptible to changes in the availability of external factors
 - 1) Positive or negative supply shocks
- 3) Resources differ in *technical discretion*
 - 1) Complementarity to factors
 - 2) Sensitivity to factors (presumed to be homogenous in industry)
- 4) Firm resources can be located in external and in internal loci creating differences in *structural discretion*

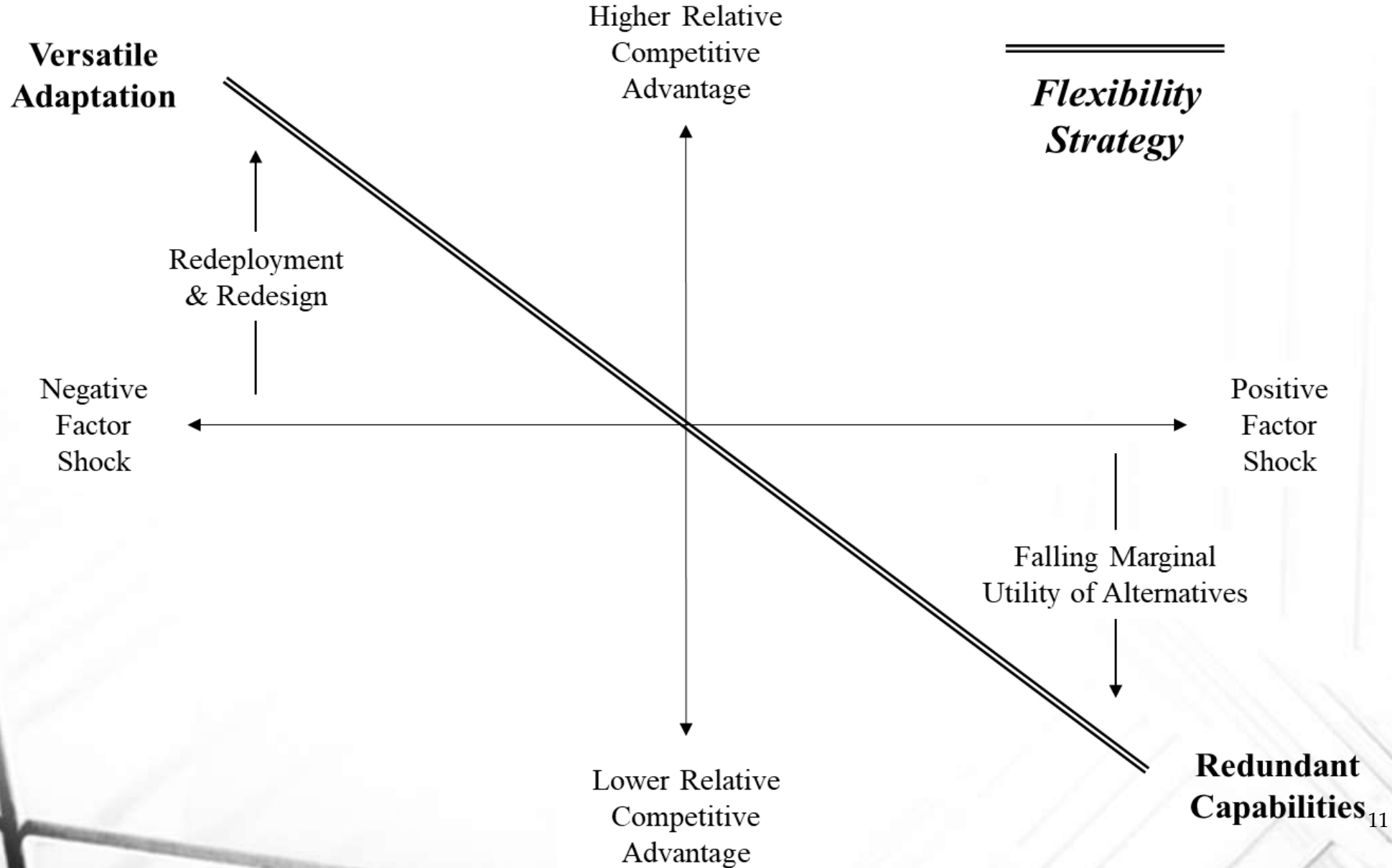
RQ: is it possible for firms to be equally well equipped to handle positive as well as negative shocks (i.e. uncertainty)?

Embedded Environmental Uncertainty			Structural Discretion	
			High	Low
			Internal Resources	External Resources
Technical Discretion	Low	Specific factor complementarity	<p><u>Specialization</u> Assets: Expertise, specialized equipment and tools, absorptive capacity, routines</p>	<p><u>Connectivity</u> Assets: Rich, dense, and diverse tight-knit networks to resource providers</p>
	High	Generic factor complementarity	<p><u>Flexibility</u> Assets: Creativity, TQM, judgement, entrepreneurial mindset, slack, marketing</p>	<p><u>Amplification</u> Assets: Brand, goodwill, legitimacy, reputation</p>

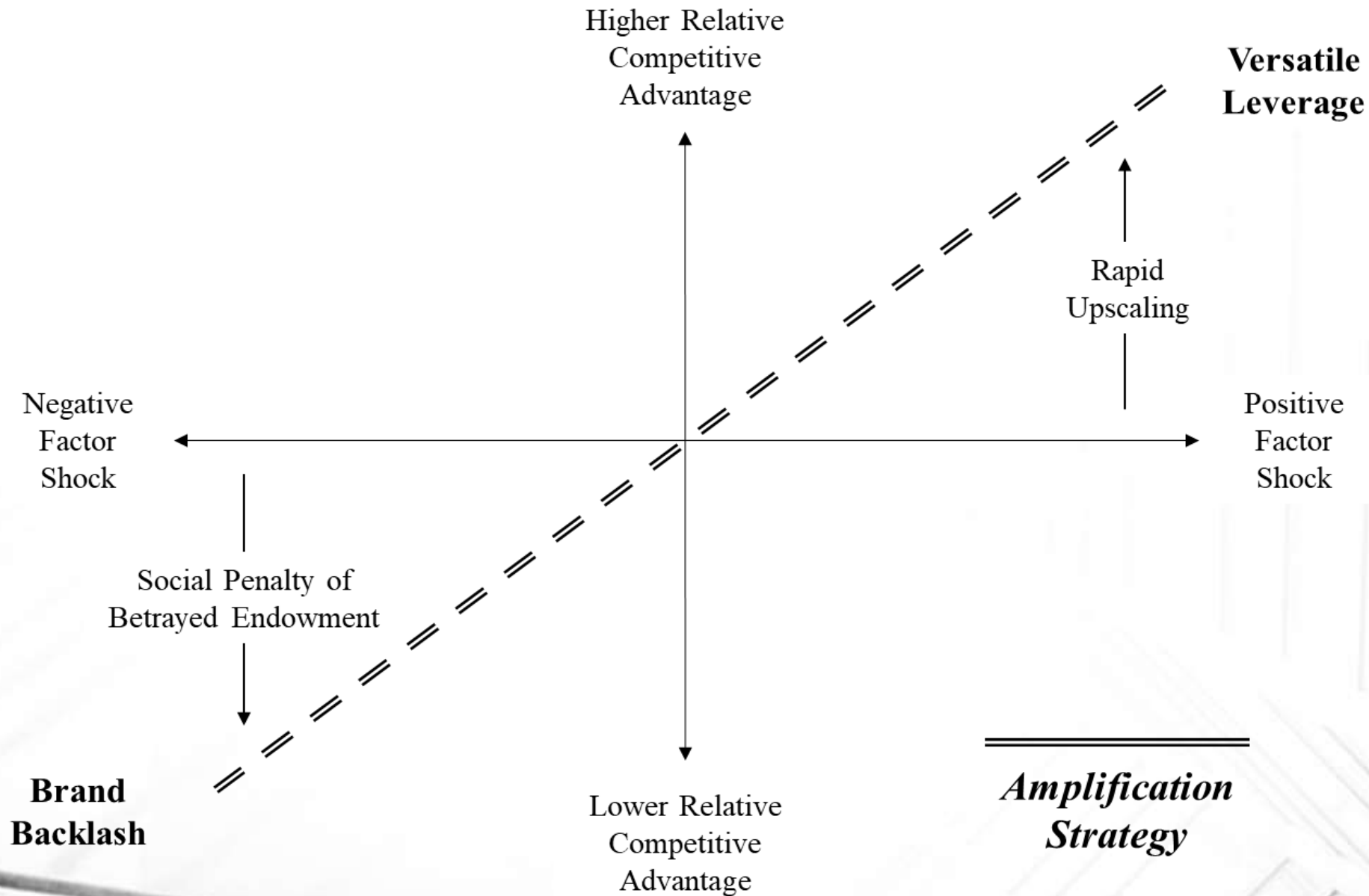
Specialization strategy



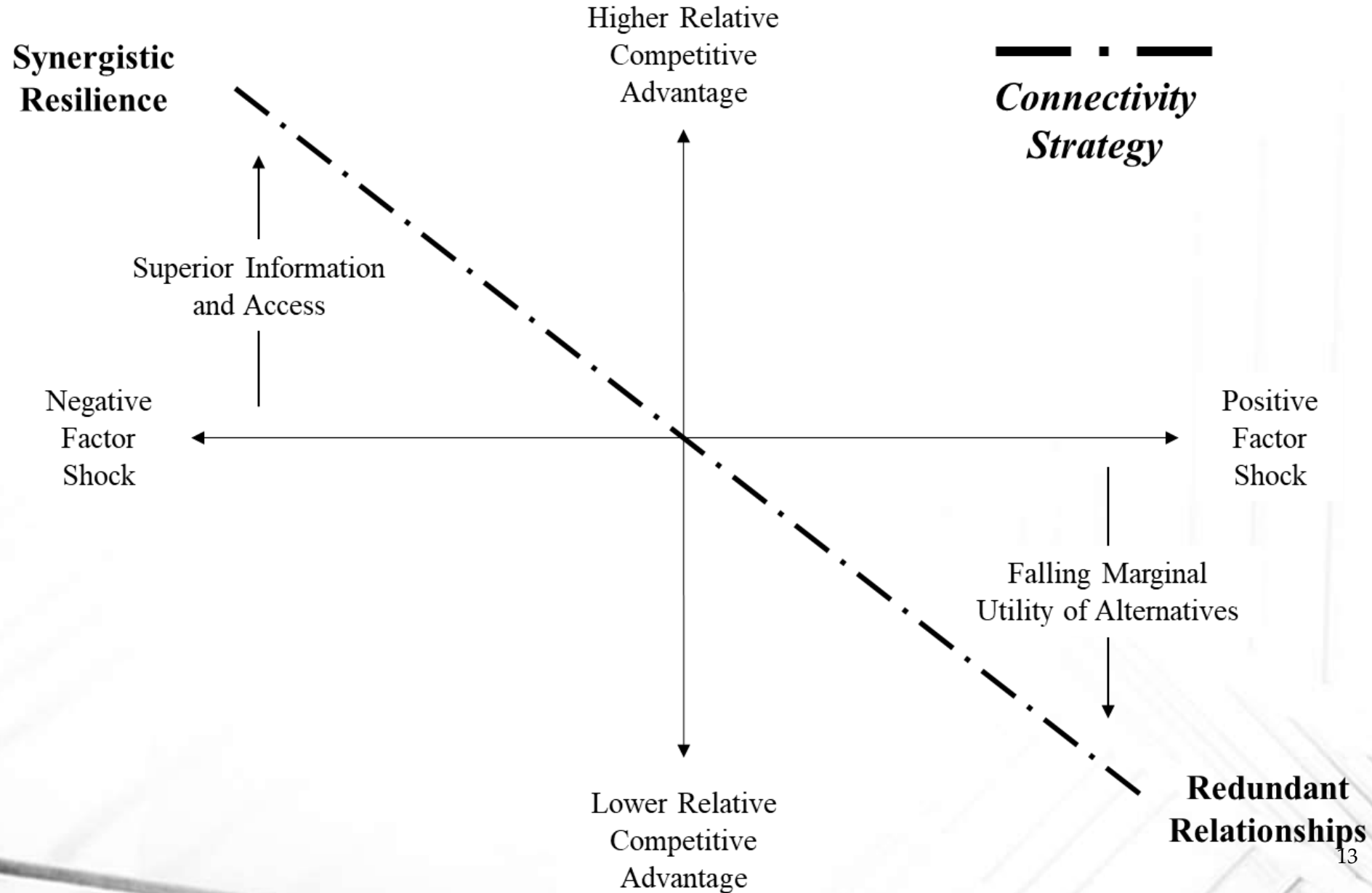
Flexibility strategy



Amplification strategy



Connectivity strategy



A country perspective

Embedded Environmental Uncertainty			Structural Discretion	
			High	Low
			Internal Resources	External Resources
Technical Discretion	Low	Specific factor complementarity	<p><u>Specialization</u></p> <p>Tourism-dependent countries and Covid-19 (e.g. Thailand) oil-importing countries under oil price slump (e.g. Japan)</p>	<p><u>Connectivity</u></p> <p>Relaxation of rare earth export quota by China (e.g. USA, Japan, South Korea)</p>
	High	Generic factor complementarity	<p><u>Flexibility</u></p> <p>Innovative economies (and those with slack resources) under Covid-19</p>	<p><u>Amplification</u></p> <p>Constraints on Free speech (e.g. Hong Kong)</p>



Thank you

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