Incumbent’s Dilemma

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Problem

Observation:
The innovation and organizations literature has focused considerably on the question of, “why large firms fail.”

In real world, there are three distinct outcomes possible:
entrants win (i.e., incumbents fail to defend their market);
entrants lose (i.e., incumbents retain or reclaim the market),
both entrants and incumbents share the market.

Question:
How to understand which of the three outcomes is most likely?
(Since the answer to this question is what ought to dictate the appropriate competitive strategies.)
<table>
<thead>
<tr>
<th>Intended Outcome</th>
<th>Disruption</th>
<th>Co-existence</th>
<th>No Disruption</th>
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<tbody>
<tr>
<td>Firm Factors</td>
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<tr>
<td>Product/Service</td>
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<td>Environment Factors</td>
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Figure 1: The decision to buy process in the context of new entrants and incumbent firms.

**NEW ENTRANT**

- **PRODUCT/SERVICE**
  - Network Externalities
  - Price
  - Quality
  - **Innovation**

- **FIRM**
  - Focus (Resources)
  - Structure (Modularity)
  - Market Share

**ENVIRONMENT**

- **CUSTOMER**
  - Network Sensitivity
  - Price Sensitivity
  - Quality Sensitivity
  - Innovation Sensitivity

- **INCUMBENT**
  - **PRODUCT/SERVICE**
  - Network Externalities
  - Price
  - Quality
  - **Innovation**

- **FIRM**
  - Structure (Modularity)
  - Focus (Resources)
  - Market Share
No Disruption
(positive feedbacks to incumbent market share from scale)

Firm-level Factors:
Incumbents have far superior cost structure

Superior Cost Structure

Economies of Scale

Attractiveness from Price

Attractiveness from Quality

Investment in Product/Service Quality

Investment in Integrating Complementary Functions and Assets

Ability to deliver quality

Environmental Factors:
Consumers value quality and compatibility over innovation and low price

Product/Service-Level Factors:
Strong network effects

Example:
MS Windows for Desktop
Disruption
(new entrant’s market share grows from lower cost innovation)

Firm-level Factors:
Entrants have far superior cost structure

Example:
Disk-drives

Environmental Factors:
Consumers highly price sensitive and willing to adopt innovation with low quality and compatibility

Product/Service-Level Factors:
Weak network effects

Market Share (Adopters)

Attractiveness from Quality

Investment in Product/Service Quality

Attractiveness from Innovation

Investment in Innovative Product/Service

Attractiveness from Installed Base

Economies of Scale

Superior Cost Structure due to the Nature of Innovation

Superior Cost Structure

WOM & Advertising

Investment in Integrating Complementary Functions and Assets

Ability to innovate

Disinvestment in Complementary Functions and Assets

Ability to deliver quality

Investment in Innovative Product/Service

Weak network effects

Attractiveness from Price
Coexistence
(incumbent successfully responds with rapid innovation)

Environmental Factors:
Consumers value availability over quality/innovation, or are willing to tradeoff quality and innovation

Product/Service-Level Factors:
No Network Effect
Incumbents can affect switching behavior heavily

Firm-Level Factors:
*Incumbents* innovate, restructure while maintaining quality

Example:
Broadcast TV

- Market Share (Adopters)
- Attractiveness from Quality
- Investment in Product/Service Quality
- Investment in Integrating Complementary Functions and Assets
- Disinvestment in Complementary Functions and Assets
- Attractiveness from Innovation
- Ability to deliver quality
- Ability to innovate

Environmental Factors:
Consumers value availability over quality/innovation, or are willing to tradeoff quality and innovation

Product/Service-Level Factors:
No Network Effect
Incumbents can affect switching behavior heavily

Firm-Level Factors:
*Incumbents* innovate, restructure while maintaining quality

Example:
Broadcast TV
Coexistence (Contd.)

(entrant successfully innovates, but struggles to gain quality)

**Firm-Level Factors:**
*Entrants* struggle to offer quality due to lack of complementary assets or market power

Example: Electric Vehicles?
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<td>• (Alternatively) consumers value innovation, but incumbent’s product has strong network effect</td>
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Case Research

• Purpose
  – To validate theoretical insights
  – To understand the predictive power of the model
  – To understand the limitations of the model

• Case Selection
  – Looking back (empirical, where outcomes can be analyzed)
  – Looking forward (predictive, where conditions can be analyzed)

• Data (dimensions discussed later)
  – Quantitative
  – Qualitative
# Framework definitions

## ENVIROMENTAL FACTORS

<table>
<thead>
<tr>
<th>CURRENT POSITIONS</th>
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<tbody>
<tr>
<td>Price Sensitivity (SoA to Price)</td>
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<tr>
<td>Quality Sensitivity (SoA to Quality)</td>
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<tr>
<td>Innovation Sensitivity (SoA to Innovation)</td>
<td></td>
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<tr>
<td>SoA to Installed Base</td>
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<tr>
<td>Contact Rate</td>
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<td>Word of Mouth</td>
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## Business Cases

<table>
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<td>Product/Service Factors</td>
<td>Skype VoIP</td>
<td>OLED Displays</td>
<td></td>
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<tr>
<td>Environment Factors</td>
<td>Linux - Windows Server Operating System</td>
<td>Linux - Windows Desktop Operating System</td>
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Potential candidates: Netflix, ??
THANK YOU!