THE STUDY OF ISOLATING MECHANISMS AS FIRM'S SUSTAINABLE COMPETITIVE ADVANTAGES

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ABSTRACT
Isolating mechanisms can create barriers to impede competitors from imitating resources, capabilities and strategies. The purpose of this study is to define key characteristics that will contribute to effective isolating mechanisms and find out a typology of effective isolating mechanisms. This study identified two types of isolating mechanisms, competitive and customers-based isolating mechanisms. And examples of normative strategies are provided for each type of isolating mechanisms to facilitate their application.

Key words: Competitive advantage, Competitive isolating mechanisms, Customer-based isolating mechanisms

INTRODUCTION
The concept of isolating mechanisms has been developed in the literature to explain barriers that firms can establish to avoid imitation by competitors (Grant, 2005; Mahoney and Pandian, 1992). Isolating mechanisms can create barriers to impede competitors from imitating resources, capabilities and strategies. Isolating mechanisms are also instrumental in influencing industry dynamics, as they provide competitive barriers to imitation for new strategies, adopted in response to environment changes (Segars and Grovers, 1995). Through the establishment of isolating mechanisms, the firms can sustain their competitive advantage and performance. Therefore, they are a key for superior performing firms.

Mahoney and Pandian (1992) had identified a wide range of isolating mechanisms from the resource-based view, mainstream strategy, organizational economics and the industrial organization literature. Although the authors recognize that there are many organizational phenomena with the potential for being isolating mechanism, they did not point out the effectiveness of those mechanisms. It is also surprised to find out that since Mahoney and Pandian’s (1992) classification of isolating mechanisms, little research has been done on this issue.

As little study has been done on how to design a set of isolating mechanism that is effective
in creating barriers to competition, this was the aim of the current study. Therefore, the purpose of this study is to define key characteristics that will contribute to effective isolating mechanisms and find out a typology of isolating mechanisms. In the next section the characteristic of isolating mechanisms are addressed, then two types of isolating mechanisms that can create effective barriers to imitation are classified and several propositions are proposed. In the final section, a discussion and future research direction are proposed.

CHARACTERISTIC OF ISOLATING MECHANISM

It may be easy for competitors to replicate resources, capabilities and strategies, such as manufacturing plant, funding allocations, information data bases, product designs and distribution channels. However, isolating mechanisms are created through the idiosyncratic way in which a firm manages its resources, capabilities and strategies, by achieving asymmetries in its managerial skills, and by learning how to develop and accumulate these skills (Oktemgil et al., 2000). Some isolating mechanisms are a mixture of resources characteristic, such as transparency, immobility, uncertain inimitability, low tradability, and durability whereas others involve managerial practice. In the literature several characteristics of the management of resources, capabilities and strategies have been described, that will contribute to creating isolating mechanisms.

(1) Inimitability: Inimitability means firms protect their resources, capabilities and strategies, so that competitors cannot easily replicate them. For example, companies such as Southwest Airline use extensive selection processes to hire individuals with spirit and passion to serve and entertain customers. These characteristics are rewarded and encourage by the company and not easy for competitors to duplicate. However, inimitability does not last forever. Therefore, if firms want to create effective isolating mechanisms, they have to take into consideration to other characteristics of isolating mechanisms. (2) History: History can play at least two role in increasing the cost of imitating a successful firm’s resources and capabilities. First, a firm’s ability to develop or acquire resources in a low-cost way may depend on a firm being in the “right place at the right time” in history (Mata et al., 1995). It is very expensive and somewhat difficult for the competitors to recreate the conditions of the opportunity. History can also play a role in increasing the cost of imitating a firm’s resources and capabilities because some of these firms’ attributes can only developed over long periods of time. That means history cannot be copied quickly. It is difficult and costly for the competitors to duplicate in a short period of time. (3) Social complexity: Social complexity refers to a firm’s culture, its reputation among customers and suppliers, and its trustworthiness with collaborating firms. These socially complex attributes evolve and
change over time. The delays associated with changing these complex social relationships suggest that firms with competitive advantages based on these types of resources and capabilities may be immune from imitation in the short time (Mata et al., 1995). (4) **Causal ambiguity**: In order to imitate a high performing company, a competitor must identify the capabilities and strategies that led to this performance and the resources on which this performance was based (Grant, 2005). Given the multiplicity of causes of performance, causal ambiguity should provide a source of isolating mechanisms for creating barriers to imitation. Reed and DeFillippi (1990) proposed three types of management skills that achieve causal ambiguity- tacitness, complexity and specificity. (5) **Low transferability and tradability**: If resources and capabilities have high transaction costs associated with their acquisition (such as search, purchase and implementation cost), then they are not easy to transfer (Peteraf, 1993). Team-based skills such as decision making style and organizational routine may be difficult for managers to relocate in a new firm. Such skills are inherent in the corporate culture and may not be simply traded in open markets.

The features of successful isolating mechanisms mentioned above can help firms creating effective barriers to imitation. Therefore, firms should consider how to design and develop a set of isolating mechanisms with these characteristics. Next section two types of effective isolating mechanisms are classified, one is competitive isolating mechanisms, and another is customer-based isolating mechanisms.

**TWO TYPES OF EFFECTIVE ISOLATING MECHANISMS**

To withstand or delay competitive imitation, the use of isolating mechanisms limits the capacity of rival firms to imitate and increase the cost associated with competitive imitation. A distinction is made between competitive and customers-based isolating mechanisms, because they represent different strategic orientations. Also, examples of strategies are provided for each type of isolating mechanisms to facilitate their application.

**Competitive isolating mechanism**

Competitive isolating mechanisms are related to reducing the competitor’s ability to imitate by enhancing the difficulty and complexity of imitation. The emphasis here is on “beating” the behavior of imitation by implementing strategies that exploit the superior capabilities or resources of the superior performing firm, and the deficiencies of competing firms. Managers employing these isolating mechanisms must have an in-depth understanding of industry competitive conditions.
Innovation-based capability: Business organizations spend a significant amount of their turnover on innovation i.e. making changes to their established products, processes and services. The relationship between the development and commercialization of innovations and superior performance is well accepted. Although imitation may erode a technology leaders’ profit advantage in a focal innovation, if individual innovations are treated as one element of an ongoing sequence of innovation, the leader can respond to such profit losses with further innovation, thereby restoring heterogeneity (Roberts, 2001; Knott, 2003). Therefore the profit differences due to innovation activity may persist. Because innovation is an important contributor to heterogeneity in performance among firms, and generally exhibits levels of path dependence (history) and social complexity, innovation-based capability is an effective isolation mechanism for firms.

Proposition 1: Innovation-based capability is an effective isolating mechanism for superior performing firms.

Speed of response: Speed of response is a capability for initiating strategies in response to competitive or environment change. Firms that speedily respond to market change can gain first-mover advantages, resulting in early market domination, superior market intelligence, valuable resources and cost advantages that will contribute to competitive advantage (Liberman and Montgomery, 1988). The competitive advantages gain through speed of response, arising from the tacitness of the acquired managerial skills and experience, and from the specificity of focusing on particular features of market change. Because the managerial skills and processes needed to achieve rapid responses are developed by individual managers, and will be inherent within team skills and corporate culture. They are likely to feature casual ambiguity and low transferable. The response lags between the superior performing firm and the competitors will create heterogeneity in profit. Therefore speed of response is an effective isolation mechanism for firms.

Proposition 2: Speed of response is an effective isolating mechanism for superior performing firms.

Marketing capability: A growing number of researchers suggest that marketing capability contributes to commercial success of the products and services marketed by the firm (Day, 1994; O’Driscoll et al., 2000). Marketing capability is defined as integrative processes designed to apply the collective knowledge, skills, and resources of the firm to market-related needs of business, enabling the business to add value to its goods and services and meet competitive demands (Day, 1994). Marketing ability of a firm is reflected in its ability to differentiate products and services from competitors and build successful brand. Firms with strong brand names can charge premium prices to enhance their profitability and maintain
superior performance. The marketing capability is achieved by the integration of marketing related resources, through the use of organizational routines (Grant, 2005). These resources are based on monitoring marketing change, and using marketing techniques to modify products or to launch new products or services as a consequence of this change. Therefore marketing capability features specificity as causal ambiguity and inimitability, and it is an effective isolation mechanism for firms.

*Proposition 3: Marketing capability is an effective isolating mechanism for superior performing firms.*

**Customer-based mechanisms**

Customer-based isolating mechanisms are economic and psychological barriers related to consumers’ brand selection decisions. The strategic emphasis here is on maintaining a superior position by taking advantage of barriers that restrict brand switching. Managers who exploit this class of isolating mechanisms must have an in-depth understanding of industry customers.

**Buyer cost related mechanisms:** This type of isolating mechanisms includes buyer switching cost and buyer evaluation cost. Buyer switching cost is the cost of switching to another provider and occurs when purchasers face barriers to changing from one brand to another. For example, the buyer of a personal computer system may face switching cost on the requirement of compatible equipment and software, and substantial investments in learning that is required using the system effectively. Buyer evaluation cost is a monetary or psychological cost for customers associated with evaluating the products they want to buy. This factor is particularly important in service industry (Fisher, 1991). By enhancing buyer switching cost and lowering buyer evaluation cost compared to competitors, firms can increase their chance of retaining existing customers and gain new customers. Customers may be reluctant to change to another brand, because they are usually averse to investing money, time and energy required to consider alternatives.

*Proposition 4: Buyer cost related mechanism is an effective isolating mechanism for superior performing firms.*

**Customer relationship related mechanisms:** Maintaining good relationship with customers is very important. Successful repeat interaction between customers and the firm provides a basis for trust (Li et al., 2006), and trust can enhance customer’s loyalty. Therefore, superior performing firms can sustain their competitive advantages through the maintenance of close relationship with their customers. The strategies firms can take include the development of market orientation as a corporate culture to enhance customer value (Narver and Slater, 1990),
and implementing customer relationship management strategy to identify customer segments, needs, and the most profitable customers (Winter, 2001).

Proposition 5: Customer relationship related mechanism is an effective isolating mechanism for superior performing firms.

How to protect firm’s competitive advantages is an important issue for firm and isolating mechanisms are instrumental in protecting firm’s competitive advantages. The excess returns earned by superior performing firm are a function of both the value of a superior competitive position to consumers, and the extent to which this position can be defended against competitors. Strategies that only focus on consumer value are not advantageous, if competitors are able to imitate quickly. Similarly, a very durable position is not beneficial if it is of limited value to consumers. Therefore, the combination of competitive and customer-based isolating mechanism can create more effective barriers to impede the imitation by the competitors. That means the greater number of strategies implemented simultaneously, the more durable the position.

CONCLUSION

To achieve a superior competitive position in the long run, firms must design and develop effective isolating mechanisms that are valuable to consumers and resist competitive attack. The contribution of this study is to provide a comprehensive isolating mechanisms framework for firms to resist competitive imitation through two types of effective mechanisms. One is concerned with enhancing the difficulty of imitation- we define it as competitive isolating mechanisms; the other is concerned with maintaining a superior position by taking advantage of barriers that restrict brand switching, we define it as customer-based isolating mechanisms. Except the development of effective isolating mechanisms, firms must understand how long the effectiveness of these isolating mechanisms exists and what is the most effective isolating mechanisms in different industry. Because the resources or capabilities that are valuable and competitive in certain markets or industry may not be equally valuable and competitive in others (Sun and Tse, 2009). Therefore, future research is needed to understand the impact of isolating mechanism in different market context, and the durability of each isolating mechanism.

[References available upon request from Yi-Pei, Li]