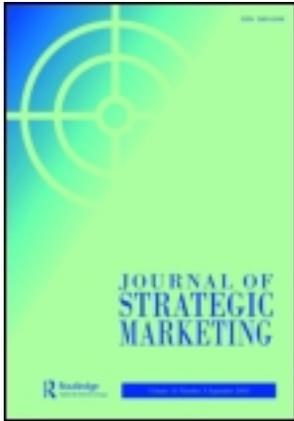


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Not complacent but scared: another look at the causes of strategic inertia among successful firms from a regulatory focus perspective

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While complacency is the most commonly offered explanation for the lack of strategic change among successful firms, research in management psychology suggests otherwise. Based on regulatory focus theory, we propose that competitive success prompts an increased sense of responsibility in managers, causing them to assume a defensive attitude and to concentrate on preserving the status quo instead of becoming complacent. Data collected from the Markstrat simulation support our predictions. The findings imply that efforts to encourage strategic change by pressurizing managers will backfire, because they will aggravate managers' defensive attitude. Instead, firms should loosen the pressure on managers and allow them to experiment with innovative strategies.

Keywords: marketing strategy; strategic inertia; regulatory focus; decision making; Markstrat

'We know as a leader now, we have a target on our back.'

(Mark Fields, Executive Vice President, Ford Motor Company and President, The Americas)

Changes in the marketplace require prompt and swift actions from managers responsible for formulating a firm's marketing strategy. Failure to react to the fast-changing environment has brought about the decline of numerous strong brands (Golder, 2000). Examples of such strategic inertia include slow innovation (Chandy & Tellis, 2000) and reluctance to enter emerging markets or to abandon declining ones (Christensen & Bower, 1996). However, history has not shown that firms are learning well how to correct their strategic inertia. This is because the precise causes of strategic inertia are still unclear, leading to ambiguous prescriptions of corrective actions. Therefore, an important first step for further research on strategic inertia is to better understand the motivational factors behind the reluctance to change strategies, so as to better inform practice about remedying such inertia.

Currently, the majority of studies in the area of strategic inertia focus on firms' prior performance as a major predictor of strategic change. Specifically, research has shown that firms that have achieved their aspired performance levels are less likely to implement new strategies (Greve, 1998; Lant & Montgomery, 1987; Marinova, 2004). The most common

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explanation for the lack of strategic change is managerial complacency (e.g. Ferdows & de Meyer, 1988; Lehu, 2004; Marinova, 2004; Slotegraaf, Moorman, & Inman, 2003; Yoshimori, 2005). However, this explanation is mostly offered in a *post hoc* manner and empirical findings do not fully reveal the psychological motivation of decision-makers that lead to strategic inertia. As a theoretical argument, it is also not compelling that managers at successful firms, who are under constant pressure to deliver superior results, would develop a false sense of security and become complacent in their actions. In fact, research in psychology and decision making suggests the opposite. From the perspective of regulatory focus theory (Higgins, 1997), the increased sense of responsibility for a successful brand may prompt a heightened sense of vigilance and avoidance behavior in managers, causing them to assume a defensive attitude associated with prevention regulatory focus. A prevention regulatory focus results in decision-makers' emphasis on preserving status-quo as opposed to seeking opportunities for advancement (Higgins et al., 2001), which in turn leads to the lack of strategic experimentation and innovation (Crowe & Higgins, 1997; Higgins, 1997). Thus, to put it wittily, the reason successful firms cease to adapt is not that their managers are complacent, but rather that they are 'scared'.

Accordingly, the purpose of this study is to test our 'not complacent but scared' proposition. We investigate how a firm's competitive position (market leader vs challenger) affects the psychological state of its decision-makers, and how the psychological state affects the extent of strategic change undertaken by the firm. We find that market leadership does not lead to complacency, thereby refuting the commonly assumed complacency hypothesis. Instead, our results show that market leaders tend to adopt a defensive (as opposed to an offensive) focus, and in turn are less likely to significantly change their strategy. Our results hold important implications for the design of remedial actions for overcoming strategic inertia. Instead of adding pressure on managers in the mistaken belief that they have become complacent, and in the process heightening their defensiveness (and thus aggravating strategic inertia), companies should design ways to reduce managerial risk-averseness and encourage experimentation of new and innovative strategies.

The paper is organized as follows: first, we review the existing literature on strategic change drivers. We then evaluate and test the plausibility of the complacency hypothesis. Next, we offer an alternative theoretical framework and develop alternative test hypotheses. We then report results of an empirical study that used longitudinal data collected from the Markstrat simulation.

Drivers of strategic change: a review of explanations

The literature contains several prominent views regarding the nature and drivers of strategic change in companies. The most widespread view focuses on the firm's past performance as a predictor of its future strategic change. Miller (1994) and Miller and Chen (1994) demonstrate that after periods of success, firms tend to become inert. Additionally, Miller (1994) shows that successful firms demonstrate inattention to changes in the environment and are slow to adapt. In explaining the roots of inertia, several studies adopt the attainment discrepancy perspective, arguing that the lack of achievement (calculated as the difference between actual and aspired performance) is a major driver of strategic change (Greve, 1998; Lant & Montgomery, 1987). For example, Lant and Montgomery (1987) examine drivers of risk taking behaviors and innovativeness of search among managers, and report that aspiration attainment reduces managers' risk taking and innovativeness of search.

Similar to the attainment discrepancy paradigm, Lant, Milliken, and Batra (1992) use the managerial learning framework to test the effects of past performance on the patterns of strategic reorientation of a firm. Among other findings, they report that poor past performance increases the likelihood of strategic reorientation. Very similar results were obtained by Boeker (1997), with poor performance increasing the likelihood of strategic change. Drawing upon research in organizational behavior, Marinova (2004) also investigates effects of satisfaction with performance on innovation effort of participating teams. She found a negative effect and suggests that satisfaction with performance is a 'complacency-producing' factor which impedes innovation (Marinova, 2004, p. 13).

Another line of research focuses on how managers' motivation to respond mediates the effect of past performance on a firm's responsiveness to competitive actions. Most notably, Jayachandran and Varadarajan (2006) demonstrate that stronger past performance reduces managers' motivation to respond, which leads to lower responsiveness to competitive actions. In light of this finding, Jayachandran and Varadarajan (2006) offer complacency as an explanation of the low motivation to respond.

Complacency and market leadership

The complacency explanation for the lack of strategic change has been suggested in numerous studies (e.g. Ferdows & de Meyer, 1988; Lehu, 2004; Marinova, 2004; Slotegraaf et al., 2003; Yoshimori, 2005). This warrants a closer look at the plausibility of the suggested relationship between market leadership and managerial complacency. On the surface, this appears to be an intuitive explanation given the aforementioned findings about the effect of past success on attentiveness to the environment (Miller, 1994) and on motivation to respond (Jayachandran & Varadarajan, 2006). Yet this explanation suffers from a number of problems. First, the explanation is mostly offered on a *post hoc* basis, without a consistent definition, operationalization, or measurement instrument. For example, in Audia, Locke, and Smith (2000, p. 849), complacency is defined as 'drifting with no attempt at improvement', creating a circular relationship between the construct and its effect. Second, if we accept the definition of complacency from the Oxford American Dictionary – 'a feeling of smug or uncritical satisfaction with oneself or one's achievements' – then complacency does not seem to be a plausible affective response of managers at successful firms.

We do not intend to argue that managers cannot become complacent. Testimonials like the one by Motorola's Gregory Q. Brown – 'sometimes, a hit product can mask the brutal reality that more work needs to be done' (*Business Week*, 14 May 2009) – suggest that managerial complacency is real and sometimes occurs within successful firms. But to say that success *can* breed complacency does not mean that complacency *will* definitely follow success. Furthermore, even if complacency is present, it is not necessarily the cause of strategic inertia. The words in the epigraph to this paper are from Mark Fields' interview with the *National Post* (5 November 2010) during which he discussed the fact that in 2010 Ford was expected to become a market leader in North America. 'We take all of our competitors seriously ... So, we're just going to stay focused and not get full of ourselves. We know as a leader now, we have a target on our back' – these words show little signs of complacency.

We observed the behaviors of participants in the Markstrat simulation which we have been administering for years. In this simulation teams of participants run their firms competing in two fictitious consumer product markets. Periodic reports submitted by participants show little evidence of complacency: while happy and jubilant for being ahead of the competition, leading team participants show little sign of diminishing rigor in

their analysis or disregard for their competitors (see Appendix 1 for representative statements from the leading teams' reports).

Subjecting the complacency explanation to a test

To address our doubts about the complacency explanation, we now subject the explanation to hypothesis tests. The Encarta Dictionary defines 'complacent' as 'self-satisfied and unaware of possible dangers', suggesting that one of the most dangerous manifestations of managerial complacency is the inability to see threats to one's competitive position. If the complacency explanation is correct, then competitive leadership should be negatively related to the level of perceived threat. Specifically, market leaders will see their position as less endangered. Conversely, laggards will feel more threatened.

H1: The closer the firm is to a leading position, the less threatened its managers will feel themselves to be.

We also wanted to look into the effect of duration of success on the perception of threat. It can be reasonably expected that long periods of successful performance will reinforce decision-makers' self confidence and create a feeling of 'invincibility' (Miller, 1994). This feeling is less likely to occur in shorter periods of success.

H2: The longer the period of success of a leading company, the less threatened its managers will feel themselves to be.

The lack of statistical support for these hypotheses will suggest that firm success does not necessarily cause complacency, and hence complacency is not likely to be a determinant of strategic inertia among successful firms.

In search for an alternative explanation

If strategic inertia is not caused by complacency, then what is a more plausible explanation for strategic inertia? As strategic change is associated with uncertainty, several studies investigated managers' inclination to take risks as a function of past success. For example, using accounting measures of risk and return, Feigenbaum and Thomas (1988) find that poorly performing firms demonstrate risk-seeking behaviors while better performing firms tend to avoid risks. On the other hand, Miller (1994) shows that managers of leading firms are more willing to take risks, albeit predominantly within the boundaries of their current practices. This suggests a need to take a closer look at the attitude toward risk as a driver of strategic change.

Associated with attitude toward risk as an affective response to market leadership is the fear of losing the leadership status. Pfeffer and Salancik (1978) argue that managers are not free in their strategic choices; the limited nature of firm's resources and the need to keep major stakeholders satisfied create a pressure on managers and dictate their strategic choices. This pressure is especially strong in successful firms with powerful stakeholders. In such conditions, managers are more likely to feel an increased responsibility rather than 'smug and uncritical satisfaction' (Higgins, 1997). Building on the theory of external control of the firm, Christensen and Bower (1996) investigate the pattern of resource allocation in the computer hard drive industry and conclude that leading firms often failed to pursue emerging technologies and emerging markets not because of complacency, but because their managers' attention and resources were dedicated to their most successful markets. This suggests that there is some kind of a defensive mindset governing the strategic behavior of successful firms.

In seeking to illuminate the psychological process that drives the lack of strategic change, we turn to regulatory focus theory (Higgins, 1997) which provides a useful framework which addresses factors related to risk attitudes and defensive mindsets.

Regulatory focus and strategy change

Regulatory focus theory has received increasing attention in the marketing literature, both in consumer behavior (e.g. Aaker & Lee, 2006; Avnet & Higgins, 2006; Herzstein, Posavac, & Brakus, 2007; Sengupta & Zhou, 2007; Zhao & Pechmann, 2007) and in managerial decision making (e.g. Atwater & Brett, 2006; Brockner, Higgins, & Low, 2004; Bryant & Dunford, 2008). Regulatory focus theory shows a great potential for explaining managers' choices in ambiguous situations. The fact that person's regulatory focus is subject to environmental changes makes it especially relevant for business environments in which strategic decisions are made by teams of managers.

The main premise of regulatory focus theory is that human actions and choice of strategies depend on one's regulatory focus – a preferred way of achieving goals (Higgins, 1997). The theory posits that individual's regulatory focus is determined by the framing of the situation, the dominating needs of a person, and the way a person identifies himself or herself. Studies in psychology (Crowe & Higgins, 1997; Higgins et al., 2001) and marketing (Grant & Xie, 2007) show that when a situation is presented in a way that focuses on possibility of gains, one's dominant needs are related to growth and advancement, and decision-makers identify themselves by their hopes and aspirations, they develop a promotion regulatory focus characterized by the state of eagerness, approach behaviors, and emotions of cheerfulness in case of success and dejection in case of failure. In promotion regulatory focus, decision-makers are more likely to try more alternatives when fulfilling tasks, experiment more with different strategies, and give up less easily. Conversely, when the situation is framed around the possibility of losses, dominating needs are security-related, and decision-makers identify themselves by their responsibilities, they are said to be in a prevention regulatory focus. In such a state, avoidance becomes a preferred strategic means and a decision-maker's focus is on preserving the status quo. An important feature of the theory is that a person's regulatory focus is not stable and can change with the situation. This allows predictions not only for individuals, but also for groups of decision-makers working in similar contexts.¹

Managers' regulatory focus in decision making is manifested in their strategic focus: managers may emphasize either defensive or offensive strategies as a result of different framing of the task environment. Defensive strategies are aimed at preventing competitors' attack and decreasing the damage if such an attack occurs, while offensive strategies are aimed at improvement of competitive position of a firm (Yannopoulos, 2007; pp. 313, 321). In other words, defensive strategies are aimed at avoiding losses (a prevention regulatory focus), while the goals of offensive strategies are to ensure gains (a promotion regulatory focus). As numerous experimental studies in psychology show, whether decision-makers adopt a prevention regulatory focus or a promotion regulatory focus will affect their readiness and willingness to change a strategy (Higgins, Shah, & Friedman, 1997; Lee, Aaker, & Gardner, 2000; Liberman, Idson, Camacho, & Higgins, 1999).

Competitive position and defensive focus

We propose that managers of strong firms are driven in their actions by feelings of responsibility that induce prevention regulatory focus resulting in preference toward

supporting the status quo. Specifically, we expect that a firm's competitive position will affect managers' preference toward defensive strategies (termed 'defensive focus' hereinafter). Market leadership is a precarious position. Less successful firms may focus on serving niche markets with a hope to avoid competitors' attention or can decide to catch up with and beat the leader, whereas the leader is fully exposed to all competitors and has much more ambiguous (and therefore risky) future goals. For managers of leading firms driven by the sense of responsibility (Christensen & Bower, 1996; Pfeffer & Salancik, 1978), the situation thus becomes framed in terms of avoiding losses, rather than approaching gains. Their dominant need becomes the one of security, and their choices will be driven more by the need to defend the firm's current position, rather than the desire for achieving new results. All these conditions are conducive for increasing managers' prevention regulatory focus (Higgins, 1997).

In contrast, challengers have a clearer goal of defeating the market leader. The prior success of the market leader has already demonstrated the workability of certain offensive strategies. Given the knowledge of industry best practices that have produced success in the past, challengers are expected to lean toward an offensive stance in the market. Therefore:

H3: The closer the firm is to a leading position, the stronger will be the defensive focus of its decision-makers.

Defensive focus and strategic change

We also expect a relationship between the firm decision-makers' defensive focus and the intended extent of strategic change. When the focus of a firm's strategy is on defense (a prevention regulatory focus), the firm's decision-makers tend to limit their actions to a small set of 'safe' strategies that carry low likelihood of making a mistake (Crowe & Higgins, 1997; Higgins et al., 2001). Liberman et al. (1999) show that subjects in prevention focus are less likely to switch to new activities or pursue new possessions. Prevention-oriented people avoid trying new approaches and new strategies, and in general prefer inaction to action (Higgins, 1997). Thus, in general, managers in a defensive focus can be expected to refrain from changing strategy unless it is absolutely necessary. Hence:

H4: Decision-makers' defensive focus is negatively related to the intended extent of strategic change.

Performance changes and defensive focus

Performance improvement or decline can be seen as a feedback informing decision-makers about the appropriateness of their strategies. Research in psychology is inconsistent when it comes to the effect of the valence of the feedback on motivation and performance. Van-Dijk and Kluger (2004) use regulatory focus theory to explain this inconsistency suggesting the 'fit' between regulatory focus and the valence of a feedback. They show that positive feedback has a stronger impact on people with promotion regulatory focus, while negative feedback affects mostly subjects with a prevention regulatory focus. Based on these findings, we can expect that performance change will interact with the firm's competitive rank in affecting decision-makers' defensive focus. Performance improvement (positive feedback) will have a stronger motivational effect on managers of lagging firms who, based on Hypothesis 3, are expected to have promotion regulatory focus, and less effect on managers of leading firms, as it does not 'fit' their regulatory focus. Performance improvement will further encourage managers of lagging

firms to pursue new strategies, strengthening the relationship between competitive position and managers' defensive focus. On the other hand, performance decline (negative feedback) will have less effect on managers of lagging firms but will fit the prevention regulatory focus of managers of leading firms, further increasing their defensive orientation. This should also strengthen the relationship between competitive ranking and defensive focus, but we also expect negative feedback to signal to prevention focused managers that preserving the status quo may be a bad strategic choice and thus elicit offensive rather than defensive focus. Thus, performance decline will change the relationship between competitive position and defensive focus to a lesser degree than performance improvement. Overall, we predict that:

- H5: The relationship between a firm's competitive position and its decision-makers' defensive focus will be weaker when the firm experiences a performance decline and stronger when its performance improves.

Method

To test the hypotheses, we collected data via the Markstrat simulation (Larréché, Gatignon, & Triolet, 2003). The value of using data from business simulations for research has been advocated as early as 1966 (Babb, Leslie, & van Slyke, 1966). Since then, business simulation data have been used in numerous studies involving Markstrat. Markstrat is a leading simulation in the field of marketing (see Clark & Montgomery, 1998, 1999; Glazer, Steckel, & Winer, 1989, 1992; Lant & Montgomery, 1987; Marinova, 2004; van Bruggen, Smidts, & Wierenga, 1998). In Markstrat, competing teams of participants manage the production, marketing, distribution, and sales of two types of products – Sonites and Vodites. Competitive performance is measured by the stock price index (SPI) – a composite measure that reflects the firm's market share, growth potential, efficiency of marketing operations, and overall profitability. Competing teams are grouped in industries of four to six teams. Industries are completely independent and the simulation develops in different ways in each industry. The simulation usually spans six to 10 decision rounds with market situations constantly changing as a result of competitive actions and environmental evolution.

We collected our data at a major Canadian university where undergraduate students participated in Markstrat as a part of their capstone marketing class. Five percent of the students' final grade rested on their competitive performance measured by the stock price index of their firms (SPI). This provided significant incentive for them to carefully consider their periodic decisions. The data included performance data imported from Markstrat software and perceptual data collected from team's reports that accompanied each rounds' decisions. We analyzed the data from nine industries that all had the same initial competitive scenario – all teams started the simulation in exactly the same position. We discarded the data collected during the first two rounds of the simulation as students were still familiarizing themselves with the software during that period and the data may not be reliable. Overall, our dataset includes information about 267 decisions made by 38 teams competing in nine industries, for both the Sonites market (196 decisions) and the Vodites market (71 decisions) over five to six rounds.

Measures

Two measures were used to assess firm performance. First, we compiled data for each firm's rank in terms of stock price index (SPI) – with lower rankings representing better performance (1 for market leader, 4 or 5 for a laggard). We decided against using the

Table 1. Descriptive statistics and correlations for variables in the study.

	1	2	3	4	5
1. Position in term of SPI	1.00				
2. Change in SPI	-.49**	1.00			
3. Strategy change	.23**	-.16*	1.00		
4. Strategic focus (1 = defense)	.10	-.03	.25**	1.00	
5. Perceived threat (1 = no threat)	.22**	-.12	.29**	-.01	1.00
Mean	2.50	.11	4.10	4.45	4.77
Standard deviation	1.30	.26	1.61	1.87	1.69

Notes: * $p < .05$ (two-tailed); ** $p < .01$ (two-tailed).

absolute SPI as this value varied dramatically across different industries and rounds making them incompatible for analysis. We also calculated percentage changes in the SPI from the previous period.

To quantify the extent of decision-makers' defensive focus, the level of perceived threat and intended extent of strategy change, we asked respondents to provide ratings for these variables on seven-point scales (see Appendix 2). We operationalized managers' defensive focus as the extent to which defense was emphasized in their strategy. All self-reported measures represented agreed overall perceptions of each team. Beyond observing the participants' actual performance from the software outputs, these self-report measures allowed us to tap the participants' strategic posture and how they *think* about their strategic actions.

Descriptive statistics and correlations between collected measures are presented in Table 1.

Results

Hypothesis 1, which suggested that success breeds complacency, was tested using multiple regression. We included SPI rank as a predictor together with a set of control variables to partial out the effects of SPI change, market type, simulation round, and peculiarities of different industries. Our data do not support Hypothesis 1. The regression coefficient for SPI rank is not significant, while several control variables – change in SPI, type of market, round, and two industry dummies – show better potential in explaining perceived threat (see Table 2). This result suggests that leading position in the market does not necessarily reduce managers' perceptions of threat, hence having no effect on complacency.

The results of multiple regression used to test Hypotheses 2, which suggested a negative relationship between the length of time in a leadership position and perception of threat, did not provide support to the hypothesis (see Table 3). For each round when a company was a leader in terms of SPI, we calculated the number of consecutive rounds it was a leader before and used this number as a predictor. We used the change in SPI, the round, market dummy, and industry dummies as covariates, of which only the round and two industry dummies were significant. These findings again contradict the idea that success breeds complacency.

Hypotheses 3 and 5 were tested together using multiple linear regression. To reduce multicollinearity issues, interaction terms were constructed using standardized scores of their constituent terms. Multicollinearity diagnostics showed that the largest variance inflation factor (VIF) was 2.48, and the mean VIF was 1.71 which was well below the threshold of 10 suggested by Neter, Kutner, Nachtsheim, and Wasserman (1996). We

Table 2. The effect of hypothesized variables on perceived danger (1 – no danger, 7 – grave danger).

	Expected sign	Betas Both markets	Betas Sonites market	Betas Vodites market
Firm's SPI rank	+	.08	.13	-.12
<i>Covariates</i>				
Percentage change in SPI from the previous round		-.14*	-.14	-.21
Dummy for Vodites vs Sonites market		.14*		
Game round		-.18**	-.15*	-.21
Number of significant industry dummies (out of 8)		5	1	1
		$N = 267$	$N = 195$	$N = 71$
		$R^2 = .12$	$R^2 = .11$	$R^2 = .22$
		$F = 3.90,$	$F = 3.26,$	$F = 2.76,$
		$p < .01$	$p < .01$	$p < .01$

Notes: Industry dummy variables not reported, five out of eight are significant at .05 level.

* $p < .05$; ** $p < .01$.

included several dummy variables for markets, rounds, and industries to account for possible effects of these variables.

Hypothesis 3 was supported. Firms with lower SPI rank (game leaders) in period t-1 reported their strategies in period t to be more defensive than firms with higher SPI rank (see Table 4). As an aside, observing the significance of the control variables, we noticed that there was a significant difference between the Sonites and Vodites markets, with strategies in the Vodites market being less defensive. This can be explained by the fact that the Sonites market is the one with which teams start the simulation, and if they decide to enter the Vodites market later in the game they do that by building on their success in the Sonites. Being in a large and fast growing market with limited competition allows the teams to behave generally more aggressively. Also, as the game progressed, strategies tended to become more defensive. Additionally, five out of eight industry dummies were significant indicating that defensive focus differed significantly among industries.

To further clarify the differences in tested relationships between the Sonites and Vodites markets we ran the regressions separately for each market. The relationship between competitive position and defensive focus holds in the Sonites market. For the Vodites market ($N = 71$), the results of the regression were not significant. This could be because only a relatively small proportion of teams entered this market during the

Table 3. The effect of the length of the leadership period on the perception of threat.

	Expected sign	Betas
Number of rounds as a leader	+	-.05
<i>Covariates</i>		
Dummy for Vodites vs Sonites market		.26*
Percentage change in SPI from previous round		-.07
Game round		-.11
Number of significant industry dummies		2
$N = 267, R^2 = .39, F = 5.12, p < .01$		

Notes: * $p < .05$; ** $p < .01$.

Table 4. The effect of hypothesized variables on strategic focus (1 – defense, 7 – offense).

	Expected sign	Betas Both markets	Betas Sonites market	Betas Vodites market
Firm's SPI rank	+	.21**	.19*	.22
Percentage change in SPI from the previous round		.13	.22*	-.18
SPI rank by change in SPI	+	.23**	.22**	.03
<i>Covariates</i>				
Dummy for Vodites vs Sonites market		.17**		
Game round		-.15*	-.22**	.07
Number of significant industry dummies (out of 8)		5	4	1
		$N = 267$	$N = 196$	$N = 71$
		$R^2 = .13$	$R^2 = .15$	$R^2 = .26$
		$F = 4.00,$	$F = 3.85,$	$F = 3.02,$
		$p < .01$	$p < .01$	$p < .01$

Notes: * $p < .05$; ** $p < .01$.

simulation and those who entered competed there for only a few rounds before the simulation ended. With the bulk of products and competitors being in the Sonites market, the Vodites market can be perceived more as a playground rather than the focal business of a company and that would change the decision-making paradigm.

Hypothesis 5 was also supported. When performance was improving, the relationship between a firm's competitive position and its defensive focus was stronger than when performance was declining (see Table 4). This result also suggests that variations of strategic focus in response to performance change are larger for lagging teams, while market leaders tend not to change their defensive focus.

To test Hypothesis 4 (that firms with defensive focus will be less likely to change their strategy), we relied on multiple linear regression. To isolate the effect of the strategic focus, we included a number of control variables into the equation. We were specifically interested to partial out peculiarities of various industries, different rounds and markets, so we included several dummy variables for markets, rounds, and industries.

Hypothesis 4 was supported as the regression coefficient for defensive focus had the expected sign, showing that the more defensive the managers are, the smaller the intended

Table 5. The effects of hypothesized variables on strategy change.

	Expected sign	Standardized coefficients
Strategic focus (1 = defense, 7 = offense)	+	.235** (.053)
<i>Covariates</i>		
Dummy for Vodites vs Sonites market		-.026 (.231)
Game round		-.075 (.063)
$R^2 = .102, F = 3.75, p < .01$		

Notes: Standard errors are in parentheses. Industry dummy variables are not reported, one out of eight is significant at the .05 level.

* $p < .1$; ** $p < .01$.

change is in its strategy (see Table 5). The regression results also suggest that this relationship is the same both for Sonites and Vodies markets and across different game rounds, but differed slightly in two out of nine industries.

Discussion

Conclusions and implications

For a long time, complacency has been offered as a universal motivational explanation for managerial reluctance to engage in strategic change. Without adequate empirical support, this approach has limited the understanding of possible alternative psychological mechanisms involved in managerial strategic decision making, and has led to potentially misleading recommendations for practitioners.

Our study complements the existing literature on managerial motivation and indicates that a more careful and systematic investigation of the motivational causes of strategic inertia is warranted. By showing that managers' perceptions of threat are not different for market leaders compared with challengers, this study demonstrates that managerial complacency may not be the most plausible cause of the lack of strategic change by leading firms. Supporting the conclusions of Christensen and Bower (1996), the current findings suggest that, driven by an elevated sense of responsibility, managers of the leading firms are inclined toward adopting defensive postures, which, as opposed to engendering a feeling of invincibility, serves to inhibit strategic change. It appears that market leaders are not only motivated by the need to serve their markets, but also are subjected to certain psychological forces that predispose their decisions toward inaction.

These findings suggest that discussions of the antecedents of strategic change in the marketing literature should incorporate regulatory focus into the set of factors affecting managers' decisions. Clarification of the role of managers' motivational states will allow the creation of more accurate models for predicting changes in firm behaviors in the marketplace. This opens up a host of opportunities to study possible relationships between various aspects of managerial motivational states and the firm's innovativeness and strategic flexibility. The vast knowledge accumulated in the study of regulatory focus can also guide the study of environmental and personal antecedents of managers' motivational states allowing researchers to relate the firm's organizational characteristics and market context to their managers' decision making.

From the practical standpoint, a better understanding of drivers of strategic change will allow companies to adjust internal policies to make their managers more amenable to strategic change. Reliance on the notion of 'managerial complacency' as a predictor of strategic inertia would misdirect companies to exert pressure on their managers to stimulate strategic change. For example, Jayachandran and Varadarajan (2006, p. 292) argue that, to avoid low motivation to respond to market change, organizations should 'develop a culture of "paranoia"'. But if in fact the lack of strategic change is driven by overly defensive attitudes of managers, this remedy will heighten nervousness and fear of blame which will bring about greater resistance to innovation. A better solution might be to 'loosen' the pressure on managers and encourage them to experiment with new/innovative strategies.

Limitations and future directions

There are several limitations to this study. First, the study was conducted using undergraduate marketing majors as subjects. Babb et al. (1966) observe that behaviors of

experienced managers differ considerably from undergraduate students. In their study, managers appeared more conservative and less erratic in their decisions than students. This indicates a limited generalizability of our study. But on the other hand, this probably resulted in an underestimation of the strategic inertia effect. Since younger decision-makers are less careful and tend to adopt a defensive focus less frequently than actual managers, relationships uncovered in this study should be stronger when older and more experienced managers are involved.

Another concern is with the measurement of perceived threat, intended strategy change, and the dominant strategic focus. The use of single-item scales could reduce the internal validity of these measures (Churchill, 1979). On the other hand, a growing body of literature suggests that multiple-item scales are not always preferable to single-item scales (Rossiter, 2002). For example, Drolet and Morrison (2001) empirically demonstrate how attempts to measure concrete, unambiguous attributes with multiple items aggravate respondents' behaviors and result in less, rather than more, reliable results. Bergkvist and Rossiter (2007, 2009) demonstrate that when single-item measures are used to assess concrete attributes of concrete singular objects, the predictive validity of such measures is similar to that of multiple-item measures. In our study we were measuring respondents' overall evaluations of threat, defensive focus, and strategy change, which are supposed to be unambiguous enough to be measured by a single-item scale (Rossiter, 2002). Still, future research should develop and incorporate better measures of these constructs. Research could also relate actual, observable changes in firms' strategies to attitudinal measures reported by managers.

Our study opens several interesting avenues for further investigation of the process of strategic change. First, researchers could utilize more diverse samples. Markstrat is being increasingly used in teaching undergraduate and graduate students and in executive training. Comparing behaviors of these three groups will allow researchers to generalize findings from student samples to real world behaviors. Studies can also incorporate cross-cultural comparisons. For example, it has been suggested that cultural background affects the dispositional regulatory focus of decision-makers (Lee et al., 2000). Observing the behaviors of decision-makers from different cultural origins operating in the similar Markstrat setting will allow researchers to clarify differences in regulatory focus across cultures and establish its implications for strategy change.

This study relies on psychological explanations of managers' actions. Managers' motivational states are affected not only by the firm's competitive position but also by a multitude of other factors. Researching the impact of internal characteristics of firms, such as the dominant culture, strategic orientation, or strategic priorities, can further advance our understanding of strategic change and managerial decision making.

Note

1. It is important to clarify the difference between the prospect theory (Kahneman & Tversky, 1979) and regulatory focus theory. While the former posits that decision-makers' weight risks more than potential benefits, the latter suggests that in different regulatory foci the perception of what is risky changes. For promotion-oriented managers, risk of an error of omission will be higher than the risk of the error of commission (i.e. they will feel that staying passive is riskier than taking actions) while for prevention-oriented managers the risk of an error of commission will dominate (i.e. it is riskier to act than remain passive). Therefore, the risk-averse *promotion-oriented* manager will be approach motivated and will eagerly try new things. The risk-averse *prevention-oriented* manager will prefer to stay passive (Bryant & Dunford, 2008). Thus, while the prospect theory still applies to the problem of strategic change, regulatory focus allows more precise delineation of perceived risks.

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Appendix 1. Excerpts from Markstrat participants' reports

We are delighted to announce that our company has emerged as the market leader despite the aggressive actions taken by competitors in the last period ... Our Sonite products continue to target the three largest segments, namely the Others, Singles and Pros. In order to protect our market leader position, we would continue our differentiation and sales force allocation strategies which had proven to be successful in the previous period ... In the Vodites market, our firm's position has strengthened as a result of VUEE's desirable product features. However, as competition is expected to intensify in the Vodites market, we intend to protect our market share in the coming period.

Participant (Northeast Industry Firm U) in Period 8

It is heartening to see that we have maintained our market leadership with net contribution increasing from \$115M to \$153M ... This period we aim to reap the rewards from R&D efforts by launching SIMI and VIVA, each targeting the Buffs and Innovators segments respectively ... Boosting Vodites advertising expenditures from \$3,750,000 to \$5,050,000 is a modest increase considering how we are launching VIVA in light of strong competition from the entry of four products, a forecast we arrived at judging from comparative R&D expenditures. We are holding back because we believe we have gained a strong foothold over two periods, and want to avoid mindlessly channeling money into the products before observing market trends and other firm's strategies.

Participant (Northeast Industry Firm I) in Period 6

We have maintained market leadership in the Sonite market, capturing 40% of total volume sold, and achieved the second highest stock price index of 1958 and a very high current return on investment of 3.02, the second highest in the industry ... After doing our market research and assessment that the Vodite market is an extremely viable and profitable market to enter, we will be introducing a new Vodite brand in the next period, and expect an increase in net contribution by at least 20% of \$68,181,000.

Participant (Northwest Industry Firm I) in Period 6

We emerged first for this round, with a net contribution of K\$104,252. Together with this astounding performance, our ROI has increased to 2.78, and our stock price index has improved dramatically to 2546. Our position as market leader of Sonites industry, coupled with the successful launch of VEFF in the Vodites industry has brought about our success. To continue our pursuit of success, we intend to consolidate our position as the market leader of the Sonites industry by being ahead of our competitors in this coming round. To combat the intense competition in the Sonites market, we have decided to match our competitors dollar for dollar. The rapid growth in the Followers' segment in the Vodites Market makes it a lucrative market to enter; hence we are focusing more on VEFF to garner a greater market share in the Followers' segment ... Overall, our strategy now is to consolidate our market position by increasing our distribution coverage. We believe that we would be able to leverage on this increase in our distribution coverage, staying ahead of competition, by ensuring that more retailers would carry our products. This would prevent us from incurring any potential lost sales due to a flaw in our distribution coverage.

Participant (Southeast Industry Firm E) in Period 8

Once again, our firm has come out tops in our industry for the last two periods. This was due to a confluence of two factors, namely our continuing success in the Sonite industry, and the savage competition in the Vodites industry, which has eroded the profitability of involved firms ... In the coming periods, we aim to continue our dominance of the Sonites market, as well as begin to explore entry into the slowly stabilizing Vodites market. Following aggressive responses from our competitors in Period 7, we expect an intensely competitive Sonites market in the next period. Given our highest advertising expenditure and strong brand positioning in terms of product attributes and consumers' brand loyalty, we are confident of counteracting competitors' actions. In the growing Singles and Others segments, an aggressive stance will be taken to leverage on the growing segment size and our brand superiority. Whilst in the stagnating Professionals and Hi-Earners segments, a defensive

stance is taken to maintain our market share and brand positioning. With perceptions already close to our consumers' preferences, advertising is used to adjust consumers' perceived prices of our brands to match evolution trends. To maintain continued competitiveness under growing competitive pressure, we have embarked on feasibility studies for all of our brands, scheduled for launch in Period 10. Facing a sudden 21.49% surge of competitive sales force sizes to 407 competitive sales personnel, we are wary of our competitors' next moves. As such, we increased our sales force by an average of 14.1% across all four brands to a total of 170 sales personnel to remain competitiveness.

Participant (Southwest Industry Firm U) in Period 8

Appendix 2. Questionnaire

Please answer the following questions in the context of your current decision period for the Sonites market and separately for the Vodites market (if applicable).

1. How big of a change in your strategy do your current decisions represent compared to your strategy in a previous period (1 – no change at all, 7 – total change of strategy)?

Sonites market	1	2	3	4	5	6	7
Vodites market	1	2	3	4	5	6	7

2. Please rate the extent to which you feel your current market position is in danger (1 – 'safe, no danger at all', 7 – 'we are in immediate and very grave danger'):

Sonites market	1	2	3	4	5	6	7
Vodites market	1	2	3	4	5	6	7

3. Please indicate what is the main emphasis of your strategy in this period: (defense vs offense):

Sonites market	Defense	1	2	3	4	5	6	7	Offense
Vodites market	Defense	1	2	3	4	5	6	7	Offense