

CHAPTER 2 : LITERATURE REVIEW

Strategic management theory, population ecology and institutional theory and strategic balance theory that emphasized the important of differentiation, legitimacy and moderate strategic similarity respectively have projected different approaches to pursue better organization performance. Literature review is carried out in the order for each theory.

2.1 Strategic Management Theory : An Organization should be Different

The strategic management study predicts that the intensity of competition among organizations is directly related to the distribution and availability of the resources. With finite resources, the competition will be intensified especially for the scare resources. Higher rivalry usually leads to lower performance, because organizations must expand resources to compete more intensely. The increase in cost for getting the scare resources will eventually lead to rational differentiation to reduces competition of similar resources to the extent of their realized strategic position ((Baum and Mezias, 1992; Baum and Singh, 1994). Porter (1991: 102) postulated that 'the organization must stake out a distinct position in an unexploited or underexploited niche from its rivals. Imitation almost ensures a lack of competitive advantage and hence mediocre performance.'

Differentiation is a continuous process in the competitive market. Profits from a distinct position will persist depending on the ability of competitors to imitate the position. Successful organizations will try to maintain their distinct position either through the building of barriers of entrance (Lieberman, 1990) or exploring new niches to reestablish their distinct position in order to continuously stay ahead of competitors (D'Aveni, 1994). A key resource of successful organization is finding unexploited niches and then erecting defensible barriers or locating profitable new strategic opportunities for its core competencies (Prahalad and Hamel, 1990).

Empirical research has been supportive of the direct relationship of differentiation and performance. Gimeno and Woo (1996) found that similarity in airline strategies was related to higher rivalry, measured as declines in revenue per passenger mile.

Baum and Mezias's (1992) study of the impact of localized competition on rates of failures in the Manhattan hotel industry from 1898 to 1990 showed that patterns of competitive interaction between single and multipoint competitors differ depending on whether they are members of the same or different groups. The results indicated that competition for the finite resources eventually leads to differentiation, the increase competition among less differentiated organizations increase the failure rate.

The results of Baum and Singh's (1994) study of niche overlap density with the number of organizations competing for the same resources; reflected the important of differentiation strategy to improve organization's performance.

2.2 Population Ecology and Institutional Theory : An Organization should be the Same

The conformity proposition derived primarily from resource dependence and new institutional theories, lead to a perspective on strategic similarity that an organization should be the same as others in order to achieve superior performance.

Formal organizations are generally understood to be systems of coordinated and controlled activities that arise when work is embedded in complex networks of technical relationships and boundary-spanning exchanges. But in the modern societies formal organizational structures arise in highly institutionalized contexts. Many of the positions, policies, programs and procedures of modern organizations are enforced by public opinion, by the view of important constituents, by knowledge legitimated through the educational system, by social prestige, by the laws and by the definitions of negligence and prudence used by the courts. Such elements of formal structure are manifestations of powerful institutional rules which function as highly rationalized myths that are binding on particular organizations (Meyer and Rowan, 1997).

Deephouse (1999) illustrated that members of the organizational field do not perceive or are indifferent to certain amounts of differentiation, organizations can be different to some degree from their competitors and maintain their legitimacy. This recognizes the empirical fact that organizations aren't exactly alike. The range of strategic similarity in which organizations maintain their legitimacy is called range of acceptability.

The literature review in Deephouse's (1999) study of the integrative theory of strategic balance reported that :-

"Legitimacy challenges diminish the ability of an organization to acquire resources from potential exchange partners in the organizational field,

such as customers, suppliers, and regulators (DiMaggio and Powell, 1983). A legitimate organization obtains resources of higher quality and at more favorable terms than does an organization whose legitimacy is challenged. There are at least three related reasons for this. First, a potential exchange partner that does not comprehend an organization's strategies or accept them as rational will not provide any resources to the organization, restricting resource supply. Second, an exchange partner may accept less favorable contract terms from a legitimate organization. This occurs because the legitimacy of the exchange partner is enhanced by contracting with a legitimate organization (Galaskiewicz, 1985; Pfeffer and Salancik, 1978: 145; Wood, 1991). In contrast, an exchange partner may require greater inducements to contract with an organization whose legitimacy is challenged. Third, less legitimate organizations are more likely to fail (Baum and Oliver, 1991; DiMaggio and Powell, 1983; Singh et al., 1986). This induces exchange partners to demand higher risk premiums in contracts (Cornell and Shapiro, 1987; Miller and Bromiley, 1990). Moreover, organizations with a greater risk of failure have difficulty maintaining quality managers and outside directors, reducing the effectiveness of organization decision-making and subsequent performance (Hambrick and D'Aveni, 1992). In sum, dissimilar organizations face legitimacy challenges that hinder resource acquisition and reduce performance."

Empirical research has been supportive of the conformity proposition. Baum and Oliver's (1991) study of impact of institutional linkages on the failure of child care services organizations in Metropolitan Toronto, Canada, between 1971 and 1987, showed that organizations with institutional linkages exhibited a significant survival advantage that increased with the intensity of competition. Institutional linkages also had a significant moderating influence on the relationship between organizational transformation and the risk of failure. Establishing collaborative linkages to

legitimated community and public institutions may be an important means by which organizations achieve reliability and accountability and increase their survival prospects.

Galaskiewicz and Burt (1991) in a study of importance of institutionalizing processes with population of 67 publicly owned organizations, illustrated that professional networks that span organizations and diffuse information and attitudes create a pool of almost interchangeable individuals who occupy similar positions across a range of organizations and possess a similarity in tradition and control that might otherwise shape organizational behavior.

2.3 Strategic Balance Theory : An Organization should be Balanced between Differentiation and Conformity

Institutionalized organizations in the competitive market face the pressure to be different and to conform to institutional rules. The extent of the organization's strategic similarity will depends on the relative strength of the differentiation and conformity propositions.

Hybels (1995) suggested that organization's efficiency is enhanced in two contexts: -

1. The demands of local relational networks encourage the development of structures that coordinate and control activities. Such structures contribute to the efficiency of organizations and given them competitive advantages over less efficient competitors.
2. The interconnectedness of societal relations, the collective organization of society, and the leadership of organizational elites create a highly institutionalized context. In this context rationalized structures present an acceptable account of organizational activities, and organizations gain legitimacy, stability and resources.

Through isomorphism process, organizations are driven to incorporate the practices and procedures defined by prevailing rationalized concepts of organizational work and institutionalized in society. But conformity to institutionalized rules often conflicts sharply with efficiency criteria and, conversely, to coordinate and control activity in order to promote efficiency undermines an organization's ceremonial conformity and sacrifices its support and legitimacy.

Past researches have illustrated the following conflicts face an organization if its success depends primarily on isomorphism with institutionalized rules.

- Technical activities and demands for efficiency create conflicts and inconsistencies in an institutionalized organization's efforts to conform to the ceremonial rules of production.
- The institutional rules are transmitted by myths that may arise from different parts of the environment, the rules may conflict with one another.
- Organizations often face the dilemma that activities celebrating institutionalized rules although they count as virtuous ceremonial expenditures are pure costs from the point of view of efficiency.
- Institutional rules are couched at high level of generalization (Durkheim, 1933) whereas technical activities vary specific, unstandardized and possibly unique conditions.

Meyer and Rowan (1977) illustrated that an organization can resolve conflicts between ceremonial rules and efficiency by employing decoupling and the logic of confidence devices. This strongly supported the need to trade off between differentiation and conformity pressures.

Some recent researches organized the tension between the need for an organization to be different and the need for an organization to be the same.

Deepphouse (1999) study demonstrated the usefulness of the perspective by examining the strategies of competing commercial banks, the integrated hypothesis of a curvilinear relationship receives stronger empirical support than either the differentiation and conformity hypotheses. In the study, two thought experiments (Hempel, 1965; Weick, 1989) are used in the synthesis. The conclusion is that the organization will achieve maximum performance at the level of strategic similarity where the gains from reduced competition are equal to the costs of legitimacy challenges. At greater levels of dissimilarity the costs of legitimacy challenges

exceed the benefits of reduced competition, leading to lower net performance. The general implication is that the organization has highest performance at moderate levels of strategic similarity.

Carroll and Hannan (1989) in the study of density dependent processes of legitimation and competition, with nine newspaper populations spanning the 19th and 20th centuries and covering 5200 newspapers illustrated that the characteristic growth trajectory reflects the operation of opposing processes of legitimation and competition. The Carroll and Hannan's (1989) model built on the assumption that processes of legitimation and competition for limited resources shape rates of founding and failure. The results showed that the non-monotonic model improved significantly over monotonic (e.g., linear) models of density dependence for both founding rates and mortality rates, it strongly supports the theory of strategic balance.

Haveman's (1993) study of density dependent processes of legitimation and competition with data covered all 313 savings and loan associations operating between 1977 and 1987; indicated an inverted U-shaped relationship with rate of entry into that market. The result can be linked indirectly to the relations among strategic similarity, competition, legitimacy and performance; which is in line with the argument of theory of strategic balance.

Barnett and Carroll's (1987) analysis of rates of founding and mortality of independent local telephone companies in Iowa countries; Mitchell's (1987) study of rates of entry into the medical diagnostic imaging industry during 1959 to 1986; Tucker, Singh, Meinhard and House's (1988) analysis of foundings of voluntary social service organizations in Toronto from 1970 to 1982; yielded estimates of density dependence supporting the theory of strategic balance