



Journal of Marketing Research
Article Postprint
Volume XLV
© 2008, American Marketing Association
Cannot be reprinted without the express
permission of the American Marketing Association.

Ignore Successful Followers – Entry is Still Urgent

Steven M. Shugan

Professor and Berrie Foundation Eminent Scholar
Warrington College of Business Administration

201 Bryan Hall

Campus Box 117155

Gainesville FL 32611-7155

University of Florida

Steven.Shugan@CBA.UFL.EDU

Commentary on:

Does Quality Win? Network Effects Versus Quality in High-Tech Markets

Gerard J. Tellis, Eden Yin, Rakesh Niraj

ABSTRACT

Even if early market entrants have few enduring advantages over later entrants, striving for early entry might still be best. When determining our best action, we must understand that both early and late entrants fail to represent the likely outcomes of our own endeavors. First, late market entrants, for example, represent the few firms that have achieved a sufficiently high quality threshold to make a viable new product launch. There is no guarantee that we will achieve the same. Second, different firms might have different odds of success at different points in time, depending on their unique skills, resources and history. Third, late market entry might involve greater risks than early market entry because a higher threshold is required for the latter. Fourth, product failure rates might diminish over time only because prediction becomes easier and not because new product development becomes easier. Finally, early entrants do enjoy a brief monopoly with diminished competition. A lack of persistent first entrant advantages can and often does provide a greater incentive to be an early entrant.

Keywords: order-of-entry, pioneer advantage, first-mover advantage, new product development, innovation

WHAT SHOULD FIRMS DO?

Network effects seem undeniable (Lieberman and Montgomery 1998, Katz and Shapiro 1994). Certainly, enjoying a telephone is difficult when there is no one to call. The user network gives the telephone its utility. Moreover, network effects could insure future compatible spare-parts, ancillary products and upgrades.

Tellis, Yin, and Niraj (2008) survey the literature and find controversy. Their empirical analysis finds that network advantages for early market entrants are weaker than previously believed and that sufficient quality can overcome these advantages. This important finding complements previous findings (e.g., Golder and Tellis 1993) and provides many useful

implications. However, it is misleading and, possibly disastrous to conclude that that a speedy market entry is unimportant. Trying to be first is not only worthwhile, but is sometimes essential for some or most organizations.

Even if public policy makers and frustrated maladroit competitors seeking to capture the gains of so-called lucky early entrants, and incumbents trying to discourage competitive entry, all vastly exaggerate the incumbency advantage in free markets (which I do believe happens), striving for early entry is still important. The question facing a firm is not whether early entrants have a persistent advantage or whether early entrants earn a greater profit (which is unlikely) than later entrants do, the question facing the firm is whether to strive for an early launch. The firm's choice is not between early entry and a more profitable later entry. The choice is between allocating more or less resources to immediate new product development efforts. Front-loading resources might allow an early launch but not guarantee it. Delaying resource allocation might increase the likelihood of facing formidable later entrants.

WHY ENTERING EARLY IS CRITICAL DESPITE NO APPARENT ADVANTAGE

Few Olympic athletes run races with the explicit goal of finishing second and taking the Silver medal. Such complacency would likely result in no medal at all. The athlete who actually finishes second might have expended as much or more effort than the athlete who finished first. Finishing second is an outcome and not the decision itself. Similarly, entering the market earlier with a new product is not the decision itself but rather a possible outcome of decisions made much earlier.

In free markets, firms strive to enter markets with new products that at least some consumers prefer over extant alternatives. We can interpret those preferences as the consequence of quality, quality per dollar (Hauser and Shugan 1983; Shugan 1987), features, value, reliability, durability, versatility and so on. However, free markets evolve with advancing

technology (Shugan 2004), improving productivity, accelerating rates of innovation, increasing knowledge, new capabilities and ever better communications. Each successful new entrant exploits this evolution to achieve still higher levels of consumer satisfaction than the last entrant does. Consequently, almost by definition, the required threshold for success steadily increases. It becomes increasingly more difficult to surpass the last entrant as each entrant raises the threshold for success. The longer an organization waits to enter a market, the higher the threshold of customer satisfaction required for successful entry. Few users of today's telephones, for example, would be happy with the telephones of a decade ago. In fact, this is exactly the implication of the quality argument in Tellis, Yin, and Niraj (2008). Higher quality overcomes network advantages, but it also raises the thresholds for future entrants.

If the threshold for success is ever increasing, then delay can be deadly. The difference between the market share or profits of an early and a successful late entrant is an inadequate, misleading and inappropriate measure of the advantage of being earlier. The successful later entrant must have achieved a higher threshold of satisfaction to be successful. The appropriate comparison for an organization making a launching decision is whether to proceed at an economical pace or devote more resources toward expediting the development process. There is no guarantee that the leisurely economical pace will yield the often-observed successful late entries. A lack of urgency might result in falling far short of the required threshold for a viable entry. The observed successful late entrant might be the fruits of a highly resource-intensive development effort by organizations that might have failed at being first but still stressed urgency. There are many examples of deadly delays resulting in disaster despite many successful late entrants. For example, the San Jose 3dfx Company, once king of the video card market, declared bankruptcy after being several months late to market with their next generation cards. Subsequent leadership among the surviving firms, ATI and nVidia, alternated depending

on which firm was first to market with each successive generation. The 3dfx company quietly left the market with many new products still on the drawing boards. We fail to observe those never launched potential late entrants.

Hence, just because a successful second entrant has much greater sales, it is unwise to conclude that that we would be such a second entrant if we waited. There is no guarantee that a leisurely effort on our part would have spawned such a propitious outcome. Observed late entrants might not be typical. Remember, we fail to observe all of the would-be second entrants who are never able to develop viable new products that achieve the required threshold. We also fail to observe all the would-be second entrants who abandon all efforts and never try to develop a superior offering. Development in a rapidly evolving economy is a matter of urgency.

Finally, if the threshold for entry is unrelentingly increasing, then waiting longer raises the required threshold shortening the expected life cycle for any given level of quality. Of course, optimal entry depends on whether our development efforts are advancing at a much more rapid pace than the pace at which improved products are entering the market (Shugan 2004). Moreover, we must also consider the option of an immediate launch while leaving open the possibility of future product improvements (Chandy and Tellis 1998; 2000) against the option of having no presence in the market at all.

Hence, less enduring advantages for the incumbent for whatever reason (network effects, location effects, preference effects), imply shorter life cycles and an ever-increasing threshold that successful new products must achieve. The faster a firm can get their products to market, the lower the threshold they need to achieve and the longer their effective life cycles before the market catches up.

DIFFERENT FIRMS HAVE DIFFERENT BEST STRATEGIES

Marketing scholars are far too quick to dismiss marketing projects as merely simple financial investments. Financial investments might be interchangeable. For example, investors

might be indifferent between investing in projects with the same distribution of payoffs and expenditures. A security enjoys the same rate of return regardless of who buys it. New product projects lack this property. They are not fungible financial securities. The outcome of new product projects is often very dependent on who executes the project.

For example, a liquor company might expect greater payoffs than an entertainment firm might from launching the same new beverage. Firms have different resources, expertise, employees, knowledge and experience. Firms are not interchangeable. At minimum, firms start with different brand reputations (Aaker 1997) and different histories. These differences change the distribution of outcomes for the same projects. Even two motion picture production companies might have different degrees of success with exactly the same script because each has access to different directors, contractual agreements with other talent and distribution opportunities.

We certainly have empirical data consistent with this conclusion in the area of publication. Academic authors who are the first to study an important research problem face a different peer review process than scholars who publish in well-established areas. It is not necessarily easier to do either. Each requires different skills, resources, publication strategies and, possibly, reputations. In any case, the opportunity cost of publishing an article is not the average difference between these two outcomes (which might be zero). It is the difference for a particular individual between trying to publish the first article in a new area and trying to improve an existing area.

Similarly, some nimble organizations might be very good at developing new markets with pioneering technology. Other established organizations might have an advantage at understanding market segmentation and differentiating products based on design rather than cutting-edge technology. Still other streamlined organizations might have the advantage of

securing lower costs for a mass market. Each organization might have different innovative expertise in different areas giving them different outcomes for the same project. Some might be better pioneers and some might be better late entrants. Moreover, a great pioneer might be an incompetent late entrant.

LATE ENTRY MIGHT BE MORE RISK THAN EARLY ENTRY

Still another reason that many firms should continue to strive for early entry despite little apparent advantage is that for many firms, early entry is far less risky than a later entry. Remember that most empirical studies have inferred risk by examining failure rates. Certainly, failure rates do reflect risk when other factors are constant. Of course, other factors, in particular, the accuracy of market research, vary over time. Perhaps, market research is more difficult for early entrants because potential buyers are unable to envision very new concepts. Perhaps, forecasting production costs are more difficult for early entrants because there might be unforeseen production problems. Perhaps, predicting distribution, advertising effectiveness and buyer responsiveness to different prices are all more difficult. These difficulties might produce more incorrect early launch decisions resulting in failure. However, these difficulties can also make failure rates a poor measure of risk because these difficulties diminish over time.

Later entrants, who enjoy better predictions, might be less likely to make launching mistakes. Hence, later entrants might avoid observed market failures. That fact fails to imply that later entry is easier or less risky. Later entrants must still expend considerable resources to exceed the threshold established by the incumbents. Moreover, later entrants also face a moving target as the threshold continues to increase as still more firms enter the market. Hence, would-be later entrants might never enter the market. After expending considerable resources, these firms might never achieve a viable product.

Empirical observation might exclude many of these firms that eventually abandon their efforts to launch new products after never succeeding in being first. Academics, for example, in

the business of producing research, do abandon research topics after painfully observing the unintentionally preemptive research presentations and the recent publications of others.

Sometimes the peer review process at scholarly journals performs that dismal function. When being beat to market by a competitor, a firm can either abandon their efforts or attempt to further improve to meet the higher threshold created by the recent new entrant. Although prior efforts are sunk costs at this point, subsequent efforts to meet the higher threshold do incur additional costs that might diminish the eventual profitability of the entire effort. Even when the firm subsequently launches and achieves the same market share as the first entrant, the eventual costs might exceed the costs of the first entrant.

In sum, although Tellis, Yin, and Niraj (2008) compellingly demonstrate that the first mover remains vulnerable to a second entrant, this important finding does not necessarily imply that a strategy of being second is any less difficult than being first. It is unclear whether, in a free market, the risks of early entry exceed those of later entry. For some, at least, the risks of waiting might be larger. Going back to the Olympic athlete example, the athlete who achieves second place may have expended more or than same effort as the athlete who achieved first place. The correct comparison is between the option of spending more resources in an attempt to be first or the option of spending less resources with a lower probability of being first. Remember, a complacent organization can easily find itself in the position of having only obsolete products and insufficient new products in the pipeline to survive. The organization quietly disappears without influencing failure rates.

Finally, empirical observation appears to reveal more new product launches in the early stages of a market's development implying that fewer organizations tried to launch during the market's decline. Hence, failure rates are unable to capture completely the concept of risk.

CONCLUSION

We must use great care when inferring theories from observation (Shugan 2007). Early entry might still be the best goal for many organizations even if late entrants earn much greater profits (which is unlikely). There are several reasons for this conclusion.

- Firms that enter later might have invested as much or more than early entrants. Higher thresholds are required for a later entry.
- Because it is easier to make predictions in more mature markets, many firms might have abandoned their efforts to enter mature markets resulting in deceptively low failure rates for mature markets.
- Given many mature markets with unobserved failures (i.e., projects never consummated with observed entry), the rate-of-return for late entry might be less than for early entry despite many observed early failures or a lack of an enduring advantage for early entrants.
- We might not observe many organizations who failed to achieve the higher thresholds required for a later entry.
- Early entrants enjoy a monopoly period where they face less competition than late entrants do.
- Some firms are more capable of executing successful early entries while other firms are more capable at entering more mature markets.

REFERENCES

- Aaker, Jennifer L. (1997), "Dimensions of Brand Personality," *Journal of Marketing Research*, 34 (3), 347–56.
- Chandy, Rajesh K. and Gerard J. Tellis (1998), "Organizing for Radical Product Innovation: The Overlooked Role of Willingness to Cannibalize," *Journal of Marketing Research*, 35 (4), 474–87.

- and —— (2000), “The Incumbent’s Curse? Incumbency, Size, and Radical Product Innovation,” *Journal of Marketing*, 64 (3) 1–17.
- Hauser, John R. and Steven M. Shugan (1983), “Defensive Marketing Strategies,” *Marketing Science*, 2 (4), 319–60.
- Katz, Michael L. and Carl Shapiro (1994), “Systems Competition and Network Effects,” *The Journal of Economic Perspectives*, 8 (2) 93–115.
- Lieberman, Marvin B., Montgomery and David B. (1998), “First Mover (Dis)Advantages: Retrospective And Link With The Resource-Based View,” *Strategic Management Journal*, 19 (12), 1111–25.
- Shugan, Steven M. (1987), “Estimating Brand Positioning Maps Using Supermarket Scanning Data,” *Journal of Marketing Research*, 24(1), 1–18.
- (2004), “The Impact of Advancing Technology on Marketing and Academic Research,” *Marketing Science*, 23 (4), 469–75.
- (2007), “Causality, Unintended Consequences and Deducing Shared Causes,” *Marketing Science*, 26 (6), 731–41.
- Tellis, Gerard J. and Peter N. Golder (1993), “Does Pioneer Advantage: Marketing Logic or Marketing Legend?” *Journal of Marketing Research*, 30 (2), 158–70.
- Tellis, Gerard J., Eden Yin, and Rakesh Niraj (2008), “Does Quality Win? Network Effects vs. Quality in High-tech Markets,” *Journal of Marketing Research* (forthcoming).