NEW ENTRANTS VERSUS INCUMBENTS IN THE EMERGING ON-LINE FINANCIAL SERVICES COMPLEX

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Abstract	The emergence of electronic commerce complexes raises important questions regarding competence building and leveraging, both for practitioners and strategy scholars. Competences of brick-and-mortar incumbents (large and mature players) are being challenged by new entrants' click-and-mortar or click-and-click business models. The implications of this challenge for the financial services industry – as for many other industries – are only starting to become clear. In this paper we contribute to these initial understandings by developing a conceptual framework that considers which strategies incumbents and new entrants might adopt to improve their competitiveness. We identify four relevant organizational types in the emerging on-line financial services complex. For each of these types we outline how ties to sponsoring organizations can be used as a buffer against environmental turbulence and as a bridge towards changing stakeholder perspectives.	
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NEW ENTRANTS VERSUS INCUMBENTS IN THE EMERGING ON-LINE FINANCIAL SERVICES COMPLEX

A co-evolutionary perspective

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ABSTRACT

The emergence of electronic commerce complexes raises important questions regarding competence building and leveraging, both for practitioners and strategy scholars. Competences of brick-and-mortar incumbents (large and mature players) are being challenged by new entrants' click-and-mortar or click-and-click business models. The implications of this challenge for the financial services industry – as for many other industries – are only starting to become clear. In this paper we contribute to these initial understandings by developing a conceptual framework that considers which strategies incumbents and new entrants might adopt to improve their competitiveness. We identify four relevant organizational types in the emerging on-line financial services complex. For each of these types we outline how ties to sponsoring organizations can be used as a buffer against environmental turbulence and as a bridge towards changing stakeholder perspectives.

Keywords : *e- commerce, competence building and leveraging, co-evolution, legitimacy, on-line financial services complex*

Introduction

The convergence of e-commerce technologies based on Internet-standards is causing a fundamental shift in the way businesses operate by creating new markets, blurring industry boundaries, and redefining the meaning of products (Rayport & Sviokla, 1994, 1995; De Boer et al., 1999; Botten & McManus, 1999; Yoffie, 1997). Today's "brick-and-mortar" companies find themselves confronted with new business opportunities in a virtual *marketspace* of processual information interactions, as opposed to a *marketplace* of physical resources and institutionalized interactions (Castells, 1996; Rayport & Sviokla, 1994; 1995). New *e-commerce complexes* are emerging in which brick-and-mortar incumbents of a main originating industry compete with new entrants using new business models – be it "click-and-mortar" or "click-and-click" companies.

To be succesful in an emerging e-commerce complex, incumbents and new entrants have to clear some liabilities that hold them back (Stinchcombe, 1965). *Incumbents* suffer from the liability of oldness, as they tend to develop up to the limit of their adaptive competence. *New entrants* on the contrary suffer from the liability of newness, since at the point of founding an organization the risk of dying is highest. Which liability will lay the heaviest burden, causing either incumbents or new entrants to get the upper hand? How should either party build competences to outperform the other? In this paper we try to give an answer to these questions by developing a simple framework that describes how new entrants and incumbents in the banking industry influence each other and reciprocally evolve – *co-evolve* – to create an on-line financial services complex. By focusing on dynamic processes rather than random indications of the current state of affairs, this framework enables us to see the co-evolution of managerial actions and environmental phenomena in an emerging e-commerce complex in its right perspective (Lewin & Volberda, 1999).

The paper is structured as follows. First, we explain why research in the financial services industry is highly interesting in light of the emergence of e-commerce complexes. Secondly, we elaborate a basic framework of competence leveraging and building strategies for incumbents and new entrants. We complement this framework by contrasting the managerial perspectives of either party with regards to the current e-commerce evolutions in the financial services industry. Subsequently, we outline how incumbents and new entrants can use the lever of "sponsoring" organizations to outdo each other, resulting in three key propositions. Finally, we conclude this paper by enumerating the most important lessons managers of well established and new entrant firms should learn in order to be succesful in the emerging on-line financial services industry.

The emerging on-line financial services complex

Our focus is on the emergence of an *on-line financial services complex*. There are several reasons why we chose financial services. The banking industry is a mature industry which is facing increasing environmental turbulence. It has long been subject to strong institutional control and been protected by high entry barriers (Scott, 1998). However, deregulation and the increasing importance of ICT are leading to the deconstruction of entry barriers. Even scale economies are not a substantial barrier to entry anymore for new entrants since succesful Internet banking is grounded in flexible processes rather than mere economies of scale (Canals, 1999; Llewellyn, 1999). What is more, operating expenses of electronic banking services are estimated to amount to only 25 to 30 percent of the cost of providing traditional banking services through existing bank branch offices (Klinkerman, 1996). Finally, customer awareness about bank products is soaring (Llewelynn, 1999, Essinger, 1998).

New entrants could well take advantage of that fact by imposing new and disruptive ways of competing to incumbents (Porter, 1996). Therefore, many banking industry analysts believe the power in the channel of retail financial services will shift very soon to innovative new entrants able to offer a more attractive and efficient consumer banking interface (Clark & Lee, 1998). But then again, other analysts predict national-historical protection and preferences are likely to favour incumbents, and delay change (Walter, 1999). For institutional constituents like the media, customers and government are likely to trust their crucial resources to more legitimate organizations in the emerging on-line financial services complex. That is, well respected banks or insurance companies.

How should new entrant and incumbent firms evolve to get the upper hand? Apart from offering technically superior services, new entrants need to develop strategies encompassing on the one hand the establishment of extra-organizational, legitimating ties to the institutional apparatus and on the other hand the de-institutionalization of incumbents. Likewise, to counter new entrants' claims for legitimacy incumbents need to adapt the nature of their extra-organizational ties to the demands of the changing environment. In this way the rationale underlying both incumbents' and new entrants' strategies involves the manipulation to their advantage of the legitimacy criteria employed by institutional constituents (Oliver, 1992).

A basic framework for new and old

The aim of this paper is to describe how incumbent and new entrant managers can build and leverage competences that are viable and legitimate in an emerging on-line financial services complex. We define a *competence* as the ability of a firm to sustain the coordinated deployment of assets in a way that helps it achieve its goals (Sanchez et al., 1996). Based on the above, in figure 1 we present a conceptual framework of basic competence building and leveraging strategies employed by incumbents and new entrants in the emerging on-line financial services complex. *Incumbents* in this framework are defined as large and mature players in the traditional financial services industry (type 1). We identify *three generic types of new entrants.* First, we consider players in industries other than the financial services industry that elaborate symbiotic resource dependencies with incumbents (type 2). Examples of this type of new entrants are the software companies Microsoft and Intuit, which cooperate with incumbent firms to build standardized customer interfaces.

Insert figure 1 about here

Autonomous outside ventures of incumbent players (type 3) are a second type of new entrants. A prominent example of this type of new entrants is Egg (www.egg.com), the UK-based Internet banking division of Prudential Banking. Finally, we discern brand new entrants (type 4) as the result of entrepreneurial efforts originating from outside the traditional financial services industry. Dublin-based First-e (www.first-e.com), backed up by a consortium of venture capitalists and technology firms, is an example of such a brand new entrant. First-e, which is now active in the UK, Spain, Germany and France, aims to be the first Internet bank to balance the global nature of Internet-technology and the local demands of customers, on a European scale. First-e has therefore tied up with Spanish Uno-e, to create an entity called the Unofirst Group. The three types of new entrants described above are ideal types. Security First Network Bank (www.sfnb.com), a US-based Internet bank set up in 1995 by Cardinal Bancshares and SecureWare, represents a hybrid of these three types. Though SFNB was taken over by Royal Bank Financial Group in 1998, it is interesting case-study material since it pioneered Internet banking. Egg and SFNB have already reached the threshold number of one million customers (Clark & Lee, 1998; Mackintosh, Financial Times, march 2000).

In this paper we assume that incumbent firms (type 1) – apart from engaging in internal renewal (Baden-Fuller & Stopford, 1994) – have two strategic options when trying to overcome their liability of oldness. A first option is to elaborate interdependent resource dependencies with players that already built complementary competences in the marketspace (type 2). Here the aim is to deploy combinatorial competence building and leveraging strategies in an integrated marketplace and marketspace. Incumbents have an other option. They can also establish fully autonomous outside ventures (type 3) in charge of independent competence building in the marketspace, as a strategic option for future competence recombinations in an integrated marketplace and marketspace. We further assume that brand new entrants (type 4) have to overcome their liability of newness by first leveraging existing Internet-technology competences in the traditional financial services industry and subsequently gradually building revolutionary competences in the marketspace.

Co-evolutionary perspectives

Banks have for most part of their history been unquestioned fiduciary parties, which led out to the delimitation of legitimate spheres of organizational activity being predominantly based on taken-for-granted social norms (Dowling & Pfeffer, 1975; Suchman, 1995). Incumbent banks are *structurally legitimate*, in the sense that their structures and procedures often serve as easily monitored proxies for less visible targets of evaluation such as strategies, goals, outcomes (Meyer & Rowan, 1991; Suchman, 1995). Big banks' status as "*too big to fail*", and in some cases weak incentives to be aggressive, resulted in the largest banking organizations in the industry exerting a unique influence on competition (Pilloff, 1999). Banks, as they grew larger, have literally become more of their environment (cf. Weick, 1979, p.167). Banks increasingly narrowed their focus on their own enactments of the environment, causing a spiral of growing consensus on a restricted set of beliefs. Consequently, dense social networks have been institutionalized in which an elite of incumbent managers exchange the same recipe or set of beliefs (Spender, 1989, 1996).

Incumbent bank managers therefore tend to view their organization as a closed system, embedded in an environment they largely *control*, without perceiving they are also for a large part new entrants in the Internet marketspace. The recent merger and consolidation wave amongst financial services institutions in the US and Europe, testifies to that (Brandman & Keeler, 2000). The lack of contesting managerial cognitions (Sanchez & Heene, 1997; Sanchez et al., 1996; Weick, 1979) induces incumbents to conduct competitive organization policies towards customers, technology, legitimacy and industry legacy in the same *taken-for-granted* way (Lewin et al., 1999; Staw et al., 1981). Obviously, this narrowed perpective can lead to serious misjudgments of situations when confronted with increasing environmental turbulence (Janis, 1982).

New entrant managers on the contrary, tend to perceive their organization as an open system, since they are not sufficiently embedded in existing social networks to control environmental selection processes (Campbell, 1975; Weick, 1979). Figures 2a and 2b illustrate the different perspectives of incumbents and new entrants on the boundaries of the emerging on-line financial services complex.

Insert figures 2 a and 2 b about here

New entrants try to embed themselves by building and participating in a brokerage network, wherein flexible information access is prevalent. In order to anticipate the selective processes that delineate the boundaries of the emerging on-line financial services complex, new entrant managers try to span these boundaries by creating resource *interdependencies* across several industry legacies, customer types and legitimacy bases. For instance Prudential's outside venture Egg tries to overcome the inherent second-utility nature of financial services, by linking its services to first-utility products as wines, books, food and drink, CD's, … (www.egg.com). Security First Network Bank leveraged the banking industry expertise of Cardinal Bancshares and the technical expertise of SecureWare, to not only sell Internet-only financial services, but also develop secure customer interface software for incumbent banks (Clark & Lee, 1998).

As noted by Campbell (1975) and Weick (1979), adaptive evolution focused on processual change works best when the evolving social organization is a small part of the total environment. Hence, to anticipate environmental turbulence and the need for changing resource dependencies, new entrants build a *modular* organization structure, which allows maximal strategic flexibility. First-e, for instance, leverages the ICT and security skills of Enba to develop Internet-only financial services, contracts out its clearing operations to Royal bank of Scotland PLC, and outsources its on-line brokerage trades to the investment bank Dresdner Kleinwort Benson. This allows First-e to keep a modular structure, which allows flexible adaptation to environmental turbulence.

However, new entrants eager to revolutionize an industry have to guard not to engage in too much exploration and not enough exploitation. New entrants face the danger of falling in an exploration trap (Volberda, 1998). Although having flexible ties focused on brokering opportunities is a powerful means for building superior competitive advantage, the exploitation of this advantage can be endangered by not ensuring sufficiently strong ties with anchoring parties. Incumbents on the other hand face the opposite danger of engaging in too much exploitation and not enough exploration. Incumbents face the danger of falling in an exploitation trap (Levinthal & March, 1993). Although being too big or old to fail, and having a lot of dense interconnections is a powerful premise in the short term, in the long run the lack of flexible brokerage ties is likely to cause the decline of such incumbents.

By applying the above findings to the four organization types depicted in figure 1, we can construct a continuum of organizational characteristics. We summarize all the above findings in table 1. In this table we map the above described organizational characteristics on a continuum of the four organization types depicted in figure 1. Players in industries other than the financial services industry– as they are engaged in symbiotic resource dependencies with incumbents – are likely to adopt a rather closed system perspective of the ongoing collaboration with the incumbents. Autonomous outside ventures of incumbent players are already more likely to adopt an open system perspective of the environment and their organization since they can act fairly independently from their originating incumbent. Finally, brand new entrants, having no links with incumbent players at all, are most likely to adopt an open system perspective.

Insert table 1 about here.

Any of the above types, be it incumbents (1) or new entrants (2, 3 and 4), will have to strike a balance between the open and closed systems perspective. On the one hand these organizations will have to keep part of the organization relatively closed to the environment to enable some rationality and planning. On the other hand, to survive, the organization will have to co-evolve with and enact the environment by keeping an open system perspective.

Buffering and bridging : levers of a dynamic strategy

Managers, as boundary-spanners, in general serve two roles (Fennell & Alexander, 1987; Meznar & Nigh, 1995). A first role is to *buffer,* or protect an organization from the external environment. A second role is to serve as a *bridge* with the external environment. Basically, buffering strategies enable an organization to temporarily seal off its core rationale from discontinuous turbulence. In this way an organization faced with increasing environmental turbulence, can maintain certain norms of rationality while elaborating bridging strategies (Thompson, 1967). Bridging strategies ensure the security of the entire organization in relation to its environment in the longer term. These strategies aim at bridging the gaps between organizations and their exchange partners, competitors, regulators (Scott, 1998) and customers through substantial organizational adaptation. In the following sections we outline the need for new entrants and incumbents to develop strategies of conjoint buffering and bridging in order to build viable competences in the emerging on-line financial services complex.

New entrants : how to overcome the liability of newness

A viable strategy of new entrants is likely to be directed towards revolutionary, disruptive change in the environment. This is especially true for brand new entrants (type 4), but also for autonomous ventures (type 3), as demonstrated by the start-up Egg, which offers cut-throat interest rates on savings accounts (Mackintosh, Financial Times, February 2000). However, upon embarking on a new line of activity, particularly one with few precedents, new entrants have to face the daunting task of winning legitimacy. Demonstrated technical superiority by new entrants is a necessary but not sufficient condition for acquiring legitimacy in an emerging on-line financial services complex. Apart from fulfilling this requirement early entrants must also devote a substantial amount of energy to so-called “sector building” in the new complex. This involves creating a sense that the endeavours of the new entrants define a sector that exists independent of particular incumbents (Aldrich & Fiol, 1994), by creating objectivity and exteriority. Therefore, new entrants should follow a double track of integrating new activities under the umbrella of preexisting taken-for-granteds (cf. Zucker, 1983) and simultaneously disentangling new activities from certain preexisting regimes, to avoid new activities being perceived as marginal or illegitimate (Suchman, 1995).

The example of First-e illustrates this. First-e piggybacks on the banking licence of French Banque d’Escompte, to become the first legitimate pan-European bank dedicated to Internet-only financial services (Rubin, 2000). Moreover, to make an impact, First-e rolled out a major ad campaign, encompassing TV, radio, print and outdoor activity, a few months after its start-up (Rosier, 1999). Likewise, Prudential Banking established its outside venture and new Internet brand Egg, to prevent its Internet-activities to be perceived as marginal and achieve a sense of exteriority about its product offerings (www.egg.com). Complementary outsiders (type 2) like Microsoft take an apparently more closed system perspective. Microsoft made it clear it does not want to launch itself as a financial services company, but only tie the services on its Microsoft Network site up to major banks, to provide a stronger proposition (Darby, 1999, Marketing).

The above examples illustrate Oliver's (1992) proposition that the affiliation of a new entrant to a legitimate institutional actor, for instance a governmental entity, has a positive effect on its life chances, and even on the life chances of the whole focal organization's population. In addition, several scholars have found that tying up to legitimate actors not pertaining to the new entrants' population, not only lowers the liability of newness of new entrants, but also enhances their economic performance (Podolny, 1993; Podolny & Philips, 1996; Sharfman et al., 1991). These ties will also help new entrants to create new allegiant constituencies. Legitimate actors in general are (Hybels, 1995) the state (for instance contracts, regulation, legislation), the public (f.i. lobbying instances), the financial community and the media. We introduce the term "sponsor" for any of the legitimacy providers in the emerging on-line financial services complex. We define an *inside sponsor* to be a legitimacy provider in the traditional financial services industry, while an *outside sponsor* in our definition is a legitimacy provider not pertaining to the traditional financial industry.

First-e, for instance, uses Banque d'Escompte as an inside sponsor, by leveraging its banking license. On the other hand, First-e uses its parent firm Enba and venture capitalists such as Intel as outside sponsors. In addition, First-e is investing a huge amount of money to establish a brand name. Extensive media coverage in both the traditional financial services press and the computer or software press, is contributing to First-e's publicity (Rosier, Marketing, 1999). The significance of Egg's tie to the banking license of its parent company and inside sponsor Prudential Banking is obvious. Moreover, Egg's launch of a web-based personal investment supermarket in which incumbents as Prudential and Legal & General offer their products, provides it with an other source of inside legitimation. Moreover, to ascertain outside legitimation, Egg initiated a virtual community for its customers (www.eggfreezone.com), in which independent or "exterior" media sources provide "objective" information about the financial services world. To further improve the credibility of this information, customers are encouraged to post all their griefs and complaints on a publicly available webpage. Egg's linkages to and discounts on a whole range of first utility products offered on the Internet, further contribute to its outside legitimation.

The example of SFNB provides us with another illustration of the importance of inside and outside sponsors for new entrant firms. Some months after its startup, three new banking company investors took a participation of 25 % in SFNB. One of these investors, Wachovia, was regarded as a very conservative and well run bank holding company. SFNB's link to Wachovia provided it with an important source of inside legitimation, and even suggested that Internet banking could be seriously considered by conservative banks (Clark & Lee, 1998). SecureWare's highly regarded banking software - which later on even became a standard for US-banks - further added to SFNB's outside legitimation (Clark & Lee, 1998).

According to Hybels (1995 : 241; italics added) "the institutionalisation of a feature of society derives from a legitimation *process* that occurs over *time*, and the legitimation process itself derives largely from institutions other than that being legitimated." Two aspects of the statement are important here; the time aspect and the notion that existing institutions provide support in the legimation process of new institutions, although this could mean cannibalizing their own legitimacy. Consequently, new entrants that try to build new competences fast by using inside and outside sponsors are more likely to disrupt the competence perspective of incumbents. The superior pace of new entrants is likely to outperform the adaptive capabilities of incumbents. In this way new entrants decrease the probability that incumbents control the changing environment in which they are embedded. As a consequence, the set of beliefs of industry incumbents is likely to become less homogeneous, which increases the probability that some incumbents will change their perspective on legitimacy criteria. The support of incumbents that are willing to cannibalize their traditional legitimacy perspectives in favour of a new legitimation process evidently suits new entrants' interests. In particular because this support is indispensable in quickly attaining a critical mass of de-institutionalizing participants in the on-line financial services complex. Based on the above findings and the condition that new entrants are technically superior in the marketspace, we suggest following propositions :

Proposition 1 : By using the buffer of an inside sponsor, an early new entrant decreases the "liability of newness" of all the new entrants, and subsequently induces incumbents to adapt their competences in a disruptive way, which facilitates bridging strategies.

Proposition 2 : Using a combination of inside sponsors and outside sponsors enables faster profitability and faster competence building in the marketspace

When evaluating different strategies both in the marketplace and the marketspace, we need to consider the type and degree of legitimating ties provided by the different sponsors. Most outside sponsors will eventually help in creating new legitimacy in the marketspace, but do not provide entrants with a strong initial legitimacy-basis to overcome their liability of newness in the marketplace. Conversely, most inside sponsors can help new entrants in gaining relatively strong institutionalized legitimacy in the marketplace, but do not provide entrants with the support of creating new legitimacy in the marketspace. New entrants therefore need to manage the tension between the flexibility of outside sponsors and the security provided by inside sponsors. Clark and Lee's (1998) case-study of Security First Network Bank revealed the importance of managing this tension. SFNB's immediate success with its secure software made it hesitate in which direction to proceed : either be an Internet-bank providing disruptive Internet-only financial services, or be a software company selling off its software packages to incumbent players (Clark & Lee, 1998). In this respect SFNB's modest successes as an Internet bank and its later takeover by the Royal Bank Financial Group, could well be attributed to its lack of focus on continued change and flexibility toward outside sponsors, and its premature profit-seeking toward incumbent insiders.

Incumbents : how to overcome the liability of oldness

One of the first and most standardized steps of incumbents in the marketspace was the comprehensive installation of an automated teller machine (ATM) network. However, this was not a strategically aligned step, as the CEO of Wells Fargo stated (Global Finance, 2000 : 70) : "over the past decades banking technology has preceded a change in customer habits, in many cases solutions preceding demand, like ATM's installed before widespread consumer acceptance. And over time banking technology has actually disconnected the customer from the bank and impaired the bank's ability to create customer intimacy." Rayport and Sviokla (1994) point out that while the ATM network continued to expand, bank customers began responding to the ATM technology and not to the individual bank providing it. This made banks the faceless providers of commodities. Because bankers originally only saw the ATM network as a banking automation, they did not notice that such automation would change the entire value proposition of retail banking (Rayport & Sviokla, 1994).

Contrary to new entrants, incumbents tend to prefer evolutionary change, which is reflected by a desire to control the changes of the environment in which they are embedded. However, incumbents have to understand that they also are for a large part new entrants in the marketspace. How can incumbents bridge sources of environmental turbulence, and at the same time protect past accomplishments? Meyer and Rowan (1977) argue that often peripheral activities are ceremonialized for external legitimacy purposes and are loosely coupled to the technical core, because they do not offer consistent guidelines to manage it. This decoupling could be particularily useful when there are conflicting demands by the environment. Moreover, Meyer (1979) notes that structural changes are often signals to external constituencies of organizational commitment regardless as to whether the new structure is effective or implemented. These propositions confirm the need for incumbents to establish buffering strategies to ensure maintenance of their embedded competences towards exchange partners, competitors, regulators and customers.

The Internet websites of many incumbent banks are an example of such a buffering strategy (e.g. www.abnamro.com and www.natwest.com). Their establishment has substantial normative significance, but limited strategic consequences; Internet is still mainly treated as an additional distribution channel, instead of the driver of a comprehensive processual change. What is more, to buffer themselves from environmental turbulence, incumbent banks like for instance Barclays and ABN-Amro "shrug off the threat of internet competition" (Graham, Financial Times, 16 february 2000, p.24) or discredit "the marketing skills" and "customer relationships" (Fairlamb, BusinessWeek Online, 25 october 1999, p.2) of new entrant firms. Meanwhile however, the incumbent banks announce themselves huge e-commerce investments (Bell, Marketing, 27 may 1999).

Yet, buffering strategies should be used with caution. Incumbents' inertia towards building processual competences in the marketspace might lead to a strategic drift (Johnson, 1987) of symbolic buffering strategies without effective operationalization of bridging strategies. This could eventually lead to a widening gap between organizational beliefs and environmental characteristics, and, as a consequence, the gradual de-institutionalization of incumbents' structural legitimacy. Incumbents willing to develop effective bridging strategies should make use of new boundary-spanning personnel, to enable contesting managerial cognitions to remould the strategic logic of the organization. Incumbents may therefore establish specific subunits with a mandate to question others' taken-for-grantedness. "Where organizations seek to perceive changing audience beliefs, the risk is not that centrifugal forces will lead boundary spanners to run wild, but rather that centripetal forces will lead them to become lapdogs" (Suchman, 1995 : 586). These propositions seem to confirm Christensen's (1997, 2000) findings, that the only way for a mature business to harness a disruptive technology like the Internet, is to start an autonomous business unit independent of the extant resource dependencies of the mature business. For instance the establishment by Prudential banking of its outside venture Egg needs to be considered in light of the above findings.

Ideally, the scope of an outside venture should not interfere with incumbents' prime product-market combinations so as to not to put in danger incumbents' controlled embeddedness. Egg for instance offers products in the UK that are not directly in competition with Prudential's main product offer. In this way, incumbents might be able to avoid cannibalization (Ghemawhat, 1991) of their product-market combinations. In addition, the know-how acquired in the Internet marketspace by the outside venture can facilitate committed (Ghemawhat, 1991) competence building and exploration in the incumbents' organizations. For instance, Lloyds plans to first launch an e-bank in Spain and only afterwards in its main market, the UK. This illustrates Lloyd's commitment to incrementally build competences in the marketspace (Anonymous, Financial Times, may 2000).

Summarized briefly, incumbents' managers should try to acquire flexible skills (Volberda, 1998) resulting out of contesting managerial cognitions, to effectively strike a balance between the protection of buffering strategies and incremental operationalization of bridging strategies. In this way incumbents' managers might be able to avoid increasing contradictions between the legitimation of their organization in on the one hand the traditional financial services marketplace and on the other hand the Internet marketspace. Based on the above findings, we suggest following proposition :

Proposition 3 : By using the buffer of outside sponsors and the bridge of autonomous processes in the marketspace, incumbents are more likely to maintain legitimacy and competences and decrease their liability of oldness

Lessons on co-evolution in emerging e-commerce complexes

A one-sided interpretation of the current evolutions in the emerging on-line financial services complex as cut-throat competition between incumbent and new entrant firms is not likely to shed much light on how to build and leverage competences in the Internet marketspace. Establishing a competitive advantage in the Internet marketspace is not solely a question of incumbents being large enough to crush fledgling new entrants, or – vice versa – of new entrants being revolutionary enough to render incumbents' business models obsolete and illegitimate. On the contrary, the strongest business models in an on-line financial services complex will build on complementarities between traditional financial services competences and revolutionary Internet-competences. Therefore, cooperation between incumbents and new entrants rather than mere competition will be the key to success, both for new entrants and incumbents. New entrants and incumbents need to *co-evolve* with each others' competences to some extent to build a competitive advantage – a critical, and sustainable mass of profitable customers. Naturally, strategies to trigger cooperation of other parties to one's own favour differ for the various players in the emerging on-line financial services complex. In addition, it is important to keep in mind that cooperation between different players is not always triggered directly, but often comes into being indirectly through institutional pressure exerted by the media, the state, banking industry analysts, competitors and other members of the financial community.

In this paper we distinguished between four organizational types as key players in the emerging on-line financial services complex, namely incumbents (type 1), complementary outsiders (type 2), autonomous venture (type 3) and brand new entrants (type 4). We deduce the following important managerial implications for incumbents (type 1) :

- incumbents – apart from engaging in gradual internal renewal – need to break away from their institutionalized way of thinking by appealing to outside managerial views
- to that end incumbents have two options (which are not mutually exclusive) :
    a) set up resource interdependencies with one or more complementary outsiders
    b) establish an autonomous venture in the Internet marketspace, which does not interfere with the prime product/market combinations of the parent company in a first stage
- anyway, incumbents need to use sponsors in the Internet marketspace, like for instance the media reporting on on-line financial services evolutions, to establish a buffer against immediate disruptive competition and to avoid untimely obsolescence or cannibalization of their core product/market combinations

- meanwhile, incumbents need to gradually establish bridging strategies towards the changing perspectives of customers, the state, the media and other members of the financial community
- therefore, incumbents need to rely on autonomous processes in the Internet marketspace – by means of an autonomous venture or an autonomous collaboration with a complementary outsider – in order to stay in touch with revolutionary evolutions introduced by new entrants

With regards to new entrants, we emphasize the need to simultaneously use linkages to players in the traditional financial services industry – *inside sponsors* – and sponsors in the Internet marketspace – *outside sponsors* – to overcome the liability of newness they are confronted with. Important to note is that the emergence of an on-line financial services complex is a collective process, and thus not only relies on revolutionary business propositions, but also on reaching a threshold of sufficient cooperation with other players. In order of increasing revolutionary perspective we deduce the following managerial implications for new entrants :

- complementary outsiders (type 2) :
    a) need to focus on control of the customer interface as the most important lever for future competitive advantage in the Internet marketspace, which is characterized by interactive supplier-customer processes
    b) need to achieve a critical mass of resource interdependencies with key players in the emerging on-line financial services complex to ensure that controlling the customer interface is valuable enough

- autonomous ventures (type 3) :
    a) need to operate as independent as possible of their parent company – in this paper by definition an incumbent firm – to be able to build viable Internet competences and a profitable business model (this also translates in a new brand name and a differentiated use of marketing channels)
    b) nevertheless to some extent need to coordinate their processes with the internal renewal processes of the parent company, to obtain succesful synergies in the longer term
- brand new entrants (type 4) :
    a) are most prone to develop revolutionary managerial views in the short term, since they are not connected to incumbent players
    b) in order to balance this revolutionary tendency with sufficient cooperation of more conservative players, new entrants need to establish ties with inside sponsors, by for instance getting a banking license or hiring "inside managers" with sufficient insight and relations in the traditional financial services industry

The above lessons might help incumbents and new entrants considerably in influencing which competences will be viable and legitimate in the emerging on-line financial services complex. However, this does not mean that the final outcomes of either party's managerial actions will be exactly the ones expected. We therefore highlight the importance of continually keeping a dynamic, co-evolutionary perspective of environmental change. In this way, incumbents and new entrants can avoid entrenching their competences untimely in an e-commerce complex which has not yet reached a threshold of sufficient maturity.

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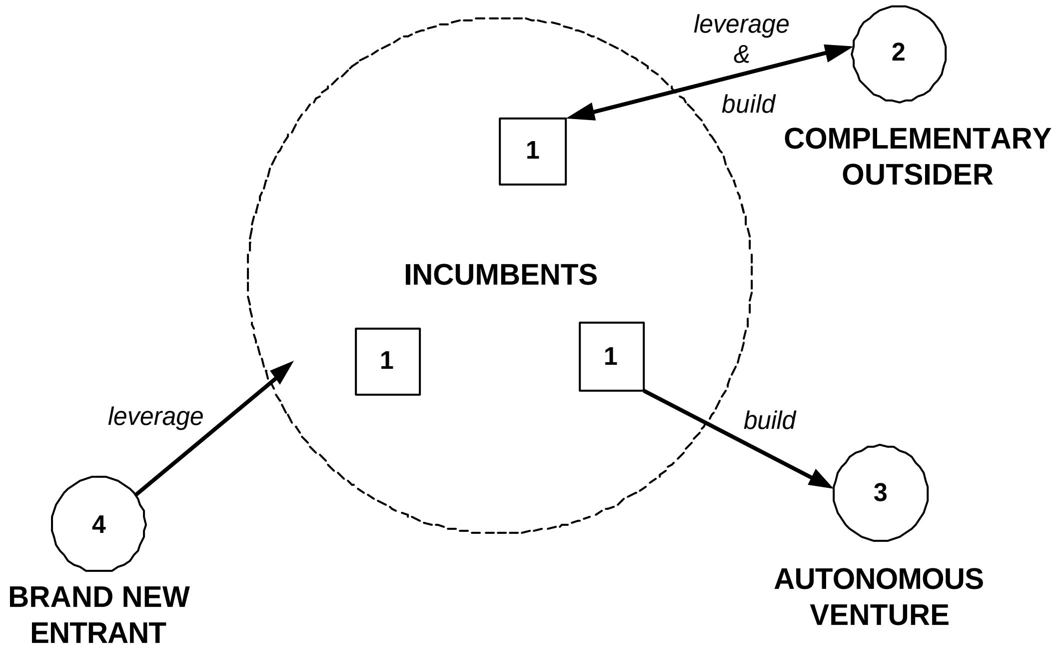
FIGURE 1

Generic competence building and leveraging strategies :

Incumbent firms and three generic types of new entrants



Type 1 = incumbents

Type 2 – 4 = three generic types of new entrants

FIGURE 2A

Perspective of incumbents

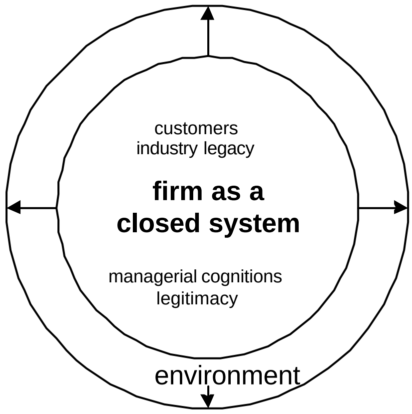


FIGURE 2B

Perspective of new entrants

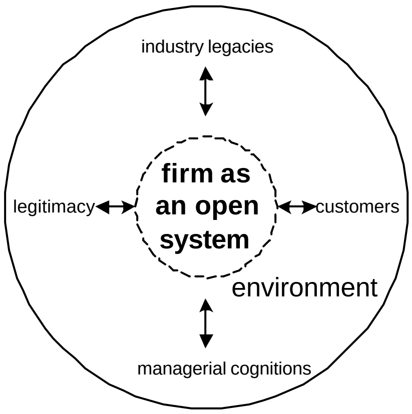


TABLE 1

Continuum of organizational characteristics of incumbents and three generic types of new entrants

	Incumbents (type 1)	**Complementary outsider (type 2)**	**Autonomous venture (type 3)**	**Brand new entrant (type 4)**
Organizational structure	---too big/old to fail---modular--------			
System perspective	----closed ---open----------			
Change	---evolution---revolution---------			
Embeddedness	---controlled---interdependent-----			
Managerial cognitions	---uniform / elitist---contesting / democratic---			
Liability of	----oldness---newness---- (competence trap) (exploration trap)			
Legitimacy **Customers** **ICT**	------structural--processual----- taken-for-grantedness enactment			

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