The unloved relationship? Dynamic capabilities and political-market strategy: a research agenda

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- In this developmental article, the authors outline a five-stage system to classify levels of relationship engagement (LRE) between firms and government actors when developing their political-market strategies (PMS) as part of a wider stakeholder management programme. In an attempt to develop the research agenda in this increasingly important area, the authors propose a set of hypotheses to drive forward the research agenda. Overall, we argue that firms can develop PMS into a dynamic capability but further research is needed to determine whether or not the capability developed is first or second order (i.e. contributing to other sources of competitive advantage).

Introduction

The emergence of a stakeholder discussion (Freeman, 1984; Mitchell \textit{et al.}, 1997b), particularly in the area of business-government relations, remains relatively under researched within the literature (Hillman \textit{et al.}, 2004; Hillman and Hitt, 1999), signifying a focus upon the motivating effect of firm profitability above other concerns (Doyle, 2000). Nevertheless, the importance of developing a firm’s relationship with government in the marketing context has long been recognized (see Morgan and Hunt, 1994, for an early consideration). Despite this lack of general recognition in the literature, the idea of government-as-stakeholder is recognized by firms who are constantly testing and reviewing their strategic decisions to ensure that they address prevailing legal or regulatory concerns, particularly multi-national companies and those operating in highly regulated industries (e.g. pharmaceuticals, brewing and public utilities).

Inevitably, in Orwellian terms, some stakeholders are more equal than others and, correspondingly, there is now a developing literature on the regulatory influences upon market strategy (Harris and McDonald, 2004; Willman \textit{et al.}, 2003; Parker, 2003; Ghobadian and Viney, 2002). We argue that this activity is often fundamentally reactive in nature, and that the extant literature tends to study how organizations react to changes in regulatory or legislative actions, paying less attention to \textit{bow} firms seek to control their strategic environment, particularly in terms of its interaction...
with vital non-market stakeholders like government or regulatory authorities—i.e. studies tend to be descriptive rather than instrumental or prescriptive in nature. This is not to argue that there is not a significant and growing literature on aspects of what is usually referred to as ‘lobbying’, ‘public affairs’ or ‘government relations’. However, we would add our voice to a growing demand (Hillman et al., 2004; Hillman, 2002; Schuler, 1999) for a more systematic understanding of how firms actively seek to influence the governmental actor as a critical element of firm strategy making, or as an adjunct to the strategy implementation process, particularly in terms of political environmental scanning (Barrows and Morris, 1989; Keim and Hillman, 2008).

However, there are a number of issues to contend with when examining this issue. Firstly, firms are notoriously reticent about discussing their relationships with government, and in particular their involvement with lobbying activity, at least partly because of firm concern that such information is commercially sensitive and of competitive value. Secondly, part of the difficulty with the discussion of lobbying is its ever-shifting (re)definition and semantics. There is no single understanding of what the term ‘lobbying’ refers to, undermining attempts to quantify its importance to the effective operation of organizations, and to dispel the common assumption that any form of business-government relations is essentially corrupt and antisocial. There is also limited interaction between discussions in the political science literature over what does, or does not, constitute lobbying and/or other terms describing business-government relations, and the growing empirical literature, particularly focused upon US Corporate Political Activity (CPA), reviewed in Hillman et al. (2004). Because most organizations engage in lobbying, public affairs, government relations activity, etc. from the perspective of the very top echelons of their organizations, and because the consequences are often felt at industry level, we propose the use of the term ‘political-market strategy’ (PMS). From a strategic marketing perspective, it is surprising that this important relationship has been neglected. It has, in the past, generally been felt that macro-environmental factors (i.e. the law and politics) are uncontrollable in strategy scanning and development activity but in fact they are not uncontrollable (Harris and Lock, 1996). Examples of firms who have taken advantage of political environmental changes include: the Abbey National Building Society who demutualized (i.e. became a bank) shortly after the 1987 Financial Services Act and several years before its competitors; Price Waterhouse and Coopers & Lybrand whose rhetoric identified the EU’s (European Union) enlargement agenda as a point of persuasion for allowing a merger case through the EU merger control process (Hatcher, 1998) and Bernie Ecclestone’s Formula 1, which achieved an exemption on the banning of tobacco sponsorship in November 1997 from a European Directive due to come into force in 2003, by arguing the ban would drive the sport and its £900m export value to the Far East (Abrams and Butler, 1997; Webster, 2002)—although in that case, Ecclestone’s £1m donation to the Labour Party caused such a media furore that the Labour Party was forced to return it and the EU directive was annulled anyway (Tempest, 2002; Osler, 2002).

**Developing a research agenda**

We aim to review the literature focusing on lobbying and regulatory affairs from the perspectives of political science, strategic management, marketing and political marketing literatures, leading to the development of hypotheses aimed at overcoming the extant semantic hurdles. In so doing, we aim to construct a rationalized classification system of PMS, focusing not so much on labels but upon levels of PMS. We argue that there are different forms of PMS, but can we effectively identify those levels based upon the specific intended outcome of each level? We use our understanding of PMS to develop hypotheses highlighting the key variables in determining levels of PMS: outcome, input and contextual...
variables. We argue that while not all organizations will seek to operate at the highest level of PMS, all organizations will be concerned to maximize the outcomes of their PMS activity, at an appropriate level of resource expenditure, and in a fashion congruent with the context in which they operate. PMS offers an opportunity to seek and obtain competitive advantage because not all firms will be operating at an appropriate level, causing inefficiency.

We attempt to establish an understanding of whether firms can build or exploit their capability and so develop market potential in the area of developing and maintaining relationships with government through PMS, according to a stage level typology. Why is this necessary? In our view, there has been a long-standing deficit in understanding the significance of how ‘lobbying’ can contribute to the successful development and implementation of firm level strategy. Consider the Abbey National case discussed above, or the PriceWaterhouse Coopers merger in 1997 or Ecclestone’s Formula 1/tobacco sponsorship for example—was PMS a significant factor in these decisions? The amount of financial and time resource expended on ‘lobbying’ by major corporations, though often difficult to determine, would certainly imply that the practice will have beneficial effects (Harris and Lock, 1996), but the extent of causality is yet to be convincingly researched. Arguably, definitional concerns could hide a wider failure amongst many firms to recognize what is possible in this arena, or what tools are at their disposal, to enable them to shape and control their competitive environment. Many large (and certainly multi-national) firms are engaged in PMS of some description although the characteristics of this activity vary in scope, range and intensity. This creates the probability that some firms do not realize that they are engaged in PMS, or are undertaking a type of PMS behaviour which is inappropriate given their needs and/or the resources at their disposal. The paper seeks to initiate a debate as to whether and how PMS might contribute to strategic marketing success. To begin this process, we explore the background to the PMS debate and introduce our stage model of PMS, before introducing a future research agenda. This considers whether an organization’s PMS should be considered a resource or capability that firms can develop/sustain/deploy to achieve competitive advantage? Is it possible that PMS might be a ‘dynamic capability’ (Helfat and Peteraf, 2003) of the firm?

**PMS: lobbying, corporate political activity, public affairs, regulatory affairs**

As we have noted, a variety of terms are used seemingly interchangeably to describe the process of interaction between a company and the governmental actor, specifically to changing the perspective of a government actor to one supportive of your organization. Nownes (2001) adopts a broad definition, suggesting that ‘lobbying’ is ‘attempting to influence government decisions’, and lobbyists, therefore, are individuals ‘who work to influence decisions of public officials’ (Green et al., 1972). The key aspects to the notion of lobbying are, therefore, the interaction with a public official and the attempt to influence decisions of public officials (McGrath, 2005; Milbrath, 1963). However, possibly as a consequence of the inherently pejorative association of the term, and its lack of specificity, other authors have preferred the term ‘government relations’ (McGrath, 2005). Mack (1997) argues a distinction can be drawn in terms of advocacy—‘lobbying’ implies advocacy of a point of view, while government relations involve the ‘application of one or more communications techniques’ to affect government decisions in the interests of a lobby or lobbyists, although as McGrath notes, ‘the practical distinction between them is a little less than obvious’ (McGrath, 2005). However, other authors have described similar activities as ‘public affairs’ (Morris, 1997). Various authors have ascribed to ‘public affairs’ the status of a particular management skill (Pedler, 2002), where capabilities in
understanding the environmental context and shaping appropriate strategies are key. Consequently, there is a need for a term which (1) connotes the process of political-market interaction and (2) integrates this understanding with the strategic intent of the firm to achieve (3) a defined political-market strategy.

A five stage classification system of political-market strategy development

We suggest it is possible to rationally analyse the lobbying activity of organizations based upon the intended outcome of their engagement with government or regulatory authorities, and offer a series of different ‘levels of relationship engagement’ which roughly correspond with differing strategy intentions and relationship marketing strategies. Furthermore, we can associate a number of characteristic activities with each of these levels of relationship engagement and equate particular sets of behaviour to those levels of intended outcomes, developing a generic classification of lobbying from a strategic marketing perspective. This opens up the possibility that organizations can, based upon the intended outcomes of engagement with legislative or regulatory authorities, assess the extent of their relationship engagement, based upon a realistic understanding of whether the resources committed to this activity will contribute to profitability and/or market potential. In making such an assessment, it is clear to us that there is a strong industry effect here. Various authors have argued (Hansen and Mitchell, 2001; Hart, 2001; Mitchell et al., 1997a; Schuler, 1999) that the necessity of building strong business–government relations is a direct consequence of the extent of government/regulatory influence upon an industry. If government either spends heavily or imposes a strong regulatory influence upon competition within your industry, or if there is a history of frequent or radical regulatory or legislative change, we would hypothesize that the importance of developing strong PMS increases. Industries such as defence (high government expenditure), pharmaceuticals, food manufacture or utilities (strong regulatory activity) would be expected to develop and maintain strong PMS capabilities, more so than industries where government intervention was limited or relatively passive, since not to do so may actually reduce the size of a particular company’s competitive marketplace.

Table 1 proposes a five stage model of PMS, with correlating levels of decreasing engagement with government actors (stakeholders) at each stage and the strategic rationale underpinning the decision to engage at each level. Underpinning our thoughts on differentiated ‘Stages’ in the activity, commonly described as lobbying, are the following observations:

- There exist organizations whose contacts with policy makers are so strong that they are involved in the co-creation of law. This represents the highest level of PMS, and arguably suggests activity beyond the scope of a term like ‘lobbying’ because ‘lobbying’ implies active attempts to persuade.
- There exist organizations who will seek to change the law in their favour as it is developed. They cannot create the law, but will seek to influence its detail before it is enacted. We see the potential for organizations to attempt to assert influence either through contributions to the legislative process during consultative periods or to challenge the interpretation of new legislation or regulatory actions as they are being introduced, and where there is still an ability to influence ‘precedent’ (for example, we can anticipate such an imperative for industries such as the nuclear industry).
- Finally, there will exist organizations that need to react to legislative or regulatory action because of a lack of influence with legislative or regulatory bodies. The focus of their PMS will largely be upon managing the potential impact of regulation or law through political environmental scanning activities.

Not all firms undertake PMS at the same level of relationship engagement. This is partially a response not only to a lack of information,
experience or opportunity (i.e. the access needed to pursue PMS at Stages 5 or 4 is likely to be limited to a relatively few organizations in any political system), but also, arguably, to a lack of need. Obtaining access at Stages 5, 4 or 3 probably requires a high level of resource deployment, either financial or otherwise. Depending on the organization, this may (not) be justified. All organizations will want government actors to develop legislation or regulations, which are beneficial to their organizational objectives. However, for some, this process is critical, justifying the extra investment needed to potentially operate at Stages 4 or 5. For many, such an investment is less critical, so they focus upon earlier stages. In defending this perspective, we seek to understand both what factors influence strategic resource deployment decisions, and its practical nature. The different stages identified in Table 1 appear to suggest a number of key variables underpinning PMS. These variables take three forms: outcomes variables (i.e. the strategic gains that organizations hope to achieve by engaging in PMS); input variables (i.e. the resources that organizations are prepared to dedicate to their PMS activity) and context variables (i.e. the factors under-

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<th>Stage</th>
<th>Nature of PMS</th>
<th>Strategic rationale</th>
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<td>5</td>
<td>To influence the creation of a law or regulation in the favour of an organization</td>
<td>Organizations, or more probably their Chairmen and CEOs, are partners with governmental or regulatory agencies and are part of the process by which laws or regulations are created and developed. Stage 5 PMS represents very high level interaction with law makers, and very high levels of influence (see Richardson et al., 2007).</td>
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<td>4</td>
<td>To amend the characteristics or impact of a proposed law or regulation in favour of an organization</td>
<td>Organizations, or more probably their Chairmen and CEOs, are closely involved with definition of laws or regulations through consultative committees, providing information or guidance that shapes the detail of laws and regulations. Stage 4 PMS represents high level interaction with law makers, and considerable influence within the process.</td>
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<td>3</td>
<td>To revise or review the interpretation or implementation of a law or regulation in favour of an organization</td>
<td>Organizations are not involved in framing laws or regulations, but through challenges (i.e. either legal or through negotiation with regulatory authorities) to the application of the law or regulation they seek to influence its practical implementation in their favour, or minimize its implications. Stage 3 PMS witnesses the exercise of external power and influence through lobbying activity.</td>
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<td>2</td>
<td>To understand how change as a product of a law or regulation affects an organization</td>
<td>Organizations seek dialogue with law-makers or regulatory authorities to determine the nature of impending legal change. Not necessarily involving privileged access, but working ‘channels of communication’ to permit effective responses to change that the organization has not been involved in creating. Stage 2 PMS assumes management of these channels rather than an attempt to exert influence. This strategy constitutes managed reactivity through political environmental scanning.</td>
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<td>1</td>
<td>To manage perceptions of change to create a favourable impression of your organization</td>
<td>Organizations respond to changes produced by laws or regulations, and attempt to manage perceptions in their wider stakeholder community. Stage 1 PMS reflects a desire to create a favourable impression of the organization and its response to political environmental change. Again managed reactivity through political environmental scanning, but aimed at image control rather than effective management of processes.</td>
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pinning a rationale to engage in PMS). We hypothesize that differences in the relationship between the three types of variable explain the different stages in PMS. Hence we propose:

- **H1a**: Firms seek to exert the maximum possible level of influence over the legislative/regulatory process, and **H1b**: Firms seek to enter the legislative/regulatory decision-making process at the earliest possible opportunity.

- **H2a**: Firms experiencing strong contextual variables in their industry will seek to establish formal links with legislative/regulatory authorities to (1) improve the performance of resources and/or (2) to improve the effective management of these resources, and **H2b**: Firm’s resource deployments reflect the intensity of their PMS.

- **H3a**: Firms experiencing high levels of governmental/regulatory oversight in their industry will be strongly motivated to engage in high level PMS, **H3b**: Firms experiencing frequent governmental/regulatory-influenced change in their industry will be strongly motivated to engage in high level PMS and **H3c**: Firms operating in industries with high levels of government/regulatory investment will be strongly motivated to engage in high level PMS.

**Concluding remarks**

Within the resource-based view of the firm (Barney, 1991; Peteraf, 1993; Prahalad and Hamel, 1990) capabilities and their link to firm performance are critical. We explore the extent to which PMS might be considered a capability, or a core competence of the firm which actively enhances its competitive position in its market sector, and whether it may be considered a dynamic capability (Teece *et al.*, 1997). We discuss whether PMS fits within this group of routines, or it is a second-order capability that contributes critically to other dynamic capabilities of the firm. We suggest that further research should be undertaken with the explicit aim of establishing whether or not organizations use PMS as an active element of the strategic marketing process and whether the relationship engagement (LRE) levels of PMS, we identify, are congruent with different types of corporate behaviour or characteristics aimed at influencing legislative change and managing government stakeholders. Future research programmes on this relationship marketing topic might gather data from a wide sample of large organizations across the EU, and determine whether they recognize PMS as a significant element of their strategic marketing decision-making processes. If they do, we can then examine the extent to which PMS shapes and directs the strategic direction of the firm, or whether it is a second-order capability, focused upon assisting with the implementation of the strategy rather than shaping and directing it.

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