Ownership Competence: The Enabling and Constraining Role of Institutions

Abstract: Monteiro and Miranda (2022) argue that owners differ in their ability to select and work within a particular institutional environment, suggesting "institutional competence" as a dimension of ownership competence distinct from what we call governance, matching, and timing competence. We agree that institutions matter and welcome the chance to describe their role in detail. However, rather than treating institutional competence as a separate channel by which owners create value from their assets, we think institutional features can be modeled as "shift parameters" that moderate the effect of ownership competencies on outcomes. In developing this argument we reflect more broadly on the interplay between ownership competence and institutional uncertainty, noting that society at large benefits from individual-level ownership competence, ownership by some owners may cause harm to other owners, and property-rights enforcement and ownership competence are complements in generating private and societal benefits.

Introduction

Ownership in the strategy and entrepreneurship fields has largely been viewed as it has in economics and finance, namely as a solution to problems of misaligned incentives. These literatures see ownership rights given to managers or employees as a tool to motivate performance and to attract and retain talent. Our objective in writing "Ownership Competence" (Foss *et al.*, 2021) was to highlight a different, and arguably more economically significant role for ownership—one that the strategy and entrepreneurship fields should be particularly inclined to emphasize (Fitza *et al.*, 2009; Fitza *et al.*, 2017). Ownership is an economic function distinct from management or labor effort that involves determining how productive resources will be deployed under conditions of Knightian uncertainty. Moreover, ownership should be understood as a capability or competence that can be exercised with greater or lesser skill by individuals and groups. Ownership is what empowers and privileges the strategic beliefs and decisions of some actors over others in shaping what resources to own, what we call matching competence, how to own resources, what we call governance competence, and when to own resources, what we call timing competence. As ownership is effectively allocated to those

competent in wielding these rights over resources, ownership allocation becomes the primary driver of value creation in an economy.

In their recent comment on our paper, Monteiro and Miranda (2022) grant our paper "opens the 'black box' of ownership" by highlighting the role of competent judgment in coordinating resources through ownership rights. However, they argue that our paper leaves other black boxes unopened, in particular the role that the institutional context plays in granting and shaping the three ownership rights essential to competent resource coordination. In other words, use rights, appropriation rights, or transfer rights that we argue enable our three ownership competencies may have different implications for value creation in different institutional contexts. They therefore argue that identifying the institutional setting that maximizes the contribution of use rights, appropriation rights, or transfer rights to value creation is an independent fourth dimension of ownership competence, what they call "institutional competence," defined as the ability to "evaluate the characteristics of diverse institutional environments and assess the impact of formal and informal rules on the feasible options for deploying resources" (p. 8). Monteiro and Miranda (2022) claim that this competence is manifest in skillfully selecting *where* to own, but also in skillfully evaluating how such institutional factors influence the exercise of matching, governance, and timing competence.

We strongly endorse the effort to highlight institutional features and explore how they shape the exercise of competent ownership (see also Foss *et al.*, 2019). While we did not discuss institutions in detail, we did not entirely overlook their role in the effective deployment of ownership competence. On page 318 we note that "legal, regulatory, cultural, or other barriers may make the process of exercising that competence difficult. But absent various transactional hazards, such as small-numbers bargaining, entry barriers, asymmetric information, and legal or institutional restrictions on exchange, the opportunity to generate value from ownership competence disappears." And when discussing future

research opportunities, we write (p. 322): "With refined measures of ownership change (asset purchases and sales, corporate acquisitions and divestitures, reorganizations and restructurings), it should be possible to establish more precise relationships between turnover and economic efficiency, controlling for asset specificity and the institutional environment."

We admit that these brief observations do not fully explicate the role institutional features play in understanding ownership competence. However, we do not think that adding an entirely new competence to our model—one that, unlike the others, lacks an associated enabling property right—as well as several new paths of influence is the best way to analyze the role of institutions. Instead, the more theoretically parsimonious path forward is to highlight, as Monteiro and Miranda (2022) do at the end of their comment, the manner in which institutional features (including institutional uncertainty) shape the underlying property rights that define an owner's capacity to wield matching, governance, and timing competence.

In the comment that follows we make two points: (1) We argue that institutions have a pervasive, underlying effect on all three ownership competencies we identified in our paper and contend that the institutional environment is best treated as an aspect of governance, matching, and timing competence rather than the basis for a competence of its own. Adding it to the model opens the door to adding many other competencies without associated property rights. For instance, one could make a case for adding competencies related to demand, supply, technology, competitive interactions, and more. (2) We unpack and expand on three main arguments or questions implicitly raised by Monteiro and Miranda (2022) on the interplay between ownership competence and institutional uncertainty, namely that a) both specific owners and society at large benefit from ownership competence, b) ownership by some owners may cause harm to other owners, and c) property rights

enforcement and ownership competence operate as complements in generating both private and societal benefits.

Institutions environment and ownership competence

Our paper touched only in passing on the characteristics of the institutional environment. From this, Monteiro and Miranda (2022; p. 3) infer that "many of the insights brought by the ownership competence perspective seem to presuppose an institutional environment in which property rights can be exercised with relative stability, even if not perfectly." We agree that the extent to which property rights can be exercised and protected is central to a theory of ownership—indeed, the analysis of property rights, and how they are protected under different institutional conditions, is the main contribution of the economic analysis of property rights by Coase (1960), Alchian (1961), Demsetz (1983), Barzel (1997), and others that forms the basis of our theorizing (see also Foss *et al.*, 2022). However, rather than taking the ability to perceive the characteristics of the institutional environment as a distinct form of ownership competence, we think of institutions as having a pervasive, underlying effect on the shape of all three types of ownership competencies. The decision regarding where to own that Monteiro and Miranda highlight as an illustration of an institutional competence can also be incorporated into governance competence and is thus not usefully conceived of as a distinct ownership competence in and of itself.

By analogy, consider other attributes than ownership competence of individuals such as cognitive capability, openness to experience, bargaining skill, and trustworthiness. Being strong in these dimensions is useful for awareness of potential trading and productive activities, assembling teams, negotiating agreements, and managing employees—all of which enhance the likelihood that high levels of matching, governance, and timing competence will create value. Likewise, the ability to recognize when institutions are working well or poorly, and how to conduct business when institutions

are weak, affects the likely success of our three forms of ownership competence. In this sense, institutional features can be modeled as "shift parameters" (Williamson, 1991) that moderate the effect of ownership competencies on outcomes (as Monteiro and Miranda also suggest). Bjørnskov and Foss (2013) take this approach in examining how the institutional matrix moderates the relation between the ownership competencies of entrepreneurs and total factor productivity at the country level: more secure and better delineated property rights make it easier for entrepreneurs to identify, exchange and combine factors of production, increasing both the aggregate elasticity of substitution and total factor productivity. Boudreaux, Nikolaev, and Klein (2019) similarly treat the institutional environment as moderating the effect of individual traits on entrepreneurial actions and behaviors.

Regarding matching competence, in an institutional setting with limited enforcement of property rights (Nason *et al.*, 2022), a resource's value should be particularly contingent on who holds it. In a weak institutional context, resources are particularly valuable when held by owners with a reputation for keeping promises or who can leverage resources under their control by reducing transaction costs, e.g. by using strong personal networks (Gao *et al.*, 2017; Luo *et al.*, 2013). Hence a resource's value should be contingent on the owner's capacity to cope with or leverage the particularities of the institutional context in which the resource is held. In this way, resource value is owner-specific.

Note that the owner-specific value of resources differs from Williamson's idea of asset-specificity (Riordan *et al.*, 1985), with the latter focusing on problems tied to incomplete contracts and hold-up concerns when assets are sunk into a contractual relationship and thus less valuable outside that relationship (see also Schulze *et al.*, 2021). In contrast, owner-specificity of resources suggests that the value of a resource varies with who holds it, specifically, with the owner's ownership competence. For the very same resource some owner may see affordances that some other owner is simply unable to

see (Felin *et al.*, 2016), and variance amongst owners in seeing this value determines their ownership competence, in particular the matching competence portion.

Regarding governance competence, Monteiro and Miranda (2022) discuss the nineteenth-century introduction of barbed wire fencing in the United States as a technological innovation that “opened new possibilities for the exercise of ownership competence” (p. 13). We see barbed wire fencing as not a technological but a governance innovation, one that allowed land owners to secure their property rights by excluding cattle held by other owners from feeding on their grounds, thereby creating an incentive to invest into the land, to plant crops, and thereby generate and capture previously unpriced value in the land resources (Foss *et al.*, 2008; Zellweger *et al.*, 2022). Before barbed wire fencing was available, farmers faced serious constraints to economically exploiting the land they owned, because as Monteiro and Miranda (2022, p. 13) write, “a rival clan group may try to expropriate valuable resources.” We agree with this assessment, but see the adoption of barbed wire fencing as the skillful exercise of governance competence by farmers. In this example, governance competence unfolds by making value expropriation by other owners, those without legal and illegitimate economic rights, more costly. Hence, the institutional context of the late nineteenth century in the United States simply provides the background against which to illustrate the value of governance competence, reflected here in the adoption of barbed wire fencing, which secures both legal and economic property rights over assets, and creates incentives to search for and exploit unpriced value in resources. In other words, we see this process of creating a new means to define and enforce property rights as a fundamental exercise of governance competence, rather than a different form of competence.

A similar, more recent dynamic with institutional implications can be observed with the advent of blockchain technology.[1] Blockchain is fundamentally a new governance technology—one that supports the specification and protection of property rights and thereby enables the securitization and fungibility of assets, be these assets physical, digital, even creative. As a peer-to-peer ledger technology, this governance technology circumvents the need for other intermediary institutions, such as government bodies, regulators, or financial institutions in establishing and enforcing contractual relationships. In consequence, assets administered via a blockchain should be less susceptible to contractual problems, such as information asymmetries about quality and monitoring costs of holding assets, and should thus help mitigate trust issues between contracting parties (Cuypers *et al.*, 2021; Scheef *et al.*, 2022). The blockchain technology may thus help owners overcome institutional deficiencies that are today sometimes exploited by crony, even corrupt, mafia-like actors. Just as in the case of barbed wire fencing, the adoption of blockchain as a governance technology is best analyzed as the exercise of governance competence in supporting an owner's skills in value creation.

Finally, institutional dynamics also feature prominently in the exercise of timing competence. For instance, in their study of the *speed* of institutional change, measured as variation in the speed of pro market reforms across Chinese provinces, Banalieva, Eddleston and Zellweger (2015) found that owners varied in their capacity to deal with institutional change. Their findings suggest that those family owners that rely on stable relationships and close network ties, had greater difficulty in coping with high velocity change than firms held by other types of owners, such as widely-held firms, which have a stronger focus on efficiency and tend to be more adaptive to changing circumstances (Aguilera

[1] A blockchain is defined as a "cryptography-based decentralized system consisting of an ongoing list of digital records that are shared within a peer-to-peer network (i.e., a chain of blocks of digital records)" Lumineau F, Wang W, Schilke O. 2021. Blockchain governance—A new way of organizing collaborations? *Organization Science* **32**(2): 500-521.

et al., 2016; Verbeke *et al.*, 2010; Wright *et al.*, 2005). Hence, when the rules of the game change quickly and in unpredictable ways (what Higgs, 1997, calls 'regime uncertainty'), timing competence should be particularly important. In contrast, long-term orientation and a concomitant lack of timing skills, as evidenced by industrial foundations that hope to hold assets for an indeterminate time horizon (Thomsen *et al.*, 2004), should be functional in stable institutional settings, as for instance found in Scandinavia. We may thus speculate that under a stable institutional regime, governance competence may be particularly valuable, while under regime uncertainty matching competence and in particular timing competence should be of particular importance.

These examples show how institutions interact with governance, matching, and timing competence, often in subtle and complementary ways. We thus applaud Monteiro and Miranda's (2022) call for thinking more about how institutions relate to ownership competence. We concur that institutional features shape ownership competence yet view them as so central, as depicted in our examples, that attempting to isolate their effects as an independent ownership complicates our understanding of ownership competence more than it illuminates it.

The value of ownership competence under uncertainty

Monteiro and Miranda (2022) make an intriguing argument about uncertainty moderating the relationship between ownership competence and value creation. Our own take on uncertainty is that uncertainty is in large part simply what fuels the need for ownership and ownership competence. Uncertainty is what leads to fundamental disagreement and differing priors regarding beliefs about what to do with resources. As we argue: "ownership affords the control that is of particular value when acting under uncertainty. Absent uncertainty, ownership itself is unnecessary, as an actor can simply contractually compose the required control over assets, and obtain the foreseen returns" (p. 308). In the following we unpack and expand on two questions and an argument implicitly raised by Monteiro and

Miranda (2022) on the interplay between ownership competence and institutional uncertainty, namely: (1) Who benefits from exercising ownership competence: owners alone or society? (2) Does the exercise of ownership competence by one owner harm other owners? (3) We finally explore how ownership competence and enforcement of property rights function as complements.

Who benefits from exercising ownership competence: owners alone or society? Monteiro and Miranda (2022) argue that higher institutional uncertainty[2] renders ownership competence less valuable. They argue that under institutional uncertainty, owners may deploy ownership competence to extract value from their environment for their own benefit, but at the broader society's expense. Monteiro and Miranda (2022, pp. 8 & 9) are concerned that owners, such as mafia groups, shop for weak institutions to then exploit institutional deficiencies to their own benefit with harmful societal effects. Similarly, the so-called "pollution haven hypothesis" posits that multinational corporations search for locations with less stringent environmental regulations (Levinson *et al.*, 2008).

We certainly agree that ownership competence—much like managerial capabilities, entrepreneurial alertness, technological innovation, and other strategic actions—can be deployed for ends that are harmful to society (Luo *et al.*, 2013). Criminals, states, and rent-seeking firms can use their ownership competence to steal, oppress, or extract value. There is nothing unique about ownership competence in this regard (see Baumol, 1996 for the case of entrepreneurship). Institutional uncertainty may boost the success of entrenched owners, who are competent enough to secure

[2] Monteiro and Miranda (2022, p. 11) define institutional uncertainty quite loosely and suggest that such uncertainty "occurs when an incompatibility exists between the institutions at different levels of social analysis. For example, people may identify new uses for a resource, carrying out transactions whose features had not been imagined by lawmakers and regulators. (…) Incompatibilities may also exist within specific levels of social analysis, as the conflicts between the federal and state laws that regulate the emerging cannabis industry in the United States show." While this understanding of institutional uncertainty seems standard in the literature (e.g., Bylund & McCaffrey 2017), it is about lack of enforcement of certain property rights rather than about uncertainty per se. Indeed, throughout their paper Monteiro and Miranda (2022) tend to equate institutional uncertainty with a weak institutional environment, in particular weakly protected property rights.

favorable deals from the government and from other nonmarket actors in return for financial and political support (Commander *et al.*, 2022). Such owners' competence consists in knowing how to secure and use ties to the political elite (Casas *et al.*, 2021) or the military (Hiatt *et al.*, 2018), to access resources, information, and support that can help these owners mitigate uncertainties in the political and economic environment (Hiatt *et al.*, 2014; Lee *et al.*, 2017; Mizruchi, 1992). While we acknowledge the possibility of an exploitative use of ownership competence, we emphasize that not all nonmarket strategies pursued by owners need to be exploitative (Webb *et al.*, 2009). Rather, it is conceivable that the exploitative effect dominates the value creating effect when ownership competence is deployed under serious institutional deficiencies.

Does the exercise of ownership competence harm other owners? Relatedly, Monteiro and Miranda (2022) fear that the exploitative use of ownership competence suppresses the entry of new owners who see their talent as owners being underused, with serious costs for these owners and ultimately also the broader state. In other words, the behavior of a small number of entrenched owners could limit the ability of potential new owners to benefit from their ownership competence. Potential new owners are thus systematically constrained in their deployment of ownership competence because a weak state is unable to provide the institutional stability that would motivate business activity among them. Monteiro and Miranda (2022, p. 14) illustrate this argument by suggesting that "the lack of basic legal guarantees fundamentally changes the nature of institutional uncertainty, creating a scenario in which some people may face more constrained sets of potential ways to exercise their ownership competence than others." Monteiro and Miranda (2022) thus call for a strong Leviathan to support the exercise of ownership rights for the many, and not just for the few. We agree that under weak protection of property rights for *any* owner, ownership competence per se may not be enough to create value. Whether empowering the state to enforce property rights to protect particular owners against

others alleviates this problem requires further justification—for example, it could be the case that state enforcement encourages cronyism and further consolidation of ownership claims among politically connected actors (Klein *et al.*, 2022).

Ownership competence and enforcement of property rights are complements. We fully agree with Monteiro and Miranda's (2022) call for a more subtle analysis of the connection between institutional uncertainty, ownership competence and value creation. If we take institutional uncertainty to mean uncertainty about the strength of enforcement of *titles* to ownership, such as when legal and market supporting institutions in the form of property rights and rule-of-law are missing or impotent (Baird *et al.*, 1984; Khanna *et al.*, 2000; Peng *et al.*, 2009), then institutional uncertainty could, as Monteiro and Miranda suggest, *decrease*, not increase, the value of ownership competence. Value creation results from a bundle of alienable assets (physical capital, land, IPR, etc.), non-alienable assets (human resources), and non-traded resources (many capabilities) skillfully composed through ownership competence in complementary patterns. If alienable assets are less protected, they may be less able to contribute to value creation (e.g., think of land resources that may be confiscated by the state, war lords, etc.). Since the value of ownership is imputed from its contribution to value creation, ownership competence will be less valuable. Thus, ownership competence and effective enforcement of ownership are complements: the more effective enforcement, the more valuable ownership competence. We thus propose that the combination of sufficiently guaranteed property rights in conjunction with ownership competence should produce a flourishing socioeconomic environment, one with high levels of value creation for all asset owners and for society at large.

Conclusions

We welcome Monteiro and Miranda's (2022) comment on our paper. As outlined above, we question the need for theorizing a fourth independent ownership competence. However, we agree that

the impact of institutions and uncertainty on ownership competence and the effect of ownership competence on value creation may be more subtle than theorized in our paper. There are both positive and negative effects of ownership competence on value creation that need to be unpacked more carefully, both theoretically and empirically. As Monteiro and Miranda suggest, negative effects are particularly likely to arise when the institutional protection of ownership is weak. Future studies may shed further light on the exact institutional settings under which the beneficial versus the detrimental effects tied to ownership competence dominate. For such research endeavors it appears important to distinguish more clearly between levels of analysis in the study of ownership competence's economic effects. Specifically, we see a need to expand the level of analysis from a single asset held by an owner or perhaps portfolios of assets, to societal level to consider more macro-level implications of ownership competence under differing institutional regimes. To conclude, Monteiro and Miranda's positive reaction to our article, as well as the specific points they raise, illustrate the need for more research on ownership within the strategy, international business, and entrepreneurship literatures. More generally, these literatures need to take a more subtle and nuanced approach to thinking about institutions, ownership and value creation.

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