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Mutual Forbearance: The Role of Intra-Firm Integration and Rewards

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Firms frequently find themselves in competition with the same competitors in multiple product and geographic markets. In such cases a firm may cede control of one product market to a competitor, in exchange for that competitor's acquiescence in another product market --- an inter-firm strategy of mutual forbearance. Despite recently increasing attention given to mutual forbearance strategies (MFS) by strategic management researchers, researchers have virtually ignored the internal arrangements necessary to implement such strategies. The present discussion thus attempts to refocus future research on MFS. Drawing on the organizational design and strategy implementation literatures, we (1) argue that the design of the mutual forbearance competitor may pose some unique implementation challenges for the firm, (2) theorize about the administrative mechanisms that we expect to characterize firms which implement MFS, and (3) suggest that, to the extent that future researchers do not model the qualities theoretically necessary to implement MFS, the full competitive consequences of MFS will not be appreciated.

Firms often compete simultaneously against the same rivals in multiple product and geographic markets. For example, Northwest Airlines faced significant overcapacity on its routes to the West Coast in the early 1990s. To mitigate this excess capacity, Northwest lowered fares to certain West Coast markets, many of which were critical to Continental Airlines. In reaction to this fare change, Continental lowered its fares in the Minneapolis market --- Northwest's most important market, both symbolically and financially. Then, having apparently recognized Continental's competitive signal, Northwest responded by increasing its West Coast fares to their original levels (Wall Street Journal, 1990). This series of interactions ended in a state of mutual forbearance, that is, the "tacit collusion as a consequence of firms competing in many markets and the resulting increase in their interdependence" (Jayachandran, Gimeno & Varadarajan, 1999: 51). Karnani and Wernerfelt (1985) provide an early, conceptually related example. They reported that BIC, in an effort to halt Gillette's incursion into the disposable pen market (BIC's core market), counter-attacked by entering the disposable razor market (Gillette's core market) with the goal of tacitly colluding in the two markets. The competitive phenomenon illustrated above, and seen in a variety of industries such as automobile tires (e.g., Goodyear vs. Michelin) and pet food (e.g., Ralston Purina vs. Mars) (Collis, 1995) is referred to as mutual forbearance --- the ceding of control of one product or geographic market to a competitor in exchange for that competitor's acquiescence in another market. This may occur when two or more competitors, operating in multiple common markets, have sufficient resource endowments to pose a credible threat to each other. Recognizing the possibility of mutual harm, they act to cooperate.

Strategic management and marketing researchers have recently begun to view multiple market presence as potentially important to an understanding of both inter-firm competitive dynamics and firm performance (cf. Barnett, 1993; Baum & Korn, 1996; Boeker, Goodstein,

Stephan & Murmann, 1997; Gimeno & Woo, 1996; Jayachandran, Gimeno, & Varadarajan, 1999; Young, Smith, Grimm & Simon 2000). Despite the increasing attention, however, theorizing and empirical research have tended to be limited to an *extra*-organizational perspective. As a consequence of the relative inattention to *intra*-organizational processes and systems, researchers have implicitly assumed that there is sufficient coordination between product and/or geographic market managers within firms such that multipoint contact results in mutual forbearance. That is, firms have been assumed to be capable of pursuing mutual forbearance strategies (MFS) whenever they confront the same rivals in multiple, common markets. Although some exceptions to this can be found in the literature, these are limited to important, but relatively brief statements alerting researchers to consider the internal arrangements necessary to implement MFS (cf. Boeker *et al*, 1997; Jayachandran *et al*, 1999).

We suggest that, in order to appreciate the scope and potential robustness of MFS, substantially greater attention needs to be devoted to the structures and systems associated with their successful implementation. We begin this discussion with the observation that coordination *between* firms often requires coordination *within* firms, and draw particular attention to the intra-firm arrangements that we expect are associated with the successful implementation of MFS. Our thesis is that a firm's success in formulating and implementing MFS is greatly influenced by (1) integrating mechanisms which *enable* intra-firm cooperation and coordination, and (2) reward and control systems which *induce* intra-firm cooperation and coordination. Throughout this discussion we attempt to show why many potential multipoint competitors should not be expected to seek or realize the potential firm-level benefits of MFS. Thus, while the studies cited earlier indicate that MFS may be pursued in a variety of markets and industries, the ability and desire to pursue these strategies may be limited to firms with certain specifiable

characteristics. Our discussion, following a brief overview of the mutual forbearance literature, develops and articulates principles that make these characteristics predictable.

MULTIPOINT COMPETITION, MUTUAL FORBEARANCE AND PERFORMANCE

Early research on multipoint competition was conducted by industrial organization economists who noted that while mutual forbearance implies the presence of multipoint competition, multipoint competitors do not necessarily mutually forbear. This observation emerges from more general arguments about the industry conditions most likely to result in collusion among firms. For instance, in one of the earliest discussions, Stocking (1955) suggested that oligopolistic conditions are required in order for multimarket firms to recognize interdependence with one another. This was later empirically supported by Scott's (1982) report of mutual forbearance activity only among firms with multimarket contacts that were also operating in highly concentrated industries. Strategic management researchers have subsequently suggested that mutual forbearance requires a variety of industry contextual conditions such as reciprocal dominance among rivals across markets (Oster, 1990; Ma, 1998) and market overlap (Chen, 1996). (See Jayachandran *et al* (1999) and Ma (1998) for reviews of multimarket competition and MFS, respectively).

Notably, the early research in economics is replete with inconsistent and/or nonsupportive findings for a relationship between multipoint competition and firm performance (Alexander, 1985; Heggstad & Rhoades, 1978; Mester, 1987; Rhoades & Heggstad, 1985; Scott, 1982; Strickland, 1985). However, the more recent strategic management research tends to be more sanguine about the presence and effects of multipoint competition. For example, Barnett (1993) observed that firms within the same strategic groups are most likely to mutually forbear, while firms tend not to mutually forbear with strategically dissimilar rivals. Boeker *et al* (1997) found that firms are less likely to exit markets when they compete with firms that are also

their rivals in other markets. More recently, Stephan and Boeker (2001) distinguished between multimarket contact and multimarket competition. They suggest a curvilinear relationship between the two, proposing that multimarket contact may *increase* competition by both providing models for potential entrants and legitimizing behaviors, but only up to a point. Beyond some level of multimarket contact, they suggest that multimarket competition results in the recognition of interdependence among competitors and consequently, the lessening of competition among multimarket competitors. Collis (1995) has also suggested that multimarket contact may increase competition under certain circumstances. He posited that when two firms each compete in markets A and B, one firm's strength in market A may allow it to hurt the other firm's related business in market B. Thus, the latter firm would be expected to compete aggressively in market A in order to reduce this spill-over.

In the U.S. airline industry, Gimeno and Woo (1996) reported that the presence of multipoint competition resulted in competitive de-escalation, thus supporting the mutual forbearance thesis. Baum and Korn (1996) reported that multipoint competition may result in greater industry stability and competitor predictability. Finally, Young *et al* (2000) reported that multimarket competition reduces the number of competitive interactions between firms. The Table presents the key studies on MFS, none of which have investigated a firm's implementation capabilities.

(Table About Here)

To briefly summarize the research findings to date, successful MFS may lead to market power (Scott, 1982), reduced rivalry and increased returns (Baum & Korn, 1996; Gimeno & Woo, 1996), and decreased rates of entry and exit (Barnett, 1993; Baum & Korn, 1996; Boeker *et al*, 1997). However, despite much anecdotal evidence (cf. Karnani & Wernerfelt, 1985), the intuitive appeal of the mutual forbearance logic, and encouraging recent research, the boundary

conditions for successful MFS have not been sufficiently specified. Recently, Korn and Rock (2001) began to address this issue by noting that the relationship between multimarket contact and competition is contingent on a variety of factors, including the resource profiles and demand functions of multimarket competitors (Berhneim & Whinston, 1990). Others have suggested that the cognitive limitations and the ability of managers to anticipate the likely responses of competitors affect the desire and ability of managers to mutually forbear (cf. Clark & Montgomery, 1999; Porac, Thomas & Baden-Fuller, 1989). To extend this discussion, we suggest that it is critical to discriminate between firms that are most and least likely to implement MFS.

TOWARD AN IDEAL TYPE MUTUAL FORBEARER

Discussions by Chen and his colleagues (Smith, Grimm, & Gannon, 1992; Chen & MacMillan, 1992, Chen & Miller, 1994; Chen, 1996) suggest that multimarket rivals require both an awareness of multimarket interdependency and the motivation to engage in multimarket interactions (e.g., mutual forbearance).¹ We propose that there is good reason to expect much variation in managers' recognition of mutual forbearance opportunities. Moreover, even when they recognize the interdependency of businesses lines, managers may vary significantly in their responses to interdependencies as a consequence of the reward systems they face. Consider, for example, the simplified case of two hospitals that compete with each other in two business lines: radiology and children's medicine. Market segmentation may benefit both hospitals. This may result because Hospital A has the resources and capabilities to be dominant in radiology, and Hospital B is similarly equipped to dominate the children's medicine market. Such a situation offers the potential for both firms to mutually forbear and divide their markets. However, mutual forbearance can only occur if, for example, Hospital A's children's medicine department gives up its market share and Hospital B's radiology department does the same. Whether this occurs is

dependent on several factors. First, by definition, these competitors must be in multiple, common markets. If Hospital A were instead a specialty radiology clinic, it would have no market share in children's medicine to trade-away (Greve & Baum, 2001). Second, none of the hospitals' business lines may be so dominant (e.g., with substantially lower costs or more valuable capabilities) that market forces would favor one competitor over the other, thus eliminating any incentive for the dominant firm to acquiesce. Third, mutual forbearance depends on whether the radiology and children's medicine departments *within* both hospitals are sufficiently integrated *and* induced to cooperate. The extent to which these conditions are met is portrayed in the Figure, which guides our discussion of the Mutual Forbearer --- a configuration of organizational systems that is well suited to recognize and pursue mutual forbearance opportunities.²

(Figure About Here)

Integrating Mechanisms

Considerations of integrating mechanisms have a long history in organization theory, and regularly evoke Lawrence and Lorsch's (1967) distinction between differentiation and integration. Differentiation refers to differences among subunits with respect to goal orientation, time orientation, and interpersonal orientation. Integration refers to the collaboration among units necessary to achieve coordinated effort within the firm (Lawrence & Lorsch, 1967). These concepts have been fundamental to the information processing perspective of Thompson (1967) and others (Galbraith, 1973; Galbraith & Kazanjian, 1986) who have identified a variety of structural mechanisms that can be used to integrate the activities of multi-unit organizations. Each of these mechanisms is based on the premise that integration comes from coordination, and coordination requires sufficient, shared knowledge about the firm's activities and environment.

Thus, these structural mechanisms are intended to enhance cross-unit information processing, thereby facilitating integration.

Burton and Obel's (1998) extensive synthesis of the organization design literature also adopted the information processing perspective, and noted four mechanisms to achieve coordination and control – formalization, centralization, lateral structures, and incentives. They suggest that these first three mechanisms are intended “to make sure that enough relevant information is available at the right time to be able to make the right decisions” (Burton & Obel, 1998:76). Incentives help to ensure that the various enabled subunits have the motivation to make the right decision subunits. Thus, given their distinct purposes (i.e., enabling vs. motivating), we treat rewards separately in the next section. Here we consider formal and informal integrating/enabling mechanisms.

With respect to formal integrating devices, Bourgeois and Brodwin's (1984) discussion of strategy implementation types is informative. They developed the “Commander Model” archetype in which the CEO acts as a “rational actor” with “access to complete information” (1984:243). The Commander (i.e., general manager) is able to act as a unitary decision maker for multiple business units, with the ability to trade performance in one unit for greater performance in another. This perspective is more recently revealed in Shafer and Hillman's (2000) authoritative corporate structure, which they suggest mitigates intra-firm conflict when implementing business government strategies. These discussions, as seen in our hospital illustration, can speak to the implementation of MFS. Specifically, we expect mutual forbearance to be facilitated when, in each hospital, the two department heads report to a common superior (e.g., Vice President of Community Health) who is able to both identify the opportunity to mutually forbear, and to identify and reward for the decisions that each department head makes. Of course, the following question must be answered in the affirmative:

"Does the common superior actively influence the behaviors of subordinate business units?" This question is critical since the extent to which hierarchical relationships may be characterized as centralized is likely to affect coordination across business units (Gupta, 1987). We expect that, to the extent that the Vice-President of Community Health centralizes decision-making, the likelihood of mutual forbearance is greater. This implies that hospital *corporate level* managers in this example are attempting to realize the scope economies of diversification that product/service managers are, by themselves, unable to realize. Thus, the initial task of corporate management is diversification into businesses that create opportunities to pursue MFS. Corporate management must then ensure the development of systems (e.g., structure and rewards) that facilitate and encourage business managers to jointly pursue MFS. We expect that corporate management of Mutual Forbearers will fulfill these roles.

Other structural qualities are also expected to affect the implementation of MFS. For instance, the ability to coordinate activities between individuals, functions, and business units has been shown to be inversely related to a manager's span of control, contingent on the routinization of the manager's activities. In general, as span of control increases, so too does the gap between information processing capacity and demands (Galbraith, 1973). For the *potential* mutually forbearing business or businesses (i.e., multipoint competitors), this is expected to result in management's reduced ability to coordinate non-routine activities across product or geographic markets.

Similarly, information processing demands are likely to exceed capacity as a function of organizational hierarchy. This results because hierarchy has deleterious effects on the firm's ability to monitor and coordinate activities across businesses (Galbraith & Kazanjian, 1986). Again, control loss results. In our earlier example, in which two business units have a common immediate superior, coordination is relatively unchallenging. However, as additional

hierarchical levels are introduced between a common superior and business units (that share common competitors), coordination between these business units is impeded. Consequently, information about how and when to mutually forbear is expected to be distorted and/or untimely.

The importance of environmental scanning is highlighted in the work of Smith and his colleagues, who have shown much variability in a firm's ability to interpret the tactical and strategic actions of competitors (Smith, Grimm, Gannon & Chen, 1991). Since MFS can only occur when two or more firms recognize the opportunity to pursue them, we suggest that our illustrative hospitals will approximate the ideal type to the extent that formal and informal mechanisms facilitate the intra-firm sharing of information. Since much has been written about the formal mechanisms commonly recognized to facilitate information sharing (cf. Thompson, 1967; Galbraith & Kazanjian, 1986), these are only briefly mentioned here. Among these are specialized boundary spanners, task forces, integrating committees, information systems, and matrix structures. Each of these design elements may increase the breadth, frequency, and quality of information shared across business units (Daft & Lengel, 1986). It is also likely that the increasing improvements in information processing technology, by reducing the "transacting costs" among units within the firm, will enhance intra-firm coordination (Gupta & Basu, 1989). Such integrating devices are expected to increase recognition of potential mutual forbearance opportunities across distinct product lines.

With respect to more informal integrating mechanisms, Ghoshal and Bartlett (1990) argued that informal relationships influence the exchange of products, information, and technology in diversified multinationals. Likewise, Hansen's (1999) study of a consulting firm revealed the impact of "weak ties" on knowledge exchange --- a form of intra-firm integration. These arguments are consistent with a growing body of social network research (Burt, 1992; Coleman, 1990; Granovetter, 1973) that focuses on the web of informal relationships within

firms, and their impact on information sharing, coordination, and cooperation. From our perspective, these relationships also create a medium by which integration can take place, thus increasing the capacity to pursue MFS.

The preceding discussion has identified a variety of integrating factors that we suggest impact a firm's ability to pursue MFS. Interestingly, while these integrating factors are well recognized in the organizational design literature, they have not been explicitly incorporated into research on the implementation of MFS. This absence, we propose, has resulted in the inability to distinguish between firms which are most and least capable of implementing MFS. Based on our discussion above, we propose:

Proposition 1: The degree to which formal and informal integrating mechanisms are present in multipoint competitors is positively associated with their *ability* to mutually forbear.

Rewards for Cooperation

By way of analogy, integrating mechanisms are akin to a country's highway or telephone systems. These systems only serve to bring willing individuals or communities together; their use is not ensured. Likewise, the formal and informal integrating mechanisms described above merely make internal coordination possible, not desirable. This observation highlights an important limitation of past mutual forbearance research, namely, little attention has been given to the incentives to cooperate across businesses within the firm. This is important since we are not yet able to distinguish between two types of multipoint competitors (1) those that are integrated across businesses but lack incentives to cooperate internally, and (2) those that are sufficiently integrated and induce intra-firm cooperation through rewards. As suggested by various theorists (Bourgeois & Brodwin, 1984; Hill, Hitt & Hoskisson, 1992; Salter, 1973), the rewards faced by division managers have a powerful effect on a division's willingness to engage in firm-optimizing, cooperative behaviors.

Specifically, Salter's (1973) early discussion reminds us that, in the context diversified firms, corporate management is responsible for determining whether the costs associated with the cooperative actions of one business unit are justified by the benefits to the other units they are intended to help. Thus, Salter suggested that inter-business unit cooperation could be enhanced by corporately designed incentive systems that reward a cluster of business units, using traditional performance metrics (e.g., ROA, ROI), rather than the unique performance of individual business units. He also reported that discretionary reward systems, rather than formula-based systems, might induce inter-unit cooperation. Such a reward scheme, by encouraging judgments about cooperative behavior, partially mitigates corporate management's inability to assess the unique contribution to firm performance of inter-related business units. Govindarajan and Fisher (1990) also identified business unit control mechanisms that encourage inter-unit resource sharing. They suggested that rewards based on behaviors (measured either objectively or subjectively) are to be favored over outcome-based rewards when two conditions are met: (1) It is difficult to reliably and validly assess the outcome of a business unit's actions, and (2) actions are observable and can be determined to be appropriate. These conditions are likely to be present in the case of potential mutual forbearers since two or more business units in a firm must cooperate with each other. For example, Hospital A's children's medicine department may act in a way that is expected to help radiology compete against their common multipoint competitor (i.e., Hospital B). Despite this assistance, Hospital A's radiology business may fail to meet its goals. For instance, Hospital B's managers may misperceive or choose to ignore the opportunity to mutually forbear. Under this scenario, Hospital A's children's medicine business would be penalized for outcomes beyond its control (i.e., the performance of the two business lines cannot be assessed independently). In order to avoid this transference of

risk, and due to expected performance ambiguities, children's medicine ought to be rewarded for those *behaviors* that increase the likelihood that radiology's competitors will acquiesce.

Related to the choice of behavior-based or outcome-based rewards is whether corporate management relies on subjective and/or objective assessments of business unit performance. Hill *et al*'s (1992) distinction between intra-organizational competitive and cooperative M-forms is instructive here. They suggested that the performance ambiguity problem endemic to cooperative M-forms can be mitigated by expanding the breadth of information available to corporate management. They argued that cooperation between business units can be enhanced when subjective measures of division performance (e.g., perceived cooperation between divisions) are considered in corporate resource and reward allocation decisions. Such measures may ensure that business unit managers (e.g., of children's medicine), who cooperate with their counterparts in other business units (e.g., of radiology), will not *necessarily* be punished if their performance falls short according to conventional measures of financial performance. Rather, corporate managers of firms that pursue MFS may partially rely on subjective judgments of business unit managers' effectiveness during the performance evaluation process. It is important to note that these subjective judgments may not replace outcome or behavioral data (both of which may be subjective), but rather, may supplement these data (Hill *et al*, 1992). By doing so, the division manager may be rewarded for cooperating with other business units, even if those other units ultimately fail.

We should also consider the managerial challenge of selecting reward criteria when *both* behavior and outcome measures are difficult to assess reliably and validly at the business unit level. In this scenario "integrated rewards," which bond business unit managers to the interests of the firm, must be considered (Hauser, Simester & Wernerfelt, 1994). Alternatives here include significant short-term and long-term rewards for corporate (not business) performance.

If combined with the monitoring of behaviors, even if imperfect, the free-rider problem often associated with these types of rewards may be mitigated (Wageman & Baker, 1997). To the extent that such integrating rewards are present in multimarket competitors, we may be more likely to observe business unit managers cooperating with their counterparts in other business units. We expect that this will increase the likelihood that firms will pursue MFS.

Finally, a substantial body of research has documented the impact of intrinsic rewards and their impact on pro-organizational behaviors (cf. Osterloh & Frey, 2000). In the strategy literature, Govindarajan and Fisher (1990) suggested that non-financial rewards might overcome a business unit manager's proclivity to engage in individual wealth-seeking at the expense of the firm. They speculated that normative control systems might be effective in reducing this likelihood. Thus, resulting from norms of reciprocity (Blau, 1964), Johnson & Johnson's surgical-needle company voluntarily shares its metal-polishing technology with its coronary implant company (O'Reilly, 1994). Likewise, recent research suggests that such cooperation may result from individuals' "identification" with the broader organization, rather than their own subunits (Dutton, Dukerich & Harquail, 1994; Dukerich, Golden, & Shortell, forthcoming; Fisher, Maltz & Jaworski, 1997). Referring to our hospital illustration, the intrinsic rewards that result from intra-firm cooperation may be sufficient to encourage cooperation between radiology and children's medicine. Therefore, when behavioral and outcome controls are inadequate, or are simply cost prohibitive, firms may turn to normative control systems in order to induce the cooperation we believe is necessary to implement MFS. Moreover, because opportunities to mutually forbear may be non-routine, thus rendering formal control systems ineffective or too costly, a culture of cooperation may be particularly valuable.

In summary, the failure to explicitly consider the reward systems of multipoint competitors has prevented researchers from distinguishing between those firms which are and

are not inclined to pursue MFS. In order to more clearly understand the mutual forbearance phenomenon, such systems must be incorporated into the design of future studies. Based on the comments above, we propose:

Proposition 2: The degree to which formal and informal incentive systems are present is positively associated with *efforts* to mutually forbear.

Relative Performance

The Figure reveals the predicted consequences when only integrating mechanisms are present, when only incentives are present, when both are absent, and when both are present. Conceptually, Quadrant 1 firms most closely approximate the Mutual Forbearer. In contrast, Quadrants 2, 3 and 4 represent different forms of divergence. For example, a Quadrant 2 firm's product managers may find it difficult to pursue coordinated multimarket behaviors, despite their desire to do so. These firms have subunit incentives to coordinate behavior for the greater good of the organization, but few integrating capabilities to facilitate this. Thus, even when mutual forbearance opportunities are identified, in the short term information flowing between units is likely to be untimely, unreliable, and/or inaccurate. In general, information-processing requirements exceed capabilities, and this can only be corrected with *subsequent* structural changes that may be pursued due to rewards to business managers associated with MFS.

Quadrant 2 firms may also lack influential central decision-makers who oversee the various business-units of the firm. To the extent that effective coordination occurs, we would expect it to be based on *ad hoc* agreements and coordination between willing business unit managers. In general, while integrating mechanisms in Quadrant 2 firms may only rarely be totally absent (e.g., even informal conversations among business managers may serve to

integrate), due to their less developed integrating capabilities, the relative likelihood of their implementing MFS is expected to be lower than that of Quadrant 1 firms.

The absence of meaningful incentives to cooperate is found in Quadrants 3 and 4. For example, if Hospital A were characterized by the conditions found in Quadrant 3, we would not expect its children's medicine department to cooperate with its radiology department (i.e., give up market share in children's medicine for a greater benefit earned by radiology). In short, incentives for it to do so are lacking, resulting in distributive conflict (cf. Shaffer & Hillman, 2000) and radiology's lost opportunity. In general, Quadrant 3 firms are expected to have a low likelihood of exploiting potential and recognized mutual forbearance opportunities, even when sufficient integrating (i.e., enabling) mechanisms exists; resulting from reward systems that are not sensitive to coordinated behavior, such integrating mechanisms will be seen to have little or no value to the business units.

In contrast to Quadrant 2 firms, in which business units are rewarded for cooperating with each other, business units in Quadrant 3 firms have no incentives --- and perhaps disincentives --- to cooperate. As suggested, business unit managers in Quadrant 2 firms may attempt to cooperate with each other, despite the current lack of integrating capabilities. Quadrant 3 managers will neither be inclined to pursue mutual forbearance opportunities, nor will they be inclined to develop the integrating capabilities necessary to do so at a later date. Thus, compared to Quadrant 2 firms, Quadrant 3 firms are less likely to successfully pursue MFS.

Finally, we expect that Quadrant 4 firms are the least likely to pursue and implement MFS. Modifying the hospital example slightly, we may find here that both the heads of radiology and children's medicine, as well as top management team members, are ignorant of the possibility of trading market share in children's medicine for market share in radiology. In

addition, even if this opportunity were to be recognized, inter-departmental coordination is inadequate. Therefore, we might observe misperceived competitive signals across both sets of business lines. Further decreasing the chance of implementing a strategy of mutual forbearance, Quadrant 4 organizations are expected to lack the incentives necessary to induce intra-firm market tradeoffs. Based on the notion that implementation success implies the capability and desire to mutually forbear, the discussion above leads to our final, integrative propositions:

Proposition 3A: The degree to which firms deviate from the Mutual Forbearer (i.e., Quadrant 1 firms) is negatively associated with success implementing MFS.

Proposition 3B: MFS are most likely to be effectively implemented by Quadrant 1 firms, followed by Quadrant 2, Quadrant 3, and Quadrant 4 firms, respectively.

REDIRECTING RESEARCH

We have argued that integrating and reward systems may limit the desire and ability of multipoint competitors to pursue MFS. Despite these theorized limiting conditions, we must acknowledge that the potential to pursue MFS has been realized in a variety of industries, and thus is important from an economic and strategic perspective. In addition to the frequently cited airline studies (e.g., Gimeno & Woo, 1996, 1999; Baum & Korn, 1999), empirical research on MFS has examined supermarket chains (Cotterill & Haller, 1992), the telephone industry (Barnett, 1993), manufacturing (Hughes & Oughton, 1993), banking (Heggestad & Rhoades, 1978; Ma & Jemison, 1994), and hospitals (Boeker *et al*, 1997). Indeed, MFS involve the segmenting of markets along product lines and/or geographic markets. Therefore, even single business firms that operate in multiple geographic markets may have the potential to pursue MFS. Whether MFS are common in these settings, however, ultimately depends on the presence and interaction of intra-firm integrating mechanisms and rewards at the level at which multipoint

opportunities exist (e.g., at the product line level within single business firms, or at the SBU level among a group of diversified firms).

Second, though many firms may regularly encounter the same rivals in multiple markets, our arguments suggest that the likelihood and success of pursuing MFS should be expected to vary substantially. Specifically, we must consider the implications for a multimarket firm when a firm approaches the Mutual Forbearer, but its multimarket competitor does not. In a multimarket context, Baum and Korn (1999) discuss familiarity with competitors as influencing expectations of competitor responses. Following their reasoning, we suggest that both competitor intelligence and the ability to anticipate competitor reactions require some knowledge of the integrating and reward systems of one's multimarket competitors. Like the tango, MFS take two partners, and a firm's potential partner may be unable to dance or may choose not to do so. The later case may occur when one of the multipoint competitors is sufficiently strong in each of its markets, thus relying on its capabilities, rather than inter-firm cooperation, for success. We have suggested that one firm must not dominate all others in each of their common markets, and importantly, that *both* partners must have *both* the requisite reward and coordination systems for mutual forbearance to result. And, even when two partners are internally aligned to tacitly collude, the presence of a third competitor that is either unable or unwilling to cooperate may destroy mutual forbearance opportunities for all competitors (Greve & Baum, 2001). This may occur when a multipoint firm competes with a single-point competitor, and may consequently ensure that multipoint competitors do not collude. Thus, our arguments about internal systems compel researchers and managers to consider whether multimarket competitors and other firms in their market (e.g., both Hospitals A and B, *as well as* other local hospitals) sufficiently approach the Quadrant 1 Mutual Forbearer described here.

Third, our arguments imply that MFS are not for everyone, despite market opportunities. For instance, firms may face operating interdependencies across businesses that preclude the pursuit of MFS (e.g., a hospital may need to operate a radiology lab *in order to* provide children's medicine services). Alternatively, consider the case of a functionally organized multipoint competitor (e.g., a single business firm, but in multiple geographic markets), which has historically operated with a mechanistic structure. Although the mechanistic design may be most appropriate for this functionally organized firm (cf., Mintzberg, 1979), the rigidity and formalization of the mechanistic organization may impede the firm's ability to quickly coordinate across multiple businesses. Corporate managers in such a firm would be faced with the question of whether to substantially change the firm's heretofore appropriate structure in order to facilitate the implementation of MFS. They may correctly choose not to do so, reducing the firm's ability to pursue MFS.

Similarly, we believe it will prove valuable for researchers to distinguish among geographically, related, and unrelated diversified firms. Firms which are either geographic or related diversifiers, or some combination of the two (e.g., airlines, banks, consumer products firms) have tended to be the subject mutual forbearance research. Based on the arguments advanced here, this was to be expected. Compared to unrelated diversifiers, such geographic and related diversifiers are more likely to have the integrating and reward systems of the Mutual Forbearer (e.g., unitary control, integrated rewards) (cf. Hill *et al*, 1992). These systems may be at odds with the demands of unrelated diversifiers, and it may be unwise for unrelated diversifiers to design their systems in order to avail themselves of mutual forbearance opportunities. We expect that researchers who include such organizations in their samples, that is, those firms with opportunity but not both capability and motive to implement MFS, will get a

distorted picture of the mutual forbearance phenomenon. Simply put, intra-firm arrangements cannot be taken for granted.

Lastly, since mutual forbearance opportunities may be present in several consequential industries (e.g., banking, hospitals, grocery), we must acknowledge the social welfare and antitrust implications of MFS. At its core, mutual forbearance is collusion between firms. Tacit collusion has regularly been shown to decrease social welfare (e.g., prices may be kept artificially high) (Scherer, 1980)), and it would be Pollyannaish to suggest that firms may not be attempting to maximize their returns at the expense of their customers. To the extent that MFS are in fact anticompetitive, and thus lessen social welfare, it is important for researchers and policy makers to understand how common such strategies are, as well as the conditions under which they are likely to be pursued. To the extent that the arguments in this paper are convincing, they may focus policy makers' attention to those settings and competitor interactions that are ripe for tacit collusion.

In conclusion, recent observations by Baum and Korn (1999) about interactions *between* competitors mirror our central arguments about intra-firm cooperation. They write, “Such coordination across markets and time is taken for granted in theoretical accounts of multipoint competition and is the main theoretical basis for expecting mutual forbearance” (1999: 252). We have suggested that coordination within firms has also been taken for granted, or ignored, to the detriment of an accurate understanding of MFS. Thus, we have attempted to demonstrate the boundary conditions of MFS. We predict that firms may be so inappropriately designed as to limit their ability to recognize or pursue mutual forbearance opportunities. In addition, we have identified a variety of researchable questions. For example, which of the organizational characteristics discussed here are most critical to successful implementation? What is the relationship among the individual organizational characteristics (e.g., decentralization, span of

control)? Are they functionally equivalent? Do they interact with each other? Are Quadrant 1 firms most likely to pursue and succeed at implementing MFS relative to Quadrant 2, 3, and 4 firms, respectively?

The propositions developed here reinforce our premise that the way in which we conceptualize and research mutual forbearance strategies should change. We believe that future researchers should now collect data that allow them to measure the administrative mechanisms theorized here to be central to the implementation of MFS. Until an intra-organizational focus begins to complement the existing extra-organizational focus of multimarket competition researchers, our understanding of the mutual forbearance phenomenon will be limited. The research implication of this is found in Hill's commentary on the larger body of diversification research: "... researchers are going to have to conduct surveys, semi-structured interviews, and the like, *within* organizations. While this is neither convenient nor easy... it is possible" (Hill, 1994: 320). We hope that our arguments have revealed the need for researchers to increase the resolution of their lenses, and to examine the fine-grained administrative mechanisms and organizing principles operating in multimarket competitors. When this is done, the empirical literature will have a greater chance of informing scholars and managers of the competitive effects, under certain specifiable boundary conditions, of multimarket competition and mutual forbearance.

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Table

Key Studies on Multimarket Competition and Mutual Forbearance¹

Sample	Findings	Source	Dependent Variables	Primary Independent Variables
3 bank holding companies (BHC), 1966-72	Greater market share stability in markets with greater multimarket contact (MMC)	Heggstad & Rhoades (1978)	Dominant firms' market share stability	MMC Concentration Growth Banking laws
Florida Bank holding companies	Service charges, loan rates and fees positively associated with MMC	Whitehead (1978)	Profits	MMC Concentration
437 U.S. manufacturers, 1974	Higher profits when both MMC and market concentration were high	Scott (1982)	Profits	MMC Concentration
BHC in 6 U.S. states, 1975	Service charges and loan rates positively associated with MMC	Alexander (1985) ²	Service charges Loan rates	MMC Concentration
391 U.S. multiproduct firms, 1982	Cost-price margins positively associated with MMC	Feinberg (1985)	Cost-price margins	MMC Concentration MMC x Concentration
1074 banks in 154 U.S. markets, 1970-1979	No association between MMC and ROA, service charges and loan rates	Rhoades & Heggstad (1985)	ROA Loan rates Service charges Interest paid Expense Mobility & turnover in deposit rankings of firms	MMC
195 manufacturers, 1963	Negative association between price-cost margins and MMC	Strickland (1985)	Price-cost margins	MMC
171 California savings and loans in 56 county markets, 1982	Negative association between MMC and market share stability, service charges and ROA	Mester (1987)	Instability of market share ROA Interest paid less service charges	MMC Concentration MMC x Concentration
100 largest U.S. bank holding companies, 1984-1989	Positive association between MMC and size rankings stability of banks	Martinez (1990)	Size rankings stability of banks	MMC
48 state markets of CPES sector, telephone industry, 1981-1986	MMC negatively associated with exit rates from state markets	Barnett (1993)	Exit rates	MMC
418 U.K. manufacturers in 134 3-digit SIC industries	Positive association between MMC and both price-cost margins and rate of return on capital	Hughes & Oughton (1993)	Price-cost margins Rate of return on capital	MMC Diversification
1000 largest U.S. airline city-pair routes, 1984-88	Positive association between MMC and fares on routes for major airlines	Evans & Kessides (1994)	Airline fares on largest routes	MMC Concentration

¹ This Table is derived from and extends the reviews of Baum & Korn (1999) and Korn & Baum (1999).

² Alexander's (1985) results were contingent on the measures of multimarket contact and performance used.

				Market Share
3000 U.S. airline city-pair routes, 1984-88	Positive association between yields and MMC for major airlines	Gimeno & Woo (1996)	Yield	MMC Strategic similarity
40 California commuter airlines, 1979-84	Negative association between MMC and both entry and exit rates	Baum & Korn (1996)	Market entry rates Market exit rates	MMC Market domain overlap Market density Dominant share Concentration Concentration x MMC
286 California hospitals, 1980-86	Negative association between MMC and exit rates from service markets	Boeker <i>et al</i> (1997)	Market exit	MMC Services contracted out Chief executive change Occupancy rate & financial performance
14120 US airline-routes over 5 years, 1984-1988	Spheres of influence in MMC results in higher yield and equilibrium market share	Gimeno (1999)	Yield Market share	MMC spheres of influence: market share dominance market dependence resource centrality
28 airlines and 14,120 airline routes, 1984-1988	MMC negatively associated with rivalry and positively associated with profitability in markets with sizable resource sharing opportunities with focal market	Gimeno & Woo (1999)	Intensity of rivalry Cost efficiency Profitability	MMC Resource sharing opportunities of focal firm & rivals
6 U.S. prescription drug markets, 1970's – 1980's	MMC negatively associated with marketing expenditures, signaling less rivalry	Shankar (1999)	Marketing expenditures of entrant & incumbent	MMC Entrant market experience Entrant relative marketing leadership New product marketing spending Anticipated incumbent response
California savings and loans, 1977-1991	Multimarket rivals seek growth and entry in markets with moderate degree of MMC	Haveman & Nonnemaker (2000)	Market entry Market growth	MMC Market dominance MMC x market dominance
20 firms in 7 software markets, 1987-1991	Negative association between MMC and mutual forbearance	Young <i>et al</i> (2000)	Competitive move frequency Time to move	MMC Interfirm resource dissimilarity MMC x interfirm resource dissimilarity

Figure

Predicted Relationships Between Integrating Mechanisms and Incentives to Cooperate

Rewards for Business Unit Cooperation within the Firm

		Strong	Weak
Effective	Q1	<ul style="list-style-type: none"> • Greatest likelihood of mutual forbearance • High intra-unit cooperation • Willingness of business unit managers to give up market share or returns for the greater benefit of other business units within the firm • Sufficient capability to coordinate among business units within the firm (e.g., adequate, accurate and timely information sharing) 	Q3 <ul style="list-style-type: none"> • Moderate (less than Q2) likelihood of mutual forbearance • Sufficient capability to coordinate among business units within the firm (e.g., adequate, accurate and timely information sharing) • Little intra-unit cooperation • Unwillingness of business unit managers to give up market share or returns for the greater benefit of other business units within the firm • Possibility that mutual forbearance opportunities are recognized, but not pursued
Ineffective	Q2	<ul style="list-style-type: none"> • Moderate likelihood of mutual forbearance • High intra-unit cooperation • Willingness of business unit managers to give up market share or returns for the greater benefit of other business units within the firm • Inability to coordinate among business units within the firm (e.g., inadequate, inaccurate and untimely information sharing) 	Q4 <ul style="list-style-type: none"> • Lowest likelihood of mutual forbearance • Mutual forbearance opportunities neither recognized nor pursued • Inability to coordinate among business units within the firm (e.g., inadequate, inaccurate and untimely information sharing) • Little intra-unit cooperation • Unwillingness of business unit managers to give up market share or returns for the greater benefit of other business units within the firm

Endnotes

¹ Chen (1996) also discusses the ability to respond, based on firm resource profiles. Because that discussion of resource profiles addresses who will compete, how, and expected outcomes, it lies outside scope of the current paper.

² To lessen awkwardness, rather than referring to an "ideal type, mutually forbearing, multipoint competitor" we will refer to these as "Mutual Forbearers." That Mutual Forbearers do in fact engage in a mutual forbearance strategy implies that they have both the desire and capability to do so, and thus approximate the "Ideal Type Mutual Forbearer" developed in the following section.