

Name your own change: the success history of



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ABSTRACT

The Dynamic Capabilities View emerged from the work of several researchers, aiming to provide an explanation for a firm's success in a fast-changing environment. This Thesis strives for the analysis of the Dynamic Capabilities literature through the real life business history of Priceline.com, an online travel agency founded in United States. The case shows that the company has a high propensity to sense opportunities and threats, to make market oriented decisions and to change their resources base while having a medium propensity to make timely decisions. In addition, evidence suggests that dynamic capabilities were key for the Priceline.com's success within a fast-changing environment, giving support to the literature that defines Dynamic Capabilities as the "firm's potential to systematically solve problems".

ACKNOWLEDGEMENTS

Writing my dissertation on the theme “Dynamic Capabilities” was a truly agreeable and interesting experience, particularly enhanced by the knowledge, motivation and accurate monitoring of Professor Ilídio Barreto, to which I am profoundly thankful.

I am also thankful to my family, which supported me across my academic path. Particularly during this challenging period, they provided me the best conditions I could ask for. They clearly constitute a fundamental pillar on my academic development.

I would also like to thank Cegedim, the firm where I am currently completing an internship, for the continuous transmission of knowledge, the fantastic work environment and the flexibility, in regards to my schedule, provided by them.

Finally, I would also thank my friends for all the support, particularly, to those who read and criticized my Thesis.

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INTRODUCTION

The Dynamic Capabilities View received plenty of attention among management scholars in recent years, especially after the Teece, Pisano and Shuen' (1997) seminal article. According to this article, this View is an extension of the Resource- Based Theory (Barney, 1986, 1991), which gives an explanation of how a firm can achieve a competitive advantage based on their bundles of resources and capabilities.

This intense academic attention towards the Dynamic Capabilities View stems from the importance of the relation between strategic choices and the environmental context (Thompson, 1967) and its impact on firm's performance (Audia, Locke & Smith, 2000). Nowadays, the frequent occurrence of major exogenous shifts – in the so called high-velocity (Bourgeois & Eisenhardt, 1988) or hypercompetitive environments (D'Aveni, 1994) - leads to shorter average periods of competitive advantage. Consequently, firms need to be able to build successive temporary advantages. This View is crucial to respond to the challenging question of how to build those advantages. The topic is particularly important for strategic management but it gains prominence in other areas such as law and economics too (Teece 2007).

Despite the clear importance of the literature, the topic has suffered several criticisms concerning the definition of the main concept (Kraatz & Zajac, 2001; Winter, 2003; Danneels, 2008), the disconnection of the literature (Barreto, 2011) and the lack of empirical grounding (Williamson, 1999; Priem and Butler, 2000).

In order to address these problems, a recent definition has emerged, based on several past studies (e.g. Eisenhardt & Martin, 2000; Helfat et al., 2007; Teece et al., 1997; Teece, 2007). The new conceptualization defines dynamic capability as the “firm's potential to systematically solve problems, formed by its propensity to sense opportunities and threats, to make timely and market-oriented decisions, and to change its resource base” (Barreto, 2011) and appears as an aggregate multidimensional construct (Edwards, 2011).

The importance of this new definition relies on the fact that it 1) captures the richness and the essence of a large body of work, 2) allows the operationalization of the construct and 3) solves the commonalities paradox, assuming that the presence of some commonalities across firms is still compatible with the potential for competitive advantage. Finally, the concept is applicable within fast-changing environments.

Based on the Dynamic Capabilities View, this Thesis involves the construction of a teaching case. The case is centered on Priceline.com's business history, which is used to illustrate several aspects of the literature.

Despite the multidisciplinary coverage of the concept (Teece et al., 2007), the present teaching case is developed particularly for the field of strategic management. It aims to contribute to the consolidation of the Dynamic Capabilities View by providing empirical evidence, especially directed to the blossoming definition. Consequently, the new concept is applied to an environment characterized by a fast-changing nature as the travel industry is.

Priceline.com is an online travel agency (OTA) founded in 1997, which faced the above mentioned dynamic environment. In summary, the company's promising start turned into a disappointing performance, within a tiny period of time. However, Priceline.com was able to respond to constant environmental challenges with renewed strategic decisions, which demonstrated a large capacity of adaptation. As a consequence, their stock has performed very well, particularly in the last five years. The fascinating story of the company will be used to illustrate the difficulty to manage and cope with fast-changing and hypercompetitive environments, as well as to demonstrate the role of dynamic capabilities.

The Thesis will be presented in five main sections. The first section encloses the literature review, where the dynamic capabilities theoretical framework is summarized. In the second section I will develop the teaching case about Priceline.com's history. The third section presents a teaching note relative to the case. The last piece is the Discussion section, where I will summarize the main findings from the case and explore its contributions and limitations.

I. LITERATURE REVIEW

PREDECESSORS OF THE DYNAMIC CAPABILITIES VIEW

Porter's Five Forces and the Resource-Based Theory are the two major approaches that have provided an explanation for the achievement of sustainable competitive advantages (SCAs) by a firm during recent decades. Michael Porter (1980) first introduced the Five Forces framework as a guideline for an industry analysis and it consists in the calibration of the role of suppliers, buyers, substitutes, competitors and potential entrants – the five distinct industry-level forces. The framework gained importance since it determined the actions a firm should take to gain position over the different forces. Consequently, Porter suggested that the industry was detrimental for a firm's achievement of SCAs.

According to Porter, SCAs are based on an exogenous market structure rather than resulting from the product (endogenously) generated by innovation and learning. Moreover, the author ignores various aspects of the competitive environment proven relevant, such as the role of path dependencies, complementarities and supporting institutions. Besides, the framework assumes that the nature of the environment is relatively static rather than dynamic. As a consequence, even though the Five Forces' framework has received massive popularity for academic and practice purposes, it appears of limited utility in turbulent environments (Teece, 2007).

The second theory - the Resource-Based Theory (RBT) – focuses instead on the internal aspects of firms to explain SCAs, serving as a complement to the former framework (Eisenhardt & Martin, 2000). First introduced by Barney (1991), the RBT proposes that the creation of distinctive competencies in an industry derives from the specific bundle of resources and capabilities the firm has. Resources (which also comprise capabilities) are physical, human and organizational assets that can be used to execute value-creating strategies (Barney, 1986; Wernerfelt, 1984, 1995), being heterogeneously distributed across firms. Creating and sustaining value implies that resources verify the so called VRIN criteria – resources must be valuable, rare, inimitable and non-substitutable, (Barney, 1991; Conner and Prahalad, 1996, Nelson, 1991; Peteraf, 1993; Wernerfelt, 1984, 1995).

VRIN matches the four conditions of the RBT, which are: resource heterogeneity, ex-post limits to competition, imperfect factor mobility and ex-ante limits to competition. One

important factor causing limitation to competition is causal ambiguity (Lippman and Rumelt, 1982) that consists in the uncertainty regarding the causes of efficiency differences among firms. Causal ambiguity avoids imitation because the development of a product/service involves sunk costs, especially R&D costs, which should be pondered under uncertainty. The imperfect factor mobility furthermore explains the difficulty on imitation since assets contain entrepreneurial and social complexity. They are also characterized by path dependencies, which exist since the new production function is derived from a known bundle of current production functions.

Across time, supplementary conditions have been added to value sustainability since the mere ownership of resources, even with all of these attributes, is perceived as non satisfactory. In fact, firms holding similar resources and within similar environmental contingencies will produce different outcomes (Zott, 2003) due to different choices of structuring, bundling and leveraging resources (Sirmon, Hitt & Ireland, 2007). These different activities compose a firm's management of resources, which is approached differently by other authors, being defined as the accumulation, combination and exploitation of resources (Grant, 1991; Sirmon & Hitt, 2003) or their evaluation, manipulation and appropriate deployment (Lippman & Rumelt, 2003). Nevertheless, they all take into consideration the firm's environmental context. For a deep understanding about the linkage between the management of resources and the creation of value, it is necessary to access the effects of a firm's environmental impact on managing resources (Aragón-Correa and Sharma, 2003; Bettis & Hitt, 1995; Lichtenstein & Brush, 2001).

However, RBT also presents a boundary condition since it has not adequately explained the achievement of competitive advantages in high velocity markets. The high environmental uncertainty leads to the difficulty of sustaining a competitive advantage once the duration of this advantage is erratic (Eisenhardt & Martin, 2000). Environmental shocks can substantially increase uncertainty (Sirmon, Hitt & Ireland, 2007) and uncertainty produces deficits in information, which are used to identify and understand cause-and-effect relationships (Carpenter & Fredrickson, 2001; Keats & hit, 1988). What are environmental shocks? They are defined as unexpected events that create discontinuities in an industry (Tushman & Anderson, 1986) and can result from competitive actions such as the introduction of a disruptive technology (Sirmon, Hitt & Ireland, 2007).

EMERGENCE OF THE DYNAMIC CAPABILITIES VIEW

From the extension of the RBT, a new subject of research emerged: the Dynamic Capabilities (DCs) literature (Eisenhardt & Martin, 2000). On the one hand, DCs literature is a breakthrough of Porter's Five Forces framework once the business "ecosystem" replaces the industry as the environmental context (Teece, 2007), being the environmental context dynamic. On the other hand, it appears as a response to the boundary condition of RBT mentioned above once DCs are necessary to cope with unpredictable environments in an open globalized economy (Teece, 2007). The unstable and challenging environment makes firms seek series of temporary competitive advantages as an alternative to sustainable competitive ones (Morrow, Sirmon, Hitt & Holcomb, in press), allowing them to maintain the value created in previous periods while creating new value (Ireland & Webb, 2006). DCs develop an important role on the accomplishment of these temporary competitive advantages.

Subsequently, DCs have been a soaring subject of research and the literature about it has rapidly evolved, moving towards different directions. The nature of DCs itself is a non-consensual point since they were defined as "abilities" (Teece et al., 1997), "processes" (Eisenhardt and Martin, 2000) or even "routines" – either new routines (Zollo & Winter, 2002) or search routines (Nelson and Winter, 1982). There were discrepancies in terms of DC's role as Zollo and Winter (2002) consider it as changing the operating routines of a firm, given that the operating routines are those which enable a firm to "make a living" and to solve problems; while Eisenhardt and Martin (2000) consider DC's role as changing specific resources and capabilities of a firm.

The divergence is also high regarding the context where DCs can be applied: some defend DCs are only relevant in fast changing environments (Teece, Pisan & Shuen, 1997), others defend that a moderated amount of change is enough for the significance of DCs (Eisenhardt & Martin, 2000) and others yet defend that DCs are relevant in stable markets although their utility increases with a faster pace of change (Zollo & Winter, 2002). Researchers also assume different perspectives regarding the heterogeneity of DCs across firms. For some (Makadok, 2001; Teece et al., 1997), DCs are firm specific and exclusive, which can be linked with the importance of a firm's idiosyncratic path-dependent history on DCs creation. For others (Eisenhardt and Martin, 2000), there are commonalities across firms in which concerns to DCs, as one dynamic capability permits different but similarly effective ways of performing a task. However, these authors also noticed that they are

constituted by idiosyncratic details beyond the common features. This second perspective about heterogeneity is not contradictory to the path dependency conjecture but implies that one specific dynamic capability can be derived from multiple paths.

Regarding the purpose, Teece et al.'s (1997) believed that dynamic capabilities are decisive to address fast changing environments while Eisenhardt and Martin (2000) extended the aim from the adaptation to the market change to the effective creation of market change. Moreover, Zollo and Winter (2002) believe that dynamic capabilities aim for improved effectiveness whilst Zahra et al. (2006) believe that the purpose of DCs is the one desired by decision makers. Finally, since the definition of DCs constitutes a starting point for researches, different definitions of DCs naturally create a wide range of possible outcomes. As so, several researchers found a direct (Makadek, 2001; Zollo & Winter, 2002; Teece, 2007) link between DCs and performance and several others an indirect (Zott, 2003; Zahra et al., 2006) link between the same elements. Still within the authors which defend the indirect link, there are different perspectives: Eisenhardt and Martin(2000) defend that long-term competitive advantage rely on the resources configurations, generated by dynamic capabilities, as well as on the approach through which dynamic capabilities are used and accordingly, firms with similar DCs may surpass rivals. Zott (2003) defend that dynamic capabilities may modify the bundle of resources and routines and so, influence performance and suggest that, as DCs can create different bundles of resources, identical DCs have differentiated performance levels.

A NEW DEFINITION

A new definition was materialized based on these previous developments, enclosing the ambition to solve problems associated with dissimilarities and inconsistencies of past researches. This new theory was suggested by Barreto (2010) and defines a dynamic capability as the “firm’s potential to systematically solve problems, formed by its propensity to sense opportunities and threats, to make timely and market-oriented decisions, and to change its resource base” (p.271). The definition solves ambiguity, obscurity (Kraatz & Zajac, 2001; Winter, 2003; Danneels, 2008) and tautology (Williamson, 1999) problems, which have been pointed to by past definitions. As it becomes operational to seek for empirical evidence, the definition meant a crucial step for the achievement of a consistent DCs theoretical framework.

According to this new definition, the purpose of DCs is clear as its nature is explicitly defined when the author infers that DCs “systematically solve problems”. The word

“systematically” highlights a structural and persistent nature of DCs and the word “potential” highlights the differentiation between DCs and success and avoids the dichotomy of the concept, as different levels of DCs are allowed. The commonalities paradox is solved since there is compatibility between the presence of some commonalities across firms and their potential for competitive advantage. Indeed, firms can have commonalities in some dimensions of the construct while the others remain idiosyncratic.

The new definition consists of a multidimensional construct (Edwards, 2011) because it comprises four different dimensions, which are related among them. Besides, it is an aggregate multidimensional construct as common variances or covariances shared by all dimensions, variances specific to any of the dimensions and covariances shared by some dimensions only are all taken into account (Law et al., 1998). The four different conditions will be analyzed in supplementary detail:

The **propensity to sense opportunities and threats** gained substance as a dynamic capability from previous work of different authors, like Gilbert (2006) who defends that framing opportunities and threats is a central part of dynamic capabilities.

This dimension can be particularly related with the discovery view comprised on the opportunity formation and exploitation literature, further developed by Alvarez & Barney (2007). The discovery view refers to opportunities that exist independently of the focal actor’s efforts (Shane & Venkataraman, 2000) as they arise from exogenous shocks, such as technological, regulatory, political, social or demographic (Kirzner, 1973; Shane, 2003). In this situation opportunities are there “waiting to be discovered” (Alvarez & Barney, 2007) through a main mechanism: search (Kirzner, 1997).

Search can be either directed or undirected. Directed search implies that people know what they are looking for and what they should do to direct their search whereas undirected search involves that people are not aware of what they are looking for, so they do not trace a specific direction for their search (Browne et al., 2007). As so, instead of a directed search, entrepreneurs can use entrepreneurial alertness (Gaglio & Katz, 2001) which is, by Kirzner (1979, p. 48)’s words, “the ability to notice without search”.

Teece (2007) has also attributed attention to this dimension and he stated that sensing opportunities involves a scanning, creation, learning and interpretive activity, normally complemented with investment in research and some related activities. Complementing,

Barreto (2012) suggested entrepreneurial interpretation as a second mechanism serving the discovery view.

Regarding **decision making**, present in the second and the third dimensions of the definition, it also finds support as a dynamic capability from other researches, such as from Slater et al. (2006) who believe that the strategy-making process ability is a central dynamic capability. Moreover, Moliterno & Wiersema (2007) considered decision making, in which concerns to changes in the resource base, an essential element of dynamic capabilities. Also encouraging the link among dimensions, Rosenbloom (2000) stated that, without materializing the resource-changing propensity via the action of leaders, the value of decision making capabilities would be nil.

Eisenhardt & Martin (2000), which also attributed significance to the change of existing resources for the achievement of long-term competitive advantages, added that the change must be made “sooner”. Other authors (Barney, Wright & Ketchen, 2001) emphasized the ability to **make timely decisions** as a dynamic capability, which gives consistency for the integration of the second dimension in the definition.

In further detail, Choi & Shepherd (2003) relate the exercise of entrepreneurial activities with the decision to exploit an opportunity, given a lead time. On one hand, these entrepreneurial activities, such as market research, prototype testing and stakeholders’ support seeking, are used to reduce the uncertainty of the market and to increase resources and capabilities of the firm. On the other hand, the perception of a longer lead time for a new product magnifies the decision to exploit the opportunity. Accordingly, there is a trade-off between the benefits of entrepreneurial activities and the costs of postponing the launch of a new product or service by developing those entrepreneurial activities. Making appropriate timely decisions involves properly managing this trade-off, which is vital for the success of the company.

Beyond time, the **content** of managerial decisions is also key for dynamic capabilities (Adner & Helfat, 2003). A decisive part forming the content of these decisions is the way a firm provides value to customers (Priem, 2007), which is particularly enhanced by their **market orientation** (Narver & Slater, 1990). Moreover, Menguc & Auh (2006) argued that market orientation is a dynamic capability when in the presence of reconfigurational capabilities.

The accuracy of decisions depends on perceiving latent demand, understanding the structural evolution of industries and markets, including supplier and competitors' response, and "probing and reprobating customer needs" (p.1322) and technological possibilities (Teece, 2007), among other variables. Teece (2007) additionally declares that the way a firm provides value to customers and converts the value delivered into profit is determined by the design and performance specification of the product and the business model employed.

Finally, the **propensity to change its resource base** finds congruence with a vast body of past research (Eisenhardt & Martin, 2000; Helfat et al., 2007; Teece et al., 1997). Altering the resource base comprises "acquiring, shedding, integrating and recombining resources" and these new configurations are achieved as "markets emerge, collide, split, evolve and die" (Eisenhardt & Martin, 2000, p. 1107).

In line with this conceptualization, Hitt et al. (2007), defend that management of resources comprises three phases: structuring the firm's resource portfolio, bundling those resources to build capabilities and leveraging those capabilities. The purpose of managing resources is to exploit opportunities, taking advantages of specific market opportunities, and to create and maintain value for customers and owners.

It is important to note that not always a company has the resources needed to accomplish the selected strategies and when this situation occurs there is a resource gap (Teng, 2007). A company possess four possible ways of filling a resource gap: through internal development, through market transactions (Barney, 1986), – either tangible or intangible - through acquisitions (Park, 2002) and through strategic alliances (Hagedoorn & Sadowski, 1999). Each one of the alternatives encompasses *pro et contra* factors. For instance, internal development can be unsuitable for a firm in terms of timing, especially in hypercompetitive environments that require fast responses to opportunities (D'Aveni, 1994), adding to the fact that there is a high development cost and a high risk of failure. As a benefit, the firm has a total control of the resources created. Market transactions can have a low cost and reach high efficiency but they can lack the competitive advantage gain. Acquisitions can represent a high purchase price, integration difficulties, hidden risks and anti-trust restrictions but can also signify rapid growth (Birkinshaw et al., 2000). Last but not the least, strategic alliances augment flexibility and speed, beyond the share of either costs or risks. However, they can be very difficult to manage and the access to resources are normally temporary (Parkhe, 1993).

Closing, the vast literature developed about Dynamic Capabilities across times can be enriched using case studies. They compose a manner of gaining supplementary evidence about the different dimensions forming a dynamic capability, as several researchers, such as Galunic & Eisenhardt (2001), Lampel & Shamsie (2003), Pablo et al. (2007) and Rosenbloom (2000) have demonstrated.

II. TEACHING CASE

Founded in July 1997 in the United States by Jay S. Walker, Priceline.com is pioneer of a distinctive type of e-commerce, as it created the innovative “Name Your Own Price” demand collection system, and leader in global online hotel reservations. The Group is composed of five primary brands, being an important provider of several online travel services, such as airline tickets, hotel room reservations, rental cars, cruises and vacations packages, in over 180 countries. In the early days though, the company dealt with successive obstacles and profits seemed difficult to achieve. Was Priceline.com able to adapt to successive shocks affecting the travel industry and strong enough to compete against their robust competitors? What was Priceline.com’s strategy and what were the results from their strategic orientation? Could Priceline.com guarantee a sustainable growth in the future?

HOPE FOR THE BEST...

When the American Jay S. Walker launched Priceline.com’s online service on 6th April 1998, he was revolutionizing the travel service market. For the first time, consumers were able to electronically bid for round-trip tickets, having the possibility to offer a price for an airline ticket, below the lowest available fare in the market.¹

At Priceline.com launched time, online auctions were not novel, either for individuals or businesses. However, Priceline.com became pioneer and patent owner of a *reverse type of* auction, also called *blind* auction, when they created the “Name Your Own Price” (NYOP) model, first applied to the airline industry.^{2 3}

With the NYOP system, Priceline.com acted as the middle man between airline customers and airline companies. The firm had access to an unpublished inventory of ticket fares made available by American and International airlines and through it, they could issue a ticket once an airline carrier had met the price proposed by the traveler on the company’s website. Additionally to the price, consumers listed their destination, travel dates and provided a credit card to be charged.^{4 5}

Consumers were not completely aware of what they were buying *a priori* (they were buying opaque products). Although they could choose price, destination and dates, they should be willing to accept a set of conditions: the airline company, the schedule – which

could vary from 6 a.m. to 10 p.m. – and the possibility of one stop or connection. Moreover, most tickets were not refundable or changeable, customers did not earn recurrent flier-miles and although their first request, which could be up to eight tickets, was free of any additional charge, every subsequent request for the same itinerary and dates was charged \$25.^{6 7}

Customers' main advantage was to obtain lower prices. In fact, they faced a trade-off between price and flexibility with respect to brands, sellers and product features. Airline companies also benefited from the model as they could sell last-minute tickets privately, through e-mail lists - opposing to the traditional price-disclosed model. The new method enabled them to clear out inventory that would have their value vanished, by the use of a non-disruptive distribution channel which generated incremental revenues for them.⁸ In other words, they could reach a huge amount of potential customers and fill hundreds of seats that went empty every day (in a total amount estimated in 600 000 at the time) with lower and unique fares offered to a niche market. At the same time, they could avoid cannibalization from customers who would be willing to pay higher fares.⁹ The way airlines liquidated excess seats would not be publicly disclosed. In the beginning, only T.W.A. and America West, among the largest U.S. airlines, accepted to work with Priceline.com but soon they were followed by Delta, Northwest and Continental.¹⁰

Priceline.com generated revenues by earning the differential between the price an individual was willing to pay and the price charged by the service company – it was a merchant model. Additionally, Priceline.com received reservation booking fees, customer processing fees and (in some cases) ancillary fees, on each flight.¹¹

Jay Walker's confidence regarding the performance of the company was high, since he anticipated the sale of 1000 to 3000 tickets a day by the end of the year. Some criticisms on the system emerged though, like from the chief executive of one of the leading online travel agencies (OTAs), Preview Travel. He claimed that the mainstream customer would rather pay more for a nonstop flight on a major airline than change planes and use a second-tier carrier. Adding to the fact, he argued, there was a lack of surplus seats since operating capacity of airlines were at its highest point in years.¹²

Richard S. Braddock, former president of Citicorp and current chairman and Chief Executive Officer (CEO) of Priceline.com, since July, 1998, had a different opinion. In fact, throughout that year and the following one, he also tried to replicate the model to other markets, such as to hotel rooms, new car sales, car rental businesses, financial market services and, indirectly, to groceries and gas.¹³

On the one hand, some characteristics of the model were applied transversally to all products and services offered by Priceline.com, particularly, its core feature which consisted on the customers' possibility to set the product or service price. On the other hand, some other features and processes were market specific: in case of a hotel room, consumers decided on its geographic area and category (star-rating or resort), in case of a car rental, customers decided on local and kind of car.

Regarding the financial market, where Priceline.com operated through partnerships made with Lending Tree and Alliance Partners, L.P., borrowers became able to submit a particular request for interest rates and other terms for mortgages of a specified term, which included purchase money mortgages, refinancings and home equity loan services. Along with the request for the financial service, consumers had to deposit \$200 guaranteed by a major credit card. Regarding the purchase (or leasing) of a car, customers identified the exact vehicle to be purchased or leased, which included the brand, model and specified options and the transaction process would be closed directly between the customer and the car supplier. An additional feature created for financial services and car sales was the supplier's possibility to counteroffer, as these products had a smaller level of substitutability.¹⁴

Finally, the company licensed its patented NYOP business model, affiliated trademarks and software systems to Priceline's WebHouse Club, Inc. The WebHouse Club operated in the groceries and gas market since November 1999, but major differences appeared when applying the model to these industries: if a seat on the plane was not sold, its value was lost, which contrasted with the non-perishable nature of gas and some groceries; moreover, the cost of adding a customer to the airplane was negligible while the unit costs of producing, shipping and storing both groceries and gas was not. Furthermore, suppliers were not satisfied about selling products at a lower price without benefiting from customers' brand loyalty like coupons do¹⁵.

Two years later, the portfolio of services also counted with long distance phone calls, cruises (which operated under the traditional model) and the vacation package product. The first service allowed consumers to name a price for domestic and international calls from their home phones while vacation packages consisted in the combination of airfares and hotel or resorts room nights.^{16 17 18 19}

From the very beginning, marketing campaigns constituted a golden egg for Priceline.com. William Shatner, which was especially known for his work as Capitan Kirk in Star Trek, was the person chosen to be the face of Priceline.com. The actor accepted to participate in

Priceline.com's commercials in exchange for a very modest salary and stock in the company. Soon, the stock ended up becoming a very profitable deal for him.²⁰

Besides the business model replication, during 1999, Priceline.com progressed in different fields. First, the company materialized the expansion of the business to Asia, through a partnership with Hutchison Whampoa Ltd. (Hong Kong), resulting in a new company that offered airline tickets and hotel rooms services, though credit cards and long-distance phone cards have been added later. The company was formed by a mutual investment of \$10 million, used Priceline's NYOP bidding system and was managed by Hutchison.^{21 22 23}

Second, Priceline.com restructured its warrant agreements with airline companies and, more importantly, enlarged their portfolio of carriers, as No. 1 United Airlines, No. 2 American Airlines and No. 6 US Airways signed up with them. Subsequently, its working partners included eight out of the nine largest United States airlines and other 20 foreign lines. This portfolio enlargement raised expectations of an endorsement in the company's current success.²⁴

... BUT PREPARE FOR THE WORST

In September 1999 though, the NYOP business model started to be used by the second biggest travel agency at the time, Microsoft's subsidiary Expedia.com, through a very similar service. Competition was not a surprise for Priceline.com, but the NYOP model was patented and soon the company filed for a lawsuit in U.S. District court against Microsoft and its Expedia Inc. travel subsidiary.^{25 26} Despite patent infringement, Microsoft had no intention to discontinue its service and the process resulted in the payment of royalties to Priceline.com.^{27 28}

Opposite to the conflict with Expedia, Priceline.com and the giant Travelocity announced a broad-based marketing alliance that offered travelers access to both companies' airline ticket services regardless the website they visited. If they preferred specific airlines and flight times, they could access Travelocity.com's services and if they preferred a lower fare in exchange for their flexibility regarding flight times and airlines, they could access Priceline.com's. Each time Priceline.com facilitated the sale of Travelocity's product, Priceline.com generated incremental revenues. The opposite was also true, benefiting both companies from larger total customer base and brand awareness.²⁹

In the end of 1999, management believed it had been a successful year as ticket sale units had increased from 5,000 a week in the beginning of the year to 50,000 a week at that moment.³⁰ Revenues had risen from \$35 million, in 1998, to \$ 482 million, in 1999 and gross margin had benefited from a positive impact deriving from new products that generated fee-based and ancillary revenues. However, the company was still unprofitable, observing only a trivial net loss decrease from \$12.7 million to \$10 million during the same period.^{31 32}

Additionally, Priceline.com became a public company in Nasdaq Stock Market on 29th March, 1999³³ and, as several other companies born during the dot-com bubble, they saw its market value suffer huge oscillations.

An economic bubble occurs when the price of an asset exchanged in a well established market “rises far higher than can be explained by its characteristics, such as the income likely to derive from holding the asset”.³⁴ The internet speculative bubble occurred in the late 1990’s stimulated by internet- and internet related-based companies, the so called dot-com companies³⁵. From 1996 to 2000, the Nasdaq Stock Index boomed from 600 to 5,000 points³⁶, peaking at 5,048 points in March 2000.³⁷ During the dot-com bubble period, massive market overconfidence on technological advancements and subsequent future profits boosted investment, resulting in a rapid increase in stock prices and ensuing huge capital raisings for dot-com companies, despite the lack of profits or even revenues by firms. In fact, supporters of the dot-com theory believed that the expansion of the company’s customer base with disregard for potential annual losses, illustrated by the phrase “get large or get lost”, was an imperative condition for the survival of an internet-based company.³⁸ Stock shifts turned company founders into owners of enormous fortunes and markets made very appealing that people quitted their job in order to become a full-time day trader.^{39 40 41} The phenomenon was so vast that, in 1999, there were 457 IPOs, having 117 from those doubled their price in the first day of trading. This can be contrasted with the 76 IPOs occurred in 2001, none of them having doubled its price.⁴²

At the IPO, Priceline.com offered 10 million shares – a 7% stake - at an initial price of \$16, which was already above its original range of \$7 to \$9 per share. Benefiting from the investors’ period of overexcitement, the initial price boomed 437.5% in the same day, closing at \$69. This turned Priceline.com’s initial market value of \$2.28 billion into \$9.82 billion at the end of the day and converted Jay Walker into a billionaire with its \$62.5 million share stake valued at \$ 5.2 billion.⁴³ Priceline.com and the dot-com bubble in

general continued booming throughout the year and, during the second quarter, the company's stock achieved its highest price, peaking at \$162.375. This meant that Priceline.com shares were 10 times more valuable than initially within a time range of only a few months.⁴⁴

The IPO aimed to raise funds for working capital and general corporate purposes and to finance anticipated operating losses, the advertising campaign and brand name promotional expenses, among other expenditures. Moreover, the purpose of funds comprised potential acquisitions or investments in businesses, technologies, products or services that might arise.⁴⁵

By early 2000 the NASDAQ Index shrank as investors started perceiving the speculation created, reaching soon 2,000 points and bringing up to bankruptcy several of the early successful dot-com companies, many never having made a profit.⁴⁶

As for gains, Priceline.com was not an exception concerning losses: its stock price shrank from its peak of \$162.375, during 1999, to \$46.75 in the beginning of 2000. Indeed, 2000 was one of the toughest years in their history. First, the company's market price continued to decline from day to day; second, some negative news in regards to Priceline.com's customer service emerged;⁴⁷ third, not receiving the expected collaboration of suppliers, Webhouse Club subsidized customers' purchases as a way to lower prices and thus enlarge their customer base. Managers believed that a larger customer base would motivate manufacturers to collaborate with reductions in prices. However, the outcome was significant losses, a \$363 million cash burn in about one year and the shutdown of Priceline.com's WebHouse Club Inc.^{48 49 50} In the end of this year, and given that the failure was particularly attributed to Jay Walker, the founder decided to leave the board of Priceline.com in order to rebuild his business incubator, Walker Digital Corp.^{51 52} Closing the WebHouse Club resulted in an additional expense of \$189 million due to its warrant write-off. Panic to sell stock was launched as well as a post-bubble economic recession, which made the Index sank to 800 points still in 2000.⁵³

Despite those bad news, Priceline.com was improving its financial performance over the previous year. During the year, the company added 5.5 million new customers and 4.3 million offers from repeated customers, which made revenues more than doubled, summing up \$1,217 million and meaning a rise of 153% over 1999.⁵⁴ About 98.5% of those revenues derived from travel businesses as a result of the refocus by the management on the travel industry. Gross profits increased to \$ 192.29 million, 77% of those being used as sales and marketing expenses, which were a priority to Priceline.com.

These expenses comprised television, radio, on-line and print campaigns as well as agency fees and production costs for television and radio. The net loss was reduced from \$1,063 million, reached in 1999, to \$329.5 million. In the end, financial results were not sufficient to satisfy investors and the stock price fell to a minimum \$1.125 in the last quarter.⁵⁵

At this point in time, Priceline.com was amongst top 5 online travel players, holding a 10% share in the market. The unambiguous leader was Travelocity (19% market share), which was an online travel brand and one of the pioneers of the web-based travel disintermediation. The second place was held by Expedia (14%), which was also an online travel brand created by Microsoft, in 1996, but that belonged to TicketMaster, at that time. Southwest Airlines (13%) was the third biggest online travel player, consisting in a major U.S. airline company operating as a low-cost carrier. Priceline was the fourth largest player, followed by Delta (6%), another major United States airline. The five largest players accounted for 62% of the U.S. online travel market.⁵⁶ Even though the importance of agencies, suppliers (such as airlines) still dominated the market, weighting 53% of its value.⁵⁷

The vulnerability of the industry to external shocks and the intense competition were nonetheless a constant challenge for travel industry players. Additional to the market crash, the U.S travel industry was vastly affected by the 9/11 terrorist attack on the World Trade Centre, in 2001. Actually, both events explained gross part of the \$5 trillion market value loss of the NASDAQ Index, from 2000 to 2002.⁵⁸ In particular, Priceline.com achieved new unenthusiastic records when their shares value shortened to \$1.10, during the fourth quarter of 2001. Adding to the collapse on stock value of the firm, Priceline.com suffered a decrease in the adoption of the NYOP business model for airline tickets, explained by the weakened demand for air travel and subsequent airline companies' downsize⁵⁹ and price discounting reactions. Actually, 2000's brought vast difficulties to airlines resulting in four major airlines filing for bankruptcy, and only American and Continental, among U.S. major airlines, were able to escape.⁶⁰ On the one hand, the airline service downsize meant a lower amount of empty seats to be sold, which affected Priceline.com's opportunity to bargain last minute tickets. On the other hand, lower prices offered by airline companies made Priceline.com's discounted prices hard to succeed.⁶¹ As a result, the company faced a 36% and 39% decrease in airline tickets unit sales, in 2002 and in 2003, respectively.⁶²

Even though the overall U.S. travel market was decreasing by 8% in 2001 and by 4% in 2002, consumers' habits were changing as the amount of online customers continued to grow over the amount of offline customers, resulting that the U.S. online travel market

uplicated in 2002, compared to 2000. The market was also changing in structure, suffering a shift in sales from suppliers to agents. In fact, during this period, suppliers lost 7% of the total market share to agents. Agents especially dominated sales in the hotel room segment where they totalized 61% of the revenues.

Nevertheless, the scenario was not bright to all agents, especially for the leader, Travelocity, and for Priceline.com. The first lost its leadership position to Expedia, holding only 12% of the market while the new leader changed its market share to 18%. With a mere 4% market share, Priceline.com lost its position among the online travel market top 5, being surpassed by a new player named Orbitz, Delta, TNI (Cendant Retail) and Marriot.com. Additionally, Hotels.com and especially Hotwire.com were gaining online travel market share and each represented already 3% of the pie. The first was a hotel booking provider while the second was a discount travel website. Orbitz, the fourth largest player in 2002, was created from a partnership of five of the six major U.S. airlines.⁶³ Its foundation explains, in part, the shift occurred in the industry from suppliers to agents. Worldwide, the travel industry suffered a particular negative impact, in 2003, also associated with epidemic diseases such as SARS and the military actions against Iraq.⁶⁴

The financial turbulence over the company was accompanied by instability within Priceline.com's management, resulting in CEO's position change for four times within a time frame of only two years. In May 2000, Braddock was fired from his CEO role to be replaced by Daniel Shulman one month later, even though Braddock maintained his chairman position.⁶⁵ However, his role as CEO ended up being a short time position since he was replaced one year later by his predecessor Richard Braddock, still holding the chairman position. Yet again, the charge was not held for a long time and by 2002, Jeffery Boyd was elected CEO.

The new CEO had been Priceline.com Chief Operating Officer since 2000, after his role of executive vice president and general counsel.⁶⁶ Right before joining Priceline.com, he had been HMO Oxford Health Plans Inc. executive vice president, general counsel and secretary.⁶⁷

WHEN THE GOING GETS TOUGH, THE TOUGH GET GOING...

Boyd stepped on a dangerous ground – in 2002, Priceline.com's stock price fall was huge, net loss was more than the double compared to the previous year and almost 20% of the company's staff had been fired⁶⁸ – nevertheless he had the courage to take risky and

controversial decisions from the very beginning. Boyd completely transformed Priceline.com's strategy, starting with the shutdown of the non-travel businesses. As a response to the decline of the airline tickets market, the new CEO decided to transform hotel booking services into the core business of the Group. Moreover, they started using the traditional price disclosed model as their major distribution model, which meant to dismiss the enthusiasm over their masterpiece, the NYOP model.

Contrary to airline tickets, hotels reservations had an increase of 39% in revenues in 2003 over 2002 and Boyd decided to take advantage of this growth. First, Priceline.com invested in and formulated an agreement with Travelweb LLC, a hotel distribution network that belonged to five major hotel companies, among other investors. Second, the company launched an aggressive campaign specified for this industry.⁶⁹

Changing the core business from airline tickets to hotel reservations was also a controversial decision, since NYOP airline bookings accounted for 80% of Priceline.com's revenues, in 2002. The price disclosed model (which was the traditional way under which travel agencies operated), launched in the fourth quarter of 2003, was already available via Priceline.com's subsidiary Lowestfare.com during the prior year. However, disclosed prices were only presented to customers that had been unsuccessful when using the NYOP model. Just in 2003 the agency model was universally applied on airline tickets, hotel rooms and vacation packages products, due to the belief that the NYOP model only fitted college students' preferences, underexploring the less flexible travelers' market.⁷⁰ However, the company continued offering services under the NYOP model, serving different types of customers in one single platform, which was Priceline.com's website. The new product revenues were mainly obtained by processing fees and third-party supplier commissions related to the sale of travel products; and ancillary fees, which included global distribution system (GDS) reservation booking fees related to transactions.⁷¹ GDS combined with the Electronic Data Interchange Standards (EDI) enabled airlines and agents to offer multiple airlines services on a single system. Since the nineties, the GDS market had been represented by three major international brands: Amadeus, Sabre and Travelport.⁷²

The strategic moves into the hotel industry, under an agency model, contributed to reverse their bookings and gross profit evolution, even though the majority of total revenues in that year still derived from the merchant business.⁷³ After a promising start under Boyd's command, the final result for the year of 2003 was a positive net income for the first time in 6 years of operations, as Priceline.com almost profited \$12 million.⁷⁴

Boyd searched for growth driven by internationalization and strategic acquisitions in the following years. Indeed, with these acquisitions, Priceline.com aimed to expand its geographical reach to underutilized areas. Rather than expanding overseas with their own brand, the company opted for the purchase of firms that were original from the targeted areas and that had proven to successfully operate and profit in those markets. As so, they acquired three online hotel reservation companies: Active Hotels (2004) and Booking.com (2005), in Europe, and Agoda.com (2007), in the Asia-Pacific region⁷⁵.

The number of Priceline.com possible acquisition targets was large. Nevertheless, Priceline.com Inc. carefully pondered their strategic acquisitions, particularly in regard to companies' management style. Additionally to the importance attributed to management, Priceline.com found value in maintaining the independence of companies after each acquisition, even though that meant facing costs that could be avoided if only one operational platform was chosen and systems were merged. One particular exception to this policy was the merger between the European companies Active Hotels and Booking.com.⁷⁶

Europe was a very attractive market in terms of size, nature and growth.⁷⁷ Regarding size, Europeans had twice the vacation days compared to Americans which made the market larger.⁷⁸ In fact, international arrivals in Europe totalized 55% of total international arrivals, both in 2004 and in 2005. Furthermore, the recent European Union enlargement from 15 to 27 countries generated an increase in European Union population from about 380 million to 485 million which, along with the Community's accession policy and the market oriented policies, facilitated tourism flows and increased the importance of the already vast intra-European tourism⁷⁹. The penetration of low cost airline companies such as EasyJet and Ryanair ([Exhibit 1](#)) were increasing the attractiveness for weekend leisure travels and consequential hotel room spending⁸⁰. The majority of European tourists travelled via land and not air, though, which still holds true today ([Exhibit 2](#)).⁸¹

Regarding nature, one most important and advantageous characteristic of the European market was its fragmented hotel industry structure. There were fewer big hotel chains than in North America, which increased demand for independent hotels. These hotels often lacked their own website and so, they could benefit from the Priceline.com's service as the company could give them access to a larger range of potential customers.⁸²

Finally, the European market had more room to grow from their lower internet purchase rate, when comparing to Americans.⁸³ In Europe, back in 2003, only about 15% of total bookings were made online: 61% of them were travel bookings and 14% hotel bookings.⁸⁴

At the moment Priceline.com acquired the UK-based Active Hotels Ltd., the English firm worked with a range of 8,000 chain and independent hotels throughout Europe, from B&Bs to 5-star hotels. Their distribution network encompassed company-owned Web sites such as activereservations.com and approximately 1,500 Web sites operating throughout Europe, being available in 5 languages (English, French, Spanish, German and Italian). The Amsterdam-based Bookings B.V. had some important presence in Europe too, when acquired by Priceline.com. The company had been created in 1996 and beyond its presence across Europe, they were also present in major cities around the world. Similarly to Active Hotels, they were working with chain and independently owned hotels. The cash transaction paid to acquire Active Hotels Ltd. And Bookings B.V. was about US\$161 million and US\$ 133 million, respectively. Revenue for the 12 months ended June 30, 2005 was approximately US\$22 million for Active Hotels, up around 115% year over year, and US\$25 million for Booking.com, up around 100% year over year.

Combining the inventory of both companies, on all of its sites, Priceline acquired a database of almost 18,000 European hotels.⁸⁵ One of the first steps after Booking.com acquisition was to smoothly integrate, under continuous monitoring, the two acquired companies' business into Booking.com, which would operate under the agency model. ActiveHotels' partners had to switch over to use the Booking.com extranet and to receive respective training. Booking.com extranet had a distinctive feature: its preview button that could be used by hotels in exchange for a higher commission. This button allowed hotels to immediately view where their properties would appear in the site search results, simplifying the process.

The renewed company had an autonomous executive team, marketing budget and growth strategy from its parent company. The brand started receiving 12% in commissions instead of the 25%-30% given to the other OTAs and had to wait months to collect on prepaid bookings since customers booked online but only paid the hotel at checkout.⁸⁶ Moreover, consumers did not have to pay booking or administration fees.

Priceline.com primary objective was to become the top online hotel reservation in Europe.⁸⁷ The goal seemed very ambitious and hard to obtain for a company that, earlier, was almost only operating in the U.S. The objective was particularly difficult as they faced such a strong competition, especially from Expedia Inc. which, since 2002, operated in Europe through Hotels.com and from Sabre Holdings (Travelocity's parent) which operated through Lastminute.com. Although a later entrant in the European market,

Priceline.com chose to compete through a local company and grew much faster than its U.S. competitors⁸⁸. Cendant also bought a European rooted company, EBookers Plc.

Hotels.com worked with around 15,000 properties, in 2005, but soon they started expanding their reach maintaining their position of one of the hotel booking leaders.⁸⁹ Lastminute.com had not made a profit up to 2005 but, through the following years, they increased profitability while narrowing their portfolio of brands at the same time, which had reached a maximum of 25 brands, in Europe. They particularly grew on their hotel booking business and achieved a huge success with its "Top Secret Hotels" franchise, under the merchant model, becoming one of the leading hotel bookings players, in Europe too.⁹⁰

Booking.com's strategic plan to succeed was based on three main pillars. The first one was to take advantage of the fragmented European hotel reservation market and so, to focus on expansion amongst standalone hotels. This led to the second pillar, which was to improve their service by investing in their width of supply. An outsized inventory of hotels would mean added value to customers as their choice in destination and category-types would be amplified. Last but not the least, Booking.com invested huge amounts of money into search engine marketing.

Booking.com also adopted a persuasive design on its website, through mechanisms such as price discounts, disclosure of number of rooms still available per hotel, number of users seeing each ad and time of the last hotel reservation. These mechanisms put pressure on interested consumers of a specific hotel that, afraid of losing the opportunity, reserve their hotels quickly at Booking.com, without further reservation conditions comparisons.⁹¹ After Booking.com acquisition and expansion, revenues and net income started growing at an incredible pace. In 2006, about 40.6% of the Group's gross bookings were already originated from European operations and the agency business was the major source of gross profits, in a total of \$213.9 million comparing to merchant gross profits of \$ 182.16 million. Priceline Inc., an unprofitable firm in 2003, had reached a net income of \$74.5 million during 2006.⁹²

On the other side of the globe, another challenge had begun with the acquisition of Agoda. Agoda was a Bangkok (and Singapore)-based online travel company specialized in hotel discount bookings. Their network included 7,000 hotels in Asia, above 33,000 worldwide and a total of \$36 million in gross bookings, representing an increase of 122% over the previous year. The transaction consisted of an initial cash payment and a multi-year compensation based on performance. Following Priceline.com common practice, the

company maintained its management team, which would work independently from Priceline.com. Glenn Fogel, Priceline.com's Corporate Development and International Managing Director, was convinced the time was right to start growing presence in the Asia Pacific region, a market where internet usage, credit card adoption and domestic economies continued to grow.⁹³

Similarly to Booking.com, online and affiliate marketing consisted of the main instrument used by Agoda to generate traffic to their websites.⁹⁴ In fact, a substantial part of gross profits of the Group was used as marketing expenses and the value kept on aggressively growing, following the growth trend of revenues. In 2007, they spent \$172.7 million on online advertising expenses and \$36.0 in offline advertising expenses.⁹⁵ On the other hand, both companies had no advertising business distracting customers in their websites.⁹⁶

Throughout 2007, Priceline.com had created a social phenomenon in the United States with its most recent television *Priceline Negotiator* advertisement. Shatner appeared as Priceline Negotiator, which was a hard-bargaining professional negotiator stopped by nothing to have the best deals and the highest savings for Priceline.com's customers. For instance, he appeared "dispatching a lemur to find bargains and threatening a car rental agent with a falcon". People re-created the karate kick popularized by the commercial and talked about the ad through Twitter, Facebook and Youtube, similarly to earliest Priceline.com commercials where William Shatner appeared.

Priceline.com, in U.S., created also the campaign *No Fee* to emphasize the elimination of airline ticket booking fees.⁹⁷ Indeed, Priceline.com surprised customers by eliminating booking fees on published-price domestic and international airfares, taking advantage over competitors.

Soon, Priceline.com decided to modify hotel service fees too. The company lowered its booking fees for published-price hotel reservations and eliminated the existing fee to cancel or change a published-price hotel reservation, when almost all other major online hotel reservation services continued to charge about \$25 in change/cancel fees for certain reservations.⁹⁸ Over 16 months, the company devoured Expedia's market share and Expedia dropped in its gross bookings by 11.1% to \$4.0 billion while Priceline.com increased theirs by 22.9% to \$1.5 billion.⁹⁹

Even though reluctant, Expedia, Orbitz and Travelocity ended up cutting their fees in airline bookings as part of promotions that extended through May 2009. Expedia and Orbitz also cut hotel booking fees temporarily, in a moment where booking fees accounted for 6% to 8% of Expedia revenues and 10% for Orbitz's.¹⁰⁰

Cutting fees did not impede Priceline.com of continuously improving their business. On the contrary, the company signed several participation agreements and extensions with major airlines, such with Jet Blue that gave full access to its published fares, schedules and inventories. Additionally, Priceline.com started combining their traveler reviews with new exclusive Zagat Survey reviews and information for hotels, restaurants and attractions, covering over 600 cities.

As for 2007, Priceline.com achieved good results again. They increased their revenues in 25.5% over the previous year and net income raised 14.5% to \$155.5 million over the same period. The boom was particularly due to international services since, internationally, gross bookings increased 113.0% during the fourth quarter, over the previous year. However, even the domestic growth rate was driving above average, as it reached 24.2%. Additionally, the company could surpass rivals' market capitalization for the first time ([Exhibit 3](#)), as the pace of growth achieved by Priceline.com's stock was much faster than the one achieved by Expedia's.¹⁰¹

KITES RISE HIGHEST AGAINST THE WIND, NOT WITH IT

Jeffery H. Boyd believed that they were achieving sustainable growth internationally due to their wide geographic reach, new market initiatives and extensive inventory. In the end of 2007, the proposed goal had been achieved: only three years after their expansion to the continent, Priceline had become the online hotel reservation leader in Europe. The next goal was even more ambitious: the company yearned to become the worldwide online hotel reservation leader.¹⁰²

As the global online market continued to gain importance in the travel industry, customers had lower search costs and an easier accessibility to information. As a result, price-based competition was more intense for equal quality standards. These aspects contributed for the already competitive travel agency industry, which had low barriers to entry. Nevertheless, even before analyzing price possibilities, destinations were the consumers'

primary decision.¹⁰³ Therefore, agencies benefited if they had a larger breadth of destination options.¹⁰⁴

Besides internet mechanisms, consumers' consciousness to price was augmented by the economic crisis that began in the United States during 2008 and that had been especially extended to Europe. In fact, Europe consisted in the most affected continent as international tourist arrivals decreased about 2% between 2006 and 2009 (Exhibit 4)¹⁰⁵ Adding to one of the most severe periods the industry has ever lived (Exhibit 5), the world witnessed an additional shock on demand as the H1N1 influenza A virus started spreading around the world. Hotel occupancy rates and average daily rates decreased in 2008 with a special impact on demand for luxury accommodation, as well as long range destinations. However, short range destinations even rose above average. Business trips have seen their length and terms reduced, being often transformed into video and telephone conferences as a cost-cutting alternative to travels. With a decrease in demand and consequential cuts in tour operators' commissions and overall supply, travel agencies' activity was limited and in the first quarter of 2009, the decline in revenues cumulated 10%, globally, when compared to the same period of the previous year.¹⁰⁶ Despite the global economic conditions (Exhibit 6), and overall travel demand (Exhibit 7, 8 and 9), Priceline.com gross travel bookings increased more than 50% over 2007, totaling \$ 1.9 billion in revenue.¹⁰⁷ Not even, the "unprecedented economic turbulence", as Boyd stated, could stop Priceline.com performance. Although Priceline.com's stock capitalization fell in 2008, the fall was softer than Expedia's,¹⁰⁸ and one year later, in 2009, the net income of the Group increased about 211.6% comparing to 2007, as the company reached \$489,472 million in profits. The stock capitalization followed net income growth and Priceline.com was valued in about \$ 9.96 billion, twice as much their value in 2007.

The financial results were, in great part, a consequence of the growth of the acquired companies. One year after the acquisition of Agoda, the company's organic gross bookings had grown by more than 100%.¹⁰⁹ At the same time, Booking.com, under Kees Kolen leadership, continued strengthening its position as the largest and fastest-growing online hotel reservations service in Europe. Booking.com's supplier base increased by 47% year-over-year and their services were then spread over 60,000 properties and 70 countries, being accessible in 21 different languages.¹¹⁰ By this time, the company benefited from a partnership with the biggest European low cost carrier: hotel booking services appearing on Ryanair's website were provided by Booking.com.¹¹¹

Mr. Glenn D. Fogel, the Head of Priceline.com Worldwide Strategy and Planning, was confident about the company's vigor and he argued that "due to our size and flexibility, we are better positioned than many to adapt as the market changes".¹¹²

Indeed, there was no shortage of market change. Regarding technology, the adoption of mobile devices was growing worldwide and internet traffic was changing from computers to tablets and smartphone devices. This growing importance attributed to mobiles started producing a shift in power from search engines to smartphone manufacturers and developers, also leveraged by geolocalization services based on GPS technology.¹¹³

Attentive to consumers' movements, Priceline.com launched new mobile services for travelers, which were especially important for last-minute customers. Results were good: Booking.com's mobile apps were downloaded more than 20 million times from 2010 to 2012. This summed up around \$3 billion in mobile travel reservations only in 2012, triple that of one year ago, which reflected the fast adoption of smartphones from European users.¹¹⁴

Priceline.com was also aware and responsive to other changes in the industry, such as demand growth tendencies. Priceline.com continued investing in new and fast-growing markets like Asia-Pacific and South America, where there was a rapid online adoption. Agoda started teaming with Asia-Pacific airlines, like Air China and Jetstar Airways, in order to extend their hotel businesses in the Asia Pacific region. Expedia, on the other hand, built a joint venture with Air Asia.¹¹⁵ If analyzing the Chinese online travel agency market, Ctrip was the clear leader, far ahead from the second player, eLong, which belonged to Expedia. Agoda was distant from the top, being surpassed by many other travel agencies in the country, in regards to market share ([Exhibit 10](#)).

At the same time, the Group sustained its growth in Western Europe and North America. Besides the Priceline.com brand, Booking.com started growing in the United States market too and so, competing with their parent although they owned a different positioning. While Booking.com was a hotel reservation leader, Priceline.com was positioned as a discount-travel leader.¹¹⁶

During this time, Booking.com had been a growth driver for Priceline.com under Kees Koolen role as CEO, representing about 61% of its bookings and 75% of its consolidated operating income.¹¹⁷ Kees Koolen was one of the founders of Booking.com B.V. and assumed the role of CEO in 2008, being responsible for the rise of Booking.com into the

number-one hotel reservation service. However, in 2011, Koolen embraced Booking.com's chairman position, being replaced by Daren Huston, a former Microsoft executive.¹¹⁸

Change within the Group comprised travel segments as well, as Priceline.com reinforced their investment in rental cars, which was a piece in the business not very explored till the moment. They acquired the English multinational car hire reservation service Traveljigsaw Ltd. and aimed to become leaders in the segment. After the acquisition, the company retained the management team, who kept their minority ownership stake. Traveljigsaw had been established in 2004, being the fastest growing online car rental agency in the world with a presence in 80 countries across the globe and owner of more than 40,000 locations with a full range of vehicles, permitting that customers could rent cars and vans they were familiarized with.¹¹⁹ Expedia Inc. operated in the rental car business especially through Car Rentals.com, a smaller and less global business.¹²⁰

Traveljigsaw enhanced its rental car platform and website and started working closely with Booking.com and Agoda, in order to build distribution and as a part of cross-promotion between brands.¹²¹ To improve cohesion among them, in the beginning of 2013, Priceline.com Inc. announced the promotion of Daren Huston, CEO of Booking.com, to manage the international brands Booking.com, Agoda.com and Rentalcars.com, although all of them continued with independent leadership teams. Huston became responsible for inter-brand relations in terms of sale of technology, best practices, coordination of relationships with customers, supply and affiliates and even, when needed, of the development strategy regarding geographic expansion and competition among brands.¹²²

From 2008 to 2011, the Group saw its net income increase about 479%, as they achieved profits of \$1,056 million during 2011, one year after surpassing their major rivals EBITDA for the first time in history, (Exhibit 11) and their stock valuation reflected the success (Exhibit3). Even though Priceline.com still operated with its NYOP model in the United States, the disclosed-price model was the major source of Priceline.com's revenues and the reason for Priceline.com hotel reservation worldwide leadership. Moreover, the international business, particularly boosted by the European market but expanding reach in the Asia Pacific area, weighted 78% of gross bookings and 88% of consolidated operating income in 2011.¹²³

Following its strategy, Priceline.com always reserved a great amount of profits for online advertising. In 2011, Priceline.com invested a total sum of \$919.2 million in online

advertising. In the particular case of Booking.com, the larger hotel inventory when comparing with competitors and the know-how on search engine owned by the marketing team allowed them to leverage their set of keywords and to have better conversion rates.^{124 125 126}

Priceline.com Inc. was one of the major investors in Google Ad words, being first among the online travel agencies (OTAs). The total advertising of the Group signified about 25% of their revenues, in 2012, above the 22% spent by its major rival, Expedia. From those 25%, about \$1.14 billion was spent with Google, the main benefited party from online travel agencies advertising rivalry.

However, more than a channel, Google had become a significant threat as a meta-search engine. In 2011, Google introduced the Hotel Finder service, an accommodation search service, and acquired ITA Software Inc., a provider of flight prices and itineraries.¹²⁷

As a response to the threat, Priceline.com acquired Kayak Software Corp. for \$1.8 billion, while Expedia bought Trivago for about \$630 million, as well as the travel-search start-up site Room 77 Inc. Kayak was a travel meta-search engine created by cofounders of Expedia, Travelocity and Orbitz, in 2004, which went officially public in April, 2011. The engine compared airline (including hacker fares which consist on the purchase of two or more one-way tickets from different airlines), hotel, car rental, cruises and other vacation products from other travel websites. Nevertheless, by this time, online travel agencies were still the most important channel used by active travelers, far ahead from meta-search engines, while branded supplier sites continued to be the second most important channel.¹²⁸ In terms of profits, online travel agencies also surpass meta-search firms, because while the first receives a flat booking fee, – around 15%, in case of Booking.com - the second only received per click – around 7%.¹²⁹

Expedia Inc. is the leader in total bookings, since they provided a total of \$34 billion bookings throughout 2012 against Priceline.com Inc.'s \$28 billion. However, Priceline.com Inc.'s dominates business related to the European market ([Exhibit 12](#)) and to hotel bookings, which is the most lucrative segment amongst travel services. In fact, commissions can reach 30% for some hotels whilst airlines only reach around 2%.¹³⁰ This can justify the difference between Priceline.com's market capitalization and competitors'. Actually, the Group was the best-performing stock company in the Standard & Poor's 500 over the past five years, rising 519%.

The results Priceline.com has been obtaining reflect their accurate decision making. Boyd and Huston seem an unbeatable team, presenting incredible growth rates, despite all inconveniences and distresses on the way. But are they really unbeatable? And will Huston continue its successful path with Booking.com even diffusing attention to other Priceline.com Inc.'s businesses? Moreover, will Priceline.com be as successful in emerging countries as they were in Europe?

On the other hand, Priceline.com has never lost track amongst strong competitors. However, can Google be transformed into Priceline.com's reason for decline? Or will the power of the meta-search engine giant be only an illusion, as mobile services gain importance? If the Google threat materializes, will Priceline.com be able to compete against the giant with its recently acquired search engine, Kayak? After all, is Priceline.com's market capitalization faithful to their performance and does it have margin to grow? There is nothing certain, but the uncertain.

III. TEACHING NOTE

Priceline.com Inc. started its online operations in 1998. They created a distinctive business model called “Name Your Own Price”, which consisted in a blind auction where customers defined the price to pay for an airline ticket in exchange for a high level of flexibility regarding time of the flight and airlines companies, among other limiting conditions. Airline companies agreed with the deal as they could continue selling their tickets through the traditional way while benefiting from incremental revenues for trading empty seats, which would have their value vanished if not occupied.

The idea seemed very promising and Priceline.com Inc. quickly replicated the model to other markets. In 1999, the company was already offering airline tickets, hotel bookings, car rentals, car sales, financial services and, indirectly, gas and groceries. The company became publicly traded in this year and benefited from all the dot-com bubble overexcitement towards internet-based companies, which allied with high expectations that investors had for the business, made the value of their stock augment ten times, in few months.

Nevertheless, problems started arising and 2001 meant a terrible year in Priceline.com Inc.’s history. The investment on groceries and gas through the WebHouse Club was a total disaster, adding to the fact that Priceline.com services were receiving a bad feedback from customers, involving several complaints. Moreover, as true as Priceline.com had benefited from the dot-com bubble created, the company was also severely affected by the burst of the bubble and their stock suffered a sharp decline: in about one year it decreased from about \$162 to only \$1. The burst of the bubble resulted in an economic recession in U.S., which allied with the terrorist attack of 9/11 and some other conflicts such as the Iraq war, had a huge impact on the travel industry and particularly, changed the structure of the airline market. In fact, it was a dark period for airline companies. In order to adapt to changes on demand, the carriers had to reduce prices and downsize the offer.

Those were bad news for Priceline.com business and actually, their “Name Your Own Price” was losing customers, affecting the company’s results, as they more than doubled their net deficit over the previous year, reaching a negative value of \$19,184 million .

After some successive changes in the board, Jeffery Boyd, the new CEO, took the responsibility to put Priceline.com back on track by making some risky and controversial decisions. First, he dismissed attention to the “Name Your Own Price” business model.

Second, he concentrated their efforts into the hotel reservation services. Third, he invested in internationalization, through consecutive strategic acquisitions.

It would have been difficult that any other new CEO could have had much more success than Boyd. In the first whole year of Boyd as CEO, Priceline.com achieved positive results for the first time in five years. From that moment on, the company achieved exponential growth, especially through Booking.com (which resulted from a merger between two acquired companies, Active Hotels and Booking B.V.). Booking.com was specialized in hotel reservations and, across time, they achieved the leadership of the European hotel reservations market. Europe was a very attractive market and their hotel business provided vastly higher commissions to travel agencies than airline services did, which can justify the difference in market valuation between Priceline.com and their competitors. Moreover, the company expanded to Asia, through an acquisition of another company: Agoda, which was an Asian online agency that operated under a merchant model. Agoda grew also beneath Priceline.com control, although the company never reached the success that Booking.com did.

Having achieved their objective of leading the hotel reservation market, Priceline.com Inc. delineated another objective: to grow in the car rental segment. Priceline.com acquired a specialized company, called TravelJigsaw and transformed it into RentalCars.com.

Priceline.com has only seen a decrease in its profits once (in 2008) since 2003. In fact, the company always presented soaring results growth, reflected in their stock valuation. For the records, the company was the fast-growing stock in Standard & Poor's 500, rising 519% from 2008 to 2012. The company is nowadays trying to expand their business in emerging markets such as in Asia and in South America and investing in their mobile services, which had their revenues tripled from 2011 to 2012. At the same time, Priceline.com is trying to fight an intimidating threat from Google with a new acquisition, Kayak, as the meta-search engine giant has invested in a search engine directed to the travel market.

TEACHING PURPOSE:

The present case is targeted for Business Administration students, preferably serving as a dynamic capabilities illustration for Strategy courses. It is suited either for undergraduate or Masters' program, having as a prerequisite some knowledge on strategy, particularly, on Porter's 5 Forces Analysis and the Resource Base Theory.

Students are required to:

✈ Analyze the different elements (clients, suppliers, competitors, substitutes and potential entrants) comprised on the overall travel industry, with particular emphasis in the online travel industry. They should use Porter's Five Forces framework and must be able to recognize structural differences in the industry along time.

✈ Notice the vulnerability and so, the fast-changing nature of the travel industry during the period explored by the Teaching Case. They must be able to perceive the dot.com bubble as a huge shock on Priceline.com market value, as well as the impact of the post-dot.com bubble recession, the terrorist attack of 9/11 and the economical crisis started in 2008 in Priceline.com's performance.

✈ Understand the main strategic directions followed by the company, concerning acquisitions, internationalization and industry specialization, especially towards hotels and recently, car rentals.

✈ Analyze Priceline.com strategy through the Dynamic Capabilities literature, particularly evaluating Priceline.com performance on each dimension of the view.

TEACHING PLAN

The teaching plan is divided into six main sections. The first section, **Contributions**, presents the body of knowledge that the case intends to offer. The second section, **Accompanying Readings**, refers to some useful supporting readings for a better contextualization of the case. The third section, **Suggested Assignment Questions**, is constituted from exploring questions which can extract a high-quality analysis from the case, in line with its teaching purpose. The fifth section, **Suggested Answers**, provides an approach for answers that students should follow, particularly mentioning the main topics to be understood and explored as well as timings required for responses. It should be noticed that there is not one single answer. The closing section, **Lessons**, refers to the principal conclusions from the case in relation to the literature of Dynamic Capabilities.

CONTRIBUTIONS

The present teaching case has the major purpose of contributing with practical evidence for the dynamic capabilities literature. In particular, the case intends to illustrate the success of a company within a fast-changing environment, subject of several shocks.

According to the literature, dynamic capabilities are vital to address this high-velocity change. Each dimension that forms the new definition of dynamic capabilities will be analyzed in order to test the presence and the magnitude of dynamic capabilities

throughout the history of Priceline.com. As we explore the decisions taken by the firm we can assess the propensity of the company to sense opportunities and threats, to make timely and market oriented decisions and to change its resource base, as well as perceive how these dimensions relate among themselves.

The ending contribution would be to support or reject the importance of each dimension for the successful performance of the company, as the literature suggests a link between dynamic capabilities and performance.

ACCOMPANYING READINGS

For the instructor to be better prepared, it would be useful a supporting reading about the dynamic capabilities' theory. For this purpose I suggest "Dynamic Capabilities: A Review of Past Research and an Agenda for the Future," (Ilídio Barreto, Journal of Management, January 2010). Students would also have benefit from other authors' articles that contribute to the literature.

Additional readings about the travel industry can be helpful, which can be obtained by the ITB World Travel Trend Report 2012/2013, created by IPK International. For a deeper understanding of the European travel industry I also recommend TOURISMLink Report, made available by the European Commission, in 2012.

Finally, Priceline.com's Annual Reports provide information in further detail about how the merchant model functioned for the different markets, as well as about strategic decisions and the financial reality.

SUGGESTED ASSIGNMENT QUESTIONS

1. Analyze the shocks that most affected the travel industry since 1998. **(25)**
2. Identify the key strategic decisions taken by Priceline.com Inc. and analyze them according to the dynamic capabilities view. **(25')**
3. In your opinion, what are the changes occurred in the travel industry that presage major challenges for Priceline.com in the future? **(15')**

SUGGESTED ANSWERS

1. **Analyze the shocks that most affected the travel industry (25').**

Students must be able to recognize a large range of shocks with an emphasis for the economic, technological and behavioral shocks mentioned below (since they had a wider and more intense impact on the industry and so, they were further developed in the case).

Students should also refer the main important consequences derived from each shock, especially relating them with the travel demand.

Type of Shock	Shocks	Major Impact
Economic	Dot-com bubble	Bankruptcy of several dot-com companies; growth and posterior decrease of online travel companies market value.
	Post Dot-com bubble Recession	Decrease in overall demand, cost reductions of airline tickets and increase of price competition; bankruptcy of airline companies.
	Debt Crisis - 2008	Decrease in demand (especially in Europe).
	Rise in domestic economies of emerging markets	Increase in demand from emerging markets, increase in online and mobile penetration; penetration of travel agencies in these countries.
Technological	Introduction of smartphones and tablets	New kind of purchase; see Mobile Penetration.
	Rise of travel meta-search engines	Cost reductions for consumers (no fees); decrease of power for online travel agencies (and increase of power for airline companies and hotels.)
Behavioral	Online penetration	Increase of consumer access to information, search costs reductions. Higher customers' sensitivity to price.
	Mobile penetration	Increase in demand for last minute customers, decrease of power for meta search engines providers.
Political	European Union enlargement to 25 countries	Increase in European intracontinental flows; increase in flights and hotel bookings.
Others	Terrorist attack of 9/11	Consumers' insecurity to travel; decrease in demand of airline tickets.
	Iraq war	Decrease in overall demand.
	SARS	Decrease in demand (especially in Asian countries).
	Penetration of low costs in the European Market	Increase of intracontinental demand in Europe; either for quantity of airline tickets or for hotel reservations.
	Japanese Hurricane	Decrease in Japanese arrivals.

2. Identify the most important shocks occurred between 2000 and 2002 and the key strategic decisions taken by Priceline.com afterwards. Analyze these decisions according to the dynamic capabilities view (25’).

Recalling the emergent definition suggested by Barreto (2010), dynamic capabilities are the “firm’s potential to systematically solve problems, formed by its propensity to sense opportunities and threats, to make timely and market-oriented decisions, and to change its resource base.” In the following table we can identify the most important shocks and the main strategic decisions taken, being analyzed according to the definition just described:

Main Shocks:
Post dot-com bubble recession and 9/11 terrorist attack on World Trade Center.
Briefly Description of the impacts:
Those shocks have generated a reduction in the market demand for flights, which cause airlines downsize the offer and diminish prices for airline tickets. Several major airlines filed for bankruptcy.
Main reactions by Priceline.com:
Focus on hotel reservation model;
Internationalization;
Introduction of the agency model.
Propensity to sense opportunities and threats (D1) was high.
Priceline.com was able to recognize opportunity factors in unexploited areas of the travel industry, which could be leveraged by them and positively contribute to their performance and growth, like:
The hotel reservations market was more fragmented and less price competitive than the airlines market, which could worth the focus of Priceline.com;
Priceline.com’s NYOP model used in the hotel reservations market was growing, which was an additional incentive for the focus in the hotel reservations market;
Both Europe and Asia-Pacific were an opportunity in terms of market size, growth and nature;
Internet penetration was growing in Europe and Asia, which could contribute for the increase of their customers base there;
Only using the NYOP model, the company was just capturing a niche of the market which included consumers who were more flexible; therefore expanding to the traditional model was an opportunity to vastly expand their customers base too.
Propensity to make timely decisions (D2) was medium.
Priceline.com was not one of the first players in the areas where they decided to invest:
The European and Asia-Pacific hotel reservations market had already important local players, which could bring difficulties for Priceline.com to grow;
The traditional purchase model was already being used by all their competitors when Priceline.com started using it.
However, the investment and exploitation time was still favorable for Priceline.com’s growth, since:
The travel market was growing in Europe and Asia-Pacific;
There was a huge potential to leverage their breadth of supply, especially in Europe;
The online penetration on customers’ purchases was growing either in Europe or Asia-Pacific;
Domestic economies and credit card use were growing especially in Asia Pacific.
Propensity to make market-oriented decisions (D3) was high.
The company has continuously delivered important value to their customers by:
The creation of an attractive and effective website design – different features and no ads;
The proximity with customers through advertisements (they created a social phenomenon);
The large range of hotels;
Low Prices;
No fees (2007);
A high response to customers’ search (high investment in Google Adwords);
Cross-sales.
The company also provided value to their suppliers, particularly because:
Some independent hotels lacked their own website and could benefit from Priceline.com’s;
Hotels augmented their access to a larger customers base.
Propensity to change the resources base (D4) was high.
The company has continuously changed their resources base, through:
The constant addition of know-how;
The continuing enlargement of the range of supply (locally and internationally);
Several acquisitions (Active Hotels, Booking.com;Agoda; Rentalcars; Kayak);
Several partnerships (Travelocity, Ctrip; Ryanair).

From the table above, we can identify the different dimensions of dynamic capabilities existent within the company, by identifying several actions taken by the firm in a way to solve problems, particularly arisen from these shocks. We can conclude that Priceline.com showed a high propensity for sensing opportunities and threats, for making market oriented decisions and for changing the resources base and a medium propensity to make decisions on a timely manner. Therefore, Priceline.com showed a high potential to solve the problems due to their dynamic capabilities.

3. In your opinion, what are the major challenges and opportunities for Priceline.com in the future (15')?

This question is up to discussion, as there are multiple challenges and opportunities one can find in Priceline.com's future path, some of them difficult to predict. Based on the case though, there are some challenges and opportunities which must gain further reflection:

Potential Challenges

One major challenge Priceline.com face is the potential rise of the importance of meta-search engines, especially attributed to Google. In fact, Google is the leader in the global search engine market, although still lacking leadership in some countries like China. If meta-search engines gain importance in the industry, it will constitute another strong source of competition for Priceline.com. Moreover, this kind of competition can achieve different remarks: on the one hand, as search engines receive money per click instead of fees paid by suppliers, they can result in price reductions over bookings. As so, there is a strong possibility that customers, more sensitive to price than ever, quickly adopt this method to purchase travel services. On the other hand, suppliers can gain their power back, lowering fees paid to intermediaries or not even using the intermediaries' service, which can make agencies very fragile.

Second, the weight of Europe in the worldwide tourism has been decreasing. As Priceline.com's revenues especially depend on this market, they can be affected by the trend. Moreover, the debt crisis has not seen its end yet, having the possibility to become more and more severe, which can augment its negative impact over the travel industry.

Third, the market value of Priceline.com is, when compared with its competitors, high. Priceline.com must be able to sustain the investors' confidence in their business, striving to maintain their growth rate trend. This can be particularly difficult to execute, as accomplishments have been extremely good for a long time now.

Potential Opportunities

Opposite to the increasing importance of the search engines, Priceline.com can take advantage of the customers' adoption of mobile services, as smartphone and tablet penetration increases, as well as travel purchases through them.

Emerging markets can signify a huge growth opportunity for Priceline.com Inc. since economic power is increasing there, which is a crucial factor for the growth of the tourism market. Moreover, online adoption rate in emerging markets is increasing. Priceline.com has still a high margin to grow in these markets, like China, where they did not achieve a solid position (yet).

LESSONS

The travel industry has suffered several kinds of shocks. The economic shocks had the highest impact on the industry, which includes the impact over Priceline.com. Social, technologic and political shocks also generated some shifts in the market.

Priceline.com has shown a high propensity in regards to the four different dimensions, therefore the company has presented a high potential to systematically solve problems.

The continuously change in the environment can generate either opportunities or threats for Priceline.com. The future geographical travel distribution and growth, allied with the importance of search engines and mobiles as travel services providers are important question marks, which will contribute to define the upcoming path of Priceline.com.

IV. DISCUSSION

The objective of this section is to provide a relation between the literature review developed on dynamic capabilities (DCs) and the real life business history presented with the teaching case. I will particularly focus my analysis on the new definition of dynamic capabilities and on previous studies which link dynamic capabilities to performance, being my intention to find evidence that supports the literature or not. I do not intend, however, to conclude on the proof or rejection of the theory based on one single real case, but to contribute for the pool of evidence that, as a whole, can do it. Furthermore, I will briefly discuss over some limitations still existent on the literature.

The business history is about Priceline.com. This company operates in a fast changing environment, which is an important condition for the analysis since the literature on DCs is especially distinctive from previous theories (Porter's Five Forces and the Resource Base Theory) because it is able to address a dynamic context (Teece, 2007). In fact, the travel industry is highly vulnerable to an enormous variety of shocks such as economic (e.g. dot-com bubble, post-bubble recession, oil price variations, the debt crisis of 2008, growing economic power of emerging countries), technological (e.g. launch of smartphones and tablets); behavioral (e.g. penetration of internet use, penetration of mobile bookings) or several other influent periodic events such as diseases (e.g. SARS), natural disasters (e.g. Japanese hurricane), terrorist attacks (e.g. 9/11 in United States) and wars (e.g. Iraq). Besides, the industry has low barriers to entry, which implies constant competitive threats for existing players.

Does Priceline.com possess dynamic capabilities to deal with those shocks? Recalling the emergent definition suggested by Barreto (2010, p. 271), dynamic capabilities are the *"firm's potential to systematically solve problems, formed by its propensity to sense opportunities and threats, to make timely and market-oriented decisions, and to change its resource base."* These four mentioned dimensions are related among them in an aggregate multidimensional construct. It is an aggregate construct because it is formed by the dimensions rather than being manifested into the dimensions (Law et al., 1998).

Starting with the propensity to sense opportunities and threats, we can perceive that the primary opportunity discovered by Priceline.com was the creation of the company itself as pioneer of the "Name Your Own Price" model. Behind the opportunity, there was a technological and a behavioral shock: the development and adoption of the internet. Priceline.com replicated the new kind of auction, firstly created for airline tickets, to a wide range of different products. Some of which revealed to be important for

Priceline.com's success (such as the hotel reservation or the car rental service), some other were negative for their performance (like in groceries and gas).

Priceline.com was also able to sense opportunities and threats that especially emerged from some of the most important exogenous shocks, during the early years of operations: the dot-com bubble, its respective dot-com bubble recession and the terrorist attack on 9th September 2001. They have generated a reduction on the demand for flights, which cause airlines downsize the offer and diminish prices for airline tickets. The travel industry was negatively affected as a whole, suffering a further structural and functional modification with the creation of Orbitz, by major U.S. airlines.

Having their environment severely changed and their performance affected, Priceline.com searched for solutions. Even though the U.S. airline market was becoming less attractive, there was still a large amount of opportunities in the travel industry to be explored. Priceline.com was able to perceive hotel bookings as an area where they should invest. Additionally, the company sensed the opportunity of growing internationally, particularly in Europe and Asia-Pacific. Both regions were an opportunity in terms of market size, growth and nature. The company was also able to perceive that, even though the company was the originator of a business model with a vast potential, they were just capturing a niche of the market consisting of consumers who were more flexible. As so, Priceline.com considered the opportunity of enlarging the choice of customers using the traditional model, the one that other agencies also used. Considering the shock of Google's entry as a direct competitor, Priceline.com was able to sense the threat and reacted to it.

It can be easily perceived that these new markets (hotel reservations, new regions and the search engine) or the traditional model were there "waiting to be discovered" (Alvarez & Barney, 2007). Priceline.com just had to notice the opportunity, not to search for it, or even just decide to invest towards those directions (decision making dimension).

The opportunities I mentioned above were the ones which actually materialized into actions, passing from a phase of decision making. There are two decision making dimensions comprised in the definition: one covers the time of the decision making whereas the other covers its market orientation, which is mainly given by the actual value perceived by customers (Priem, 2007).

As we could perceive throughout the case, Priceline.com had a first mover advantage with their NYOP model. When the company started to offer services under the agency model, which resulted in their major source of profits, the traditional model was already being

used by all their competitors; therefore Priceline.com was a late player. Regarding internationalization, the European hotel reservation market had already important local players, including the major U.S. OTAs, such Expedia and Travelocity. The same held true when they entered in the Asia Pacific market. However, the investment of Priceline.com still meant a time-to-market decision, since the context was one of growth in both regions.

As a meta-search engine provider, Priceline.com lacked the desirable timing since Google was the global search engine leader, not giving much space for competition. In several other operational decisions, Priceline.com was timely effective, such as in the offer of mobile services, as they responded in a timely manner to customers' demand. Consequently, though the potential for making timely decisions existed and was important in some crucial moments, it was not so evident in others, which can compromise Priceline.com's future.

The propensity to make market oriented decisions was high and clear across Priceline.com's history, as the company has continuously delivered important value to their customers. On the one hand, the investment on the hotel reservations revealed to be market oriented. On the other hand, they revealed to be extremely focused on customers' needs in all their segments, as their decisions on marketing, website design, prices and range of supply, among others, show).

Last but not the least, the company has shown a high propensity to change their resources base, which is worth to be explored using the GAP model (Teng, 2007). According to the GAP model, when a company set a specific strategy lacking the resources to achieve it, there is a gap of resources that must be fulfilled. The company opted to obtain those resources outside, through acquisitions. The main advantage of these acquisitions was enabling Priceline.com Inc. to grow rapidly, which is important in a hypercompetitive environment (D'Aveni, 1994). However, according to the literature, acquisitions could have brought some difficulties, especially at firm's integration level. Maybe for that reason, Priceline.com Inc. opted to have larger costs in maintaining the independence of companies. The only exception occurred with the merger between Active Hotels and Booking.com, which operated in the same business and in the same geographical market (Europe). Similarities between companies can suggest less integration problems. The acquisition strategy has been used several times across Priceline.com Inc.'s history: Active Hotels, Booking.com, Agoda, Rentalcars.com and Kayak were the most important acquired companies. Resources were constantly changing if considering the expansion of the width

of supply in one region too. Partnerships made by Priceline.com can also be considered as an alternative to achieve resources, although giving only a temporary access to them.

Overall, after important shocks Priceline.com has shown a high propensity to sense opportunities and threats, a medium propensity to make timely decisions, a high propensity to make market oriented decisions and a high propensity to change their resource base. Summing up, the mentioned propensity for the four dimensions converges to the firm's high potential to systematically solve problems within a fast-changing environment.

However, the propensity regarding these dimensions was not so evident in the early years, before Jeffery Boyd's role as CEO, which can be related with a lower performance by the firm during this period. Later, the case though showed a link between the existence of dynamic capabilities and the good performance of Priceline.com. In fact, the company has continuously and exponentially increased their revenues, gross profits, net income and market capitalization, even during a severe crisis. The only year when net profits decreased was 2008 but the economic recession did not affect Priceline.com Inc.'s business as the post-bubble recession did, proving that the company has created some mechanisms against the negative economic impact on the industry

Following Teece et al.'s (2007) belief, Priceline.com's DCs were decisive to address the fast changing environment where the company operated. Nevertheless, there was no evidence that the aim of DCs was extended to the effective creation of market change, defended by Eisenhardt and Martin (2000).

Moreover, the case demonstrated a positive relation among dimensions. However, making timely and market oriented decisions can be complementary (such as in the case of the internationalization to the European hotel reservations market) or opposing (such as in the case of the groceries and gas investment, as they launched the service soon but they lacked market orientation).

Furthermore, Eisenhardt and Martin (2000) stated the existence of idiosyncratic details beyond the common features of DCs across firms. They defended that one specific dynamic capability could be derived from multiple paths and that DCs can produce differentiated performance levels. We can verify this throughout the case, if comparing Priceline.com and their competitors' decisions. For example, Hotels was the subsidiary chosen from Expedia to compete in the European hotel reservation market, but contrary to Booking.com, this

acquisition was not originated in Europe. Both companies were market-oriented despite the difference in this important detail. Their performance was different too.

Adding to the contributions, the case also encloses some limitations. The literature still lacks precision on defining the concept of the timely decision making. If we know that market oriented decisions are those who create value for customers, particularly through the design and performance of the product or business model, we are not able to define what is to make timely decisions. Sometimes, companies benefit as first movers, sometimes they benefit from avoiding the problems that first movers went through. Decisions should not be taken too soon or too late, but what determines the correct moment? The theoretical development of this dimension would be useful to better understand success and to be applicable on real-life situations.

Other limitation is the extent to which the case represents a contribution to the literature. It must be reminded that this case should be complemented with other real world business cases, in order to provide substantive evidence to the literature.

CONCLUSION:

The Dynamic Capabilities View strives to provide insights on how a company can accomplish competitive advantages on fast-changing environments. However, this View refers to the pursuit of temporary competitive advantages instead of sustainable competitive advantages considered in previous theories. Companies which present a higher adaptation capacity to change will be more able to succeed.

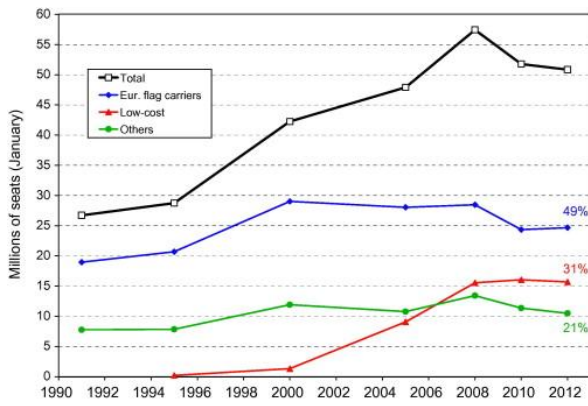
The literature of Dynamic Capabilities that has been developed by several researchers revealed to be important for managerial decisions but provided though some margin for improvement and solidification, which Barreto (2010) tried to fill when suggesting a new definition for DCs. The new definition encompasses the objective of being non-tautological, on the one hand, and operationalizable, on the other.

The mentioned literature was particularly analyzed through a teaching case. The case involves Priceline.com's story, having for scenario the travel industry, which is strongly and constantly affected by different shocks. Priceline.com moved from a trembling performance in the early years to become one of the leaders within the travel industry. The company has shown that they owned dynamic capabilities and, in consequence, the capacity to attain growth and success. As a matter of fact, Priceline.com has presented a high capacity for sensing opportunities and threats, for making market-oriented decisions and for changing its resource base, while showing a medium capacity to make timely decisions. Thus, the company has been vigorous in the four dimensions of the Dynamic Capabilities view.

Concluding, the case contributed for the literature with important elements about DCs and provided additional evidence for the relevance of the Dynamic Capabilities View. This View is extremely important as, beyond research purposes, it has a crucial role on the practice of management and the achievement of a successful performance by a firm.

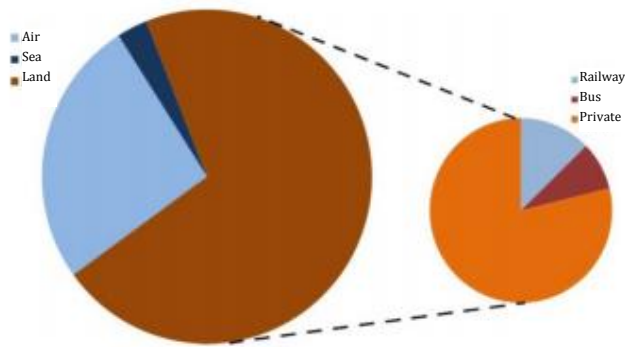
APPENDIX:

Exhibit 1: Intra-European air services (take-offs from UE27, Iceland, Norway and Switzerland)



Source: The geography of European low-cost airline networks: a contemporary analysis, Journal of Transport Geography, 2013, Vol. 28, p.

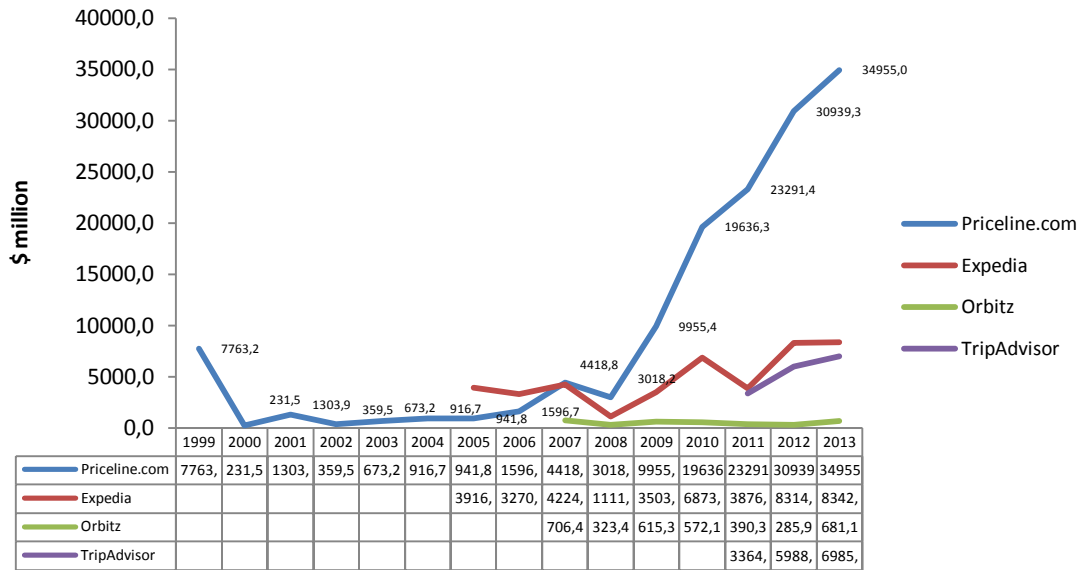
Exhibit 2: Main means of transport for European tourists



Source: Eurostat, 2009

Exhibit 3: Stock Market Capitalization of main U.S. OTAs

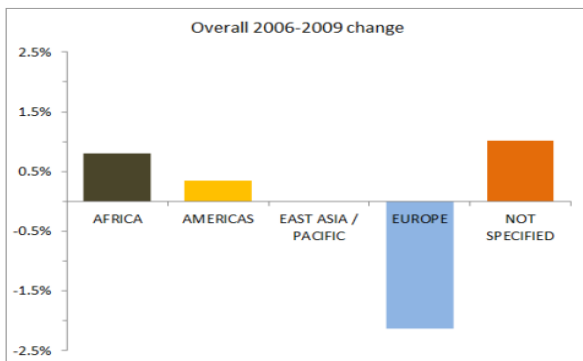
Stock Market Capitalization of the main U.S. OTAs*



Source: Bloomberg, 2013

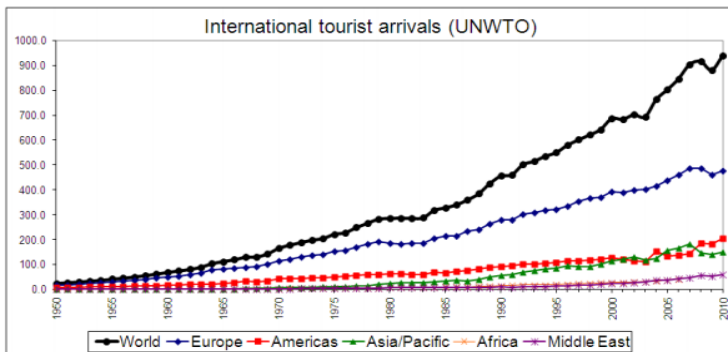
*Main U.S. OTAs include Travelocity which is not a public company.

Exhibit 4 – International tourist arrivals variation, 2006-2009



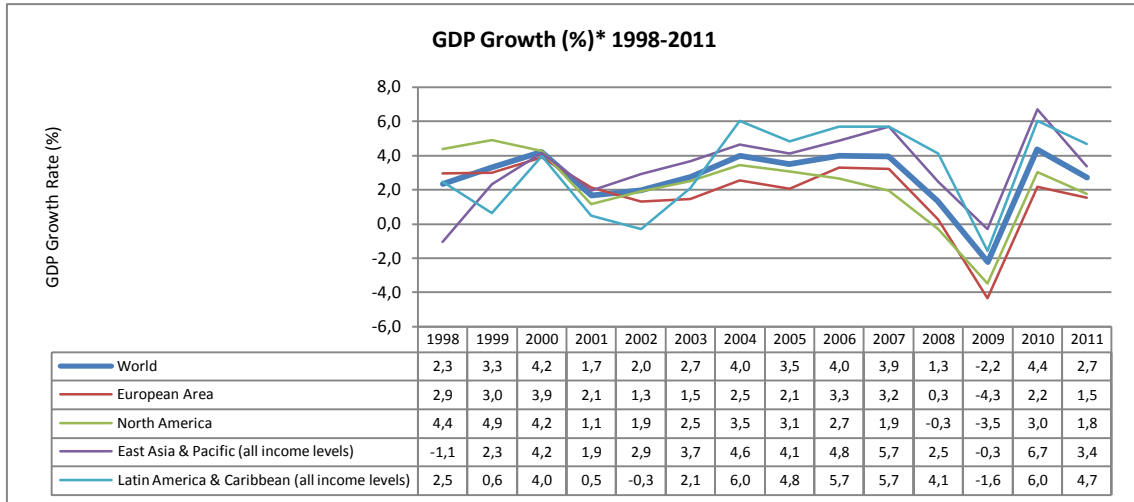
Source: UNWTO, 2011

Exhibit 5 – International tourist arrivals



Source: UNWTO, 2011

Exhibit 6: GDP Growth, 1998-2011



Source: World Tourism Organization (UNWTO) ©

*GDP data are in current \$US and euro (based on the average annual exchangerate for euro or ECU to \$US) and can be strongly influenced by exchange rate fluctuations.

Exhibit 7: Impact on global tourism, 1996 -2009

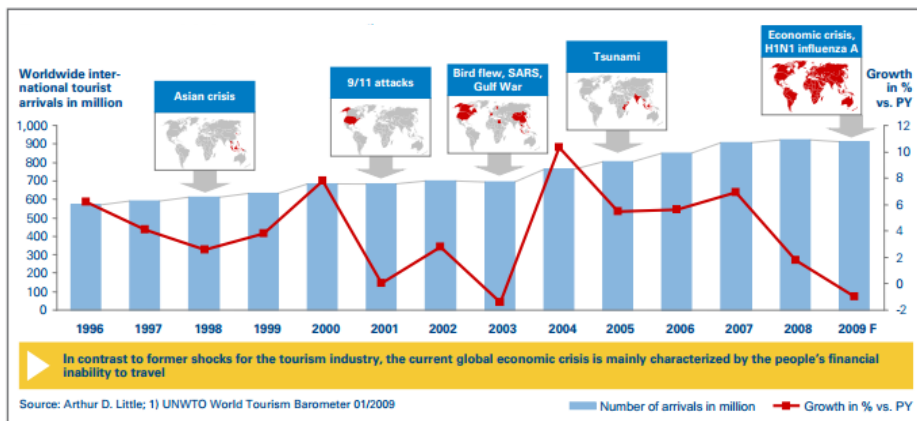
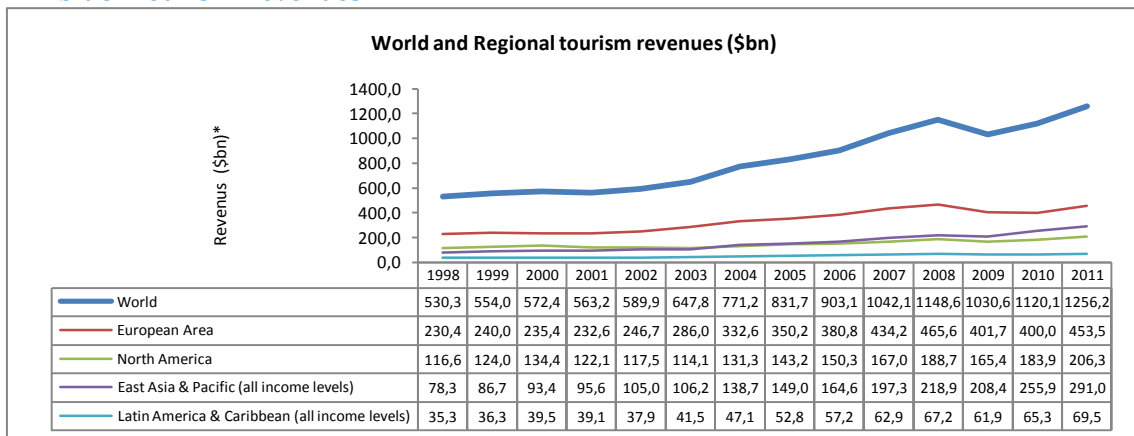


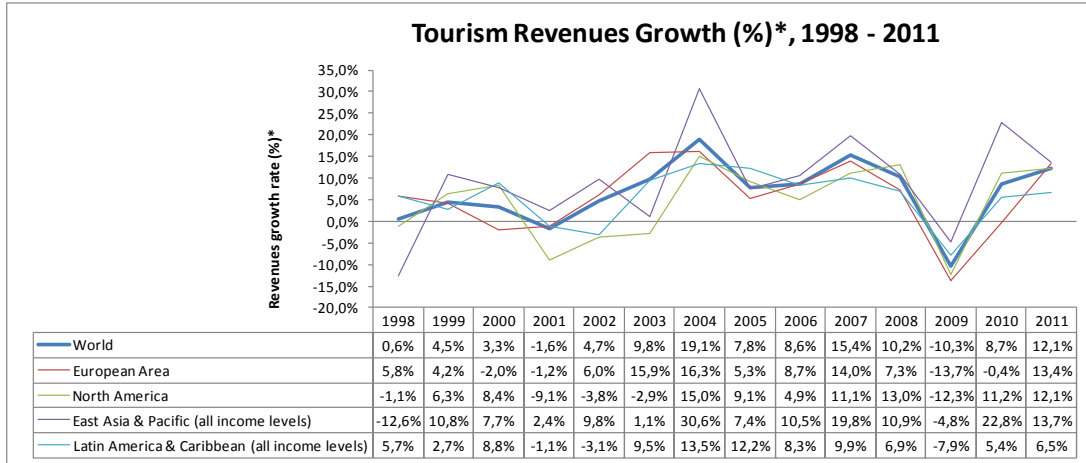
Exhibit 8: Tourism Revenues



Source: World Tourism Organization (UNWTO) ©

*Revenues data are in current \$US and euro (based on the average annual exchangerate for euro or ECU to \$US) and can be strongly influenced by exchange rate fluctuations.

Exhibit 9: Tourism Revenues Growth



Source: World Tourism Organization (UNWTO) ©

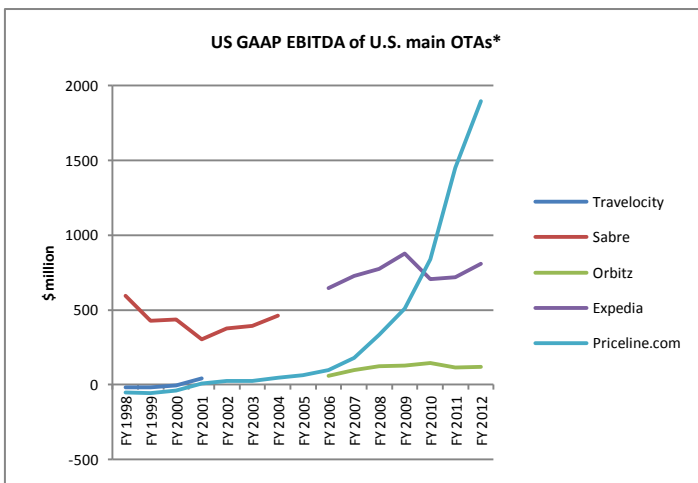
*Revenues data are in current \$US and euro (based on the average annual exchangerate for euro or ECU to \$US) and can be strongly influenced by exchange rate fluctuations.

Exhibit 10: China Online travel Agency Market Share, 2012



Source: Entodesk

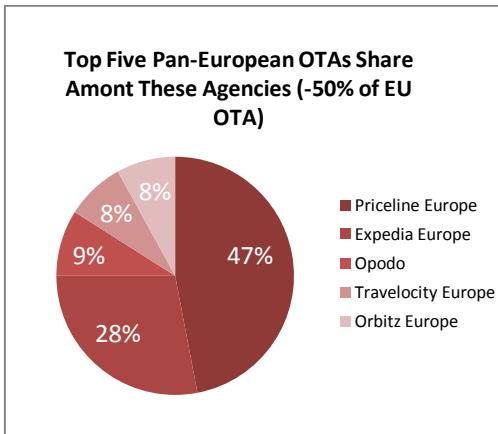
Exhibit 11: U.S. GAAP EBITDA of U.S. main OTAs



Source: Bloomberg, 2013

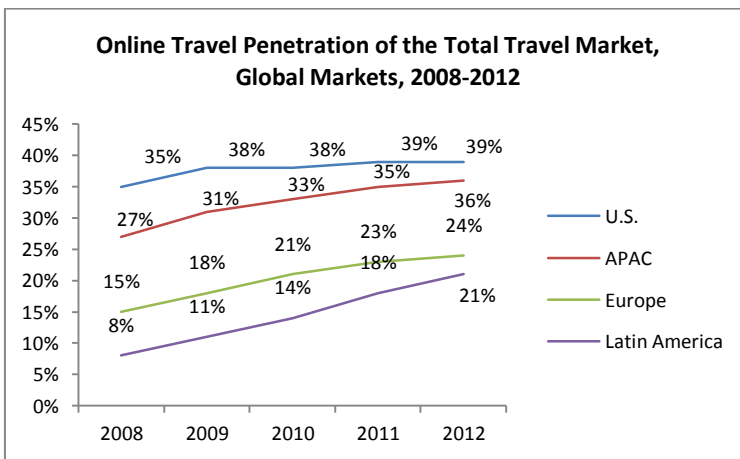
*values disclosed only for public traded companies. In 2002, Sabre acquired owned Travelocity, which was acquired later by TPG Capital and Silver Lake Partners. Expedia was owned by multiple firms and Orbitz was owned by Cedant.

Exhibit 12: Market Share among Top Five Pan-European OTAs



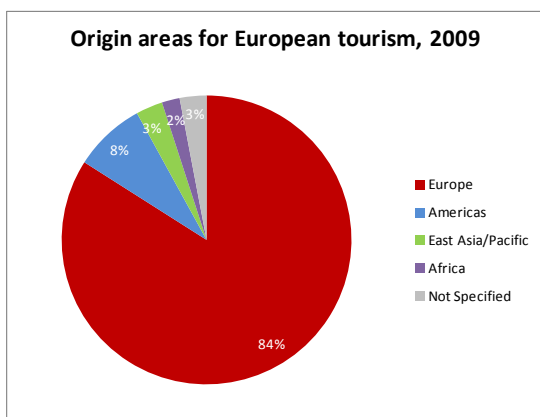
Source: PhoCusWright, 2011

Exhibit 12: Online Travel Penetration, 2008-2012



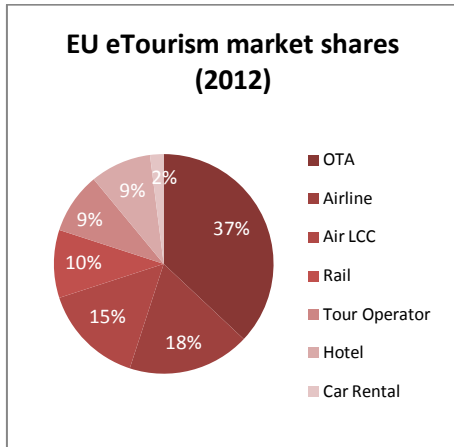
Source: PhoCusWright, 2011

Exhibit 13: Origin areas for European tourism, 2009



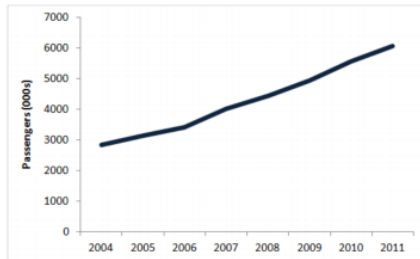
Source: EUROSTAT, 2009

Exhibit 14: EU eTourism market shares, 2012



Source: PhoCusWright, 2011

Exhibit 15: Cruises growth, 2004-2011



Source: European Cruise Council, 2012

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