Mindful Transacting as a Source of
Competitive Advantage

Mehdi Hossein Nejad
Richard Ivey School of Business
University of Western Ontario

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Mehdi H Nejad

Richard Ivey School of Business

Abstract

This paper aims to explore conditions by which transacting becomes a valuable capability and a source of competitive advantage. By examining how a mindful approach to transacting can be a source of heterogeneity, arguments are presented to shed light on the micro-foundations of competitive advantage resulting from a unique approach to inter-firm transactions. It is discussed that mindful organizations can use their current repertoire of transacting options to create new transaction forms that lower transactions costs without raising the possibility of opportunism. More importantly, mindfulness allows organizations to detect opportunities for non-contractual trust-based relationships built on day to day interactions between individuals within the organization and their counterparts outside it. These established ties can then be institutionalized by managerial and structural characteristics to form the basis of future transactions with the trustworthy party. The arguments in this paper explain how micro-foundations are formed for transacting capability which can then be related to the firm-level outcomes of trust-based relationships discussed in prior literature.
Introduction:

The issue of trust in inter-organizational exchanges has received considerable attention in the strategy literature (e.g., Barney & Hansen, 1994; Foss & Foss, 2005; Poppo & Zenger, 2002), and empirical studies have shown its effectiveness in reducing transaction costs and improving firm performance (e.g., Dyer, 1997; Dyer & Chu, 2003). Although each study has a different definition of trust in economic transactions, all view it as something over and above the usual transactions with governance structures (e.g., contracts). While these studies do discuss the benefits of trust in inter-organizational transactions, they do not discuss the process through which trust is created and used as a basis for economic transacting. It is also important to understand how trust-based transacting can become a capability and a source of competitive advantage. According to the resource based view of the firm (Barney, 1991; Nelson, 1991), a resource can become a source of competitive advantage if it satisfies the VRIO (valuable, rare, inimitable, organized) criteria. Capabilities are “organizational routines by which managers [and other individuals] acquire and shed resources, integrate them together, and recombine them to generate value-creating strategies” (Eisenhardt & Martin, 2000, p. 1107). We will discuss how mindful individuals are able to integrate improvisation and routine-based behaviors to develop transacting capabilities that allow the firm to achieve competitive advantage. These individuals can be both the boundary spanners conducting the transaction, or managers attempting to institutionalize the novel forms of transacting and trust-based relationships.

While the value of novel and trust-based transactions has been theoretically and empirically examined in the studies mentioned above, it is important to discuss why they are also something rare and inimitable and what organizational characteristics and decisions are influential in their
development. This paper focuses on “mindfulness” (Levinthal & Rerup, 2006; Weick, Sutcliffe, & Obstfeld, 1999) as a lens through which these issues can be tackled. We will discuss how only those organizations that encourage mindfulness amongst members, and build up on their success in creating strong ties with others outside the organization will be able to gain advantage over those who pursue traditional governance based transactions. Mindfulness will provide the basis for exploration into novel ways of transaction, including those that are based on trust. It also explains how these novel ways are developed through a lengthy process and become a source of heterogeneity. Being mindful is difficult and is something that unfolds over time. It requires ongoing effort to sustain and rebuild (Rerup, 2005). Based on this premise, it can be argued that those organizations who approach economic transactions mindfully will develop resources that are hard to imitate and rare. If this mindful entity is then organized to develop capabilities to take advantage of this resource, it will gain competitive advantage over competitors.

The approach taken in this paper is in line with the current interest in micro-foundations of capabilities and competitive advantage (Abell, Felin, & Foss, 2008; Felin & Foss, 2009; Gavetti, 2005), and also efforts to bridge the organizational economics and the resource-based literatures. We are proposing that transacting itself is a learned capability gained overtime through a mindful approach to inter-firm relationships. In this approach, it is important to consider that viewing resources and capabilities as collective entities is problematic and ordinary day to day actions of individual agents in creating opportunities for capability development plays an important role (Salvato, 2009). This becomes more important in transactions and trust, since exchanges between firms are often actually exchanges between individuals (Barney & Hansen, 1994). Transactions are carried out in many everyday forms such as meetings, calls, and biddings and these can
provide the chance for individuals to establish relationships with other individuals and organizations (Dyer & Chu, 2003).

**Transaction cost economics:**

Transaction cost economics (TCE) has added to our understating of firm productivity by stating that firms maximize value by minimizing both production costs and transaction costs (Williamson, 1985). According to Williamson’s (1985) version of the theory, transaction costs include all the efforts and expenses involved in finding a partner to deal with, developing contracts or other governance structures, monitoring the contractual relationship, and following up on the other party’s possible opportunistic behaviors through appropriate channels. Dyer & Chu (2003) have labeled these search, contracting, monitoring and enforcement costs with the first two being ex-ante contracting costs as opposed to the last two which are ex post costs. They also state that these “subtypes” are not necessarily correlated and an increase in one does not necessarily increase or decrease others. In this paper, we consider the total transaction costs since using trust as a substitute for many of the routinized established forms of contracting can reduce all these subtypes of transacting (Barney & Hansen, 1994).

The version of TCE introduced and developed by Williamson (1985) has two major assumptions which he uses as a basis for his conclusions. The first assumption is that most human beings pursue self-interest and are opportunistic with guile. The second assumption which is shared by many others in the Carnegie School is the principle of bounded rationality. Based on these two premises, Williamson concludes that it is difficult to distinguish between trustworthy and opportunist parties in a transaction and therefore safeguards are needed. These assumptions and
the conclusion drawn from it have major implications for asset specificity. Higher transaction costs are associated with higher levels of asset specificity since a more sophisticated governance structure is needed to curb opportunistic behavior aimed at obtaining higher profits from specialized assets (Williamson, 1985, 1991). According to Dyer (1997) those firms who can simultaneously achieve high asset specificity and lower transaction costs may have competitive advantage over competitors. This calls for attention towards alternative forms of governance structures such as trust, which are the main focus of this study.

A number of management and economics scholars have spoken against the assumptions and conclusions of TCE (e.g., Ghoshal & Moran, 1996; Granovetter, 1985) or have offered alternative explanations for inter-firm relationships by looking at social structures and embeddedness (e.g., Granovetter, 1985; Uzzi, 1997). Ghoshal & Moran (1996) posit that viewing human beings as self-interest seeking individuals with guile might actually make this true through self-fulfilling prophecy. They do at the same time admit that “opportunistic behavior is not uncommon and its dysfunctional effects are substantial” (p. 38) and therefore it should be considered in economic transactions. We do agree with Ghoshal & Moran in stating that in some instances “efficiency” within predefined rules of the game may not determine the desirability of the outcome. It is also important to keep in mind that long-term gains sometimes come at the expense of short-term inefficiencies. Firms engaged in economic transactions should keep in mind that in some forms of relationships (e.g., trust) it is possible to incur short-term losses in order to keep the relationship intact or even to reinforce it in order to harvest gains in the long-run.

Additional criticism towards TCE has come from Granovetter (1985). He describes TCE as a very “under-socialized” view of relationships and exchanges which has overlooked personal ties
between individuals, and the impact these ties can have on transactions. He is providing an alternative view by suggesting that economic action is embedded in networks of social relations and these relationships can serve as a basis for economic exchange. Uzzi (1997) also depicts a network view of social embeddedness and discusses how social relationships can lead to lower transaction costs and better performance. These discussions offered in by these two scholars are especially important to the arguments we are developing in our understanding of how transacting can become a source of heterogeneity. Organizations that are connected to exchange partners through networks of embedded ties have access to benefits such as information sharing and trust which are very hard to establish in traditional arms-length ties (Uzzi, 1997) and are thus in advantage over competitors. In this paper, we discuss how mindful individuals at lower levels of the organization and also in managerial ranks are important to the development of social networks with trust as a replacement for traditional contractual governance structures. This can be achieved by being alert to potential opportunities for establishment of ties and new forms of exchange based to attain maximum value. Before doing so, it is important to define trust as it has been used with different conceptualizations in previous studies.

**Trust-based interactions:**

Previous studies have shown that trust can lower transactions costs and facilitate information sharing in response to changing situational conditions (Dyer, 1997). In this paper, trust-based relationships are studied as alternatives to governance based transactions. It is discussed that through a process of mindful attention to details of day to day activity, an organization is able to identify and exploit opportunities created by established trust-based social networks between its
members and their counterparts in other organizations. But trust has many definitions and levels, each with different implications for economic transactions. Mayer, Davis, & Schoorman (1995) have defined trust as “the willingness of a party to be vulnerable to the actions of another party based on the expectation that the other will perform a particular action important to the trustor, irrespective of the ability to monitor or control that other party” (p. 712). This definition clearly states that in a trust-based relationship, the other party will not act opportunistically, even without safeguards or governance structures in place to monitor the exchange. A party can be trustworthy for different reasons. Some might engage in trust-based relationships for its long-term mutual gains and as a means for escaping costly governance structures, while others adhere to certain principles to avoid damage to reputation which itself is an important asset in establishing future ties with different exchange partners. There are also those who are trustworthy as a result of values and beliefs and refrain from opportunistic behavior because it goes against their values as trustworthy individual (Barney & Hansen, 1994). What is important to note is that no matter which of these intentions are accepted as the underlying cause for trustworthiness, the two parties can enjoy lower transaction costs as a result of fewer or no ex ante or ex post governance structures (Dyer & Chu, 2003; Poppo & Zenger, 2002). The most important issue here is to recognize a trustworthy party and this is often a very difficult and time consuming task (Barney & Hansen, 1994). Trust emerges as a result of previous experiences (“shadow of the past”) and more importantly, expectation of future continuity of this trust-based relationship (“shadow of the future”)(Poppo, Zhou, & Ryu, 2008). Detecting and building up on this perceived experiences and expectations is crucial in establishing these ties and this is where mindfulness can contribute by creating focus on the issue and attention to weak cues in the relationships (Rerup, 2009; Weick et al., 1999).
An important issue in examining trust in inter-firm transactions is establishing the level of analysis which can become a source of ambiguity if not addressed adequately (Zaheer, McEvily, & Perrone, 1998). Barney & Hansen (1994) clearly state that “Exchanges between firms are, more often than not, exchanges between small groups of individuals in different firms”, and if identified trustworthy, these individuals can engage in a transaction based on “strong form trust” (p. 181-182). They do discuss how influential individuals can create a culture of trustworthiness in the organization but crucially, it is the individuals who are conducting the transactions and are evaluated for trustworthiness. Abell et al. (2008) also suggest that it is very difficult to find interactions between macro-entities and these relationships are grounded in individual level mechanisms. Zaheer et al. (1998) also confirm the importance of interpersonal trust in economic exchange but also illustrate through empirical results that inter-organizational trust defined as “the extent of trust placed in the partner organization by the members of a focal organization” is also a very important factor (p. 142). This issue can be discussed in detail but is somewhat irrelevant to the current study since Zaheer et al. (1998) emphasize that interpersonal and inter-organizational trust are highly related and in many cases, inter-organizational trust originates in the interpersonal trust established between two boundary spanners from the transacting organizations. They continue by arguing that through institutionalizing processes, this trust can continue even after the boundary spanners are out of the picture. This process is an important element in arguing how through mindful attention and detection of emerging interpersonal trust amongst individuals from two organizations, management can establish the basis for future transactions and eventually inter-organizational trust.
Mindful transacting

Mindfulness has been described at the individual level as rich awareness expressed by active refinement and development of existing categories, creation of new categories from day to day activities, openness to novel information and experiences, and finally, sensitivity to context and alternative approaches to dealing with it (Langer, 1989). Weick et al. (1999) have shifted the concept to the organizational level by examining high reliability organizations (HROs) and how they enact a distinctive set of cognitive processes to avoid failure. They discuss preoccupation with failure, reluctance to simplify interpretations, sensitivity to operations, commitment to resilience and under-specification of structure as the underlying processes for mindful organizing (p. 91). Mindfulness has been discussed in contrast to mindlessness. Levinthal & Rerup (2006) in their attempt to bridge the gap between mindful & less mindful behaviors, cite Langer (1997, p. 4) in suggesting that “being mindless, colloquially speaking, is like being on automatic pilot” which requires fewer cognitive resources. By being less mindful individuals rely on established routines or best practices in reacting to situational stimuli or conducting day to day activities and this automatic behavior is not without benefit as they are the result of past experiences and mindful behaviors (Abell et al., 2008; Levinthal & Rerup, 2006). Salvato (2009) suggests that a possible description for mindfulness and the enhanced organizational awareness implied by it is the “conversion of experience into reconfiguration of assumptions, frameworks and actions” (p. 401).

The interrelationships between mindful and less-mindful behaviors play an important part in the development of new forms of transaction. This is in line with Gavetti’s (2005) argument that in
order to develop plausible micro-foundations for capabilities, it is necessary to consider both the cognitive and automatic processes and their interactions. Levinthal & Rerup (2006) have discussed four important manifestations of this complementarity, while acknowledging that this list is not exhaustive. First, they argue that the effectiveness of mindful acts depends heavily on the quality and availability of less-mindful routines. Mindfulness is described as the spontaneous and creative recombination of available routines. Second, are the processes by which mindfulness is sustained in the organization. Due to the limited capacity of individuals for mindfulness, they cannot be mindful about everything and it is necessary to have coordination and communication routines in place to turn individual mindfulness into a “higher order pattern of organizational mindfulness” (p. 506). Third, is the ability to select and execute less-mindful routinized behavior in face of ambiguous situational stimuli requires mindfulness. It is important for individuals to be flexible and adaptive in mapping appropriate routines to a novel or ambiguous situation. And finally, Levinthal & Rerup (2006) point to mindful encoding of ambiguous outcomes as the fourth interrelationship between mindful and less-mindful behavior. Here, the repertoire of less-mindful routines is expanded by mindful encoding of events and outcomes that are unclear and ambiguous. This fourth interaction plays an important role in institutionalizing trust at the individual level to form inter-organizational trust.

It is important to note that in a large body of literature, mindfulness has been associated with an enriched state of awareness towards early signs of trouble or failure (Rerup, 2009; Weick et al., 1999). Recently, studies have applied the same concept of awareness to organizations that passionately seek opportunities from small signals in the environment (Rerup, 2005) or in day to day activities (Salvato, 2009). What is crucial is the quality of attention to these weak signals and what is done with them after they are noticed (Weick & Sutcliffe, 2006; Weick et al., 1999). In
the following sections, mindfulness and attention to small signals in day to day activities is incorporated into the concept of inter-firm economic transacting. We will discuss how firms can build new forms of transacting and also move towards trust-based exchanges if they approach the subject mindfully. It will be argued that this new approach will lead to competitive advantage through lower transaction costs and better performance.

**Mindfulness and new governance structures:**

Before discussing trust-based transactions, it’s important to examine how a mindful approach to transacting can lead to new governance structures. There are countless alternative procedures to establishing governance-based ties, and improvisation based on situational contingencies can play an important role in lowering transaction costs. For example, Foss & Foss (2005) describe an interesting sales practice by DeBeers diamond cartel which maximizes total created value by lowering negotiation and bargaining costs which are both sub-items in what we know as transaction costs. Dyer & Chu (2003) suggest that creating new sales practices, contractual forms, or sorting and monitoring technologies may result in lower transactions costs while at the same time reduce the dissipation of value. These new methods are often created by combining previous forms of contractual and market-based governance devices in reaction to the conditions of a particular transaction. We draw from Levinthal & Rerup’s (2006) definition of mindfulness and their proposed interrelationships between mindful and less-mindful behavior to explain how mindful organizations encourage and support their employees in improvising new forms of transaction and how these new forms emerge from day to day activities at various levels of the organization.
It was discussed previously that most transactions are conducted between an individual or a group of individuals from one organization, and their counterparts from another organization. This is done through many mundane day-to-day interactions which, if dealt with in a mindless manner, will go unnoticed. Salvato (2009) has conducted an empirical study linking these micro, ordinary activities by individuals within and around the organization to the development of capabilities over time. According to the first and third interrelationships (Levinthal & Rerup, 2006), mindful individuals, faced with novelty and ambiguity, will use the current repertoire of contractual forms and governance devices to improvise and develop a transacting structure in accordance with situational contingencies. The quality of the outcome is determined both by the richness of the established routine repertoire and also the ability of individuals in being mindful in enacting the routines (Salvato, 2009). Individuals do have to follow certain procedures in transacting with counterparts but sometimes these are systematically reshaped by mindful ordinary acts based on developed relationships between the two individuals or between the two groups of individuals. This is highlighted even more when individuals have specific information about their counterparts through their personal or professional social network and this can be used in determining the type of governance structure or contract for a transaction. It is also possible that a degree of trust will build up between the two parties as a result of continuous interaction or through other social ties. While the issue of trust-based transaction will be discussed in detail, it can have implications for the type of governance device employed for a particular transaction. Trust and conventional governance devices can function as complements in economic exchanges (Poppo & Zenger, 2002).

The improvisation mentioned above requires timely mindful interventions from the management and also organizational requirements that help learning as a result of this process. A major
precondition for mindful improvisation is the under-specification of structure to leave room for creativity and resilience in face of novel or ambiguous situations (Bigley & Roberts, 2001; Weick et al., 1999). Under-specification of structure allows for local flexibility and adaptability so that local opportunities receive adequate attention as they unfold. This will in turn make opportunity exploitation easier since established routines and procedures are adjusted in response to the situation (Rerup, 2005). In addition to this structural consideration for mindfulness, mindful managerial intervention (“managerial mindfulness”) is also required to aid learning from these new forms of transaction. In line with the fourth interrelation between the mindful and less-mindful acts, mindful management will detect promising developments in various transactions across the organization and expand the repertoire of less-mindful routines by encoding of events and outcomes. This systematic encoding of experiential outcome will result in learning and the new routines can then be used by others in the organization as basis for subsequent improvisations. As we will discuss, this accumulated knowledge of different transacting alternatives and the ability to improvise in face of novelty and ambiguity is a valuable capability which will lead to lower transaction costs and competitive advantage over competitors.

The process described in the previous paragraphs is what Salvato (2009) describes as the interplay between improvisation and intentionality. The acts of individuals in adopting different routines and reshaping them to meet specific transaction demands are conducted automatically based on their conception of day to day signals they receive and the amount of trust built up in a relationship. The result of this automatic enactment of routines is a new set of governance devices and contractual forms which might be of use for other transactions with similar circumstances. Intentional mindful managerial intervention is needed to observe, detect, select, and develop these new routines for future use. Through this ongoing process, the organization is
learning new economic exchange procedures and is adapting to the changing environment which will result in lower transaction costs.

**Mindfulness and trust-based transactions:**

The mindful transacting described in the previous section is often a useful approach in reducing transaction costs by producing new and creative ways of contractual transaction. According to Barney & Hansen (1994) in these kinds of transactions, “rational actors find it in their best self-interest, for both economic and social reasons, not to behave opportunistically” (p. 178). An alternative to these forms of economic exchange is to substitute them with trust in face of asset specificities and vulnerabilities. While the importance of trust in reducing transaction costs and improving performance has been discussed frequently in the literature (Barney & Hansen, 1994; Dyer, 1997; Dyer & Chu, 2003; Poppo & Zenger, 2002; Uzzi, 1997; e.g., Zaheer et al., 1998), questions still remain regarding the methods for identification of trustworthy counterparts and the process through which the trust-based relationship is established and used as a substitute for contracts and governance devices. Discussing these processes can help explain some of the micro-foundations of inter-organizational trust and the development of capabilities in establishing trust-based relationships. In this paper, we define trust-based relationships as those transactions which are conducted in the absence of clear and strong governance structures. Although in its strongest form, trust can be related to internalized values, principles, and standards of behavior (Barney & Hansen, 1994), other factors such as the value of reputation, salience of social networks, and long-term mutual benefits can lead the two parties towards establishing trust-based transactions with no governance structures. We argue that identifying
these developing relationships and using them as a basis for future transactions, require mindful
attention and action both by individuals and the managers of an organization.

Mindfulness is all about the quality of attention and it’s about what one does once a weak signal
or a small window of opportunity has emerged (Weick & Sutcliffe, 2006; Weick et al., 1999).
These signals are present in the day to day interactions between individuals within the
organization and their transaction partners from outside. Trust can build up as a result of
numerous processes in the midst of these interactions. It can be both through past experiences in
contractual transactions or other social interactions between individuals. As a contractual
relationship evolves over time, parties in a transaction often gain insights and information about
their counterpart and are then able to judge their trustworthiness (Barney & Hansen, 1994). This
process unfolds gradually and in a long period of time through numerous work-related or social
interactions. Individual mindfulness plays an important role in both the identification of
possibilities for trust-based ties based on the current nature of the relationship, and also in the
ability to improvise a procedure for the trust-based transaction. The trick here is to look for
signals that can help in drawing conclusions regarding the trustworthiness of another individual,
or another organization as a whole. While trust is mostly an individual level construct, it is
sometimes possible that an organization’s culture or control systems will serve as cues for the
level of trustworthiness of its members and thus can be used as an input in deciding on trust-
based transactions.

A number of organizational characteristics guided by managerial mindfulness are crucial for this
new approach to transacting. Firstly, under-specification of structure is an important factor in
allowing these new forms of transaction to emerge. As discussed previously, this is a
characteristic of mindful organizations (Weick et al., 1999) and allows different individuals to
improvise in face of changing environmental circumstances. In contrast to what we saw in the previous section on improvisation and new forms of contracting, here individuals might make ad-hoc decisions to abandon contracts or other governance devices to allow for lower transaction costs. Trust will replace these conventional methods and in doing so, the costs of ex ante negotiations and ex post monitoring will be decreased (Dyer & Chu, 2003). By easing some of the structures that dictate certain forms of transacting, organizations are allowing mindful individuals to conduct the hardest and most valuable stage of a trust-based relationship: finding a trustworthy partner. The important issue to note here is that this under-specification does not imply that all the transactions in the organization are to be conducted on the basis of trust. As we will discuss, there are downsides to this and will lead to negative outcomes (Uzzi, 1997). What is implied here is that mindfulness and attention to detail will replace contracts with trust when the conditions demand this form of transaction.

Managerial mindfulness is an important element in both building up on the established ties for future transactions and also in converting the emergent individual level interpersonal trust to inter-organizational trust. Unlike what was discussed in the section on new contractual forms and the manager’s role in mindful encoding of these newly developed routines, here it is not recommended for management to routinize the conditions of trust-based relationships for future use. Each relationship is unique and the level of trust fully depends on the parties involved and thus the procedures are not transferable to other transactions with different parties. What can be done is for managers to establish closer ties with the particular individual or organization for future transactions. Since the specific counterpart has been identified as trustworthy, the organization can enjoy the benefits of lower transaction costs and information sharing (Dyer, 1997) in all subsequent transactions with the specific partner. The fourth interaction between the
mindful and less-mindful behaviors (Levinthal & Rerup, 2006) is important here since managers must put in place “institutional processes to codify informal commitments made by individual boundary spanners, which over time become established and taken-for-granted organizational structures and routines” (Zaheer et al., 1998 p. 144 from Zucker, 1977). Zaheer et al. (1998) also suggest that the trust orientation of boundary spanners influences the other organizational members’ orientation toward the partner organization in the transaction. The institutionalized norms then influence the trust orientation of the next set of boundary spanners in their interaction with their counterparts. This “creation and recreation of trust structures and action at the interpersonal and inter-organizational levels is akin to Giddins’ (1979) concept of structuration” (p. 144). These arguments highlight the importance of managerial mindfulness in creating the right routines to build up on interpersonal trust for future transactions. They also point to another important issue regarding the reputation of the organization. Individuals in all levels of the organizations need to be mindful of the impacts of their actions on how the organizations will be perceived in future transactions. This also needs to be considered when institutionalizing norms and routines, so that they are consistent with the trustworthy image an organization is trying to present. Reputation is a valuable asset which can facilitate the establishment of trust-based relationships at both the individual and organizational levels.

**Mindful transacting as a source of competitive advantage:**

According to what we have discussed so far, it is apparent that creating new forms of governance procedures and also basing transactions on trust can lower transaction costs, facilitate information sharing, and eventually lead to improved performance (e.g., Barney & Hansen,
The abovementioned benefits indicate that these forms of transacting are valuable resources for organizations but in order to serve as a basis for competitive advantage, resources also need to satisfy the rarity, inimitability and organization criteria (Barney, 1991). In addition, organizations need to develop capabilities that lead to the development of trust and also allow it to institutionalize it for future transactions.

Trust is a rare and hard to imitate basis for transaction since it is extremely difficult to identify a trustworthy partner (Barney & Hansen, 1994). While the existing literature fails to discuss how some firms go about doing this, our arguments on mindful transacting bridges this gap. Mindful organizations that encourage mindful individuals are able to detect weak signals suggesting a possibility for trust-based transaction with a trustworthy party. This is a skill available to only a few organizations that are able to develop and nurture mindfulness. We reiterate that not everyone can be mindful and if it was easy, then anyone can become so. “Mindfulness unravels. It varies over time and people and requires ongoing effort to sustain and rebuild. It is demanding and difficult to be mindful” (Rerup, 2005, pp. 452-453). Based on the descriptions we’ve already discussed on the organizational characteristics associated with mindful organizations for trust-based transaction, it is also apparent that these organizations are well organized to take advantage of the new forms of transacting. Only those few organizations that are successful in being mindful transactors can benefit from the lower transaction costs that result from it and can therefore enjoy a sustainable competitive advantage. Since capabilities such as these accumulate over time and are inertial and path dependent, they are hard to transfer from one organization to another (Gavetti, 2005). This adds to their value as a sustainable competitive advantage, since as Winter (2003) suggests, the extent to which a firm’s competitive advantage is rooted in its capabilities, their continuity acts as a deterrent to imitation. The important issue to note here is...
that a mindful organization understands when it is not suitable to engage in trust-based relationships and is aware of the possible negative outcomes associated with it. These organizations know when it is necessary to be mindfully mindless.

**Mindful mindlessness**

While discussing how a mindful approach to economic transactions can lead to lower transaction costs and better performance, it’s easy to forget that these social trust-based relationships are not always necessary and can sometimes even lead to negative outcomes. We base our discussions on three important premises: (1) breakdown in trust-based link, (2) loss of opportunity, and (3) cost of mindfulness. Examining these issues illustrates the importance of mindfulness in deciding on when to behave mindfully and when to behave less-mindfully. An important element of mindful transacting is to be sensitive to environmental stimuli and choose an appropriate form of transacting, based on the requirements. If the conditions are ripe for establishment of trust-based transaction, one must decide whether this is indeed the correct path. There is an element of mindfulness in this decision and in many instances, there are no standard procedures and routines to follow. There is a need for mindful enactment of routines (Levinthal & Rerup, 2006), or simply being mindfully mindless.

In a trust-based relationship, parties are highly vulnerable to each other (Mayer et al., 1995) and in the case of organizations, they often become somewhat overly reliant on their trustworthy partners. “Diligent commitment, backed by expectations of reciprocity and social pressure to perform, intensifies an organization’s involvement with certain … partners while raising the concomitant costs of keeping to extra-network partners that can provide a safety net for
unexpected or random fluctuations” (Uzzi, 1997, p. 57). According to Uzzi (1997), being overembedded limits an organization’s ability to obtain information from outside the close social network and fewer links with the outside impedes the attainment of innovative ideas. There are even harsher outcomes in circumstances where the trust-based relationship is broken intentionally or unintentionally. It is totally possible for one of the parties in a trust-based relationship to make an unforeseeable exit from the transaction (Uzzi, 1997) due to bankruptcy or other similar reasons. In these situations, and in absence of formal contracts and limited ties with other parties, there are major difficulties for an organization that has provided high asset specificity based on the now non-existent relationship. It is also possible for one party to end the trust-based relationship out of opportunism. As we discussed in the section on trust, parties might follow the principles of game theory and engage in trust-based relationships for mutual benefit. If this is the basis of the transaction, an actor might act opportunistically if it sees an end state approaching (Hill, 1990). It is also possible that parties avoid opportunism to keep their reputation intact (Barney & Hansen, 1994) or to build a reputation in order to take benefit from it in future transactions. When the benefits of opportunism outweigh the costs of lost reputation, a party might end the trust-based relationship. It is very difficult if not impossible, to predict any of the abovementioned circumstances beforehand. A mindful approach to finding trustworthy transaction partners can reduce the probability of these issues occurring but as we will discuss, mindful organizations must put procedures in place to minimize their negative effects.

As an organization enters a trust-based relationship, in most circumstances it is agreeing to refrain from any opportunistic behavior and also to share information (Dyer & Chu, 2003) and engage in joint problem-solving arrangements (Uzzi, 1997). It is important to keep in mind that “the cost of building trust includes the opportunity cost of not taking advantage of one’s [partner]
and the loss of the opportunity to use a lower-cost [alternative] if they come along” (Dyer, 1997, p. 552). It is important to be aware of the environmental details before deciding on the type of relationships an organization builds with other parties. For example, an organization might feel that it needs to establish arms length relationships with a large number of parties to deal with only a few at any time based on the fast changing environmental contingencies. This does not mean that one should be less mindful in detecting weak signals and opportunities for establishment and development of social relationships. What is important is that not all the possibilities for trust-based relationships need to be tapped and taken advantage of in economic transactions.

Finally it is important to note that mindfulness itself has an opportunity cost (Rerup, 2005), and by experimenting with novel ways of transaction, one is overlooking the use of established economic exchange (Levinthal & Rerup, 2006). Mindfulness requires cognitive capacity and ongoing effort to sustain and it is often demanding and difficult to be mindful (Rerup, 2005). Being mindful about one thing will normally result in less mindfulness on other issues (Levinthal & Rerup, 2006). An organization is deals with a diverse set of issues on a day to day basis and it’s unrealistic to expect it to dedicate all the cognitive ability of its members to the issue of economic transactions. If so, other important issues who do in fact require a great deal of mindfulness to detect possible threats (Weick et al., 1999) or opportunities (Rerup, 2005) might go unnoticed.

A mindful organization can follow certain approaches in order to overcome the three important issues described above. The optimum solution to avoid the negative outcomes of a breakdown in trust-based relationships and also to lower the opportunity costs of trust, is maintaining a mixture of governance enforced and trust-based ties (Uzzi, 1997). By pursuing this strategy, the
organization is enjoying the benefits of trust-based relationships and is at the same time lowering the risk of breakdown in ties. The organization is looking for optimized performance in the long-run, which might be contradictory to short-term maximization strategies. To address the limited capacity of individuals for mindfulness, Levinthal & Rerup (2006) have pointed to specialization of attention and also the need for institutionalization and integrating mechanisms as discussed by Bigley & Roberts (2001) to tie individual mindfulness to what is described as organizational mindfulness. By putting in place routines and structures to specialize attention, the cognitive load for mindfulness can be shared between individuals. This is to some extent naturally present when discussing economic exchanges and transactions. Mindful individuals at different levels of the organization are engaged in day to day interactions with other parties outside the organization. Mindfulness allows them to detect opportunities for new forms of governance in transactions or to substitute some governance with trust which is built through a lengthy period of relationship or information from other sources. Routines must be put into place by managers to allow for improvisation by the individuals involved in the transaction. It is also important for managers to monitor these new developments closely for possible opportunities in conducting future transactions with the identified trustworthy partner or to apply the newly developed form of governance to other economic exchanges with similar circumstances.

**Discussion:**

This paper is written in response to calls for more attention to the micro-foundations of capabilities and competitive advantage in the strategy literature (Abell et al., 2008; Felin & Foss, 2009; Gavetti, 2005). We discussed how mindfulness at different levels of the organization can
lead to the development of capabilities regarding novel forms of transaction. What is in focus here is an organization’s capability in examining the situational contingencies, developing appropriate governance structures, and institutionalizing the new procedures for future transactions. More importantly is the organization’s capability in identifying trustworthy partners through the daily interactions of its members with their counterparts, and turning this into inter-organizational trust through the process of institutionalization. Boundary spanners involved in day to day interactions with counterparts from outside the organization need to be highly sensitive to small signals pointing to opportunities for trust-based interactions or novel forms of governance. This is something management itself is often incapable of conducting. In most cases, management’s distance from the action diminishes its ability to interpret the day to day experiences (Gavetti, 2005) and what’s important is that the interpretations and experiences in the lower levels of the organization are given the opportunity to develop through mindful improvisation. Management can facilitate this process by under-specifying structure (Weick et al., 1999) and allowing for creative enactment of current routines.

The organization’s developed capability in identifying trustworthy partners and establishing trust-based relationships, and also its capability in improvising new governance structures in response to situational contingencies can serve as a source of competitive advantage. These alternative forms of exchange lower transaction costs and lead to better performance. “Mindful transacting” is also rare and hard to imitate, since being mindful requires persistent effort and attention. Mindful firms are organized to both encourage mindfulness and also to take advantage of emergent opportunities in order to learn and improve their repertoire of routines. Under these circumstances, mindful transacting can become a source of heterogeneity and competitive advantage. It is also important for these firms to identify situations when it is necessary to simply
follow established routines automatically. Mindful transaction can sometimes imply the use of mundane routines which require lower cognitive capacity.

Future empirical studies can provide additional insights regarding the role of mindfulness in establishing trust-based ties and their impact on transaction costs and firm performance. They can also provide valuable information on the role of different organizational players in developing interpersonal and inter-organizational trust and the process through which this trust is used as basis for transactions. The theoretical arguments presented in this paper, and adequate empirical evidence that support and extend them can shed light on the micro-foundations of transacting as a capability and a source of competitive advantage.
References:


