Is being first to enter a market worth the price tag?

The rise of AI makes an evergreen question newly relevant: Is being a first mover really an advantage, when it can raise establishment costs by up to 5%?

September 16, 2026

In emerging sectors, deciding when to enter a market counts among companies' most critical dilemmas. Though much is made of the first-mover advantage, the numbers don't always bear this up.

The early phases of market entry are very expensive, particularly in new sectors, and the technology often hasn't matured. In contrast, once the sector has developed and the quality of components improves, installation costs often decrease. Far from an advantage, moving early to deter rivals can paradoxically *reduce* profitability.

Research by IESE's Ricard Gil, with Jean-François Houde (University of Wisconsin, Madison), Shilong Sun (Compass Lexecon) and Yuya Takahashi (University of Washington, Seattle), analyzes this dilemma through a surprising case: Their research is based on how drive-in movie theaters evolved in the United States between 1945 and 1957. If you can smell the hairspray and leather jackets from here, consider the modern parallels. Drive-ins represented an emerging, tech-dependent sector undergoing rapid technological evolution. Think of how other industries — from 1990s fiber-optic telecommunications to many aspects of today's AI rollout — show similar features.

Gil and co-authors' conclusion? Early entry doesn't improve the competitive position in the long term, but it *can* make establishment costs 5% more expensive and reduce the value of the firm by up to 1%.

Market size defines strategic behavior

The authors show that the incentive to get ahead of rivals depends on the size and profitability of the market, and that in different-sized markets, firms have marked preferences.

The researchers used the proportion of warm days per year in each county as an indicator of market size, due to the weather-dependent nature of drive-ins. The data confirms that early entry (before 1950) was concentrated in a very significant way in places with an intermediate demand potential.

This is because:

- **In small markets**, there's only enough demand for a single profitable firm once the market matures, so established players don't feel any real threat from rivals. Here, new entrants prefer to wait for establishment costs to decrease.
- **In large markets**, there's room for multiple profitable competitors. Since

competition is inevitable, firms also prefer to wait for the technology to mature and become cheaper before landing.
- **The medium-sized market**, on the other hand, can sustain a single operator very profitably, but the arrival of a second would make the business unfeasible for both. Therefore, firms rush to establish themselves earlier than operational efficiency would advise, in order to protect their monopoly.

It pays to wait to enter a developing market

According to the research, there are three major factors that affect the decision to delay entry into a new sector:

- **5% increase in entry costs**

Early movers assume a significantly higher capital outlay from the start. In medium-sized markets, that rush meant an average increase of 5% in initial investment.

- **Reduction in firm value**

The benefits of operating alone during the initial phases do not offset the cost overrun of starting in an immature market. The study estimates that the expected value of the firm fell by an average of 1%.

- **Same number of competitors in the long term**

Simulations show that getting a head start in a market doesn't prevent more competitors from showing up in the long term. In large markets, the pioneer will end up having competitors. In medium-sized markets with capacity for a single firm, the pioneer will be the first and likely only one to operate in that market, although with higher costs.

What managers should keep in mind before entering a new market

Entering in the initial phases of a sector implies much higher establishment costs. Companies should, therefore, incorporate the real toll of being pioneers into their feasibility reports. For many, missing the first-mover advantage, and waiting for establishment costs to drop as the sector matures, is the best path to value.

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