Middle Management Involvement, Incentives, and the Corporate Strategic Decision-Making Process

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ABSTRACT

We respond to the challenge laid down by Wooldridge and Floyd (1990) and their pioneering work on middle management research. But we have to disagree with their model and propose one of our own that comes from the game-theoretic stable. Strategy implementation is seen as playing a mediating role between strategy formulation and organizational performance. We put incentives firm and center in our endeavor to understand the corporate strategic decision-making process. Our research finds evidence that offering incentives to the middle management helps high productivity firms and harms low productivity firms.

INTRODUCTION

We take a look at the Nash's (1950) bargaining game model, its three properties and the solution it offers.

Property 1: Independence of equivalent utility representations.

Property 2: Independence of irrelevant alternatives.

Property 3: Individual rationality.

For each strictly positive Pareto solution P such that,

$$\sum_{i=1}^{n} p_i = n$$

there is a unique solution possessing properties 1,2, and 3, such that the symmetric game has a solution P. For any bargaining game, the solution x is such that $x \geq$ d, d being the disagreement solution and

$$\prod_{i=1}^{n}(x_i - d_i) > \prod_{i=1}^{n}(y_i - d_i)$$

for all $y\ in\ S$, such that $y \geq$ d and $y \neq x$ (Roth, 1979).

In particular, the implementation component of the middle management involvement in the strategy process is likely to be prone to agency problems (Jensen & Meckling, 1976). The commitment construct in Wooldridge and Floyd comes out to be uncorrelated with the involvement variable which is further uncorrelated with firm performance. We posit this to be the case because of a lack of an appropriate incentive structure that prohibits strategy implementation apart from facilitating superior strategy generation. We make our case to include a systematic incorporation of this ameliorating mechanism championed by Laffont and Martimort (2002) which will have the disagreement solution at the heart of the resolution. The model also accounts for a subsequent bargaining game at the top management level.

MODEL

The corporate profit function is calculated as:

$$\pi = p(AL^{a}) - wL$$

(Hackman, 2008) where w is the wage rate, L is labor, A is productivity, and p is the quality adjusted price commanded in the market.

The middle management utility function is taken to be:

$$\frac{(C_t^{\gamma}(l_t)^{(1-\gamma)})^{1-\sigma} - 1}{1-\sigma}$$

(Brissimis & Bechlioulis, 2017) where the notations stand for standard consumption and ratio of leisure to total time. The estimated parameters are used in our computations.

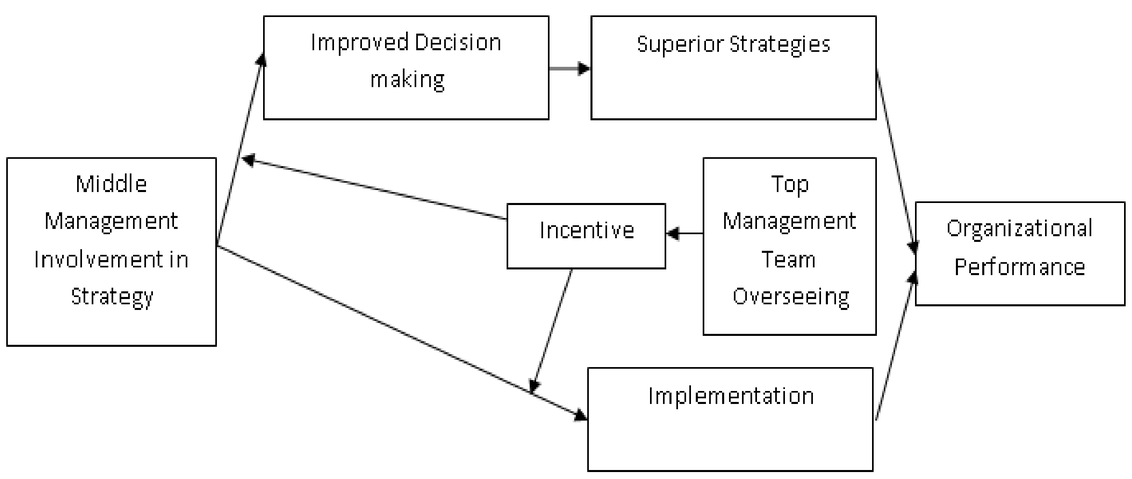
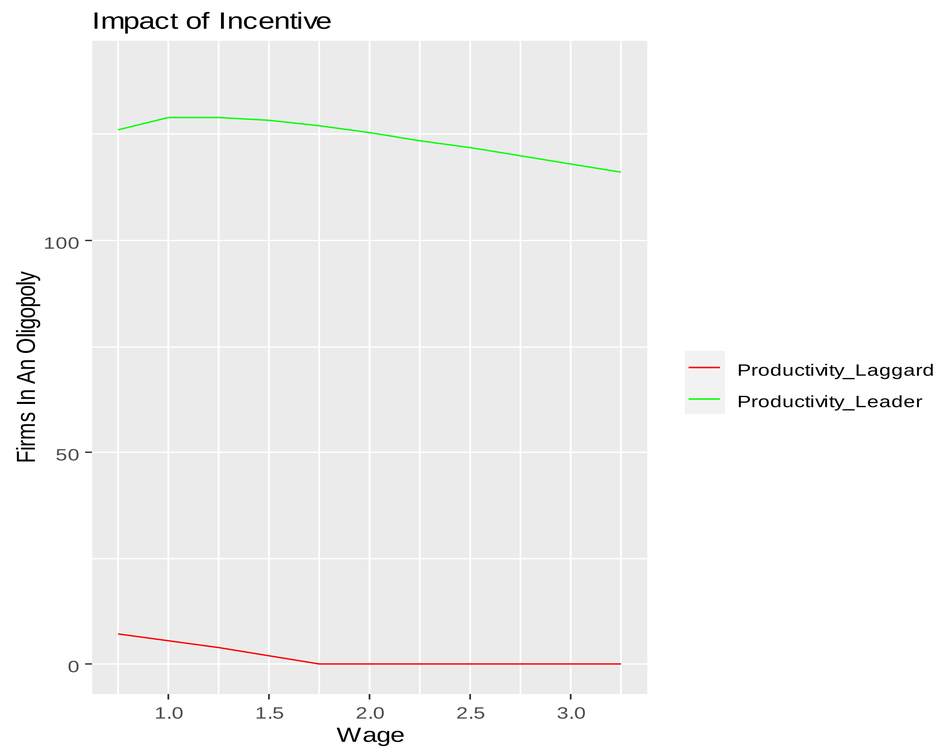


Figure 1. Theoretical model of middle management involvement in strategy

We investigate an oligopoly with a productivity leader and a productivity laggard. We model incentives as having a moderating effect on the relationship between middle management involvement in strategy and implementation and improved decision making alike. It is hard to imagine that the middle management has no impact on the organizational performance during the strategic decision-making activity (Dess, 1987). We take inspiration from the Activity-based costing literature (Staubus, 1971). We investigate a scenario in which the low productivity firm charges and can command the same price as the productivity leader. This is because they have a large common quality pool of middle management human resource workers that they can access. We assume they do not compete in factor markets. This seems like a realistic proposition for an oligopoly in a fairly large economy.

RESULTS



The numerical simulations in our model reveal there is no incentive for the productivity laggard to offer incentives to its middle management. The high productivity firm though can look to improve its rent collection by a judicious offer of wage incentives. As expected there is a substantial divide in terms of profit collection between the productivity leader and the laggard in an oligopoly. This despite facing similar factor markets.

CONCLUSION

We hope our effort to drastically recast the corporate strategic decision-making process will inform researchers and practitioners alike. It is indeed a surprise that Wooldridge and Floyd (1990) gets wide citations till date. We offer the following suggestion:

1) Investigate the impact of incentives on firms that lie in between the simulated productivity levels which will throw light on the wider industry landscape.

Going forward we will conduct robustness checks and hope to publish the poster in an A rated peer-reviewed strategy journal like the Strategic Management Journal or Strategy Science.

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