THE EFFECTS MANAGERIAL CHARACTERISTICS AND ORGANIZATION GROWTH ON STRATEGIC CHANGE

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Abstract

This study investigates the extent to which chief executive and top management characteristics will interact with organizational performance in order to bring about strategic change. Data and information elicited from top executives of banks in the banking were analyzed and results of the analysis show that poor performance long tenure executive and top management team tenure, couple with high diversity in top management team tenure will collectively contribute to strategic change.

Introduction

One of the principal reasons that companies fail is their inability to change themselves and adapt to a new competitive environment because of organizational inertia. It is generally believed that once an organization is created and task and role relationships are defined, a set of forces is put into operation that makes an organization resistant to change and organizational inertial ensues.

Evidences from researches on organizational management in the last few decades have proved that investigations has moved from organizational static's to an investigation of organizational dynamics much of which are focused on organizational change (Chakravarthy. 1991) Similarly, researchers in the area of strategy seem to vary in the extent to which they adopt an adaptive or inertia view of strategic change, although the two perspectives can be viewed as poles in a continuum (Gersick 1994). Those who argue for the predominance of strategic

adaptation emphasized the role that managers play in monitoring environmental changes and modifying organizational strategy to better match environmental contingencies. Theorists adopting a more inertial view of strategy argue that organizations are constrained in their ability to adapt, and that it is the general tendency for strategy to be preserved rather than radically change (Hannan and Freeman 1989).

It has equally been argued that executive change, in particular, changes in a company's chief executive and top management team, is an important mechanism for overcoming inertia, social, technological, and political resistance (Ocasio. 1993). This is based on the belief of Tushman and Romanelli (1985) that only executive leadership has the position and potential to initiate and implement strategic change. Thus, a position commonly maintained by some researchers is that as top management remain stable, they become more insulated over time, and chief executive and top management are less likely to deviate from earlier course of action, especially when change involve organizational strategy. In addition to these kinds of characteristics, conditions of poor performance make it easier to overcome resistance to organizational and strategic change.

Another fact commonly observed by researchers is the extent to which an organization performs. Performance is considered as one of the clearest indicators of the viability of organizational strategy. It is an important predictor of whether change can be sustained in the market the organization it competes in. Poor performance signals top management that the existing manner of operating is inappropriate. That strategic and organizational changes may been necessary (Booker & Goodstein, 1991).

It is against this background that this study examined the dynamics of change in corporate strategy which refers to decisions about the products and markets firms compete in.

The primary purpose of this study is to explore an integrated model of strategic change that considers the direct and interactive effects of performance and managerial characteristics on change in corporate strategy. Corporate strategy in this respect specifically takes into consideration the range of products a firm competes in. More importantly, this study aligns itself with the fact that managerial characteristics can interact with organizational performance to create a situation through which product-market change can be seen.

Theoretical Framework

A: Performance

Kiesler and Sproull (1982) contend that poor performance acts as a catalyst to organizational change when managers take actions in response to a decline in performance. This was in support of March and Simon (1958) who were among the first to argue that poor performance will lead organizations into problem-motivated search, which in turn will lead to pressures for change. In the same vein, Tushman and Romanelli (1985) pointed out that only when poor performance signals that an existing manner of operating is inappropriate do managers attempt to change an organization to respond to environmental change.

Managers of organizations that are performing poorly are in a position to more easily overcome resistance to change and may be able to use poor organizational performance to bring about changes that may be socially, politically, and technologically difficult achieve. This may not be unconnected with the fact that under conditions of adversity, failure to meet performance targets will lead to increased change and risk seeking (Bromiley, 1991).

Perhaps it can also be argued that if poor performance can lead to organizational change, good performance can as well lead to inertia. This is on the belief that as long as performance is

above a threshold level, organizations will have a tendency to persist in repertoires and routines established and also be complacent. Organizational success can therefore make top managers feel that they can safely ignore external change (Barney, 1991). This is because as long as performance is satisfactory, firms will continue to allocate internal resources. Organizations that have recently been successful will resist changes in their basic strategies and missions. The longer such firms have been successful, the greater the extent to which resistance to change and inertia will prevail (Boeker and Goodstein, 1991), and the less likely it will be that changes in external conditions will lead directly and immediately to change. This submission leads this study to its first hypothesis given below.

Hypothesis 1:

There is a positive relationship between poor performance and the need for greater strategic change in organization.

B: Managerial Characteristics

1. Succession.

Various literature of strategic management contends that organizational leaders are viewed as the motivating force behind changes in the products or markets an organization competes in. This is because the chief executive plays an important role in helping to define the strategy of an organization. Thus, change in the chief executive carries with it the likelihood that changes will be made in the organization's strategy (Ocasio, 1993). Empirical examinations of the effects of executive succession on organizational and strategic change have stressed the important role played by executive succession in overcoming inertia and initiating changes in the strategy of an organization. It is believed that when chief executive succession occurs, a new individual, with

new skills and perspectives, including new ideas on the range of markets in which a firm should compete take charge of an organization. Since succession often implies change in the way in which a firm operates, it carries with it the likelihood that prevailing norms and expectations within the organization will be upset. Similarly, a successor is likely to make substantive changes in an organization's products, strategy, and manner of operating, which in turn will disrupt the firm's existing strategy and internal power structure. The process of chief executive succession provides an opportunity for existing power relationships to be altered, for new strategic perspectives to be introduced, and for strategic change to take place. From this discussion comes the second hypothesis of this study.

Hypothesis 2:

There is a positive relationship between executive succession and the occurrence of greater strategic change in an organization.

2. Tenure**.**

In the preceding discussion emphasis on the occurrence chief executive succession was give as probable cause for greater strategic change. However, it should be borne in mind that chief executive successions are relatively rare events. Even if no succession event occurs, the length of time a chief executive has been in the job may have an important effect on the likelihood that he or she will initiate change in strategy.

Some strategic management theorists have posited that tenure in an organization affects an executive's cognitions. The longer the tenure of an individual, the more rigid his or her cognitive structures and the less likely he or she is to promote or champion change. Organizational tenure is thought to be associated with rigidity and commitment to established policies and practices

(Katz, 1982) and may also restrict information processing through the establishment of routines and other strategies for dealing with problems and issues.

Hypothesis 3:

There is a positive relationship between longer-tenured chief executives and the exhibition of less strategic change in organization.

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Notwithstanding the above submissions it should equally be borne in mind that that the effects of performance may interact with chief executive tenure. Organizations with shorter-tenured chief executives may generally be more likely to change strategy, but this effect is, expected to be stronger when the performance of the firms has been poor. Conversely, successful organizations with longer-tenured chief executives may be less likely to change strategy.

Hypothesis 4:

There is a positive relationship between poorly performing organization with longer-tenure chief executive and the exhibition of strategic change

C: Other Managerial Characteristics

At the top management level, Hambrick and Mason (1984) emphasized that strategic decisions are associated with characteristics of the top managers in an organization. Wiersema and Bantel (1992) further demonstrated how top management characteristics, such as tenure and tenure diversity, influence the likelihood of strategic change.

1. Top management tenure.

Top management groups with long organizational tenure are expected to have great social cohesion, lessening the likelihood that individual members of a team will challenge the present situations. Long tenure provides a better understanding of organizational policies and procedures and a reluctance to change past ways of operating (Hambrick & Mason, 1984).

Katz (1982) empirically demonstrated and supports the argument that lengthy top management tenure lowers the likelihood of organizational and strategic change. He further stressed that organizational tenure was associated with increased commitment by top managers to their organizations' established policies and practices. Similarly, Bantel and Jackson (1989) showed that teams with longer organizational tenures exhibited a greater commitment to the present situation of their organizations. Hambrick (1990) equally demonstrated and found a negative relationship between top management organizational tenure and strategic change. Finally, Wiersema and Bantel (1992) found that shorter average top management tenure can lead to changes in corporate strategy.

Hypothesis 5:

There is negative relationship between organizations with longer-tenured top management teams and the exhibition of greater strategic change

Similarly, combining the effects of performance and team tenure we can have the sixth hypothesis as follows:

Hypothesis 6:

There is a positive relationship between poorly performing organization with longer-tenure top management team and the

exhibition of greater strategic change

2. Tenure diversity.

Tenure diversity can viewed from homogeneity and heterogeneity perspectives. Group-level homogeneity on demographic traits can lead to perceptions of similarity with and attraction to others. Conversely, top management teams with diverse tenure distributions will be composed of individuals likely to have different attitudes toward an organization and its strategy because of their tenure-stage differences. Demographic heterogeneity is associated with cognitive heterogeneity, both of which increase the number of strategic alternatives considered by a top management team and the evaluation of those alternatives.

Differences in cognitive structures will create more diverse information collection, interpretation, and solution generation among top management team members, which, in turn, will contribute to a greater impetus for organizational and strategic change. Wiersema and Bantel (1992) argued that top management teams that were heterogeneous would also be more creative and more likely to rely on a broader set of information sources and perspectives when making strategic decisions than more homogeneous top management teams.

Hypothesis 7:

There is a negative relationship between homogeneous top management team tenure and the exhibition of greater strategic change, but positive relationship between heterogeneous top management team tenure and exhibition of greater strategic change

Like the effects of the other managerial variables on strategic change, the effects of tenure diversity should be moderated by performance.

Hypothesis 8:

There is a positive relationship between poorly performing organization with homogeneous top management team tenure and the exhibition of less strategic change.

Methodology

This study was carried out with a sample drawn from the manufacturing in Nigeria. This single industry was chosen to control for potentially confounding inter-industry effects, especially on the dependent variable, strategic change. Moreover the manufacturing industry was chosen for this study because of depth and comprehensiveness of the data available on the firms of this industry, particularly for the variables of interest in the study: strategic change and chief executive and top management team characteristics.

All the 25 firms currently operating in the manufacturing industry are publicly traded. 10, however, constitute the sample for this study and data on these firms were elicited through two sources: (1) a structured questionnaire (2) personal interviews with top managers of each bank (typically including the chief executive officer). In addition reports from annual general meetings were used to gather complimentary information.

Analytical tools

Data elicited from respondents and records of annual general meetings were subjected to descriptive statistics in which means, standard deviation, and correlations coefficients were obtained. This was followed with the regression analysis which employs which employs a two-

stage generalized least-squares method to iteratively correct first for autocorrelation and then for heteroscedasticity.

Measures

Strategic Change

This is the major dependent variable of interest in this study. A distinction is made in the strategy literature between business and corporate strategy. Strategy at the business level constitutes decisions regarding the basis of competition within a specific business. Strategy at the corporate level pertains to decisions on a firm's mix of businesses and what to compete in.

For this study, the corporate strategy question within the context of the manufacturing industry was assessed. Using data from the three sources identified above 20 specific segments that comprised the product-markets within the manufacturing were identified.

Strategic change was operationally defined as the absolute percentage of annual change in degree of diversification across product-markets and measured using entropy measure of diversification suggested by Cohen and Cohen (1975). This measure of corporate strategy captures the extent of diversity across a firm's products. It is calculated as follows:

-- Let P_t be the percentage of total firm sales in the *ith.* business and

-- Let n be the number of a firm's businesses.

Then

$$entropy = \sum_i P \ln\left(1 / P_j \right)$$

Changes in strategy were measured by taking the absolute percentage of in a firm's entropy measure each year, represented in this study as the period t to $t + 1$.

Independent Variables

Performance

Performance was measured as industry-adjusted average growth for two years: the year prior to one in which strategic change was measured and the year a strategic change was measured. For example, for a strategic change occurring in the period 2001-2002, performance .would be measured as industry-adjusted average growth for the two years 2001-2002. Because firm strategy was first measured in 1990, firm growth was first measured in 1999. Two-year average growth was used because organizations may not ordinarily react to poor performance by making important organizational changes (such as changes in strategy)-in the same year that poor performance occurs.

Because many firms in the manufacturing industry and their owners (who are often shareholders) frequently do not expect to realize positive returns for the first several years of their operations, financial performance may be misleading for firms in this industry. Even better-established firms have historically been willing to accept years of marginal or negative returns in order to increase sales. Therefore, performance was measured for a given two-year period by comparing average firm growth (measured as two-year revenue growth) to average revenue growth for the manufacturing industry for the same two years.

Other Variables Measures

Chief executive tenure was measured as the number of year a firm's current chief executive had held the job at time *t.* Chief executive succession was measured from *t* - 1 to *t* and was dummy-coded as 1 when a succession event .occurred. Top management team characteristics was defined as those individuals reporting directly to a firm's chief executive, while organizational tenure of each

top manager was calculated using biographical data available from the market companies and the firms themselves. Team tenure was measured by taking the average of the aggregate tenure of all top managers.

Top management tenure diversity was measured using the coefficient of variation, defined as the standard deviation divided by the mean. Following Wiersema and Bantel (1992) the logarithm of the heterogeneity measure was taken to capture the decreasing rate of the effect of dissimilarity of team tenure on strategic change. To measure top management team homogeneity, the heterogeneity measure was reverse-coded.

Control Variables

Environment

Five control variables were identified for measure in this study. They include environment, firm size, firm age, time, and type of ownership.

The level of environmental munificence affects the flow of resources into an organization, making it easier for firms to expand their product mixes. Environmental munificence was operationally defined as inflation-adjusted changes in overall manufacturing industry performances.

No hypothesis was formulated about the effect of firm size on strategic change, but included size, measured as the logarithm of firm sales, as a control.

On firm age, most literature on strategic and organizational change seems to argue that older firms should be more inert than younger firms (Hannan & Freeman, 1989). As firms age, numbers of routines, programmes, and structures increase and become more internally consistent. Precedent gradually dictates an increasing portion of organizational action. Others argue, however, that young firms, suffering from potential liabilities of newness, are less willing to make changes that might

disrupt already tenuous links with suppliers, customers, and other stakeholders. Given possible temporal variation in strategic change, time was included as a control in the model.

Two types of ownership structure were considered in this study. These are public and private ownership. This study accepted that publicly held organizations may operate differently than privately held organizations with respect to strategic change. One might expect, a priori, that publicly owned firms will be generally less inert and therefore, more likely to change strategies. Public ownership was coded as 1, private ownership as 0.

	Variables	Means	S.D	1	2	3	4	5	6	7	8	9	10	11
1	Strategic Change	0.24	0.65	0.64										
2	Performance	0.16	0.11	0.12	-.33									
3	Succession	0.24	0.53	0.53	.23	-.14								
4	Tenure	4.34	8.22	8.22	-.16	-.16	-.07							
5	Top mgt. tenure	6.50	10.24	10.23	-.17	-.14	-.06	.13						
6	Team heterogeneity	0.60	0.32	0.34	.21	.04	.04	-.06	-.18					
7	Environmental munificence	0.14	0.12	0.13	.19	.04	-.12	-.04	.10	-.14				
8	Size	3.28	1,64	1.54	.04	.10	-.03	.04	.08	.06	-.08			
9	Age	12.45	8.54	7.86	-.12	.11	-.06	.04	.05	.04	-.11	.22		
10	Time	6.55	4.54	4.27	.07	-.08	.14	.02	.02	.04	-.04	.18	.64	
11	Ownership	0.63	0.38	0.45	.18	.13		-.08	-.03	.03	-.03	.21	.17	.12

Table 1: Descriptive Statistics

Data Analysis and Results

Means, standard deviation, and correlation among study variables for all years of data pooled are presented in Table 1 above. The effects of the variables on strategic change in two models are also presented. The first model includes only the control variables. The second model adds the direct effects of performance, chief executive characteristics, and top management characteristics, and it also includes the interactions between organizational performance and managerial characteristics.

The five control variables were entered in the first model of Table 2. They explained 11 percent of the variance in strategic change. The main and interactive effects of the variables were entered in model 2 of Table 2. Hypothesis 1 predicts that performance will exhibit a negative relationship with strategic change. In addition, this study argued that top management characteristics such as chief executive succession (Hypothesis 2), chief executive tenure (Hypothesis 3), top management team tenure (Hypothesis 5), and top management tenure diversity (Hypothesis 7) will influence strategic change. Results shown under model 2 of Table 2 indicate that the effects of performance and of three of the four main effects are significant. Performance, chief executive tenure, top management team tenure, and tenure homogeneity all had a negative relationship with strategic change. There was no significant relationship between chief executive succession and strategic change. The final set of hypotheses examined the interactive effects of performance and managerial characteristics.

Variables	Model 1	Model 2	Change in R2
Performance		-.27**	.05
CEO		.07	.00
Tenure		-.21**	.04
Top mgt. team tenure		-.13*	.02

Top mgt. team homogeneity		-.16*	.03
Performance * CE0 succession		.07	.00
Performance *CEO tenure		-.23**	.04
Performance * top mgt. team tenure		-.17*	.03
Performance * top mgt. team heterogeneity		-.18*	.03
Environmental munificence	.14	.12	
Size	.22*	.18*	
Age	-.04	-.04	
Time	.08	.06	
Ownership	.18*	-.14*	
Adjusted R2		.13	

Table 2: Results of Regression Analyses for Strategic Change

Results of Regression Analysis and Partial Derivation of the Interactive Variables

In model 2 of table Hypothesis 4, which states that there is a positive relationship between poorly performing organization with longer-tenured chief executive and the exhibition of strategic change, is supported. However to o investigate this interaction effect in more detail, a partial differentiation of strategic change was examined with respect to chief executive tenure. This to estimate the effect of the interaction of that variable and performance on strategic change:

d(strategic *change) / d(CEO tenure)*= -.21 - .23(performance). (1)

The value of *d(strategic change)/ d(CEO tenure) from this equation* is 0 when *performance* = -.72. This finding indicates that chief executive tenure decreases the likelihood of strategic change unless performance is less than .72 standard deviations below its mean. This result therefore support the prediction contained in hypothesis 4 and it explains the interactive effect between chief executive tenure and performance on strategic change. Thus as performance increases, the relationship

between chief executive tenure and strategic change grows increasingly negative.

Similarly from model 2 of table hypothesis 6 was supported explaining the situation that successful organizations with long-tenured teams may be particularly reluctant to change strategy. Taking the partial derivative of strategic change with respect to top management team tenure:

d(strategic change)/d Top management team tenure) = -.13 - 17(performance) (2)

The value of *d(strategic change)/d(TMT tenure)* is 0 when *performance* is -.62 standard deviations below the mean, indicating that top management team tenure decreases the likelihood of strategic change unless performance is less than .62 standard deviations below its mean. The results therefore supported the prediction of an interactive effect between top management team tenure and performance on strategic change. Thus, as performance increases, the relationship between top management team tenure and strategic change grows increasingly negative.

Hypothesis 8 was equally investigated and taking the partial derivative of strategic change with respect to top management team homogeneity:

d(strategic change)/ d(top management team homogeneity) = -.16 - 18*(performance).* (3).

-.87 was found indicating that top management team tenure homogeneity will decrease the likelihood of strategic change unless performance is less than .87 standard deviations below its mean.

Effects of Control Variables

Firm size and public ownership were found to have positive effects on the extent of strategic change in all the models. This confirmed the fact that larger firms in this study sample have the affinity to initiate strategic change. It therefore support the argument that when an organization controls extensive resources, it is easier for it to initiate and implement strategic change.

Public ownership was also found to have positive relationship with greater strategic change. This may not be unconnected with fact that the greater availability of funding and resources generally commanded by publicly held companies made the initiation of strategic change easier.

Environmental munificence, firm age, and had a no significant effect on strategic change in either of the models.

Discussion, Implications and Conclusion

The primary purpose of this study was to explore an integrated model of strategic change that took into account the direct and interactive effects of performance with chief executive and top management characteristics. Results of the data analysis revealed the extent to which organizations change their mix of businesses in response to both declines in performance and characteristics of their chief executives and top managers emerged from the results.

In the order of preference this study first examined the relationship between firm performance and strategic change giving room for exploring the combined effects of four managerial characteristics on strategic change. The four characteristics are:

(1) chief executive succession,

(2) chief executive tenure,

(3) top management tenure, and

(4) top management tenure diversity.

Secondly, the beliefs that poor organizational-performance may make the effects of managerial characteristics on strategic change more pronounced led to the examination of the interactive effects of performance and the four managerial characteristics.

Three sets of findings were recorded from this analysis.

1. First, poor organizational performance makes strategic change more likely. This is in line with argument of Kiesler and Sproull (1982) which states that declines in performance has the tendency to alert management that the existing strategy of an organization may not meet the requirements of the environment, thereby necessitating a change in strategy.

2. Second, Hambrick's (1993) view that top managers have an important independent influence on the directions of firms through their decisions regarding strategy was supported. Therefore by investigating the effects of chief executive characteristics on strategic change showed that chief executive tenure had a significant effect on strategic change, whereas chief executive succession did not. The results for top management Characteristics indicated that both the tenure of the top management team and the degree of homogeneity in the tenure of top managers were also important predictors of strategic change. It was equally proved that not only the average level of team tenure but also the diversity of team tenure that affects the degree of change in strategy.

3. Third, examining the combined effects of performance, chief executive characteristics, and top manager characteristic on strategic change within the regression model gave an important result for this study. This is because managerial characteristics may themselves cause organizations to change strategy poor performance increases their motivation to do so. Similarly the support for hypotheses 4, 6, and 8 specified a performance interaction. The findings point to the opportunity poor performance provides for initiating change in strategy. Poor performance has the capacity to signal managers that change in strategy may be necessary.

The study has endeavored to establish the fact that chief executives and top management of an organization should be considered important links between organization's performance and the possibility of making any strategic change. More importantly is the inevitable interaction between performance and the role played by the organization's top management team in

encouraging or inhibiting strategic change.

It is obvious from this study that most chief executive and top management team are likely to initiate change when performance is seen to be on the decline. However, modern strategic management will not support a situation in which performance is declining before strategic is effected, rather a pro-active strategic approach need to be taken to effect strategic change in order to avoid the dynamism of the market and compete effectively.

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