

# **Success Catalyst or Hidden Impediment? The Moderating Role of Governance Power of Top Management Teams in the Strategic Process**

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## **Abstract**

Although the literature on strategy formulation or implementation has been accumulating, whether to keep strategy stable so as to maximize firm performance has not yet been conclusively determined, particularly when the strategy-making process is intertwined with different levels of top management team's (TMT) governance power. This study is an attempt to revisit the performance implication of strategic persistence from the contingency perspective, which argues that such a relationship is sensitive to TMT power status. TMT power is characterized as ownership power structural power. Our evidence, in a sample of Taiwanese firms, lends support to the positive moderating effects of these two dimensions of governance power on the elusive relationship between strategic persistence and firm performance, while the deviation from the two dimensions weakens firm performance. This study demonstrates the critical role of top managers in the strategic process, and cautions against drawing universalistic normative implications for governance arrangement of TMT.

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*Having a strategy in the first place is hard. Maintaining a strategy is even harder. ~ Michael Porter (2011)*

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## 1 Introduction

As strategy research has long concerned with the process through which strategy is crafted and implemented, whether or not to keep strategy for an organizational stable remains debatable. Organizational outcomes are sometimes more likely a result of emergent strategies than intended strategies (Mintzberg et al., 1998) so strategic change, defined as the difference in the 'fundamental pattern of present and planned resource deployments' (Rajagopalan and Spreitzer, 1997), is deemed necessary to keep adaptive in ever changing environments (Carpenter, 2000). However, as strategy formulation may be driven by not only rational considerations but socio-psychological factors, keeping the strategic course of a company unchanged, as argued by Finkelstein and Hambrick (1990), reflects a dysfunctional decision-making process and yields negative consequences for long-term organizational viability. Kodak's failure to sustain its competitive advantage in the digital revolution due to its over-commitment to chemical photography is one of the recent examples of how strategic rigidity leads to a disastrous consequence.

Empirical evidence gathered so far does not unanimously support the performance effect of strategic change (e.g., Finkelstein and Hambrick, 1990; Leonard-Barton, 1992). More effort is needed to learn whether organizations are rewarded or censured for flexibility on strategy (Grossman and Cannella, 2006); that is, top managers may be berated for changing too slowly and too little, also possibly changing too much or in the wrong direction. As marketplaces are usually full of competitive signals and noises, most managers are hardly unaffected by all kinds of information and remain on the previously chosen course all the time (Abrahamson, 1991). The issue is getting complex particularly when strategic change is caused by the institutional rather than adaptive purposes (e.g., Staw and Epstein, 2000; Henderson and Cool, 2003a, 2003b). The market of hybrid vehicles shows the value of strategic persistence in the changing technological environments. Before the advent of the hybrid age, executives at GM, Ford and Daimler-Chrysler all chose to place multiple bets on different power systems, including internal combustion engines, battery/fuel cells and electric motors. Although petroleum-electric hybrid vehicles were derided as transitional products and money-losers, Toyota, as Japan's leading vehicle manufacturer, commits unflinchingly to the advancement in hybrid technologies and eventually takes precedence over its rivals. Toyota's unwavering attention to the chosen course is a great element of its market success.

In light of the mixed consequences of strategic persistence, it is necessary to go behind the scenes to gain a more comprehensive understanding of the strategic process. However, the success of a strategy relies not only in the plan itself but in the ability to formulate and execute it (Beer and Eisenstat, 2000). Furthermore, as the strategic process is essentially the game of politics (Eisenhardt and Zbaracki, 1992), the power of strategy makers, specifically the top management team (TMT), over strategy formulation and implementation is decisive and very likely leads to different performance outcomes (Talaulicar et al., 2005; Hambrick, 2007). In examining the performance effect of strategic persistence, prior studies seldom take into consideration the influence of TMT's governance power on the firm's strategic orientation-performance link. In response to the recent calls for more empirical inquiries into the interplay between TMT's power status and strategic process (Eisenhardt and Zbaracki, 1992; Golden and Zajac, 2001), this study therefore is an attempt to revisit the strategy-performance link from the contingency view by incorporating the governance power of the TMT.

Top managers, usually employee-owners, obtain ownership power from their equity shareholdings and structural power when they are offered seats on the company board. The two dimensions of governance power allow the TMT to have a say in formulating and putting strategy into practices, but also creates conflict and tension when their structural power deviates from the ownership power. Although the literature has not sidelined the role of the TMT in the strategic process, the presence of TMT power may contribute to disentangling the elusive performance effects of strategic persistence, and suffice for the contingency perspective that the effectiveness of any given managerial practice varies considerably with organizational and environmental settings (e.g., Murray, 1988). For example, the IPO of Facebook in 2012 is viewed not only as the largest internet IPO since Google in 2004, but also as a case which attracted public attention to the influence of a change in TMT's governance power; that is, how the founder, CEO Mr. Zuckerberg, and other top managers with a diluted ownership are still able to keep the original strategy stable and grow the company into a more dynamic and uncertain mobile cyberspace after IPO.

In a sample of 442 ICT (Information and Communication Technology) firms in Taiwan, this study develops and tests the hypotheses that the performance effect of strategic persistence is moderated by TMT governance power. The findings contribute to the strategy research and corporate governance literature in three aspects. First, despite the fact that strategy literature has been accumulating on the role of the CEO (e.g., Balkin et al., 2000), managerial responsibilities are rarely an exclusive CEO domain, as argued by the upper echelon theory (Hambrick and Mason, 1984). The members of TMT are equipped with different sources of information and responsible for strategy formation and implementation (Covin et al., 2006). The issues related to the strategic process thus need to be more meaningfully studied within the context of the TMT rather than the CEO *per se*. The inclusion of the governance power of the top management team as a whole into the contingency view could enhance our understanding of the complex interplay of power status of strategy makers, strategic persistence and organization outcomes. Second, from the agency perspective, this study is among the first to empirically demonstrate the moderating effects of TMT governance power on the performance effects of strategic persistence. This attempt not only clarifies the mixed blessings of strategic persistence (e.g., Nickerson and Silverman, 2003) but also highlights the boundary conditions as to how strategic persistence has a bearing on firm performance. Therefore, our evidence cautions against drawing universal normative implications for strategic persistence. Third, in order to heed the long-standing call for more empirical inquiries into non-western style governance systems of newly industrialized markets (Globerman et al., 2011), we test our hypotheses on a sample of Taiwanese firms in high-tech industries where top management teams have gradually gained governance power through decades of stock bonus programs. The traditional line between ownership and management is increasingly blurred, further confusing the responsibility for strategy making and implementation in these companies (Brandes et al., 2008). In light of such unique governance characteristics in Taiwan's sample, the study sheds new light on of the nuances of the interaction between the strategy making and governance power of top management teams and the consequent performance outcomes.

The rest of the paper unfolds as follows. The next section presents the theoretical background and develops hypotheses. Section three describes the sample and measures. The subsequent section reports the empirical results, and the final section concludes with managerial implications and limitations.

## 2 Literature Review and Hypotheses

### 2.1 Strategic Persistence

Strategic persistence is characterized as the extent to which a firm's strategy remains stable over time (Finkelstein and Hambrick, 1990), or represents a commitment to the chosen course of actions, implying steadiness or stability of resource allocation (Ghemawat, 1991; Hambrick et al., 1993). Literature on path dependence shows that firms are likely to routinize their decision-making patterns in order to economize the search and learning costs (Sydow et al., 2009). Persistence is beneficial until the strategy-environment fit is eroded by inertia and external dynamism (Finkelstein and Hambrick, 1990). In contrast to the economy of strategy-environment fit, some scholars suggest that strategic persistence is a result of psychological or social process (e.g., Haveman, 1992); that is, top managers, constrained by limited information processing capacity (Lant et al., 1992), may boldly assume a strategy that has worked in the past to be still effective in the future (Prahalad and Bettis, 1986) and thus respond slowly to market signals, falling into a pattern of dysfunctional strategic persistence (Tushman and Romanelli, 1985). One typical example is IBM's escalating commitment to the mainframe computer business, given the emerging trend of personal computers that started in the mid-1970s (Bresnahan and Greenstein, 1999). Commonly witnessed across industries, cases of this kind illustrate why and under what conditions decision makers may ignore negative feedback and stick to losing courses of action (Staw, 1981). In this vein, strategy studies seem to favour strategic flexibility more than strategic persistence particularly in the fast changing markets.

Although strategic flexibility highlights a firm's adaptability to ever changing environments, it is questionable as to whether frequent changes in strategic course of actions serve the purpose for maintaining competitive advantage. In the case of Yahoo's falling market shares from early 2006, Brad Garlinghouse, senior vice president of communications and communities at Yahoo at that time, was quoted as saying that "*...we lack a focused, cohesive vision for our company because we want to do everything and be everything — to everyone. We are scared to be left out. We are reactive instead of charting an unwavering course.*" On the theoretical front, some literature remains conservative about the benefits of strategic changes. For instance, Abrahamson (1991) argues that most change initiatives simply reflect fads or fashions which have little to do with enhancing long-term viability. In Staw and Epstein's (2000) study, top managers are found to receive higher levels of compensation when they adopt popular management practices such as TQM, MBO (management by objectives), team-based structure or empowerment. Similarly, managers under earning pressure tend to focus on actions in pursuit of short-term profits at the expense of long-term competitiveness (Zhang and Gimeno, 2010). The evidence above implies that top managers, either tempted by higher compensation or worried about being social misfits, may follow strategic changes without sufficient reasons or without considering any justifiable contributions of such changes to the long-term viability of the firm (e.g., Henderson and Cool, 2003a, 2003b).

Drawing on the above literature, this paper holds that neither strategic persistence nor change may always guarantee firm performance. Both of them is a double-edged sword for organizations (March, 1991). Specifically, proponents of strategic persistence contend that keeping a company strategically stable is conducive to achieving legitimacy with external stakeholders or deepening the competencies that have proven valuable in the past

(Hannan and Freeman, 1984). In Ghemawat's study (1991), the managerial commitment to the 747 wide-body aircraft project despite the pessimistic market outlook during the development period is thought to be the key to the success. However, opponents argue that persistence or commitment to a previously chosen course may lead to destructive consequences, especially when firms are operating in rapidly changing environments (March, 1999; Haveman, 1992). Firms that remain strategically unchanged over time may get trapped in organizational inertia and become too slow to recognize new opportunities and reluctant to react to environmental changes. For example, Mr. A.G. Lafley strategized for Procter & Gamble (P&G) in his 10 years as CEO and revived the global consumer-goods giant, roughly doubling its sales and increasing profit margins. However, since his retirement from P&G in 2009, the company has stumbled badly, and his successor is struggling to keep his job. Rather than argue whether his strategic successes somehow sowed the seeds of later problems, Mr. Lafley concludes that, "no strategy lasts forever" (Lafley and Martin, 2013).

In summary, strategic persistence seems to yield both positive and negative effects on firm operations and performance. The mixed results lead us to seek explanations beyond the existing empirical evidence. We argue that performance implications may be not clear until some hidden factors have been identified and tested for their influence. Thus, our aim is not to agree or disagree with prior research standpoints but to explain the elusive evidence by linking strategy research and corporate governance literature. The TMT plays a crucial role in strategy formulation and implementation (Finkelstein, 1992). Their influence on corporate governance may interplay with strategic persistence and jointly influence firm performance; that is, the benefits of strategic persistence may be better augmented by a fine-tuned governance arrangement which not only restrains TMT's self-serving intention but encourages them to act in the best interest of their organizations (e.g., Dalton et al., 2007). For example, during the 2008-2009 financial tsunami, the majority of commodity DRAM (the dynamic random access memory) manufacturers significantly reduced their capital expenditure to avoid worsening disappointing earnings and hurting stock prices, whereas Mr. Jae-Yong Lee along the executive team of Samsung Electronics, based on the equity ownership and board seats of the Lee family, persistently maintained the company's efforts on the new manufacturing processes regardless of the rivals' actions. To the present, Samsung has dominated the commodity DRAM market with share of over 40% and leads the advancement of commodity DRAM technology. The case further suggests that the alignment between strategy making and strategy makers' governance power jointly determines firm performance in a turbulent environment.

## **2.2 The Role of the TMT in the Strategic Process**

The upper echelon theory prescribes that what an organization does and the way it carries out its functions can be explained, in part at least, by the profile of its upper echelon or reflected in the values and cognitive bases of the TMT (Hambrick and Mason, 1984). The relevant literature demonstrates a significant link between firm strategies and TMT's functional backgrounds (Govindarajan, 1989) and lends further validity to the influence of top managers on strategic decisions and the consequent outcomes (Datta et al., 2003; Nadkarni and Narayanan, 2007). Studies on bounded rationality (Simon, 1991) or on managerial cognition (Weick, 1995) also share the view that the attributes of top managers dispose them toward specific strategic decisions.

Although the influences of top managers on strategy and firm performance have been studied, the extent to which their governance power intertwines with the strategic process has been sidelined in the literature. While some evidence casts doubt on the full explanatory power of top managers on organizational outcomes (e.g., Milliken and Martins, 1996), recent studies suggest moving beyond TMT demographic characteristics and including more substantive constructs, such as the power status of the TMT (Dunn, 2004, Haynes and Hillman, 2010). TMT power is defined as the ability of top managers to exert their will over other organizational members (Pfeffer, 1981; Finkelstein, 1992). Even though the power of the TMT in determining how strategic choices are developed and decisions made has been identified, few attempts have been made to investigate the influence of TMT power on the performance effect of strategic persistence. TMT gains power from multiple sources, such as structural power, ownership power, expert power, prestige power and others (Finkelstein, 1992). However, according to the literature (Dunn, 2004, Haynes and Hillman, 2010), structural power and ownership power are the most fundamental and realistic aspects of the decision-making process among the various executive powers. In line with Dunn's approach, TMT power in this study is characterized by two dimensions: (1) ownership power, which is based on equity shareholding and (2) structural power, which refers to executive duality: TMT members also serving as board directors.

In this study, we concern ourselves with the influence of these two dimensions of governance power on the performance effect of strategic persistence. We also consider whether deviation from these two dimensions of governance powers causes any problems for the strategic process and consequent outcomes.

### **2.3 Ownership Power of the TMT**

To address the problems associated with the diffusion of equity shares and the separation of ownership and control, agency theorists prescribe a cure for the principal-agent conflicts by introducing incentive or/and monitoring mechanisms (Fama and Jensen, 1983). Managerial ownership is, therefore, viewed as an important mechanism that potentially aligns the interests of managers and shareholders, thereby reducing agency problems (Jensen and Meckling, 1976; Jensen and Murphy, 1990; Porter, 1992). As noted by Hill and Snell (1989), when top managers become shareholders through stock bonuses or options, they are more likely to act in the best interests of shareholders. They make decisions more as owners and less as self-serving agents.

In addition to the interest alignment effect, ownership provides the rights and power of decision making (Finkelstein, 1992); that is, ownership power manifests itself in the boardroom where most of strategic decisions are made. Those who control the most voting shares make the final decisions and impose their will on other shareholders (Poulsen et al., 2010). In this vein, the interplay of decision making power and equity stakes not only make top managers more able to realize their strategic intents but also to bear the financial consequences of their decisions (Sundaramurthy et al., 2005). Zahra's (1996) study shows that top managers powered by sufficient equity ownership exhibit a high level of entrepreneurial orientation, which is important to organizational renewal and survival. Similarly, McClelland et al. (2012) conclude that ownership power provides executives an anchor for long-term horizon goals.

Although the quality of managerial decisions always matters, empirical evidence supports that increasing ownership power induces top managers to better accomplish their goals by

softening the interference of stakeholders of the organization (Cheng et al., 2005); that is, whatever strategy is taken, top managers with ownership power are motivated to achieve strategic goals since their interests align more with the desired returns from their strategic actions than those who do not have a similar vested interest (e.g., Combs et al., 2007). We thus argue that ownership power of top managers not only makes their interests align with the firm's, but also has a positive bearing on strategic moves and organizational outcomes.

*Hypothesis 1: The stronger the ownership power of a top management team, the stronger the performance effect of strategic persistence.*

## **2.4 Structural Power of the TMT**

The second dimension of TMT governance power refers to their structural power, which is based on hierarchical arrangements or structural control systems (Finkelstein, 1992). Formal structures confer power by specifying duties, responsibilities and levels of authority within a hierarchical framework. Pfeffer (1981) argues that power and control are positively associated with one's position in a formal hierarchy. Therefore, managers in high positions are conferred with the structural power to make strategic decisions based on their preferences and affecting the entirety of the firm.

In light of the potential conflicts between shareholders and management, boards of directors are expected to be vigilant protectors of shareholder interests. Directors can monitor the TMT and influence firm strategy by being involved in the strategic decision-making processes. Drawing largely on agency theory (Jensen and Meckling, 1976; Fama, 1980), researchers endeavor to show that an independent board, which normally consists of members without vested interests in the firm, is more effective in monitoring and enhancing firm performance. However, executive duality, in terms of sitting in pivotal managerial positions and being on the board, skews the power balance in corporate governance and poses a risk to shareholders. Top managers who also serve on a board can control agendas, thereby furthering their own preferences. These might include such tactics as self-dealing and limiting criticism against a chosen strategic course of actions (Finkelstein and D'Aveni, 1994; Boyd, 1995). The literature likewise views the concentration of power in few board members who act in concert as a red-flag indicator of poor corporate governance (Dunn, 2004) or a warning sign for firm performance (Eisenhardt and Bourgeois, 1988).

However, despite doubts on the dual roles of top managers (Castañer and Kavadis, 2013), the reality is that a large number of firms persist with this combined leadership structure in their corporate governance arrangements, thereby enhancing the structural power of top managers (Finkelstein and Mooney, 2003). According to a survey conducted by McKinsey & Co. in 2002, 75% of S&P 500 companies had executive duality in their corporate governance structure. Contrary to the agency theory, stewardship theorists argue that executive duality reflects both a structural and psychosocial empowerment of top managers, which is an encouragement for them to better serve their firm and shareholders (e.g., Chahine and Tohmé, 2009). When compared to inside directors who serve as active managers, outside directors are more independent in monitoring managerial activities but less informative about the firm's operations. As such, inside directors are in a better position to inform outside directors (Hillman et al., 2000), clarify their strategic intention and advocate for their chosen strategies (Grossman and Cannella, 2006). By contrast, when the board is dominated by outside directors, intensely monitored

managers are likely to refrain from sharing information with the outside directors (Adams and Ferreira, 2007) and to prefer allocating organizational resources to activities that are more likely to yield a visible impact on short-term profitability at the expense of long-term viability (Connelly et al., 2010).

Due to the legal responsibilities of boards of directors in corporate governance, they are obliged to get involved in any significant change in strategy (Tushman and Romanelli, 1985). Thus, strategic persistence or change may be facilitated or hindered by the composition of the board. Because of their varied backgrounds and independence (Grossman and Cannella, 2006), outside directors are likely to question TMT's existing strategies and favor strategic change rather than keeping strategy unchanged. Nevertheless, as outside directors are not necessarily familiar with a firm's operational details and competitive environments, their suggestions or even decisions, though well intentioned and independent, may not always be constructive to the firm. In contrast, a board is able to function better in the presence of inside directors who provide the most updated information from their managerial positions and carry sufficient clout to exert their will.

In this vein, the performance implications of outside directors inevitably meet with skepticism (e.g., Fama and Jensen, 1983; Jensen, 1993), though it is empirically difficult to find robust evidence that outside directors matter at all in terms of performance (Fields and Keys, 2003). As increasing outsider representation on boards may amount to "quack corporate governance" (Romano, 2005), the top manager's dual role in corporate governance is worthy of more positive attention. Departing from the long-standing debate on the pros and cons of TMT's structural power, the study contends that the structural power of top managers influences firm performance through the interplay of their decision making on firm resource utilization (Peng et al., 2007; Peng et al., 2010). Thus, we hypothesize that the performance effect of strategic persistence may be higher under conditions of high structural power.

*Hypothesis 2: The stronger the structural power of the top management team, the stronger the performance effect of strategic persistence.*

## **2.5 The Power Deviation**

As discussed above, managerial ownership makes the managers' interests become more aligned with those of other shareholders and lowers the odds of pursuing any value-reducing actions. However, the presence of TMT ownership power may not always ensure the desired organizational outcomes, especially when it deviates from their structural power. It is not unusual that insiders of public-traded firms have voting rights in excess of their cash flow rights (e.g., La Porta et al., 1999; Claessens et al., 2000; Claessens et al., 2002). Under such circumstances, manager-owners maintain control of a firm by keeping managerial positions to themselves and making it difficult to judge the value of their decisions by filtering the information released to outsiders. Furthermore, through their seats on the board, the insiders' will can prevail in decision making and further entrench them in their positions, leading to the so-called "managerial entrenchment problem" (Shleifer and Vishny, 1989). Succinctly put, when voting rights significantly outnumber cash flow rights, the insiders are more likely to dominate all key decision making without having to bear the full risk of their decisions (La Porta et al., 1999) and pursue their private interests at the expense of other shareholders (Yeh, 2005). The evidence thus far also shows a negative effect of the deviation in the cash flow rights



of insiders from their voting rights on firm value (Gugler and Burcin, 2003; Wu, 2011). In addition to the performance-reducing consequences of governance power deviation, the managerial entrenchment problem caused by an excess of managerial control power on the board also allows cash flow rights to contort the strategic process. Among several elements of the strategic process, strategic decision-making participation, characterized as the extent to which a firm's major strategic decisions are made through either consensus-seeking among key stakeholders or individualistic orientation by top managers, remains the most critical to the comprehensiveness of decisions made to maximize the firm value (Covin et al., 2006). When entrenched in their positions due to their control power in the board, top managers benefit themselves by pursuing more personal goals while bearing relatively lower costs if their decisions went wrong (Shleifer and Vishny, 1997). They are also likely to become more autocratic, impeding other stakeholders' participation in the strategic process. Therefore, as the self-serving motivation of entrenched managers may bias their decisions, managerial entrenchment inevitably hurts the persistence and comprehensiveness of strategy formulation and implementation. The negative moderating effects of managerial entrenchment are also echoed by Wei and Zhang's (2008) study showing that an entrenchment problem worsens managerial discretion on free cash flow and leads to serious overinvestment.

Given that autocratic and arbitrary decision making of entrenched managers may impair the strategy-performance link (Goll and Rasheed, 2005), we hypothesize that a deviation in the structural power and ownership power of top managers very likely makes the strategic process less participatory and more self-serving. Both of these factors attenuate the relationship between strategic persistence and firm performance.

*Hypothesis 3: The greater a top management team's structural power deviates from their ownership power, the weaker the performance effects of strategic persistence.*

### **3 Methods**

#### **3.1 Sample**

ICT (information and communication technology) firms in Taiwan are selected for hypothesis testing in the study, not only because they are always compelled to decide whether and when to change or remain on the previously chosen course of actions in the face of global competition, but also because a Taiwanese sample is well suited for contrasting the generalizability of western wisdom, given Taiwan's culture, economic and institutional differences from the western context. The sample was drawn from the 2010 Taiwanese public-listed firms across several segments, including semiconductor, computer and peripheral equipment, optoelectronic, communications and internet, electronic parts and components, electronic products distribution and information services, during the period 2006~2010. The ICT industry in Taiwan provides a relatively rich variety of data, and its success has been well recognized as an East-Asian catch-up model (Huang, 2011). Moreover, such an industry-specific study yields an inherent control for extraneous factors such as variances of environmental dynamism or differences in business models. We collected company data from the Taiwan Economic Journal (TEJ) database, which has been validated by extensive and rigorous studies (e.g., Wu, 2008; Lin and Liu, 2011). After removing some samples with incomplete data, we obtained a sample of 422 firms.

### 3.2 Variables and Measures

*Dependent variable.* Firm performance is measured by the return on assets (ROA) which is defined as the earnings before interest, tax, depreciation and amortization (EBITDA) and divided by total assets (Guthrie and Datta, 2008). Since ROA incorporates both firm efficiency and profitability, it serves widely in the literature as an important proxy for firm performance (Kinney and Wempe, 2002). Although the use of a single performance measure invokes some concerns, organizational studies have validated the use of ROA by demonstrating its high correlation with other performance indicators such as return on sales (ROS) and return on equity (ROE) (Simonin, 1997).

*Independent variable.* *Strategic persistence* is characterized as the extent to which a firm's strategy remains stable over time. A composite measure of strategic persistence is adopted from Finkelstein and Hambrick's approach (1990), which breaks down the notion of strategic persistence into six dimensions: (1) advertising intensity (advertising expense/net sales); (2) research and development intensity (R&D expense/net sales); (3) plant and equipment newness (net P&E/gross P&E); (4) non-production overhead (SGA expenses/net sales); (5) inventory levels (inventories/net sales) and (6) financial leverage (total debt/total equity). Since the data on advertising intensity is noncompulsory disclosure data in the TEJ database and usually incorporated into non-production overhead costs, we used the other five dimensions to form a composite measure of strategic persistence in the current study. Following Datta et al. (2003), we first computed a five-year (2006~2010) variance for each dimension and standardized the variance scores for each dimension (mean = 0, standard deviation = 1). Finally we multiplied the score of each dimension by minus one and averaged them into a composite measure of strategic persistence. The higher the composite score is, the greater the strategic persistence of a sample firm will be.

*Moderator variables.* Each of the relevant governance variables was obtained from the TEJ database, which collects data from each firm's annual reports and proxy statements. The TEJ database reveals information about the composition of the board of directors and the ownership structure of firms. Following Michel and Hambrick (1992), this study defines a top management team as those who are at or above the level of vice president and any other executive officers who are required to be present at the company board meetings. Following Dunn's (2004) definition, we measured *ownership power* by the proportion of a firm's outstanding stock owned by top managers and *structural power* by the percentage of board directors in managerial positions in the meantime. When top managers hold a high percentage of shares in their firms, they are thought to own more ownership power. Similarly, when top managers also serve as board directors in their firms, they possess greater structural power. Finally, in line with the measurement of deviation of control from ownership (Claessens et al., 2000; Claessens et al., 2002), *power deviation* was measured by the structural power/ownership power ratio.

*Control variables.* Several control variables are included in our model to avoid alternative explanations. Control variables are categorized into two groups to represent institutional- and firm-level factors affecting firm performance. The Asian corporate landscape features a predominance of family ownership and inter-firm cross-holdings, both of which create institutional differences from western countries. To eliminate the potential effects of alternate explanations caused by the idiosyncrasies of the Taiwanese sample and make the empirical results generalizable beyond the Asian context, we introduced two control variables for the institutional differences: *family ownership* and *business group*

*membership* (e.g., Ramaswamy et al., 2012). Following Anderson and Reeb (2003), we measure family ownership by the fractional equity ownership held by the founder and his or her immediate family members. For the measurement of business group membership, we used the definition of the Taiwanese Fair Trade Commission, which legally defines a business group as: “a group of companies, more than 30% of whose shares are owned by some individuals or by companies controlled by those individuals or those that are practically controlled by them despite lower ownership control.” A sample company affiliated to any business group was coded 1 and otherwise 0.

In addition to the two variables used to control for institutional differences in the Taiwanese sample, we considered another one at the industry-level and two at the firm-level. To control for industrial variances, we included *segment dummies* to correct for possible performance differences among segments. By adopting the classification of TEJ, we sorted sample firms by seven segments: semiconductor, computer and peripheral equipment, optoelectronic, communications and internet, electronic parts and components, information service and electronic product distribution. We treat the electronic products distribution segment as an omitted dummy variable. Furthermore, the data for two firm-level control variables were also collected from the TEJ database. *Firm size* was measured as the log of total assets over a five-year average. *Firm age* was measured by the number of years from founding to 2008 (the median of the observation period).

## 4 Results

The means, standard deviations and correlations of variables are shown in Tables 1a and 1b. Overall, the correlations among the independent variables are general or modest. For the hypothesis testing, hierarchical multiple regression analysis was used to test the influence of strategic persistence on firm performance. We first entered control variables in the baseline model (Model 1). As expected, firm size, firm age and business group membership were correlated with firm performance. After entering the control variables, we then entered strategic persistence in Model 2. The results of Model 2 reveal that the performance effect of strategic persistence is not significant, but the negative sign supports the plausibility of the argument that strategic persistence is probably driven by irrational strategic planning or implementation processes.

Table 1a. Descriptive statistics and correlation matrix

		Mean	S.D.	1	2	3	4
1	Firm performance	10.935	8.503				
2	Semiconductor segment	0.185	0.389	<b>0.133</b>			
3	Computer segment	0.182	0.387	0.050	<b>-0.225</b>		
4	Photovoltaic segment	0.111	0.315	-0.103	<b>-0.169</b>	<b>-0.167</b>	
5	Telecommunication segment	0.118	0.324	0.031	<b>-0.175</b>	<b>-0.173</b>	<b>-0.130</b>
6	Electronics segment	0.299	0.458	0.003	<b>-0.311</b>	<b>-0.308</b>	<b>-0.231</b>
7	Electronic channel segment	0.055	0.227	-0.111	<b>-0.114</b>	<b>-0.113</b>	-0.085
8	Firm age	18.379	8.300	<b>-0.170</b>	<b>-0.166</b>	-0.016	-0.025
9	Firm size	5.769	1.216	<b>0.245</b>	0.090	-0.002	<b>0.172</b>
10	Family ownership	35.566	28.361	-0.028	-0.057	0.044	-0.074
11	Business group	0.531	0.500	-0.087	0.044	0.002	<b>0.137</b>
12	Strategic persistence	0.860	0.042	-0.037	-0.054	<b>0.181</b>	<b>-0.192</b>
13	TMT ownership power	2.680	3.012	0.099	-0.006	0.012	<b>-0.124</b>
14	TMT structural power	15.488	13.473	<b>0.127</b>	0.068	0.077	<b>-0.105</b>
15	TMT power deviation	10.901	17.425	<b>-0.207</b>	-0.028	<b>0.098</b>	0.029

The bold letter means significance level is greater than 5%.

Table 1b. Descriptive statistics and correlation matrix

	5	6	7	8	9	10	11	12	13	14
6	<b>-0.239</b>									
7	-0.088	<b>-0.157</b>								
8	-0.089	<b>0.269</b>	-0.025							
9	0.014	<b>-0.130</b>	<b>-0.120</b>	0.065						
10	0.002	0.055	-0.018	-0.017	-0.009					
11	0.036	<b>-0.154</b>	0.037	0.007	<b>0.283</b>	<b>0.177</b>				
12	-0.075	<b>0.230</b>	-0.065	0.024	<b>-0.158</b>	-0.019	-0.022			
13	-0.043	0.038	0.092	-0.117	<b>-0.168</b>	<b>-0.177</b>	-0.038	0.010		
14	-0.047	-0.028	0.012	-0.012	0.087	<b>-0.253</b>	0.050	0.002	<b>0.500</b>	
15	-0.069	0.033	-0.080	<b>0.171</b>	<b>0.100</b>	0.002	0.064	0.023	<b>-0.245</b>	<b>0.176</b>

The bold letter means significance level is greater than 5%.

In Model 3, we tested the moderating effects of ownership power. The results show that the relationship between strategic persistence and firm performance was positively moderated by ownership power ( $p < 0.05$ ). In order to confirm the moderating effect of ownership power on the relationship between strategic persistence and firm performance, we plotted the regression lines in subsamples classified by the level of moderators. To plot the moderating effects of ownership power on strategic persistence, we took the values of one standard deviation below (i.e. Low ownership power) and above (i.e. High ownership power) the means of both variables. Figure 1 shows that a high ownership power alleviates the negative effect of strategic persistence on firm performance, lending support to Hypothesis 1. In Model 4, the moderating effect of structural power on strategic persistence also positively relates to firm performance ( $p < 0.05$ ). Figure 2 illustrates the moderating effects of structural power by showing a positive slope in the presence of a higher level of ownership power, giving support to Hypothesis 2. In Model

5, we tested the moderating effects of the deviation between ownership power and structural power and found a negative effect for the strategic persistence-power deviation interaction term. Figure 3 further demonstrates that the slope of high power deviation is negative and lower than the low power deviation. This result supported the argument of Hypothesis 4 that the relationship between strategic persistence and firm performance is negatively moderated by the deviation of structural power and ownership power. Thus, we confirmed the moderating effects of ownership power, structural power and power deviation. In this study, all of the hypotheses have been supported.

Table 2. Regression results

N = 422	Model 1	Model 2	Model 3	Model 4	Model 5	Model 6
Semiconductor segment	.267 **	.295 **	.294 **	.305 **	.267 **	.276 **
Computer segment	.242 **	.284 **	.273 **	.282 **	.296 **	.287 **
Photovoltaic segment	.039	.052	.038	.064	.039	.044
Telecommunication segment	.182 *	.203 **	.195 *	.212 **	.194 *	.198 **
Electronics segment	.292 **	.342 **	.326 **	.354 **	.328 **	.333 **
Electronic channel segment	.050	.062	.044	.063	.042	.032
Firm age	-.202 ***	-.205 ***	-.184 ***	-.207 ***	-.187 ***	-.181 ***
Firm size	.312 ***	.302 ***	.304 ***	.282 ***	.267 ***	.247 ***
Family ownership	-.010	-.014	.003	.014	-.019	.012
Business group	-.152 **	-.147 **	-.154 **	-.152 **	-.137 **	-.142 **
Strategic persistence (SP)		-.073	-.089	-.075	-.098	-.108 *
Ownership power (OPR)			.115 *			.034
Structural power (SPR)				.098 *		.107
Power deviation (PD)					-.115 *	-.125 *
SP × OPR			.129 **			.072
SP × SPR				.092 *		.081
SP × PD					-.153 **	-.136 *
F for Model	8.333 ***	7.792 ***	7.959 ***	7.312 ***	7.884 ***	7.126 ***
R <sup>2</sup>	.169	.173	.202	.189	.206	.237
Adjusted R <sup>2</sup>	.148	.151	.177	.163	.180	.204

1. Standardized coefficients are reported

2. \* $p < 0.05$ ; \*\* $p < 0.01$ ; \*\*\* $p < 0.001$

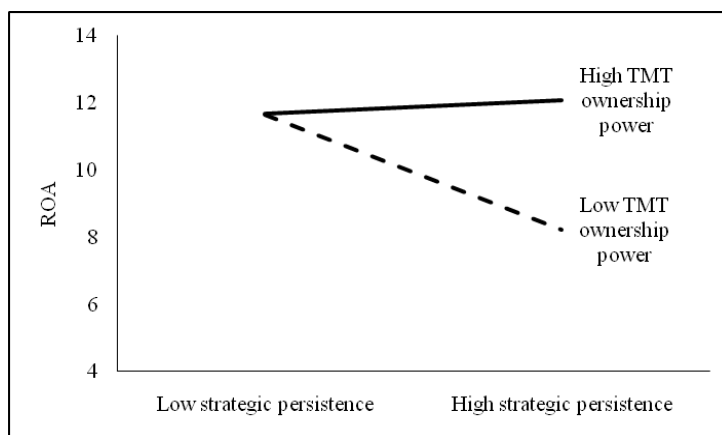


Figure 1. The moderating effect of TMT ownership power

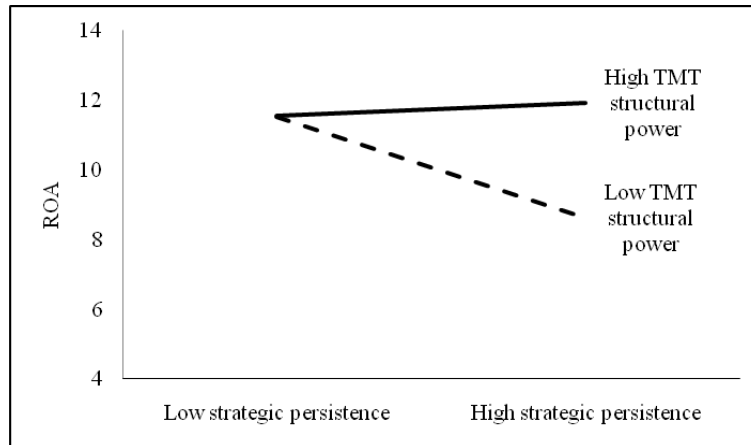


Figure 2. The moderating effect of TMT structural power

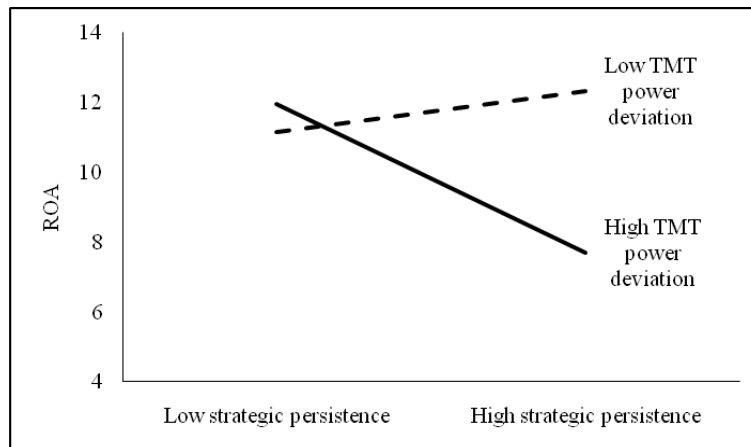


Figure 3. The moderating effect of TMT power deviation

## 5 Discussion

Strategic persistence and change seems to lie at opposite ends of a spectrum, so are prior findings divided as to which one contributes more to firm performance. The resignation of Andrea Jung as CEO of Avon in April 2012 illustrates the key contingency of the elusive performance effects of strategic persistence. Andrea Jung successfully led Avon out of trouble in the early 2000s by reinvigorating the direct sellers (Avon ladies) and repositioning prior product lines, but her entrenchment at the top of the company ever since and the deviation of her governance power gradually soured her strategic renewal. In addressing cases of this kind, this study inquires into the role of the top management team in the strategic process and empirically captures the situational efficacy of strategic persistence by identifying the boundary conditions where strategy interacts with executive governance power at its best. That is, the findings confirm the general thesis that the performance implications of strategic persistence are not uniform but rather contingent upon the governance power arrangements of the top managers.

Given that continuity of strategy is one of the five pillars of a good strategy (Margretta,

2011), this study shows that strategic continuity yields more performance implications in the presence of "well tuned" governance power of a top management team. Executive ownership enhances the performance effect of strategic persistence because equity ownership presumably makes executives more accountable to the best interests of shareholders and softens agency conflicts caused by the separation of ownership and control. On the other hand, empirical support for the moderating effect of structural power implies that the linkage between strategic persistence and firm performance is more significant in the presence of inside directors on the board. Top management team members exert their power not only by making strategic decisions but, in the dual role of manager-owner, by influencing the decisions made by the board at the same time. This stylized fact is echoed in a survey by the *US Business Week* on practicing managers, which refutes the agency argument that structural power leads definitely to the opportunistic behavior of top managers (Dobrzynski, 1995). Instead, TMT structural power contributes to improving mutual communication in the board room and conduces to a unified strategic leadership at the apex of the firm, which enhances the steadfastness of strategy formulation and implementation. Our evidence thus suggests that the performance effect of strategic persistence will be contextually determined by the extent to which the top management team plays a balanced role in strategy making and corporate governance.

In terms of the deviation of the two dimensions of governance power, our findings confirm a negative moderating effect when structural power becomes relatively stronger than ownership power. The evidence on power deviation is consistent with so called "managerial entrenchment," which is one of the costliest manifestations of the agency problem between shareholders and managers (Yeh, 2005). Furthermore, the results shed a different light on the above discussion of the governance power of a top management team. Although structural power of top managers relates to a unified leadership, an overweight structural power relative to ownership power more likely leads managers to pursue self-interest with fewer checks and controls. Their opportunistic orientation in such circumstances may undermine persistent strategy formulation and implementation and weaken the strategy-performance relationship. Our findings confirm that the asymmetry of the two powers leads to detrimental consequences for strategic persistence.

A managerial implication based on our results is that keeping strategy persistent *per se* does not ensure performance gain. Instead, with well-tuned TMT governance power, firms are more likely to achieve the desired outcomes of the strategic choices made by top managers. We suggest that greater ownership power or structural power of the TMT helps firms conquer elusive performance implications when they attempt to keep strategies on track; that is, when top managers obtain sufficient governance power to guide and bolster their strategic choices it is likely to yield better performance. Our results also caution against firms where managerial power configuration is dissymmetrical. In these cases, the managerial entrenchment, if any, very likely makes the strategic process less participatory and more self-serving. The study evidences a situational efficacy of strategic persistence and recommends a circumspect arrangement of the two types of TMT power.

Although our evidence suggests practitioners cope discreetly with the risk of abuse of governance powers by TMTs, the results should be viewed in light of several limitations which pave the way for further research. First, although our measure of strategic persistence is based on Finkelstein and Hambrick's (1990) instrument, which has been adopted in a number of studies (e.g., Datta et al., 2003; Grossman and Cannella, 2006), the accounting ratios included by the measure may not comprehensively encompass all

possible dimensions of strategic actions. For example, in the study of Zhou and Wu (2010), the strategic actions, including strategic flexibility and explorative/exploitative learning, are measured by self-reporting questions rather than the variation of accounting ratios. Future research could; therefore, consider a more fine-grained approach to the construct of strategic persistence based either on surveys or case studies to complement the current measure.

Second, while we acknowledge the moderating role of TMT power in the performance effect of strategy persistence, more recent studies view company boards as not only having a critical role in shaping the domain of discretion for managers (Tang et al., 2011) or overseeing chosen strategy (Pugliese et al., 2009) but also as being a constraint on management activities (Haynes and Hillman, 2010). Tensions between board directors and executives influence their harmony and the ways that strategy is formulated and implemented. Future studies could broaden the scope to cover the internal dynamics between boards and the TMTs so as to better evaluate the moderation effects of corporate governance on the performance implications of strategic persistence.

Finally, the empirical findings of this study are based entirely on a sample from the Asian context, which features a predominance of family ownership businesses. The performance effect of strategic persistence is inevitably influenced by a longer planning horizon and higher accountability of a TMT due to family involvement (Sciascia and Mazzola, 2008). The stewardship perspective of corporate governance not only contrasts with the agency perspective but implies marginally discrepant outcomes of strategic persistence. This study paves the way for more empirical probes into the interplay of the two theoretical perspectives on strategic persistence and the sensitivity of each perspective to different contexts.

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