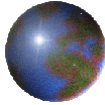




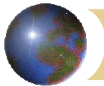
## Fundamental Insights from Penrose (1959)



### Why do Managerial Resources and Management Teams Matter?

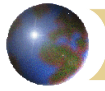
**YASEMIN Y. KOR**

Darla Moore School of Business  
University of South Carolina



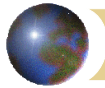
## Penrose (1959) The Theory of the Growth of the Firm

- ✦ 1996, 2001
- ✦ “I am very grateful to the distinguished scholar, Edith T. Penrose, for inspiring me with her great ideas... **Without her footprints, I would not even know where to start.**”
- ✦ **Critical roles played by managers and entrepreneurial management teams:**
  1. Interacting with the firm’s resources,
  2. Subjectively perceiving and creating new uses for resources, and
  3. Driving the rate and direction of the firm’s growth and strategic experimentation.



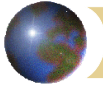
## Managers Interacting with Resources

- ✦ **Firm growth** can be studied as a **dynamic process** of management interacting with resources
- ✦ “As management tries to make the best use of resources available, a truly “dynamic” interacting process occurs which **encourages continuous growth but limits the rate of growth**” (Penrose, 1959, p.5)
- ✦ The **services** of resources are upstream from the end product
- ✦ The catalyst for this conversion process is the **resource of management** (Mahoney, 1995)



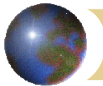
## Managers Interacting with Resources

- ✦ Resources as cognitive drivers for strategy (Itami and Numagami, 1992)
- ✦ “There is a close **relation between** the various kinds of **resources** with which a firm works and the **development of ideas, experience, and knowledge** of its managers and entrepreneurs” (Penrose, 1959, p. 85)
- ✦ Firm as a unique bundle of resources  
→ **Firm-specific managerial experience**
- ✦ Intimate and tacit knowledge of the firm’s resources, capabilities, organizational structures, standard operating procedures, unique historical conditions, and personnel, including human capital asset specificity (Williamson, 1996)



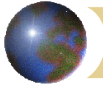
## Managers Interacting with Resources

- ✦ Compared to managers who are relatively new to a firm, managers with tacit knowledge of the firm's capabilities and organizational routines may envision a superior "subjective productive opportunity" set for the firm (Penrose 1959, p. 42)



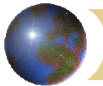
## Firm-Specificity of Managerial Experience

- ✦ Proper matching of resources and capabilities with opportunities (Kor and Mahoney 2000)
- ✦ **Identifying and creating** appropriate productive opportunities unique to a firm
- ✦ **Effectively allocating** financial and human resources to seize these opportunities can create entrepreneurial growth and competitive advantage
  - ✦ With tacit understanding of the firm's technology knowledge bases, managers can effectively assess the performance potential of different R&D paths and deploy the financial funds to projects in which the firm is more likely to become competitive
  - ✦ With experiential knowledge of the firm's employees, managers can also match employee skills to projects and employees to each other in team settings (Prescott and Visscher 1980)
- ✦ **Resource-specificity of managerial experience**



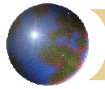
## Managers Interacting with Resources

- ✦ There are both **value-adding** and **counter-productive effects** of managerial experience in the firm
- ✦ Long tenured managers are inclined to **invest less** in research and development (Kor, 2006). However, because of their intimate knowledge of the firm's technology and human resources, they are able to make superior investment decisions, shown by **superior returns** to R&D (Kor and Mahoney, 2005).
- ✦ Important **dilemma** in configuration of the top management team
- ✦ While an experienced management team can generate higher returns for every dollar invested in R&D, the firm may suffer from an R&D under-investment problem
- ✦ More intuitive and empirical understanding about resource and firm-specificity of managerial experience



## Founders Interacting with Resources

- ✦ **Higher intensity and impact** of interactions between managers and resources
- ✦ Intimate understanding of human, technology, and organizational assets
  - ✦ → effective resource allocation and creative resource combinations
  - ✦ → efficiency in resource utilization -- scarcity
  - ✦ → integrative capability needed for business model construction
- ✦ Business models and competitive advantage frequently **break down during the transition** from founder teams to professional teams
- ✦ Founders and managers can be different in their goals, priorities, and level of engagement, leading to a divergence between their strategic choices (Kor, 2003, 2006)



## Knowledge, Experience, Transferability

- ✚ Transferability of resource-specific knowledge

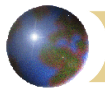
- ✚ Penrose (1959, p. 53) explains:

- ✚ “Experience produces increased knowledge about things and contributes to ‘objective’ knowledge in so far as its results can be transmitted to others. But **experience itself can never be transmitted**; it produces a change – frequently a subtle change – in individuals and cannot be separated from them.”

- ✚ **(Non)transferability** of experience (e.g., entrepreneur’s passion, emotions, Cardon et al., 2009; energy, ownership, and ego )

- ✚ Shareable, teachable, and diffusible

- ▣ Specificity in time and place (Hayek, 1945)
- ▣ Homegrown vs. Not (Impediments to Internalizing)



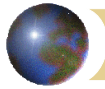
## Managers Interacting within Teams

- ✚ “An organizational team is ‘something more than a collection of individuals; it is a collection of individuals who have had **experience in working together**, for only in this way can *teamwork be developed*” (Penrose, 1959: 46)

- ✚ **Subjective productive opportunity of the firm** is based on teamwork and associational experience
  - ▣ Knowledge about the integrity and ability of team members

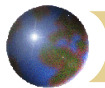
- ✚ An organization’s sensing, creative, and learning functions will come to full fruition only if a firm’s top executives can **co-produce and co-learn as a team** (Barnard, 1938)

- ✚ An **integration skill** at the CEO level—knowing which managerial resources to bring together and how to effectively integrate them (Kor and Mesko, 2009)



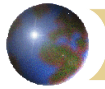
## Subjectively Perceived Uses for Resources

- ✚ **Heterogeneity in productive services from resources**
  - ▣ Productive services are discovered over time, as managers make **subjective decisions** about resource allocation, deployment, development, and maintenance (Mosakowski, 1993)
- ✚ **Versatility of Entrepreneurial Resources**
  - ✚ The imaginative effort, the sense of timing, the instinctive recognition
- ✚ **Heterogeneity in managerial mental models** (Mahoney, 1995)
- ✚ Plurality in knowledge and expectations about new business opportunities → creative resource combinations



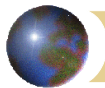
## Versatility in Entrepreneurial Resources

- ✚ Penrose notes that some firms may have these visionaries by **luck**, but other firms have them because they developed the appropriate corporate culture, human resource practices, and reward systems to **nurture** the entrepreneurial faculties in their employees
- ✚ Team-specific internal absorptive capacity (Foss et al., 2008)
  - ▣ Collective capacity to learn from each other during debates and idea exchanges despite diversity-induced disagreements.
- ✚ Future Research:
- ✚ Effective development and deployment of **entrepreneurial human capital** -- at various levels in the firm



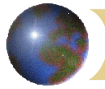
## Firm Growth and Experimentation

- ✚ Managerial capability is the binding constraint that limits the growth rate of the firm the so-called **Penrose effect**
- ✚ Penrose submits (1959: pp. 47-8):
- ✚ “If a firm deliberately or inadvertently expands its organization more rapidly than the individuals in the expanding organization can obtain the experience with each other and with the firm that is necessary for the effective operation of the group, the **efficiency of the firm will suffer** ... and a period of “stagnation” may follow ... Since the services from **“inherited” managerial resources** control the amount of new managerial resources that can be absorbed, they create a fundamental and inescapable limit to the amount of expansion a firm can undertake at any time.”
- ✚ Limits on the **“absorption of modern technology”** (1965, p.8) can be the binding constraint on growth.



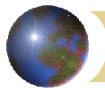
## Idiosyncratic Capacity to Learn, Expand & Diversify

- ✚ Professional service firms (law firms) – human assets are key
- ✚ Bottleneck to profitable growth is the availability of **partners** (Kor and Leblebici, 2005)
- ✚ **Limits to partner leveraging while diversifying**
  - ☒ Compromise in coordination of complex cases (multiple areas of expertise)
  - ☒ Compromise in oversight and mentoring of associate lawyers
  - ☒ Partner leveraging – Service/Geog. Diversification – Less profitable jointly
- ✚ **Limits to partner leveraging while hiring laterally**
- ✚ **Adjustment costs:**
  - ☒ Time and effort to accumulate firm-specific knowledge (business practices, values, specific clients), and knowledge of co-workers (Prescott and Visscher, 1980; Slater, 1980)
- ✚ **No Short Cuts in Learning, Growing, and Diversifying Profitably**



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