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Managerial Discretion: An Empirical Review and Focus on Future Research Directions

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Abstract

Scholars have long been interested in when and to what degree managers are able to exert control over their organizations. In this review, we examine managerial discretion, or the latitude of action available to managers. Since its introduction, scholars have attempted to explain when managers will have discretion, what discretion means for organizational outcomes, and how discretion may differentially influence organizational outcomes when it enables or constrains leaders. Our review indicates that while a significant number of studies have examined discretion, few have attempted to validate the prescriptions of the managerial discretion construct. Furthermore, studies to date have primarily focused on the industry task environment as a measure of discretion, with less attention focused on the manager's characteristics and the internal organization. We then assess construct validity and the measurement of managerial discretion, offering recommendations to future researchers for improving the operationalization of this construct. Finally, we consider how discretion forces may interact as either complements or substitutes and how such interactions may have both organizational- and individual-level consequences.

Keywords [managerial discretion](#), [executive discretion](#), [CEOs](#), [top management team](#), [latitude of action](#), [discretionary forces](#)

How and when do leaders matter? Management scholars have long attempted to identify when managers can alter firm decisions, actions, and performance. While management theorists have long implicitly understood the role of constraints in the ability of firms and managers to undertake decisions (see, e.g., [Hannan & Freeman, 1977](#); [Lieberson & O'Connor, 1972](#); [Salancik & Pfeffer, 1977](#)), it was not until [Hambrick and Finkelstein's \(1987\)](#) conceptualization of "managerial discretion" that scholars formally developed a model for what factors may provide executives with the ability to influence firm outcomes. Managerial discretion can be defined as the latitude of managerial action available to a decision maker (e.g., a top manager) in a given situation (Hambrick & Finkelstein). Higher discretion enables leaders with a wider range of options ([J. T. Campbell, Campbell, Sirmon, Bierman, & Tuggle, 2012](#)) and a greater latitude of action ([Hambrick & Abrahamson, 1995](#)). Because top managers are appointed to executive positions with the goals of sustaining and improving organizational performance and effectiveness ([Barker, Patterson, & Mueller, 2001](#)), it is critical to understand what constrains leaders and, alternatively, to understand what enables them to influence organizational outcomes.

In this review, we seek to examine how research has advanced the concept of managerial discretion and explore both its antecedents and consequences. [Hambrick and Finkelstein \(1987\)](#) argued that managerial discretion comes from sources at three levels: the environment, the organization, and the individual. A majority of managerial discretion research focuses on the role of the task environment, or industry characteristics, in creating managerial discretion. Indeed, only one literature review to date has examined managerial discretion ([Boyd & Gove, 2006](#)). That review focuses solely on the measurement of discretion based upon [Dess and Beard's \(1984\)](#) depiction of the task environment. We seek to more broadly examine managerial discretion research to advance understanding of discretion's antecedents. Additionally, our review illustrates that research on the direct consequences of managerial discretion primarily focuses on executive compensation and firm performance. Since much of the research looking at the consequences of managerial discretion also focuses on the task environment, we feel there is tremendous opportunity to better understand the consequences from discretionary forces within an organization and from an executive's psychological attributes.

Coming more than 25 years after [Hambrick and Finkelstein's \(1987\)](#) introduction of managerial discretion, we illustrate how the concept has progressed, been measured in studies, and where future research should address gaps in the field's knowledge. We provide several contributions to the managerial discretion literature. First, we illustrate where research has identified value in the managerial discretion construct, while also illustrating where the initial construct remains untested. Second, we highlight opportunities for future research to extend the concept that will allow research on managerial discretion to continue progressing and provide greater influence. In particular, little research has focused on microconcepts, such as executive personality or cognition. Consideration of such topics may explain why some top executives perceive and act on opportunities or threats to the firm while others do not.

In the remainder of this review, we provide background on managerial discretion and its theoretical underpinnings. Next, we summarize our review methodology. While many of managerial discretion's concepts are applicable to divisional general managers and, in some cases, functional and middle managers, we focus on CEOs and top management team (TMT) members since almost all discretion research has been focused on top executives. We then review how managerial discretion has been used as an independent variable, as a dependent variable, and as a moderator and mediator to examine relationships between top managers and firm-level outcomes. Finally, we conclude with an analysis of gaps in managerial discretion research and recommend future research directions.

Historical Background of the Managerial Discretion Construct

As noted earlier, managerial discretion is the latitude of action, or potential strategic options, afforded to executives. While [Hambrick and Finkelstein \(1987\)](#) developed the seminal managerial discretion model employed in management research, the concept existed in several forms for many years prior to their article. Sociology, for instance, offers a comparable view of managerial discretion. [Lieberson and O'Connor \(1972\)](#) argued that the leadership effect in organizations accounts for variance in organizational performance, but that organizational progress and success over time are shaped by the leader's traits and constrained by the organization's characteristics and environment. In their study, Lieberson and O'Connor empirically examined positions in prior research arguing that in complex organizations there are a multitude of forces that constrain or magnify a leader's effect ([Guest, 1962](#); [Thompson, 1967](#)). They found that managers act in a substantially differing role in affecting organizational performance across industries and organizations, with the quality of management having less effect on established companies and a greater effect in new or recently merged organizations.

Managerial discretion acts as a bridge between two previously conflicting organizational theories: population ecology and strategic choice ([Hambrick & Finkelstein, 1987](#)). Population ecology theorists argue that organizations are inertial and limited by internal and external pressures ([Hannan & Freeman, 1977](#)). Internal pressures include nontransferable personnel and investments in plant and equipment, while external pressures include legal and fiscal entry and exit barriers, constraints on available information, and a need for legitimacy within the organization's domain. Conversely, strategic choice theorists argue that management's chosen strategies shape organizational outcomes ([Andrews, 1971](#)). Managers determine long-term goals and objectives and implement courses of action (such as diversifying or discontinuing current activities) to pursue these goals and objectives ([Chandler, 1962](#)). Decision makers (i.e., the dominant coalition) have a "strategic choice" to implement structural change, determine the environmental domain in which to compete, and alter performance standards ([Child, 1972](#)).

[Hambrick and Finkelstein's \(1987\)](#) managerial discretion model reconciles these conflicting views by recognizing that many forces act on a continuum. A manager's latitude of action can be constrained or enabled depending on the degree to which each force exists. For example, CEOs with an internal locus of control pursue more innovation and undertake greater risks, while CEOs with an external locus of control are more likely to follow competitors ([Miller, Kets De Vries, & Toulouse, 1982](#)). Furthermore, strategic choice can be limited by inertial forces and the need for incremental action and internal consistency ([Mintzberg, 1978](#)).

In their development of the managerial discretion construct, [Hambrick and Finkelstein \(1987\)](#) focus on three forces that determine an executive's latitude of action: the task environment, internal organizational factors, and managerial characteristics. While all managers are decision makers and are influenced by such factors, a substantial majority of empirical work to support and advance the concept of managerial discretion has been focused on whether and how factors affect the CEO's latitude of action. Before analyzing this research, we briefly discuss the three managerial discretion forces and the factors within each force.

Task Environment

The task environment is characterized by factors in the organization's domain (e.g., industry) and how the organization functions within its domain. Since the task environment alters managerial discretion, managers have substantially differing roles in affecting organizational performance across industries. The task environment is expected to positively influence managerial discretion when product or service characteristics vary greatly across industry competitors, the market for the industry's products or services is growing, and demand for the industry's products or services is volatile. Conversely, the task environment may constrain discretion when an industry is highly concentrated, highly regulated, and powerful external forces, such as

competitors, suppliers, and buyers, exist ([Hambrick & Finkelstein, 1987](#); [Pfeffer & Salancik, 1978](#); [Porter, 1980](#); [Thompson, 1967](#)). Relatedly, [Dess and Beard \(1984\)](#) introduced munificence, dynamism, and complexity as dimensions of the task environment relevant to industry firms. Many of the managerial discretion task environment factors closely resemble these three dimensions ([Boyd & Gove, 2006](#)), and it is reasonable to conclude that industry munificence, dynamism, and complexity all potentially increase a manager's latitude of action.

Internal Organization

Internal organizational factors influenced by inertial forces, powerful internal stakeholders, and resource availability are the second force shaping discretion. The internal organization defines the degree to which the organization is amenable to a variety of possible actions and subsequently empowers the CEO to execute those actions ([Hambrick & Finkelstein, 1987](#)). Inertial forces include an organization's size, age, and culture. Indeed, [Hannan and Freeman \(1984\)](#) argue that highly inertial organizations change their core features at a much slower rate than environmental conditions in their domain change ([Kelly & Amburgey, 1991](#)). Thus, an executive seeking to initiate change can be severely constrained by the ingrained culture of a larger or older organization as a result of standardized routines or more formally defined roles and control systems ([Hannan & Freeman; Quinn & Cameron, 1983](#)).

Relatedly, powerful internal stakeholders that are linked to the status quo may resist or even work against change. Individuals and groups may derive power from their ability to cope with contingencies related to the status quo and, thus, prioritize retaining the firm's existing structure ([Pfeffer & Salancik, 1978](#); [Tushman & Romanelli, 1985](#)). Powerful stakeholders can perceive a potential loss of expert power and informational power in the organization's current strategy and domain ([French & Raven, 1959](#)) but also may perceive a loss of legitimate, coercive, or referent power as a result of the executive's impending actions ([Boeker, 1997](#); [Nutt, 1989](#)).⁴

Capital intensity and resource availability can also constrain or enable a manager's latitude of action. Organizations that have made tremendous capital outlays are likely to be highly committed to their current course of actions ([Hannan & Freeman, 1977](#)) and potentially tied closely to their current products and processes ([Hambrick & Macmillan, 1985](#)). Conversely, executives in organizations with abundant transferable resources (e.g., cash reserves, unused debt capacity, and available managerial and technical talent) may pursue a broader array of options ([Cyert & March, 1963](#); [Hambrick & Finkelstein, 1987](#)). Firms such as Google, Microsoft, and Intel currently have an abundance of available resources and are thus able to explore a wider range of strategic options. However, despite these firms having abundant available resources, executives in these firms likely confront bureaucracies and costs that constrain their discretion, illustrating the complex interaction of organizational discretionary forces.

Managerial Characteristics and Psychological Microfoundations

A top manager's psychological characteristics and their relationship with the firm can also limit or enhance the degree to which the executive can envision and create multiple courses of action across various contexts ([Hambrick & Finkelstein, 1987](#)). In advancing strategic choice theory, [Child \(1997\)](#) argued that executives in the same environmental situation will set different levels of discretion for themselves on the basis of their interpersonal linkage to the environment. A top manager's tolerance for ambiguity, locus of control, and ability to deal with cognitive complexity compose the psychology-based personal characteristics in this force. Attributes of the top manager's relationship with the firm, including his or her power base and commitment to the status quo, are also included in defining personal characteristics affecting discretion.

The psychological microfoundations of managerial discretion are unique among the three factors influencing latitude of action because they are not determined by external forces. As an example, let us consider locus of control where the “external” person believes that events and outcomes are beyond their control and attributes subsequent performance to luck or destiny ([Rotter, 1966](#)). In contrast, an “internal” person believes that events and outcomes are primarily under his or her own control ([Hambrick & Finkelstein, 1987](#)). While we might expect that a CEO would always have an internal locus of control, multiple studies have found that this is not the case. [Miller et al. \(1982\)](#) were among the first to link a CEO’s behavior to performance, finding that more internal CEOs tended to pursue more innovation, take greater risks, and follow strategies different from industry competitors. More recently, [Carpenter and Golden \(1997\)](#) found that top managers with an internal locus of control had more discretion and that top managers who exhibited greater discretion were able to increase their perceived power within the organization. Similar connections can be made between other psychological constructs and managerial characteristics that influence managerial discretion (such as domain-specific self-efficacy and confidence). In short, executives’ characteristics will influence the degree to which they see the need for action and take such action.

Having reviewed the foundational theories and concepts from [Hambrick and Finkelstein’s \(1987\)](#) managerial discretion model, we now provide a comprehensive review of empirical studies examining one or more forces in the model.

Review of Managerial Discretion Research

Method

The objective of our review was to examine articles that operationalized managerial discretion in top journals² or other highly cited articles. We sought articles that were empirical in nature and specific to CEO or TMT discretion. This review was limited to empirical studies to examine research designed to test the managerial discretion construct.

Using Google Scholar, we searched specifically for the term “managerial discretion” or variants of the term, such as “industry discretion,” in each top journal. We searched for the 100 most relevant articles from each top journal that applied aspects of the [Hambrick and Finkelstein \(1987\)](#) model or developed and examined additional factors affecting discretion, such as isomorphic pressure ([Hambrick, Finkelstein, Cho, & Jackson, 2004](#)) and national culture ([Crossland & Chen, 2013](#)).³ This process yielded over 500 articles. To find highly cited articles not in the top journals, we used Google Scholar to search specifically for the 100 most cited articles citing Hambrick and Finkelstein. This process yielded an additional 21 articles.

All of the articles were then reviewed to determine whether they should be included in our literature review tables. First, we found that the managerial discretion term has been used in many articles as a convenient theoretical hook. Often managerial discretion is used as a passing term to justify why it is important to examine top managers or firm actions without directly examining the sources, consequences, or moderating and mediating effects of managerial discretion. Articles not really focused on managerial discretion were filtered out because they did not operationalize the managerial discretion construct. Second, since our objective was to include articles that were empirical in nature and specific to CEO or TMT discretion, we filtered out all articles that did not operationalize managerial discretion. Third, each remaining article was then reviewed in detail to determine whether the article substantially operationalized managerial discretion specific to the CEO or TMT, with substantial operationalization defined as empirical studies focused solely on one or more aspects of the managerial discretion construct, studies that operationalized two or more hypotheses developed from or prior to [Hambrick and Finkelstein \(1987\)](#), or studies that developed and examined additional factors affecting discretion.⁴ This process yielded the 45 articles that are included in our literature review.

Our review and synthesis of the empirical research on managerial discretion suggested that each of the 45 studies identified that operationalize managerial discretion could be classified into one or more of three distinct groups representing different approaches to modeling managerial discretion. Four articles modeled antecedents of managerial discretion, 26 used measures of managerial discretion as independent variables to show the consequences of managerial discretion, and 19 examined managerial discretion as a moderator or mediator variable between other executive-controlled antecedents and firm-level outcomes.

Studies Examining the Antecedents of Managerial Discretion

Determining whether the expected aspects of the three forces truly yield discretion is vital to validating the managerial discretion construct. [Table 1](#) details the four studies that model managerial discretion as a dependent variable. Two studies used survey measurements of perceived managerial discretion as an outcome measure. In a food industry simulation, [Carpenter and Golden \(1997\)](#) surveyed master of business administration students with 15 items on perceived discretion, finding an external locus of control to be negatively related to perceived discretion, while [Key \(2002\)](#) surveyed managers in manufacturing and service industry firms, finding that an external locus of control was associated with lower perceived discretion only in low discretion situations. [Hambrick and Abrahamson \(1995\)](#) measured discretion using a panel of academics and analysts rating the level of managerial discretion in 17 industries. These discretion ratings were compared with objective measures of the task environment leading to the finding that market growth, R&D intensity, and advertising intensity were positively related and capital intensity was negatively related to discretion at the industry level. Additionally, the authors did not find a relationship between two task environment factors (demand instability and regulation) and discretion.

Table 1 Articles Examining Antecedents of Managerial Discretion

Managerial Discretion Force Used in Study	Author(s)	Methods or Measures Used to Represent Discretion	Independent Variables	Key Findings
Managerial Characteristics	Carpenter & Golden (1997)	Food industry simulation executed with MBA students responding to 15 survey items on perceived managerial discretion	Locus of control, manager's perception of discretion	A more external locus of control was associated with managerial discretion perceptions in low discretion situations. Individuals' perceptions of discretion tended to affect the power others attributed to them only in situations where the managers were purported to have little discretion.
Task Environment and Internal Organization	Hambrick & Abrahamson (1995)	Panel of academics and analysts rated level of discretion in 17 industries	Product differentiability, growth, industry structure, demand instability, regulation, power of outside forces, capital intensity	Three of six industry factors (R&D intensity, advertising intensity, and market growth) were positively related to discretion. Capital intensity was negatively related to discretion. Two factors (demand instability, regulation) were not related to discretion.
	Hambrick, Finkelstein, Cho &	Standard deviation over time of capital,	Six macrosocial factors characterizing	Isomorphism (the need to be like other firms in the industry) decreased over 40 years by finding significant standard deviation increases for capital

	Jackson (2004)	advertising, and R & D intensity for the industry by year	isomorphic pressure by year	intensity, advertising intensity, and R&D intensity. Similar findings were noted for 18 additional industries tested
Internal Organization and Managerial Characteristics	Key (2002)	Survey of managers focusing on perceived discretion regarding ethical intentions of other managers in the firm	Individual and organizational demographic variables, loss of control, firm having an ethical organizational culture	Manager's external locus of control was negatively related to perceived discretion. Presence of an ethical culture was positively related to perceived discretion. Individual and organizational demographic variables did not predict perceived discretion. Interaction of all independent variables accounted for only 0.1% of additional variance of perceived managerial discretion.

Note: MBA = master of business administration.

[Hambrick et al. \(2004\)](#) considered isomorphic pressure as an additional external factor, finding that decreased isomorphism in the steel industry increased discretion. They replicated these findings for the 20 largest firms from 18 additional industries.

[Figure 1](#) summarizes findings of research on managerial discretion's antecedents. Given the small number of studies, it is not surprising that many of the factors in task environment and internal organization have not been studied or, in the cases of demand instability, regulation, and firm size, no support was found from a single study. Additionally, many psychological factors (including ambiguity tolerance, cognitive complexity, and aspiration level) and the manager's power base and political acumen have yet to be empirically examined. Furthermore, it is apparent that researchers have struggled to measure discretion. Two articles used survey methods to measure perceived managerial discretion, one article ([Hambrick & Abrahamson, 1995](#)) used a panel of academics and analysts to measure discretion at the industry level, and one article ([Hambrick et al., 2004](#)) measured discretion using industry task environment factors to build a composite measure of industry-level managerial discretion. In short, limited research has focused on examining the antecedents and measurement of the managerial discretion construct.

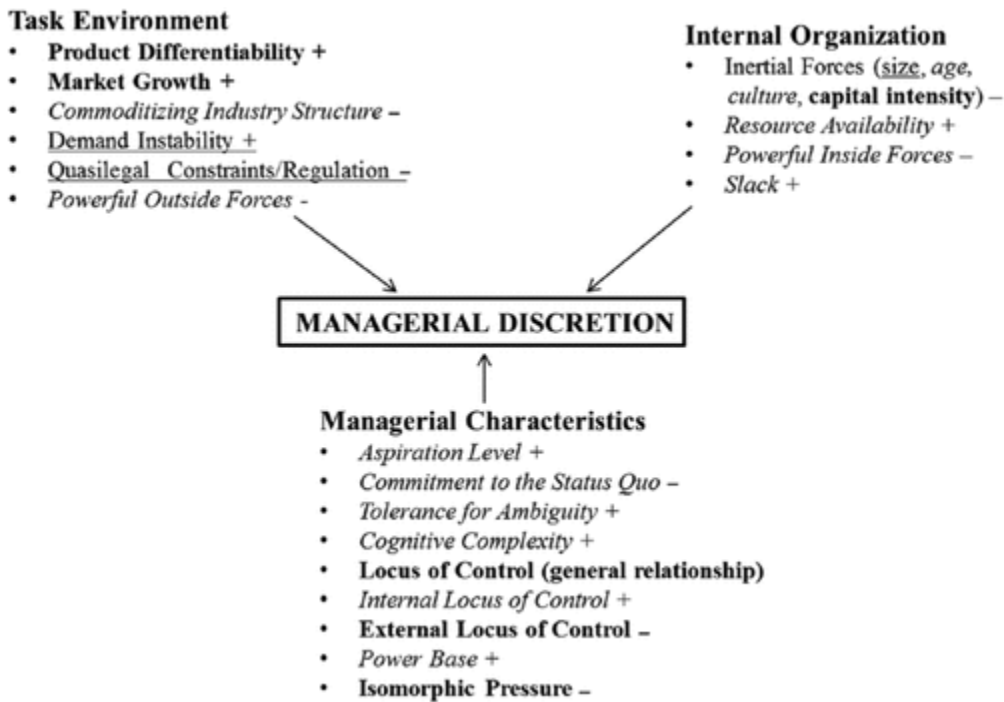


Figure 1 Summary of Results of the Antecedents of Managerial Discretion

Note: Factors in bold have been found to significantly affect managerial discretion; underlined factors have been empirically tested but no significant support has been found; italicized factors have not been empirically tested with managerial discretion as a dependent variable. Plus and minus signs indicate factors increasing and decreasing managerial discretion, respectively. Adapted from [Hambrick and Finkelstein \(1987\)](#) and [Finkelstein, Hambrick, and Cannella \(2009\)](#).

Studies Examining Consequences of Managerial Discretion

If leaders do indeed matter, then the discretion held by CEO and TMT members should affect performance and organizational effectiveness. [Table 2](#) provides a summary of articles examining the consequences of managerial discretion, while [Figure 2](#) illustrates how studies have examined managerial discretion's influence on various outcomes. We identified 25 studies that used managerial discretion as an independent variable and that utilized measures from the task environment, internal organization, or managerial characteristics to assess the effects of discretion. Of the 25 studies identified, 3 studies examined task environment and internal organization within the same study, while 1 study examined both task environment and managerial characteristics. Finally, 4 studies addressed an additional force and its effect on firm-level outcomes: the institutional environment, emphasizing how nationality-based factors enable or constrain managers.

Table 2 Articles Examining the Consequences of Managerial Discretion

Managerial Discretion Force Used in Study	Author(s)	Method for Measuring Managerial Discretion	Dependent Variables	Key Findings
Task Environment	Abrahamson & Hambrick (1997)	Panel of academics and analysts rated 14 industries	Attentional homogeneity (from content analysis)	There are significant negative correlations between industry discretion and lexical commonality and lexical density measures of attention homogeneity. Industries with less

				discretion have more attentional homogeneity among different firms' top managers.
	Datta & Rajagopalan (1998)	Industry capital intensity and growth, product differentiation	Organizational tenure, executive age, education level, throughput functional background, firm performance	Advertising intensity was negatively related with organizational tenure and throughput background and positively related to education level. Industry growth rate was negatively related with organizational tenure and age. Industry capital intensity was shown to have a weak relationship with throughput background. Firms with greater postsuccession performance improvements appeared to match CEO successor characteristics more closely to industry conditions.
	Finkelstein & Boyd (1998)	Growth, R&D, advertising and capital intensity, demand instability, concentration, regulation	CEO compensation	Managerial discretion is positively related to CEO compensation. This relationship was shown to be much stronger for high performers versus low performers.
	Finkelstein (2009)	Growth, R&D, advertising and capital intensity, demand instability, concentration, regulation	CEO compensation, performancecontingent compensation	Discretion was modeled as a construct using the independent variables as indicators. For both compensation dependent variables, discretion was significantly related to compensation. Concentration and demand instability were the only two factors not significantly related to discretion.
	Graffin, Carpenter, & Boivie (2011)	Growth, R&D, advertising and capital intensity, demand instability	Likelihood of a "noisy" CEO succession	Firm-related managerial discretion was not significantly related to the likelihood of a noisy CEO succession event.
	Hambrick & Quigley (2014)	Discretion ratings for each industry using Hambrick and Abrahamson (1995)	CEO effect on variance in ROA on the basis of new method	Stronger CEO effect was shown overall and for low, medium, and high industry discretion subsamples using the CEO in context method. CEO in context method points to a much greater aggregate CEO effect. Effects are strongest for CEOs in high discretion industries and stronger in medium discretion industries than in low discretion industries.
	Keegan & Kabanoff (2008)	Attentional homogeneity (using lexical commonality and density) used as proxy for industry-level discretion	Debt usage, significant account adjustments, disciplining effect of debt	Industry-level discretion was negatively associated with industry debt usage. Firms in high discretion industries perform significant account adjustments more than firms in low discretion industries. When industry-level discretion is high, debt's disciplining effects within an industry decrease.
	Peteraf & Reed (2007)	Data on airline cost function	Cost function of various airlinespecific factors	Managerial behavior changed when regulations were lifted; managers

		separated into regulated and deregulated periods		choose more efficient strategies without regulation. Regulation restricted managerial choice of network structure in the presence of economies of network density and forced executives to choose strategies that had wasteful levels of quality in the form of costly meals and amenities.
	Sahaym, Treviño, & Steensma (2012)	Composite industry measure of task environment variables: growth, product differentiation, capital intensity, structure	Industry exports measured as export intensity	Higher managerial discretion leads to greater industry exports. When innovations or uncertainty are high, the effect of managerial discretion on industry exports is stronger. The relationship between managerial discretion and exports are weakest for industries where levels of innovation and uncertainty are low.
Internal Organization	Boyd & Salamin (2001)	Strategic orientation from interviews and archival sources	Compensation plan	Strategic orientation affects the pay of all employees, not just top managers. Base pay is higher with change-oriented strategies. Bonus pay and bonus pay-to-base pay ratio are also higher with changed-oriented strategies but only at upper levels of hierarchy.
	Kim (2013)	CEO duality; percent of inside directors	Entry by an independent power producer into the renewable generation market	Weak support for CEO duality increasing likelihood of market entry. CEO duality (greater discretion) with a higher presence of independent power producers in the market significantly increases the likelihood of market entry. Percent of inside directors (alone or with a higher presence of independent power producers) did not significantly affect the likelihood of market entry.
	Quigley & Hambrick (2012)	Each firm-year can be low discretion (predecessor CEO as board chair) or higher discretion (departure of CEO as board chair)	Strategic change; firm performance	Predecessor retention suppresses strategic change, which leads to diminished performance changes. When the predecessor CEO leaves as board chair, strategic change increases, resulting in greater performance changes. Predecessor retention as chair was significantly negatively related to resource reallocation, divestitures, and TMT departures. The 1st year that the successor CEO is free of the predecessor is positively related to resource reallocation, divestitures, and TMT turnover. Performance tends to be in line with presuccession performance when the predecessor is board chair, but there are large changes in performance once the predecessor departs.
	Roth & O'Donnell (1996)	Lateral centralization: directly stated to	Subsidiary senior management pay mix, competitive positioning	Subsidiaries with increasing degrees of lateral decentralization (greater discretion) have higher levels of

		increase managerial discretion of subsidiary management	of executives' pay, salary adjustment criteria	incentive-based compensation or a greater mix of senior management pay. Market positioning of subsidiary's executives' salaries is positively related to lateral decentralization.
	Singh & Harianto (1989)	Nonmanagement-owned stock constraining management's ability to influence a board	Likelihood of adopting a golden parachute	Higher concentration of stock ownership in nonmanagement hands (decreased discretion) reduces the likelihood that a board adopts a golden parachute.
	Werner & Tosi (1995)	Firm ownership structure; management controlled (highest discretion structure), designated for firms not having greater than 5% ownership by an individual or organization	Pay-level policy, pay differentiation	Base pay and bonus of managers in owner-controlled and ownermanaged firms (lower discretion) was significantly lower than in management-controlled firms. Change in performance was related to the change in base salary and bonus for ownercontrolled firms but not for management-controlled firms. Change in size was not significantly related to change in base and bonus for any organizational structure. Managementcontrolled firms made greater use of long-term incentives. Owner-managed firms have significantly greater percentages of bonus-eligible employees than management-controlled firms. Management-controlled firms had significantly higher bonus pay-to-base pay ratio and bonus pay than ownercontrolled or owner-managed firms.
Managerial Characteristics	McClelland, Liang, & Barker (2010)	Dummy variables for low and high discretion; groupings selected based on previous research and validated using R&D, advertising and capital intensity, growth	CEO CSQ; future firm performance	CEO CSQ associated with industry-level managerial discretion but only in low discretion industries. CEO CSQ associated with lower future accounting performance in high discretion industries. No support found for lower industry discretion moderating the relationship between CEO CSQ and accounting performance. For market performance (Tobin's Q), CEO CSQ in low discretion industries has a positive moderating effect, while CEO CSQ in high discretion industries has a negative moderating effect.
	Miller, Kets De Vries, & Toulouse (1982)	Via interview to obtain a locus of control score for CEO (24 of 33 firms) and TMT (all 33 firms)	Aggregate innovation, risk taking, proactiveness, and planning horizon all via interview	Innovation, risk taking, proactiveness, and planning horizon in all firms were significantly correlated to an internal locus of control (greater discretion). Innovation and internal locus of control were not significantly correlated for lower tenure executives. For executives in small firms, locus of control was significantly correlated with innovation,

				risk taking, proactiveness, and having a planning horizon. However, executives' locus of control was significantly correlated only with proactiveness in large firms.
	Roth (1992)	Decision-making factors; risk taking; openness	ROA and sales growth	Risk-taking behavior by TMT members significantly related to ROA more in a multidomestic strategy than a global strategy. No support for openness in decision making having a greater impact on firm performance between business units following a multidomestic strategy versus a global strategy.
Task Environment and Managerial Characteristics	Adams, Almeida, & Ferreira (2005)	CEO power to influence decisions via three dummy measures; industry discretion via Hambrick and Abrahamson (1995)	Variability of stock returns, Tobin's Q, and ROA for 1992 to 1999	Retention of the CEO title by one of the founders is the most consistent variable affecting performance variability, but there is some evidence that the other two measures of CEO power (CEO's concentration of titles and CEO as the only board insider) are positively related to performance variability. All three measures of CEO power have a stronger positive effect on performance variability in high discretion industries.
Task Environment and Internal Organization	Papadakis & Bourantas (1998)	Environmental dynamism via CEO/TMT survey responses on frequency of environmental changes; firm size	Firms' innovation position in industry	Environmental dynamism significantly related to major product innovation. Both environmental dynamism and firm size related to incremental product innovation.
	Rajagopalan & Finkelstein (1992)	Strategic orientation via CEO survey: innovation, efficiency, domain expansion; uncertainty deemed lower prior to 1978 and higher after 1983	CEO compensation, CEO salary, CEO annual bonus, and average executive team cash compensation	Prospector firms, presumed to have the highest discretion, had higher executive pay. Defenders have higher overall executive pay than reactors. Prospectors have higher outcome-based compensation than other typologies and have a greater proportion of compensation based on outcomes. During periods of uncertainty, executives have higher overall compensation, more outcome-based compensation, and a higher proportion of cash compensation based on outcomes.
	Wasserman, Anand, & Nohria (2010)	Opportunity scarcity; industry growth; resource availability	CEO effect based on Tobin's Q	In industries more highly concentrated or constrained by external relationships, companies have fewer opportunities to act and, thus, the CEO impact is larger. When industry growth is low, opportunities are scarce and the CEO effect is high. CEOs have less impact on performance when opportunities are plentiful and when debt levels and servicing requirements are high. When

				slack is high, CEOs can proactively take advantage of opportunities that may change company performance.
Institutional Environment	Crossland & Hambrick (2007)	Three countries classified using Hofstede's typology emphasizing individualism versus collectivism and uncertainty avoidance	Firm performance via ROA, ROS, sales growth, market to book	Performance variance explained by the CEO was consistently greater in the U.S. sample than in the German or Japanese samples. Countries with lower constraints, presumed to impart greater discretion upon executives, increase the CEO's effect on firm performance outcomes.
	Crossland & Hambrick (2011)	Country-level rating of managerial discretion via surveys from expert panel	Firm performance via ROA, ROIC, ROS, MTB	National-level of discretion was a significant predictor of national-level CEO effects (i.e., the amount of variance in firm performance attributable to CEO-level factors), suggesting that nations with a greater level of discretion have firms with greater CEO effects.
	Gedajlovic & Shapiro (1998)	Ownership concentration; nationality-based constraints	Firm profitability	For U.S. and German firms, typified by external constraints, ownership concentration was related to profitability. In France (typified by internal constraints), United Kingdom (typified by external constraints), and Canada (typified by both internal and external constraints), no relationship was found between ownership concentration and profitability
	Makhija & Stewart (2002)	Survey results from four questions on perceptions of government control; discretion deemed low for United States and high for Czech Republic	Organizational accountability; decision-making orientation	Managers in more free market-oriented countries perceive more outcome accountability, are more comfortable with uncertainty, and have a stronger sense of power over decision outcomes than managers in planned institutional environments. A decision-making orientation that reflects a greater comfort with uncertainty and a sense of power over decision outcomes leads to greater risk taking, while greater perceived organizational accountability leads to less risk taking.

Note: ROA = return on assets; TMT = top management team; CSQ = commitment to the status quo; ROS = return on sales; ROIC = return on invested capital; MTB = manage to budget.

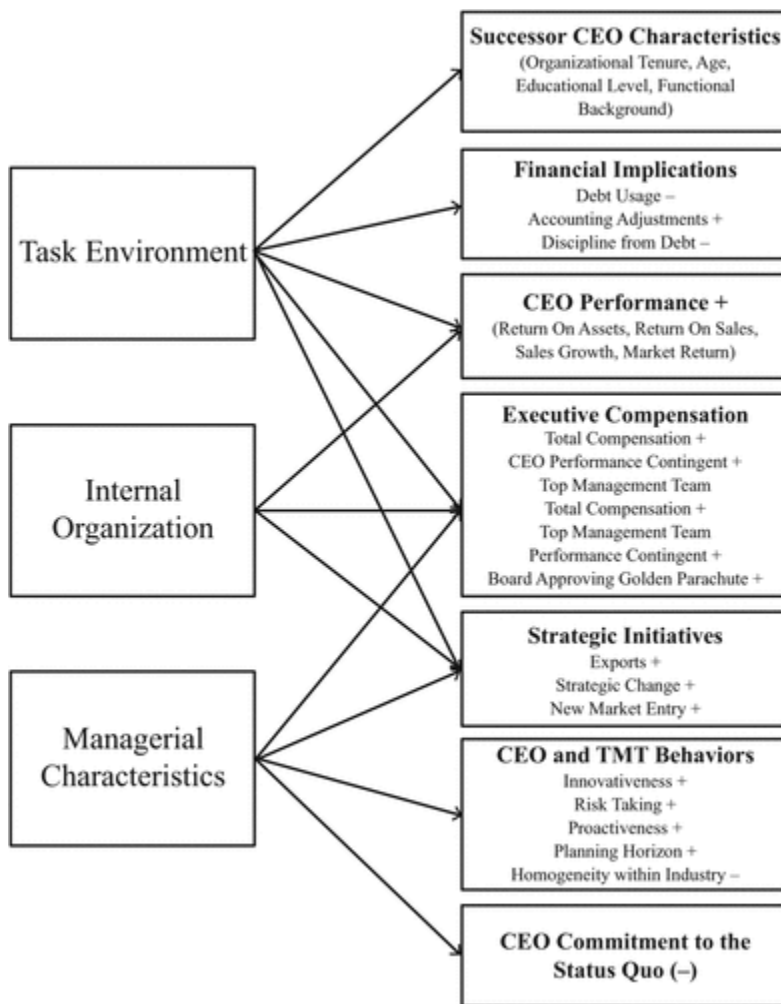


Figure 2 Summary of the Consequences of Managerial Discretion

Note: Plus and minus signs indicate outcomes increased and decreased by managerial discretion, respectively.

The managerial discretion model argues that when a CEO's ability to influence decisions is high, his or her effect on firm-level outcomes is greater. Several studies find support for this notion. For instance, [Hambrick and Quigley \(2014\)](#) devise a new method to predict CEO effects on firm performance and divide their sample into high, medium, and low discretion industries. The authors find that in industries with greater discretion, CEOs have a greater effect on performance, with their "CEO in context" method pointing to a much greater aggregate CEO effect than shown previously. These results are consistent with prior studies examining the relationship between discretion from CEO power and performance variability, finding that discretion from CEO power is positively related to performance variability (e.g., [Adams, Almeida, & Ferreira, 2005](#)). Using nation-level measures of discretion, [Crossland and Hambrick \(2007\)](#) find that CEOs in countries with fewer institutional constraints have a greater effect on firm performance. In a follow-up study, the authors find that national-level discretion is a predictor of national-level CEO effects, whereby nations with greater discretion have greater CEO effects ([Crossland & Hambrick, 2011](#)). Alternatively, [Wasserman, Anand, and Nohria \(2010\)](#) find that a scarcity of opportunities to act, due to high industry concentration or low industry growth, increases a CEO's effect on Tobin's Q. In short, studies provide greater support for the notion that discretion increases CEO effects on firm performance; however, this may be based on how the level of discretion is measured. Despite these findings, only one study has explored how managerial characteristics influence CEO effects on firm performance.

The second most commonly studied outcome of managerial discretion is compensation. Using a variety of task environment factors as proxies for discretion, studies show that higher discretion yields greater CEO compensation ([Finkelstein, 2009](#); [Rajagopalan & Finkelstein, 1992](#)), and such effects are stronger for high performing CEOs ([Finkelstein & Boyd, 1998](#)). Examining internal factors, [Roth and O'Donnell \(1996\)](#) find that decentralized foreign subsidiaries have a higher degree of incentive pay, while [Werner and Tosi \(1995\)](#) find that owner-controlled and owner-managed firms have lower base and bonus pay for executives. Finally, a firm's strategic orientation has been shown to affect the pay of all employees, as firms with change-oriented strategies have higher base and bonus pay ([Boyd & Salamin, 2001](#)). These findings are significant, as greater discretion indicates a need for a higher quality manager to choose proper strategic choices, increasing the level of compensation that executives receive.

A third important set of outcomes examined relates to firm strategic behavior. In an early study, [Miller and colleagues \(1982\)](#) find that innovation, risk taking, proactiveness, and planning horizon were all correlated to an internal locus of control, a managerial characteristic that increases discretion. [Kim \(2013\)](#) finds that CEO duality, a measure of CEO power that increases discretion, increases the likelihood of market entry. [McClelland, Liang, and Barker \(2010\)](#) find that discretion significantly influences a CEO's commitment to the status quo. Industry factors (low discretion industries), internal factors (smaller organizations), and managerial demographics (older executives) all lead to greater commitment to the status quo. Examining an institutional measure of discretion, [Makhija and Stewart \(2002\)](#) find that managers in free market-oriented countries engage in greater risk taking. Consistent with these studies, results from [Quigley and Hambrick \(2012\)](#) show that an internal factor relating to a powerful force, the retention of a prior CEO on the board, limits the amount of strategic change that happens under a new CEO. The retention of the predecessor as board chair results in less resource reallocation, fewer divestitures, and fewer TMT departures, suggesting that allowing a prior CEO to remain as board chair significantly decreases the discretion of a new CEO. In short, findings suggest that proxies for discretion are related to the level of organizational risk taking, innovation, and strategic change.

Our review of the literature on the consequences of discretion suggests that the four factors of discretion tested strongly relate to CEO effects on performance outcomes, the level and mix of CEO compensation, and firm strategic behavior. Despite these studies, only a small number of studies examine alternative consequences, such as level of debt usage ([Keegan & Kabanoff, 2008](#)), corporate governance ([Singh & Harianto, 1989](#)), industry attention patterns ([Abrahamson & Hambrick, 1997](#)), CEO characteristics ([Datta & Rajagopalan, 1998](#)), and efficiency of organizational strategies ([Peteraf & Reed, 2007](#)). Future research could focus on new, significant organizational decisions likely to be affected by the level of discretion.

We also found that over half of the 25 studies examining discretion's consequences used archival data to measure discretion. Nine of these studies used a combination of measures from the [Hambrick and Finkelstein \(1987\)](#) task environment force. With a small set of studies using other measurement methodologies, such as attentional homogeneity via content analysis ([Abrahamson & Hambrick, 1997](#)) or industry changes from a deregulating event ([Peteraf & Reed, 2007](#)), a reasonably robust set of measures exists for the task environment force. However, all but 2 studies examining the consequences of managerial discretion from organizational forces use archival data to measure discretion. This has limited our understanding of how organizational forces of discretion affect outcomes since only readily available factors (e.g., CEO duality) have been examined. Challenges associated with using nonarchival methods also seem to have limited the study of the consequences of an executive's psychological traits, as only 4 of the 25 studies have measured managerial discretion using executives' psychological traits. Future research using alternative methods (e.g., surveys, interviews, and content analysis) would greatly enhance our understanding of how organizational culture and powerful inside forces may constrain an executive and our understanding of the consequences of discretion.

Studies Examining Managerial Discretion as a Mediator or Moderator

While discretion is theorized to directly affect a number of outcomes, many studies have focused on discretion as an important moderator or mediator between strategy variables and firm outcomes. [Table 3](#) presents the 19 studies we have identified that utilize managerial discretion as either a moderator or mediator, while [Figure 3](#) pictorially identifies how studies have theorized that discretion may mediate or moderate important outcomes. Within these 19 studies, only 4 have utilized managerial discretion as a mediating variable, while the other 15 have used discretion as a moderator.

Table 3 Articles Using Managerial Discretion as a Mediator or Moderator

Managerial Discretion Force Used in Study	Author(s)	Managerial Discretion and Measure Usage	Independent Variables	Dependent Variables	Key Findings
Task Environment	Datta, Guthrie, & Wright (2005)	Moderator: industry capital intensity, growth, product differentiation, dynamism	HPWS	Labor productivity (log of firm sales to total employees)	Industry capital intensity, growth, and product differentiation all found to positively strengthen the relationship between HPWS and labor productivity. No significant effect was found for industry dynamism as a moderator between HPWS and labor productivity.
	Goll, Johnson, & Rasheed (2008)	Moderator: airline pre deregulation and postderegulation	TMT age, tenure, education level, functional diversity	Business strategy (differentiation, cost leader, breadth of strategic scope)	Environment exerts a moderating influence on the TMT demographics-strategy relationship in the deregulated industry but not the regulated industry. Younger and less tenured managers place marginally greater emphasis on differentiation during deregulation but also emphasize a low-cost strategy. Better educated executives place more emphasis on differentiation in the deregulated environment. TMTs with greater functional diversity emphasize low-cost strategies in deregulated environments.
	Haleblian & Finkelstein (1993)	Moderator: industry's average advertising and R&D intensity and annual sales growth; standard deviation of annual sales growth; degree of regulation	TMT size, CEO dominance	Firm performance	Team size and CEO dominance significantly related to firm performance when discretion in the task environment is high but not when discretion is low.
	Hambrick, Geletkanycz, & Fredricks	Moderator: three high discretion and three low discretion industries	Organizational performance, organization and	CSQ measured using executive surveys	Strong current performance was positively related to CSQ for leadership and strategy. Executives in high discretion situations, but not those in low discretion situations, interpret poor performance as a signal that an organization needs to change. Current performance and CSQ

	on (1993)		industry tenure		are more strongly related in high discretion industries than in low discretion industries.
	Liebersohn & O'Connor (1972)	Moderator: variance explained by administration after year and company effects are removed	Year effect, industry effect, company effect, administration effect	Sales, net earnings, profit margin	Administrative effect on sales varies only on the degree of industry concentration. Profit margins affected by management when: industries have low labor intensity or where worker pay is a smaller part of total employment costs, industry is growing, advertising is important, consumers form a sizable market, TMT is larger
	Magnan & St-Onge (1997)	Moderator: sum of five binary variables for distinct dimensions of discretion	Bank performance: ROA, stock market return	Total CEO compensation	Managerial discretion positively influences the strength of the relationship between bank performance and executive compensation. Each individual dimension of managerial discretion moderates the relationship between bank performance and executive compensation.
	Messersmith, Lee, Guthrie, & Li (2013)	Moderator: industry instability; industry munificence and complexity	TMT turnover	Firm performance	Industry sales growth positively moderated the relationship between TMT turnover and firm performance, contrary to predictions. No significant moderating effects from industry complexity or instability were found.
Internal Organization	J. T. Campbell, Campbell, Sirmon, Bierman, & Tuggle (2012)	Moderator: spline function used to classify firms between low and high discretion based on net PP&E/employees	CEO discretion	Shareholder value change on the day of the announcement of a new SEC proxy access rule	Abnormal shareholder returns from the announcement of a new SEC proxy access rule were positive and significant for low and high discretion but significantly larger for firms in high discretion industries.
	Preston, Chen, & Leidner (2008)	Mediator: CIO and other TMT member responses on CIO strategic decision-making authority	Organizational decision-making climate, support for IT; CIO effectiveness, structural power; CIO/TMT partnership	IT contribution via survey responses from TMT members	CIO strategic decision-making authority found to significantly mediate the relationship between organizational climate, organizational support for IT, CIO structural power, CIO strategic effectiveness, and CIO's partnership with other TMT members and IT's contribution to firm performance.
	Quigley & Hambrick (2012)	Mediator: each year can be low discretion (predecessor	Predecessor CEO retained, 1st free year	Strategic change; firm performance	Predecessor retention suppresses strategic change, leading to diminished performance changes. When the predecessor CEO leaves as board chair, strategic change increases, resulting in greater performance changes. Predecessor

		CEO as board chair) or higher discretion (departure of CEO as board chair)			retention as chair was significantly negatively related to resource reallocation, divestitures, and TMT departures. The 1st year that the successor CEO is “free” of the predecessor is positively related to resource reallocation, divestitures, and TMT turnover. Performance tends to be in line with presuccession performance when the predecessor is board chair, but large changes in performance occur once the predecessor departs.
	Rajagopalan (1997)	Moderator: survey of senior executives on strategic orientation	Annual bonus plan, long-term performance plan, stock option plan	Return on capital, stock price return	Strong support for incentive plans including cash and stock rewards associated with better firm performance for prospectors. Most annual bonus or long-term plans did not show association with better firm performance for defenders.
Managerial Characteristics	Buchholtz, Amason, & Rutherford (1999)	Mediator: survey response from CEOs on discretion for decisions regarding charitable contributions; validated discretion versus 14 other business discretion items	Firm resources via survey validated using financial performance from archival data	Corporate philanthropy measured via survey responses	Availability of firm resources significantly affects the amount of corporate philanthropy. When managerial discretion related to charitable contributions was added, the results supported full mediation of firm resources and corporate philanthropy by managerial discretion. When the TMT's values related to charitable contributions was added, the effect of managerial values was shown to be moderately significant while the effect of managerial discretion was no longer significant, supporting partial mediation of managerial discretion and corporate philanthropy by the values of the TMT.
	Dollinger, Golden, & Saxton (1997)	Moderator: MBA student survey responses on tolerance for ambiguity and locus of control	Firm reputation	Approval of alliance with competitor or supplier	Individuals with high tolerance ambiguity or with internal locus of control were more likely to suppress both the most positive and most negative reputation information in alliance decision.
	Geletkanycz & Hambrick (1997)	Moderator: intraindustry and extraindustry ties	Absolute differences of strategic indicators for each firm versus industry means	ROA, ROS	Weak support for moderating effects of hiring executives in the same industry and no support for trade association ties as a moderator between strategic indicators and firm performance. Hiring executives from outside the firm's industry and TMTs serving on other firms' boards found to moderate the relationship between strategy and firm performance. Directors outside the firm's industry had an unexpected negative moderating effect on firm performance. No significant moderating effect found from professional association ties.

Task Environment and Internal Organization	Finkelstein & Hambrick (1990)	Moderator: three sample industries (high, medium, low)	TMT member tenure, firm size, immediate slack, firm performance	Strategic persistence and conformity; performance conformity	The associations between team tenure and strategic conformity and persistence are stronger in the high discretion computer industry than in the medium and low discretion industries. The association between team tenure and performance conformity was significantly positive for the high discretion industry but significantly negative for the medium discretion industry.
Task Environment and Managerial Characteristics	Adams, Almeida, & Ferreira (2005)	Moderator: CEO power to influence decisions; industry discretion via Hambrick and Abrahamson (1995)	CEO power to influence decisions	Variability of stock returns, Tobin's Q, and ROA	CEO title retention by one of the founders is the most consistent variable affecting performance variability, but there is some evidence that CEO's concentration of titles and CEO as the only board insider are also positively related to performance variability. All three measures of CEO power have a stronger positive effect on performance variability in high discretion industries.
	McClelland, Liang, & Barker (2010)	Moderator: dummy variables for low and high discretion; groupings selected on the basis of previous research and validated using R&D, advertising and capital intensity, sales growth	Membership in a low or high discretion industry; CEO CSQ via content analysis of CEO letters	CEO CSQ; future firm performance	CEO CSQ associated with industry-level managerial discretion but only in low discretion industries. CEO CSQ is significantly associated with lower future accounting performance in high discretion industries. No support found for lower industry discretion moderating the relationship between CEO CSQ and accounting performance. For market performance (Tobin's Q), CEO CSQ in low discretion industries has a positive moderating effect, while CEO CSQ in high discretion industries has a negative moderating effect.
Institutional Environment	Crossland & Chen (2013)	Moderator: country-level rating of managerial discretion via surveys from expert panel of analysts	Firm performance	CEO dismissal/succession	For the six countries used in this study, the probability of dismissal due to poor performance varied for the six countries. Probability of dismissal due to poor performance was highest in the United States, followed (in order) by Canada, United Kingdom, France, Germany, and Japan. When the six countries are aggregated, the probability of dismissal when performance is poor is significantly higher when managerial discretion is high.
	Crossland & Hambrick (2011)	Moderator: country-level rating of managerial discretion via surveys from expert panel	Individualism; uncertainty tolerance; power distance; cultural looseness; ownership	Firm performance	Discretion fully mediated the relationship between uncertainty tolerance and CEO effectiveness. The effects of individualism, cultural looseness, ownership dispersion, and legal origin on CEO effectiveness were partially mediated by discretion. National level of discretion was a significant predictor of national-level CEO effects, suggesting that nations with a greater level of discretion have firms with greater CEO effects.

			p dispersion; legal origin; employee flexibility		
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Note: HPWS = high performance work system; TMT = top management team; CSQ = commitment to status quo; ROA = return on assets; PP&E = property, plant, and equipment; SEC = Securities and Exchange Commission; CIO = chief information officer; IT = information technology; MBA = master in business administration; ROS = return on sales.

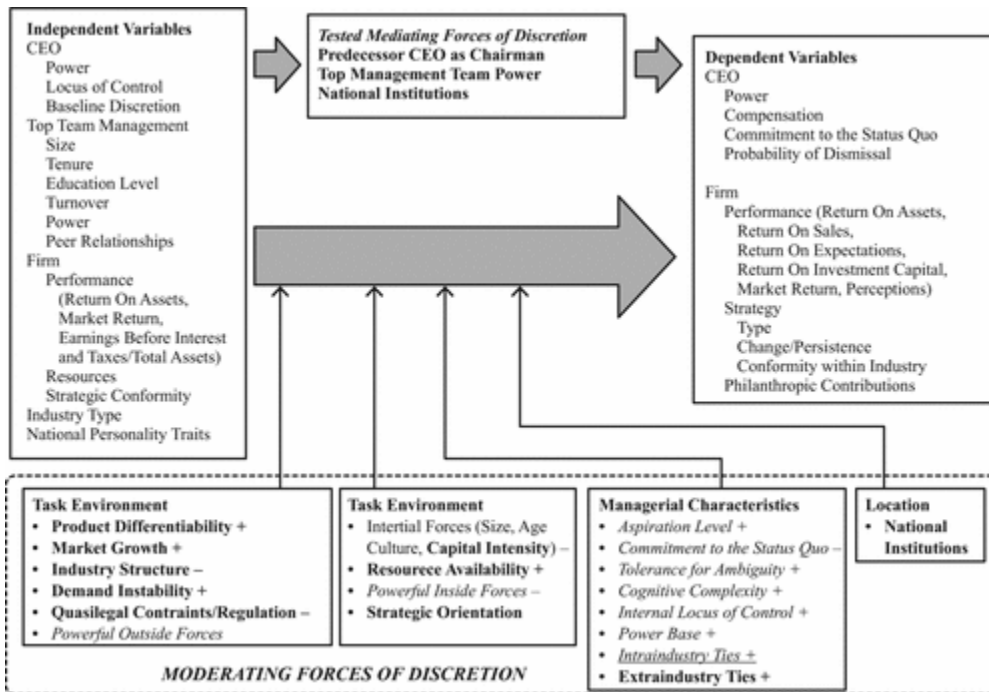


Figure 3 Summary of Managerial Discretion as a Mediator or Moderator

Note: Factors in bold have been found to significantly support moderating or mediating effects; underlined factors have been empirically tested but no significant support has been found; italicized factors have not been empirically tested as moderators. Independent and dependent variables shown are those used in empirical studies where significant moderating or mediating effects were supported. Plus and minus signs indicate factors acting as positive and negative moderators, respectively. Moderating factors adapted from [Hambrick and Finkelstein \(1987\)](#) and [Finkelstein, Hambrick, and Cannella \(2009\)](#).

Discretion as a moderator

Studies utilizing managerial discretion as a moderator have examined a number of important outcomes largely related to firm performance and strategic changes. With regards to strategy, [Finkelstein and Hambrick \(1990\)](#) find that TMT tenure is associated with strategic conformity and persistence; however, these relationships were stronger in a higher discretion industry than in a lower discretion industry, suggesting that high discretion industries enable TMTs to have a greater influence on strategy. Similar findings are echoed by [Hambrick, Geletkanycz, and Fredrickson \(1993\)](#), who find that strong performance leads to a management commitment to the status quo in high discretion industries. Relatedly, [Goll, Johnson, and Rasheed \(2008\)](#) found that the association of TMT demographics and the type of strategy firms pursued was contingent upon a firm

being in a high discretion industry. The authors note that in deregulated environments, younger and less tenured managers and TMTs with greater functional diversity emphasized a low-cost strategy during deregulation, while better educated executives emphasized pursuing a differentiation strategy in the deregulated industry.

Discretion can also influence the relationship between management characteristics (or strategy) and firm performance. For instance, [Adams et al. \(2005\)](#), using [Hambrick and Abrahamson's \(1995\)](#) industry measures, found that discretion from CEO power has a greater effect on firm performance variability in industries with greater discretion. Furthermore, a CEO's commitment to the status quo is associated with lower accounting firm performance only in high discretion industries ([McClelland et al., 2010](#)). Similar results hold for market performance in a high discretion industry; however, a CEO's commitment to the status quo combined with low discretion industries positively enhances market performance. [Haleblian and Finkelstein \(1993\)](#) find that CEO dominance and team size were related to firm performance only when discretion was high, while [Messersmith, Lee, Guthrie, and Li \(2013\)](#) found a significant relationship between TMT turnover and firm performance as moderated by industry growth rate.

Researchers also illustrate discretion's moderating effects on CEO dismissal ([Crossland & Chen, 2013](#)), CEO compensation ([Magnan & St. Onge, 1997](#)), and abnormal shareholder returns ([J. T. Campbell et al., 2012](#)). One interesting study by [Datta, Guthrie, and Wright \(2005\)](#) found that three task environment factors positively strengthened the relationship between high performance work systems and labor productivity, suggesting that high performance work systems more strongly influence productivity in high discretion industries. These studies suggest that discretion influences firm-level outcomes and strategic decision making. Future research should continue to use discretion as a contingency moderator to examine factors that enable or constrain strategic decision making and how such factors influence firm outcomes. Furthermore, the majority of research employing discretion as a moderator has examined it using task environment factors, rather than exploring managerial characteristics or internal organization factors.

Discretion as a mediator

A relative paucity of work has attempted to use discretion as a mediator. Despite this, the research that has employed measures of discretion as a mediator has identified fruitful findings. [Preston, Chen, and Leidner \(2008\)](#) examined chief information officer (CIO) decision-making authority as a measure of discretion, finding that CIO decision-making authority mediated the relationship between four measures of the organizational environment and information technology's ability to contribute to firm performance. [Buchholtz, Amason, and Rutherford \(1999\)](#) examine the effect of resources as a factor in corporate philanthropy. Managerial discretion was found to fully mediate the relationship between firm resources and corporate philanthropy, with the relationship between managerial discretion and corporate philanthropy partially mediated by the values of the TMT. Finally, [Crossland and Hambrick \(2011\)](#) find that managerial discretion, measured via country-level ratings by an expert panel of academics and analysts, mediates the effects of uncertainty tolerance, individualism, cultural looseness, ownership dispersion, and legal origin on CEO effectiveness.

In sum, research to date has begun to explore questions of how managerial discretion affects a wide variety of outcomes and what contributes to discretion. Despite this, many gaps remain, given the limited number of studies that measure discretion directly. Similar to methodologies employed in examining managerial discretion's consequences, well over half of the studies applying discretion as a moderator or mediator use archival data as a proxy for discretion. Thus, our understanding of how the relationships between executive, firm, and industry antecedents and outcomes (e.g., firm performance, executive compensation, and strategy change) are affected by organizational culture and other inertial forces and a manager's psychological traits is very limited. Additionally, only a limited number of studies attempt to examine firm-level decisions affected by

discretion, and the role that discretion can play in enhancing the effectiveness of certain actions in certain environments.

Future Managerial Discretion Research Opportunities

Our review illustrates that since [Hambrick and Finkelstein \(1987\)](#) formally introduced the concept of managerial discretion, a number of studies have attempted to examine the antecedents and consequences of managerial latitude of action. Despite these studies, however, significant opportunities still exist for researchers to explore how managerial discretion is influenced by a variety of forces, as well as how such forces influence many organizational outcomes, both individually and in combination. In this section, we examine some of the empirical gaps that remain and describe important questions and areas for future research.

Improving Measures of Managerial Discretion

We see an excessive reliance on archival data in measuring managerial discretion. While there are substantial challenges associated with surveys and interviews of senior executives, and content analysis of annual reports and correspondence with the media, it seems unlikely that we can develop support for many of the human factors that affect discretion without such efforts. Thus, we encourage researchers to devote their creative energy towards methods that will give us a more complete assessment of the managerial discretion construct. Relatedly, we also encourage researchers to seek discretion measures that discriminate the construct from its closely related psychological (e.g., locus of control), organizational (e.g., inertia), and environmental (e.g., market growth) antecedents.⁵ Additionally, we call for future research to develop composite measures of discretion. We encourage developing composite measures that appropriately weight the various factors within the internal organization and managerial characteristics forces. Such a composite measure will likely need to use a mix of archival data and data derived from nonarchival methods, but we would encourage researchers to seek to validate all measures and weightings using a variety of methods. Using more sophisticated modeling techniques may allow researchers to create latent constructs related to each discretion force and ultimately an overall construct based on discretion forces identified in research, furthering validation of the construct.

Assessing Managerial Discretion's Construct Validity

Despite the many studies that rely upon the managerial discretion construct, we identified only four studies that measure discretion as a dependent variable as well as a handful of other studies that use direct measures of managerial discretion. These studies have enhanced our knowledge of what yields discretion, providing support for measures such as locus of control and industry R&D and advertising intensity increasing managerial perceptions of discretion. Despite these findings, many of the original concepts proposed by [Hambrick and Finkelstein \(1987\)](#) remain untested. Many studies reviewed merely use proxies for discretion proposed by Hambrick and Finkelstein as indicators of discretion without testing their validity.⁶ Studies that measure task environment discretion with a continuous variable often use variants of [Hambrick and Abrahamson's \(1995\)](#) calculation of managerial discretion. While this provides some basis for measuring task environment discretion, that study is nearly 20 years old and has never been replicated with its measures validated with other samples.

Prior management research has suggested that "the substantive stream has been relatively overemphasized in strategic management research without corresponding concern for measurement" ([Venkatraman & Grant, 1986](#): 71). Validating measures provides construct validity and reduces the likelihood that measurement errors, such as random error and method variance, bias results ([Bagozzi, Yi, & Phillips, 1991](#)). Without further research validating many commonly used proxies as indicators of discretion, research has not achieved construct validity for many managerial discretion measures currently employed. Failing to achieve construct validity may yield both Type I and II errors when researchers employ measures designed to represent managerial discretion.

Indeed, the limited studies performed to date examining managerial and task environment characteristics on discretion find that not all proposed factors examined yield discretion. Relying upon [Hambrick and Finkelstein's \(1987\)](#) model as the basis for identifying measures of discretion is not enough to establish construct validity. In order to accomplish this, researchers have several opportunities. First, as described in the previous section, composite measures of discretion across the forces identified by Hambrick and Finkelstein could be evaluated to determine whether managerial discretion serves as a higher order construct based on indicators of the latent variables associated with each force. Second, future research could pilot additional studies with industry experts, academics, and managers to assess the level of discretion in firms, industries, and nations and test the validity of previously employed managerial discretion measures, in accordance with prior construct validation studies. Measuring such variables with expert ratings would allow researchers to determine whether commonly used proxies of discretion still are indicative of discretion. Finally, nonarchival methods, such as surveys, interviews, and content analysis, should be used by researchers studying organizations to seek an in-depth understanding of how discretionary forces influence executive decision making and perceived discretion. A significant opportunity exists for researchers to identify and determine which factors yield discretion and triangulate such proxies with alternative means of measuring discretion.⁷

Beyond an increased focus on methods used to examine managerial discretion, we call for research to further examine causal relationships. For example, [Hambrick and Finkelstein \(1987\)](#) posited that a CEO's power base influences discretion, yet it is also reasonable to posit a reverse causation. Future research that also seeks to illuminate potential causal paths that are not supported would greatly help disentangle the managerial discretion construct from the psychological constructs that compose the managerial characteristics force.

Managerial Characteristics and Perceived Discretion

Our review identifies that significant research attention has been paid to the task environment's influence on managerial discretion, while a paucity of research focuses on managerial characteristics. Literature from psychology provides a number of characteristics that alter how individuals perceive situations and make decisions that would greatly enhance an executive's perceived level of discretion. While gaining access to more fine-grained data on top manager characteristics is a significant challenge for management researchers, a number of important insights could be gained with access to such data. As noted earlier, the psychological microfoundations of the manager can indicate whether he or she acts enabled or constrained. While locus of control and other managerial characteristics detailed in the managerial discretion model may strongly influence managerial discretion, several additional characteristics beyond the model could strongly affect managerial discretion research, including domain-specific self-efficacy, executive confidence, and preference for novelty versus stability.

Domain-specific self-efficacy refers to executives' confidence that they can successfully carry out the tasks of their leadership role, resulting in improved and sustained firm performance ([Gist & Mitchell, 1992](#); [Judge, Bono, Ilies, & Gerhardt, 2002](#)). Domain specificity simply focuses [Bandura's \(1977\)](#) concept of generalized self-efficacy to the executive's sphere of influence. Many of the managerial characteristics related to discretion, such as commitment to the status quo and aspiration levels, are driven by whether executives believe that they can control events and achieve positive outcomes. Furthermore, successful outcomes will increase executives' self-efficacy within the firm and industry and, thus, will increase their perceived discretion ([Lindsley, Brass, & Thomas, 1995](#)), while poor outcomes and performance will ultimately reduce executives' perceived discretion.

An executive's confidence may also affect the degree to which an executive perceives a need for change or believes that actions taken will yield successful results ([Moore & Healy, 2008](#)). More confident CEOs invest in a greater variety of projects ([Malmendier & Tate, 2005](#)). Thus, executives' confidence influences their latitude of action in undertaking certain decisions. Furthermore, insights based on domain-specific self-efficacy may

indicate that executives' discretion changes over time as they gain confidence in their abilities as a manager, suggesting that a manager's perceived level of discretion may increase, possibly over the course of the manager's tenure in a top executive position ([Hambrick & Fukutomi, 1991](#)). However, a series of poor decision outcomes for a top executive over time may have the opposite effect, reducing his or her self-efficacy and, thus, perceptions of discretion.

A third psychological microfoundation applicable to managerial discretion is a manager's preference for novelty versus stability. [Hambrick and Finkelstein \(1987\)](#) discuss how executives who are intolerant of ambiguity may simply not consider actions that lack a clear "line of sight" in their execution. Such executives prioritize order over developing new possible strategic directions. Alternatively, executives who embrace novelty are more likely to be more innovative, encourage organizational playfulness, and lead their organization in addressing new opportunities ([Katsaros & Nicolaidis, 2012](#); [Wilkinson, 2006](#)).

The Institutional Environment and Managerial Discretion

[Crossland and Hambrick \(2007, 2011\)](#) illustrate how nation-level institutions affect the degree to which CEOs matter to firm outcomes. This line of inquiry adds an important, fourth force related to managerial discretion: the institutional environment. Insights from sociology on institutional analysis and from political science on comparative political economy provide evidence of how institutions can both constrain and enable the behavior of organizations (for a review, see [J. L. Campbell, 2004](#): Chapter 1). While Crossland and Hambrick begin to examine the role of institutions in altering executives' latitude of action, considerable room still exists to examine country-level traits that affect behavior and the role of institutional forces that limit behavior. For instance, [J. L. Campbell \(2007\)](#) notes that governmental institutions can significantly alter firm behaviors, such as social responsibility through regulation, but such regulations are also likely to have a stronger impact when negotiated between the government and corporations. Furthermore, such regulations are likely to be effective when self-instituted by a set of firms. Thus, either formal or informal norms created through a joint institution of competing firms may limit managerial discretion by indicating a set of appropriate behaviors. Previously used management concepts, such as power distance, openness, and level of referent power, may also significantly influence the level of discretion provided by institutions. Finally, the presence of nongovernmental institutions and third party stakeholders, such as watchdog agencies, may place pressure upon organizations to act in certain manners ([Schneiberg & Bartley, 2001](#)), limiting the latitude of actions available to managers. Future research should consider how such institutional pressures affect the discretion that is afforded to managers independent of the organization's immediate competitive task environment.

Managerial Discretion as a Time Varying Construct

Our review further indicates that research has examined managerial discretion as a static construct. Longitudinal analyses on managerial discretion are likely to illustrate a complex interplay of discretion over time. In some cases, events, such as changes in the task environment encountered by all firms in an industry, occur which may alter managerial discretion. For example, the managerial discretion of U.S. airline executives was dramatically constrained after the terrorist attacks of September 11, 2001, shut down the industry for several days and dramatically reduced the demand for air travel, with demand not recovering to pre-9/11 levels for 3 years ([Notis, 2005](#)). In the close aftermath of 9/11, managerial discretion was severely reduced at most U.S. airlines to actions primarily focused on avoiding bankruptcy. Such fluctuations in managerial discretion over time have largely been absent from the literature.

Furthermore, changes in internal forces, such as the firm's size, age, and powerful inside forces, such as the composition of the board of directors and turnover of top managers following a CEO succession, may model changes over time in discretion. However, only limited research examines how executives may influence their level of managerial discretion over time. For instance, [Westphal \(1998\)](#) illustrates how executives use

ingratiation and persuasion toward board members when the board increases its independence to maintain their influence. The limited work done in this area, however, primarily focuses on how executives employ power and influence tactics against the board to achieve desired outcomes (e.g., [Bebchuk & Fried, 2006](#); [Zajac & Westphal, 1996](#)). While studies from agency theory explore how CEOs may gain domination of a board using influence and nomination tactics, fewer studies, such as Westphal, have explored in-depth processes related to influence and persuasion. Future studies may explore whether additional factors, such as firm performance or CEO reputation or celebrity, may also enhance CEO discretion. For instance, poor performance may enhance shareholder and board monitoring, reducing the latitude of action CEOs have. Alternatively, higher reputation CEOs may gain more discretion given the positive beliefs regarding their actions.

Finally, as noted earlier, not all managerial characteristics are static. Executives' domain-specific self-efficacy may increase during their tenure as they become more familiar with the new position and learn more about the task environment ([Hambrick & Fukutomi, 1991](#); [Lindsley et al., 1995](#)). Therefore, over time, executives' managerial characteristics may enhance their perceived level of discretion. Such arguments would be consistent with prior research, such as [Ocasio \(1994\)](#), who finds that the level of an executive's power changes during the course of his or her tenure. Research could examine such characteristics that affect the degree to which executives are likely to undertake significant strategic decisions within their firms. Alternatively, research also shows that as executives achieve success, they become committed to an existing course of action or the status quo ([Audia, Locke, & Smith, 2000](#)). Such commitment may reduce executives' perceived level of discretion by limiting the choices the executives perceive to preserve their legacy.

Managerial Discretion Forces as Substitutes Versus Complements

Insights and research from corporate governance (e.g., [Rediker & Seth, 1995](#)) and transactional governance (e.g., [Poppo & Zenger, 2002](#)) suggest that mechanisms designed to control behavior may serve as complementary forces or substitutes. From the substitution perspective, for example, significant monitoring behavior by the board may be unnecessary if high-powered incentives align the interests of self-interested managers with shareholders. A significant opportunity exists for managerial discretion scholars to examine whether and under what conditions the forces identified as constraining or enabling discretion serve as complements or substitutes or whether these forces complement or substitute for other firm activities. For instance, when the task environment is highly regulated, overly competitive, and/or lacks product differentiation, discretion is likely to be limited. In such cases, is it necessary for boards to closely monitor managerial behavior to ensure managers do not act opportunistically? Alternatively, further managerial discretion research may yield insights to corporate governance research by suggesting that when discretion is high, corporate governance mechanisms may be more necessary and beneficial. Whether discretionary forces serve as complements or substitutes has interesting implications for both organizations and individuals.

Organizational consequences

Research from corporate governance suggests that organizations perceive governance mechanisms as complements ([Schepker & Oh, 2013](#)). With regard to discretion, multiple forces may complement each other to enhance discretion or serve as substitutes, with limited forces needed only to constrain such discretion. If discretion forces serve as complements, executives are likely to have greatest control when their characteristics, the internal organization, and the task environment provide greater discretion. In these situations, outcomes would be expected to be highly variable with managers receiving greater compensation. Furthermore, such firms may be more likely to lack strategic conformity and commitment to the status quo. Alternatively, discretion may be most limited when managerial characteristics, internal forces, and the task environment all constrain discretion, likely leading to strategic persistence and few strategic choices undertaken. If forces serve as complements, future research could illustrate how these forces work together to further alter variability of outcomes.

If managerial discretion forces serve as substitutes, a different story arises. For instance, powerful inside forces may not limit managerial discretion when other discretionary forces, such as the manager's characteristics or the institutional environment, limit perceived discretion. Consistent with perspectives on governance mechanisms as substitutes, powerful monitoring by inside forces may yield only costs to the organization without any additional benefits. From an agency theory perspective, governance mechanisms may be less necessary when the manager's characteristics or the task environment constrain discretion. Alternatively, firms may need to be more conscious of the need for strong monitoring when managers' characteristics lead managers to perceive greater discretion and/or when the task environment yields discretion. Discretion may inform agency theory research on corporate governance such that corporate governance mechanisms may be most necessary and beneficial when discretion is high, as executives have the greatest ability to pursue their own self-interests. Failure to appropriately monitor behavior may exacerbate potential problems related to discretion.

A final situation may arise where an executive's characteristics lead to him or her lacking (having) discretion at the individual level while operating in a high (low) discretion environment. In such situations, the individual may undertake or fail to undertake decisions that are consistent with the environment in which the executive's firm operates, thus either destroying value or failing to capture value creating opportunities. Additionally, if the environment in which the firm operates or various organizational forces constrain executives' latitude of action associated with strategic decisions, such as product development and marketing, the executives (driven by their psychological traits) may focus on other areas where they feel they can have a greater influence. Indeed, executives may have significant discretion towards some types of organizational decisions and outcomes while having little in other types. Future research should consider what types of organizational actions discretion limits and whether all actions are affected by discretion or whether only certain types of organizational actions may be affected. In short, organizations, executives, and boards of directors should be aware of and understand how each of the four discretion forces affects their organizations and account for them appropriately. Future research can examine the interplay between different levels of discretion to understand how each type of discretion differentially and interactively affects executive decision making across the firm's operational and strategic domains and firm-level outcomes. Research on discretion could greatly benefit from a discussion of which discretionary forces complement and substitute each other and under which conditions. This line of inquiry could have significant implications for researchers in additional fields, such as corporate governance.

Individual outcomes

Discretion has primarily been examined from an organizational perspective with research failing to examine how perceptions of discretion influence individual managers. Microresearch may reveal psychological and career consequences for managers affected by different levels of managerial discretion. First, psychology research notes that the fit between an individual and his or her environment is an important consideration "that necessarily includes one's compatibility with multiple systems in the work environment" ([Kristof-Brown, Jansen, & Colbert, 2002](#): 985). Thus, choosing an appropriate organization and environment for an individual is an important concern for individuals ([Rynes & Cable, 2003](#)). Aligning an individual with his or her organization is related to job performance, organizational citizenship behavior, turnover, job satisfaction, and commitment ([Hoffman & Woehr, 2006](#); [Kristof-Brown, Zimmerman, & Johnson, 2005](#)).

An important consideration for executives is whether they are placed in a situation where they can exercise the appropriate amount of discretion for their own satisfaction. For instance, an executive with an internal locus of control may feel hampered when placed in an older firm with an established, resistant culture. The executive may feel that efforts to change the organization are thwarted and may experience negative personal outcomes, such as job dissatisfaction or greater intentions to quit. Firms should understand that selecting high discretion executives in a low discretion environment may yield greater turnover, which may lead to major consequences

for the firm as it cycles through executives. Such frustration is also likely to increase stress and anxiety, while low discretion managers in high discretion environments are likely to face greater perceived job demands ([Hambrick, Finkelstein, & Mooney, 2005](#)). Future research could examine the role that fit between a potential executive and the firm's environment plays in selecting the appropriate executive. Furthermore, research should examine how mismatches in the executive's personal discretion and the organization and environment's afforded discretion influence negative outcomes for executives, including stress and anxiety. For instance, [Jex and Beehr \(1991\)](#) note that organizational constraints increase the level of stress experienced. Their research further illustrates that such stress leads to strains, which affect employee health and well-being. Discretion researchers may be able to utilize such research to examine the effects of such strain in executives who fail to fit in their organization or environment. Failure to consider such outcomes may yield both poor strategic outcomes and poor individual outcomes.

Applying the managerial discretion construct to other management disciplines can provide greater meaning and understanding to those disciplines. For instance, researchers might examine the value of constructs such as organizational commitment, organizational identity, and organizational citizenship behaviors in high discretion industries (e.g., foods/beverages) versus low discretion industries (e.g., public utilities). While such employee traits and behaviors may always be highly desirable, understanding their value in different industry environments may provide a greater grasp of when and how resources should be used to develop and enhance these traits and behaviors. Additionally, while one study has shown that the effectiveness of high performance work systems is enhanced in industries with higher discretion ([Datta et al., 2005](#)), additional research should examine whether discretion has implications for how employees are managed, developed, and rewarded.

Managerial Discretion Within the Organization

Our review also indicates the role that managerial discretion plays at the organizational level with regard to outcomes such as firm performance variability, commitment to a defined course of action, or even CEO compensation. Absent from research, however, is the level of discretion that middle managers within an organization perceive. The role of organizational members outside of the TMT, such as middle managers, in influencing internal outcomes is also important. Studies on change management and strategy implementation suggest that middle-level managers are important conduits for explaining changes in strategy and ensuring that strategy is implemented appropriately. Effective strategy implementation is likely to require discretion at all levels of the organization to implement actions that are consistent with the strategy composed by the organization's leaders. For instance, prior research identifies five antecedents to middle-level manager entrepreneurial behavior: (1) management support, (2) work discretion and autonomy, (3) rewards and reinforcement, (4) time availability, and (5) organizational boundaries ([Kuratko, Ireland, Covin, & Hornsby, 2005](#)). In short, research provides evidence that organizations can promote behavior by middle managers that leads to positive outcomes. Failure to provide discretion to managers hampers their ability to implement the strategy without effectively seeking approval and limits the speed at which strategy may be implemented. Future research should continue to further consider the role of discretion directly on internal strategy implementation and the role that middle managers play in implementing strategy.

Conclusion

Strategy studies have long considered the ability of executives to affect organizational strategic decision making. However, upon the publication of [Hambrick and Finkelstein's \(1987\)](#) discussion of managerial discretion, research began more thoroughly examining the forces that affect managerial latitude of actions, leading executives to have stronger effects. While this research has extended our knowledge of how and when executives matter, there are many important and challenging questions that remain open for researchers. As research on managerial discretion continues to grow, it is important to ensure we have a strong understanding

of what yields discretion. Additionally, work is needed to develop more robust ways to measure discretion and how it can change over time. Furthermore, significant questions still abound with regard to how executive characteristics and internal factors affect the level of discretion managers perceive. Finally, understanding how these factors interact to further affect executive decision making remains a strong avenue for researchers to consider.

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Notes

1. [Hambrick and Finkelstein \(1987\)](#) also posited that powerful internal stakeholders may be extraordinarily confident as a result of past successes ([March & Simon, 1958](#)) or may have tremendous zeal for traditional prioritization of actions ([Peters & Waterman, 1982](#)).
2. The following journals were considered "top journals" in our literature review: *Academy of Management Journal*, *Academy of Management Review*, *Administrative Science Quarterly*, *Journal of Applied Psychology*, *Journal of International Business Studies*, *Journal of Management*, *Journal of Management Studies*, *Strategic Management Journal*, *Management Science*, and *Organization Science*.
3. Google's Web site ranks articles for relevance in the following manner:
Google Scholar aims to rank documents the way researchers do, weighing the full text of each document, where it was published, who it was written by, as well as how often and how recently it has been cited in other scholarly literature.
(<http://scholar.google.com/intl/en-US/scholar/about.html>)
- While Google does not release their specific ranking algorithm, we feel strongly that these are richer criteria than citations since it reduces the potential of missing more recent articles. Furthermore, since Google Scholar's algorithm accounts for journal quality, recent articles in high quality journals are likely to be higher on the relevance list.
4. During our review process, we felt that several articles prior to 1987 strongly operationalized forces in the [Hambrick and Finkelstein \(1987\)](#) model (e.g., [Lieberson & O'Connor, 1972](#); [Miller et al., 1982](#)).
5. We are grateful to one reviewer for suggesting the need for future research that discriminates the managerial discretion construct from closely related psychological antecedents.
6. Proxies for task environment-provided discretion include comparing industries selected for research described as either being high or low in managerial discretion. In some cases, industry selections in studies are justified by researchers using qualitative descriptions of the industry as either providing high or low latitude of action to industry top managers. In other studies, researchers may corroborate an industry selection as having either high or low discretion on the basis of quantitative differences with other industries on variables theorized to affect managerial discretion, such as capital intensity, regulation, or industry growth.
7. For exemplars in management research in attempting to assess construct validity, see [Bagozzi et al. \(1991\)](#) and [Hoskisson, Hitt, Johnson, and Moesel \(1993\)](#).

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