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Management Insights

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Accelerated Learning of User Profiles (p. 215)

Pelin Atahan, Sumit Sarkar

How helpful is a website for a user? A regular user might have profile information that helps him use the site more efficiently; for example, weather.com might have the zip codes he has previously queried, or Expedia might retain the last destination he wanted to fly to. These sites might also offer specials, discounts, and other links of interest that relate to his recent visits or profile options. But if the user is new to the site, it cannot effectively target products, promotions, and advertisements. In those situations, the site can learn the profile of a user as the user traverses the site. Naturally, the faster the site can learn a user's profile, the sooner the site can benefit from personalization. The authors develop a technique that sites can use to learn the profile as quickly as possible. The approach effectively learns multiple attributes simultaneously and works particularly well when a user's traversal is influenced by the most recently visited pages on a site. The insight for management: New methods that lead to quick interpretation of mouse clicks can lead to more effective target marketing on the Internet.

Organizational Change and Employee Stress (p. 240)

Michael S. Dahl

Who Moved My Cheese? by Dr. Spencer Johnson addresses the psychological elements of change management in organizations; people generally resist change because they are afraid of change. But rarely have researchers considered or quantified this cost on an organizational level. Researchers have quantified the organizational cost of change such as employee attrition, and hiring and firing costs and training costs from loss of productivity as an organization changes direction. The author delves into the cost of change to the employees themselves: What human toll is there, then, in a changing, evolving organization? The author analyzes detailed data on stress-related medicine prescriptions for 92,860 employees working in 1,517 of the largest Danish organizations to analyze the relationship between organizational change and employee health. The findings suggest that the risk of receiving stress-related medication increases significantly for employees at organizations that undergo change and that, as the breadth and scope of the

organizational tumult expand, so does the use of such stress-related medication. The insight for management: Radical organizational change has a real cost for your employees.

The Impact of Founders' Professional-Education Background on the Adoption of Open Science by For-Profit Biotechnology Firms (p. 257)

Waverly W. Ding

This paper investigates the effect of founders' professional-education background on the adoption of an "open science" technology strategy, which allows a firm's research personnel to do basic science research and publish the results in academic journals. Using a sample of 512 young biotechnology firms, the author finds that firms with proportionally more Ph.D.-holding entrepreneurs on the founding team have a higher probability of adopting an open science policy. This Ph.D. influence on open policy is especially notable in crowded technological niches and in an institutional environment in which open science has yet to become the industry norm. The insight for management: Entrepreneurial founders' background is an important factor in new-venture open science strategy and research structure.

Status, Quality, and Attention: What's in a (Missing) Name? (p. 274)

Timothy S. Simcoe, Dave M. Waguespack

John Grisham, James Patterson, Mary Higgins Clark, and Danielle Steel, among others, are all well-known authors whose works are regularly New York Times Best Sellers. But does nearly every book they write deserve to be a best seller based on the merits of the work, or are they best sellers predominantly because of the reputation of the authors? If the author's name were not on the cover, would the book be as well received? The authors of this article ask this question: How much are we influenced by an author's identity when evaluating the quality of his or her work? The authors find that in academic circles name-based signals can explain up to three-quarters of the difference in publication rates between high- and low-status authors. That is, well-known authors get the benefit of the doubt and are more likely to be accepted for publication than those who are less well known.

Interestingly, when attention is scarce, or search costs are high, the reputation effect is more pronounced. So the broader the pool of potential authors, the more pronounced the reputation effect can be. Furthermore, the better the reputation one has, the more attention one's idea gets, which helps give the idea more credibility and momentum, resulting in a virtuous cycle driven by author reputation. The insight for management: Don't be overly swayed by reputation when evaluating the quality of new ideas.

Determinants and Outcomes of Internet Banking Adoption (p. 291)

Mei Xue, Lorin M. Hitt, Pei-yu Chen

What factors drive the decision to adopt an Internet banking service and subsequent customer profitability? The authors examine the drivers of adoption of Internet banking and the linkages among adoption drivers and outcomes such as product acquisition, service activity, profitability, and customer loyalty. They relate Internet banking adoption to customer demand for banking services, the availability of alternative channels, customers' efficiency in service coproduction, and local Internet banking penetration. They find that customers who have greater transaction demand and higher efficiency and reside in areas with a greater density of online banking adopters are faster to adopt online banking. Consistent with prior research the authors find that online customers significantly increase their banking activity, acquire more products, and perform more transactions. These changes in behavior are not associated with short-run increases in customer profitability, but customers who adopt online banking have a lower propensity to leave the bank. Customers who live in areas with a high branch density or high Internet banking penetration increase their product acquisition and transaction activity more than Internet banking adopters in other regions. The insight for management: Efficient customers and those with high service demand show greater postadoption profitability.

Economic Interpretation of Probabilities Estimated by Maximum Likelihood or Score (p. 308)

D. J. Johnstone

How are forecasting and risk aversion related? The author evaluates forecasting methodologies in the face of the user's risk aversion and finds that the two are related. Simply, a highly risk-averse forecast user may need a much bolder forecast to obtain the same certainty equivalent as a more risk-tolerant one. Probabilities produced by maximum likelihood estimation can be either too conservative or too bold relative to those found by maximizing utility under more risk-tolerant or risk-averse score functions. A very (not very) risk-averse user who bets characteristically small (large) fractions of wealth based on a conservative

forecast is bound to make a rapidly (slowly) increasing bet as the forecast probability becomes progressively bolder or more distant from the market probability. The insight for management: Professional forecasters should anticipate how a client with given risk aversion expects to gain from any given forecast, or forecast revision, before committing resources toward making a better informed forecast.

Portfolio Choice Under Cumulative Prospect Theory: An Analytical Treatment (p. 315)

Xue Dong He, Xun Yu Zhou

That "losses loom large" is a basic tenet of understanding individuals' choices under uncertainty. The well-known cumulative prospect theory (CPT) holds that most people evaluate an outcome relative to a reference point; falling below that point can create more disutility than exceeding it by the same amount. People tend to evaluate options relative to a benchmark rather than according to a final wealth position. The authors extend CPT with a new measure of loss aversion for large payoffs, called the large-loss aversion degree (LLAD), and they show that the size of the loss relative to a benchmark is important for accurately describing and predicting behaviors. The insight for management: A better understanding of individuals' decision making under uncertainty helps to reveal the psychology and outcomes of investment and other decisions.

Channel Stuffing with Short-Term Interest in Market Value (p. 332)

Guoming Lai, Laurens Debo, Lin Nan

Does desire to meet end-of-the quarter sales targets to placate investors and inflate the firm's short-term market value result in "channel stuffing"? A channel stuffing manager ships excess inventory to the downstream channel, allowing him to report sales in excess of demand in order to influence investors' valuation of the firm. The authors' modeling shows that when demand is lower than a certain proportion of the initial inventory level, the manager will pad sales and release the inflated sales report. Interestingly, savvy investors are able to "correct" the reported sales and are able to accurately infer the firm's value. However, when the demand exceeds this proportion of inventory, the manager will report that the initial inventory is sold out. Then the investors infer only that the real demand is relatively high, and the short-term value of the firm can be artificially inflated. Interestingly, this result influences the inventory decision, too. The authors find that both over- and underinvestment in the initial inventory can arise in this situation. The insight for management: Short-term managerial focus can result in inflated sales claims and poor inventory decisions and in some cases will not generate the anticipated short-term boost in company valuation.

Managing Consumer Returns in a Competitive Environment (p. 347)Jeffrey D. Shulman, Anne T. Coughlan,
R. Canan Savaskan

The day after Christmas is a nightmare for retailers, as hoards of shoppers descend upon them with merchandise to return. Between one-fifth and one-third of all returns are not due to defect, but simply because the product does not meet the needs of the consumer. In the United States, the annual value of product returns is \$60 billion, with an additional \$40 billion spent to manage the return process. As a result, retailers might charge a restocking fee to defray these costs; for example, Best Buy charges 15% for returns of opened digital cameras, and the Apple Store charges 10% for opened iPods. The authors find that optimal restocking fees are more severe when consumers are less informed about product fit at the time of purchase. They further show that consumer uncertainty may result in higher equilibrium prices. Finally, they find a surprising result: Equilibrium restocking fees in a competitive environment can be higher than those charged by a monopolist. The insight for management: Retailers should promote gift cards. The inherent uncertainty of gift giving creates the inefficiency of high returns and the disincentive to purchase of higher prices and restocking fees. In product sales, firms should not use solely restocking fees as a way to defray product return costs.

Cooperation in Games with Forgetfulness (p. 363)

Raphael Thomadsen, Pradeep Bhardwaj

Is it better to forgive and forget, or is revenge a dish best served cold? Which axiom holds in cooperative behavior situations? Companies and managers are apt to forget information; however, classic game theory analysis has assumed that all players have perfect recall. The authors examine how introducing forgetfulness into a multiplayer game-theoretic framework can help or hinder cooperative behavior. They find that forgetfulness impacts the ability of firms to cooperate in two different directions. On one hand, forgetfulness can diminish the ability to punish deviators, making cooperation more difficult; that is, to gain cooperation, it is in fact not better to forgive and forget. On the other hand, under some conditions forgetfulness can make meting out severe punishments more credible and decrease the ability for players to effectively deviate, facilitating cooperation even in circumstances where cooperation cannot be sustained under perfect recall; that is, members are less likely to deviate if they might forget that revenge is on the way. The insight for management: Perfect recall is not essential for the application of game theory to cooperative games, but more or less cooperative outcomes depend on what might be forgotten. In the presence of

forgetfulness, more cooperation results if members do not forgive and forget and suffer unexpected revenge.

Product Recalls in the Medical Device Industry: An Empirical Exploration of the Sources and Financial Consequences (p. 376)

Sriram Thirumalai, Kingshuk K. Sinha

The \$90 billion market for medical devices is growing at 6% per year; medical devices play an increasingly significant role in the delivery of health care today. However, persistent quality problems with medical devices and the associated recalls present potential health risks to patients and personnel using these devices; for example, there were nearly 5,000 product recalls over the 2002–2005 time frame. Surprisingly, based on data from manufacturers in the medical device industry over that four-year period, the authors find that, at an aggregate level, the market penalties for medical device recalls are not as severe as one might expect. First, they find that the magnitude of financial consequences of device recalls depends on the product scope, sales, growth prospects, and the capital structure of a firm. Second, they find that device recalls are more common among firms with a research and development focus on developing broader product portfolios. Finally, they find that the likelihood of recalls decreases after a company has undergone a recall. The insight for management: In the cutting-edge medical instrument industry, recalls on products are common and the market reaction is surprisingly mild. The smaller-stakes products tend to have lower financial repercussions from a recall, and firms that do more new product development are more prone to recalls.

**“I Think You Think I Think You’re Lying”:
The Interactive Epistemology of Trust in
Social Networks** (p. 393)

Mihnea C. Moldoveanu, Joel A. C. Baum

It is widely held that trust is essential in business relationships. The authors model trust as a state of knowledge or belief that is the result of the frequency and quality of communication in a large network. For instance, the telecommunications industry relies on chip makers like Intel that embed their chips into products. A system manufacturer with private information about a chip’s limitations can cultivate Intel’s trust by informing it of the limitations of the chip and of new market opportunities. The manufacturer can also undermine Intel’s trust in software developers that target their applications to a chip’s capabilities by communicating information that it privately knows. Thus, interaction intensity can be used to seed breaches of trust based on asymmetries of understanding. The insight for management: Trust is important to mobilization and coordination in a network and influences social capital arising from the network structure.