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Management Insights

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Teams Make You Smarter: How Exposure to Teams Improves Individual Decisions in Probability and Reasoning Tasks (p. 1255)
Boris Maciejovsky, Matthias Sutter, David V. Budescu, Patrick Bernau

Does team decision making have a positive impact on the decision making of individuals? Many important decisions are routinely made by transient and temporary teams, who perform their duty and disperse. Subsequently, team members often continue making similar decisions as individuals. The authors study how the experience of team decision making affects subsequent individual decisions in two seminal probability and reasoning tasks: the Monty Hall problem and the Wason selection task. Their results show that teams trade closer to the rational level, learn the solution faster, and achieve this with weaker, less specific performance feedback than individuals. Most importantly, the authors observed significant knowledge transfers from team decision making to subsequent individual performances taking place up to five weeks later. The insight for management: Exposure to team decision making has strong positive spillovers on the quality of individual decisions.

Inferring Reporting-Related Biases in Hedge Fund Databases from Hedge Fund Equity Holdings (p. 1271)
Vikas Agarwal, Vyacheslav Fos, Wei Jiang

Are there biases in financial self-reporting? The authors match the quarterly equity holdings of a complete list of 13F-filing hedge fund companies with five major commercial databases of self-reporting hedge funds between 1980 and 2008, and they find that funds initiate self-reporting after positive abnormal returns that do not persist into the reporting period. Termination of self-reporting is followed by both return deterioration and outflows from the funds. The propensity to self-report is based on benefits such as access to prospective investors and costs such as partial loss of trading secrecy and flexibility in selective marketing. The insight for management: Returns of self-reporting funds are higher than those of nonreporting funds using characteristic-based benchmarks; however, the difference is not significant using alternative choices of performance measures.

Price Dispersion and Loss-Leader Pricing: Evidence from the Online Book Industry (p. 1290)
Xinxin Li, Bin Gu, Hongju Liu

What is the appropriate response to price competition in the face of changing demand? In October 2009, Walmart, Amazon, and Target cut their online prices for 10 best-selling items from \$25 to \$9, reportedly as loss leaders. Meanwhile, independent bookstores decided not to cut their prices as much to match their mega competitors. The authors develop a theoretical model to analyze the pricing strategies of competing retailers with different cross-selling capabilities when product demand changes. Their results suggest that retailers with better opportunities for cross-selling have higher incentives to adopt loss-leader pricing on high-demand products than retailers with low cross-selling capabilities. As a result, price dispersion of a product across retailers rises when its demand increases. The insight for management: Major retailers will demonstrate greater price dispersion than boutique sellers because of cross-selling opportunities.

Treatment Effectiveness and Side Effects: A Model of Physician Learning (p. 1309)
Tat Chan, Chakravarthi Narasimhan, Ying Xie

How do treatment effectiveness and side effects affect the prescription decision of a risk-averse physician? How can patient feedback help reduce the physician's uncertainty about effectiveness and side effects? The authors identify the impact of patient feedback on drug effectiveness and side effects by studying erectile dysfunction prescription choices based on self-reported reasons for switching. Their results show that the drugs Levitra and Cialis have higher mean effectiveness than the older drug Viagra, but physicians have higher uncertainty about the effectiveness of Levitra and the side effects of Cialis. The insight for management: Patient self-reporting is critical for detailing the effectiveness and side effects of new entrants competing with incumbent drugs.

Capital Markets and Firm Organization: How Financial Development Shapes European Corporate Groups (p. 1326)
Sharon Belenzon, Tomer Berkovitz, Luis A. Rios

How does financial development affect corporate groups in Europe? The authors investigate the effect of financial development on the formation of European corporate groups. They examine a comprehensive firm-level data set on European corporate groups in 15 countries and find that countries with less developed financial markets have a higher percentage of group affiliates in more capital-intensive industries. This relationship is more pronounced for young and small firms and for affiliates of large and diversified groups. The insight for management: Internal capital markets may, under some conditions, be more efficient than prevailing external markets, and this may drive group affiliation even in developed economies.

The Fragility of Commitment (p. 1344)
John Morgan, Felix Várdy

Can we count on your commitment? The authors show that the value of commitment is fragile in many standard games. When the follower faces a small cost to observe the leader's action, equilibrium payoffs are identical to the case where the leader's actions are unobservable. Applications of the result include classic standard Stackelberg–Cournot and differentiated product Bertrand games, as well as forms of indirect commitment. The insight for management: Weakening full rationality in favor of boundedly rational solution concepts such as quantal-response equilibrium restores the value of commitment.

Total Cost Control in Project Management via Satisficing (p. 1354)
Joel Goh, Nicholas G. Hall

How can projects with uncertain activity times and the possibility of expediting or crashing them best be managed? The authors established an objective that considers total completion time penalty plus crashing and overhead costs. They developed a robust optimization model that uses a conditional "value-at-risk" satisficing measure, and they developed decision rules for activity start time and crashing decisions that are designed to perform robustly against all possible scenarios of activity time uncertainty. They compare their procedures against the previously available Program Evaluation and Review Technique and Monte Carlo simulation procedures. Their computational studies show that, relative to previous approaches, their crashing policies provide a higher level of performance. The insight for management: New methods for project management under uncertain conditions can lead to higher success rates and lower project budget overruns.

An Axiomatic Approach to Systemic Risk (p. 1373)
Chen Chen, Garud Iyengar, Ciamac C. Moallemi

As highlighted by the financial crisis of 2007–2008, the measurement and regulation of systemic risk of an economy or a financial market are of particular interest. Can such systemic risk be identified and managed? Systemic risk refers to the risk of collapse of an entire complex system as a result of the actions taken by the individual component entities or agents that comprise the system. Systemic risk is an issue of great concern in modern financial markets and, more broadly, in the management of complex business and engineering systems. The authors propose an axiomatic framework for the measurement and management of systemic risk, and they define a broad class of systemic risk measures that accommodate a rich set of regulatory preferences. The authors suggest that the systemic risk can be decomposed into risk due to individual agents. The insight for management: Think locally to have global effect; externalities of individual agents' behaviors can be a driver in systemic risk in markets.

Sourcing for Supplier Effort and Competition: Design of the Supply Base and Pricing Mechanism (p. 1389)
Cuihong Li

Manufacturers increasingly rely on suppliers to create value, reduce costs, and improve products or services. How can manufacturers balance the need for a diverse supply base and low costs? In the auto industry, most original equipment manufacturers (OEMs) create only 30%–35% of value internally. The author studies a buyer's sourcing strategy along two dimensions—the supply base design and the pricing mechanism—considering supplier competition and cost-reduction efforts. The supply base design concerns the number of suppliers (one or two) included in the supply base and the capacity to be invested in each supplier. The pricing mechanism determines the timing of the price decisions, with the buyer making price commitments before suppliers exert cost-reduction efforts that may be renegotiated afterward. The author finds that symmetric capacity investment in suppliers and low price commitments (more likely to be renegotiated) are effective in fostering supplier competition, whereas asymmetric investment and high price commitments (less likely to be renegotiated) are better at motivating supplier effort. A complementary relationship exists between the supply base design and pricing mechanism: A more symmetric supply base should be combined with lower price commitments, leading to more renegotiation opportunities. The insight for management: Three possible sourcing structures result depending on the emphases placed on pricing and competition: sole sourcing, symmetric dual sourcing, and asymmetric dual sourcing.

On Implications of Demand Censoring in the Newsvendor Problem (p. 1407)
Omar Besbes, Alp Muharremoglu

How can demand be estimated when inventory runs out? The authors consider a "repeated newsvendor" problem in which the newsvendor does not have access to the underlying demand distribution. The authors compare the performance of two hypothetical vendors: One that has access to true demand and one that relies on sales data. The one that knows demand only exploits the knowledge; the one that does not must decide how much to "explore" (carry inventory to learn demand) and how much to exploit. The insight for management: A "lost sales indicator" that records whether demand was censored by inventory limits significantly reduces "exploration" and allows for "exploitation," i.e., profit taking.

Social Ties and User-Generated Content: Evidence from an Online Social Network (p. 1425)
Scott K. Shriver, Harikesh S. Nair, Reto Hofstetter

How do content creation and consumption relate? The authors examine activity at Soulrider.com, a privately held community website based in Europe that focuses on extreme sports such as windsurfing, surfing, and snowboarding. The site was launched in 2002 and as of June 2011 had a total of 10,677 registered users. Users can either consume or create content. The authors use changes in wind speeds at surfing locations in Switzerland as a source of variation in users' propensity to post content about their surfing activity on an online social network. They exploit this variation to test whether users' online content-generation activity is codetermined with their social ties. They find that increasing a user's social ties on the network may induce him to post more content, which then causes him to obtain more ties, which in turn causes him to post more content and so on. This process generates local positive feedback between ties and content, which thereby produces a self-reinforcing "virtuous cycle." Economically significant effects of this type can produce positive feedback that generates local network effects in content generation. When quantitatively significant, the increased content and tie density arising from the network effect induces more visitation and browsing on the site, which fuels growth by generating advertising revenue. The authors find evidence consistent with such network effects. The insight for management: An active social network member generates tremendous value for online networks.

Social Networks, Information Acquisition, and Asset Prices (p. 1444)
Bing Han, Liyan Yang

In financial markets information is power, but what's your source? When information is exogenous, social communication improves market efficiency. However, social communication crowds out information production due to traders' incentives to "free ride" on informed friends and on a more informative price system. The insight for management: Social communication may hurt market efficiency when information is endogenous; the network effects on the cost of capital, liquidity, trading volume, and welfare are also sensitive to whether information is endogenous; there are great implications of information networks for financial markets.

Tiers in One-Sided Matching Markets: Theory and Experimental Investigation (p. 1458)
Yu Wang, Ernan Haruvy

How should "matching markets," such as fractional ownership markets in real estate, be structured? In fractional ownership markets, a household purchases a share of a property, which allows the owner to use the property for a specified period of time every year for the duration of the ownership. For example, a household can purchase a week of a three-bedroom house in Orlando. A secondary matching market allows the exchange of ownership rights of their properties. In some settings, speculators might purchase low-priced properties with the intention of trading up, which is an undesirable behavior. In an experiment, the authors propose a tiered structure. They find that both firm revenue and total social surplus are improved by tiered matching, and the amount of improvement depends on the exchange mechanism that the firm uses: deposit first or request first. The insight for management: Subjects are less likely to take advantage of the match under a tier-free deposit-first mechanism, possibly because of risk aversion. Thus, a tiered approach is more critical under the request-first mechanism.