

Online Appendix: Dormancy as a Strategic Response to Detrimental Public Policy

Illustration of Dormancy

Figure 1 illustrates the theory of organizational dormancy. It presents a nomological network that links the observable manifestations of dormancy to its antecedents and its consequences. I also present the underlying assumptions and their links to the theorized constructs. Figure 2 shows the pattern of annual branch banking expansion for the 35 private banks in the sample from 1970 to 2003. As shown, there was a substantial decline in the branch banking activity of private banks (rural and urban) when the detrimental policy was in place (1981 to 1990), but some of these banks (mostly in urban areas) revived their branching activity when the favourable policy resumed.

Illustration of the Impact of Slack on Dormancy

Figure 3 graphically illustrates the non-linear effect between organizational slack and organizational dormancy. This figure actually resembles a J shape more than a U shape, but it is consistent with my argument that organizations with very low slack will enter dormancy – not as readily as organizations with very high slack, but more readily than organizations with a moderate amount of slack.

Additional Analysis

An important premise for the empirical analyses presented thus far is that the 1981-1991 period was detrimental for private banks in India because policy required them to become active in less lucrative rural areas. However, was this period definitely detrimental to private banks? Two additional analyses were conducted to ascertain this. The first tested whether or not banks actually entered rural areas against their will during the period. If organizations engage in activities that they find uncomfortable in conditions of duress due to coercive pressure, they will presumably cease those activities once the pressure is withdrawn. Private banks that expanded in rural areas during the period of the detrimental policy period would therefore reduce their expansion in rural areas after the policy is reversed.

This idea was tested using a panel data ordinary least squares regression with the proportion of new branches opened in rural areas as the dependent variable and “Detrimental public policy” as the independent variable. “Detrimental public policy” was an indicator variable that used the value ‘1’ for the period between 1981 and 1990 and ‘0’ for the subsequent period. The control variables were those included as controls and the theoretical variables in the main analyses. The results are reported in Table 5. “Detrimental public policy” had a positive and significant coefficient. Consequently, private banks in India probably entered rural areas merely to be compliant with the detrimental branch banking policy, as they avoided rural areas once the policy was reversed.

Another analysis examined whether conforming to the supposedly detrimental policy was detrimental to a bank’s performance. Conformity presumably promoted legitimacy (DiMaggio and Powell 1983), which can be a key to organizational survival (Hannan and Freeman 1977, 1984), but legitimacy alone doesn’t automatically yield good performance. If, on balance, the branching policy was actually detrimental, the proportion of expansion into rural areas should correlate with poorer ROA. This was tested with another panel data of ordinary least squares regression with return assets as the dependent variable and the proportion of new branches opened in rural areas as the independent variable of interest. The controls and theoretical variables in the main analysis were again included as controls. The results are reported in Table 6. Proportion of new rural branches did in fact have a negative and significant coefficient, so the policy was detrimental to those firms which complied with the detrimental policy.

In the second stage analyses of the consequences of dormancy, the variable “Net Dormancy” was a time invariant measure, which implies that the effect of dormancy on performance doesn’t change over time. But it is possible that organizations would have taken some time to revive from dormancy. Consequently, it is possible that the effect of remaining dormant in the previous detrimental environment would have resulted in better performance during the favorable new period after some time had elapsed. To test this possibility, I interacted the time-invariant measure of “Net dormancy” with historical time. The effect of the interaction was significant and positive, confirming that the performance consequence of remaining dormant during the period of the detrimental policy was strengthened over time during the favorable period. The results are reported in Table 7.

In this paper I have argued that dormancy is a strategic response to detrimental policies and that organizations are rewarded for it when a favorable policy resumes. One implicit argument in this line of reasoning is that

organizations that remained dormant during the detrimental period were able to revive their level of activity after the implementation of the favorable policy. Consequently, I employed an additional analysis to test whether this revival had occurred. In so doing, I constructed the following new measure for “Revival Rate”:

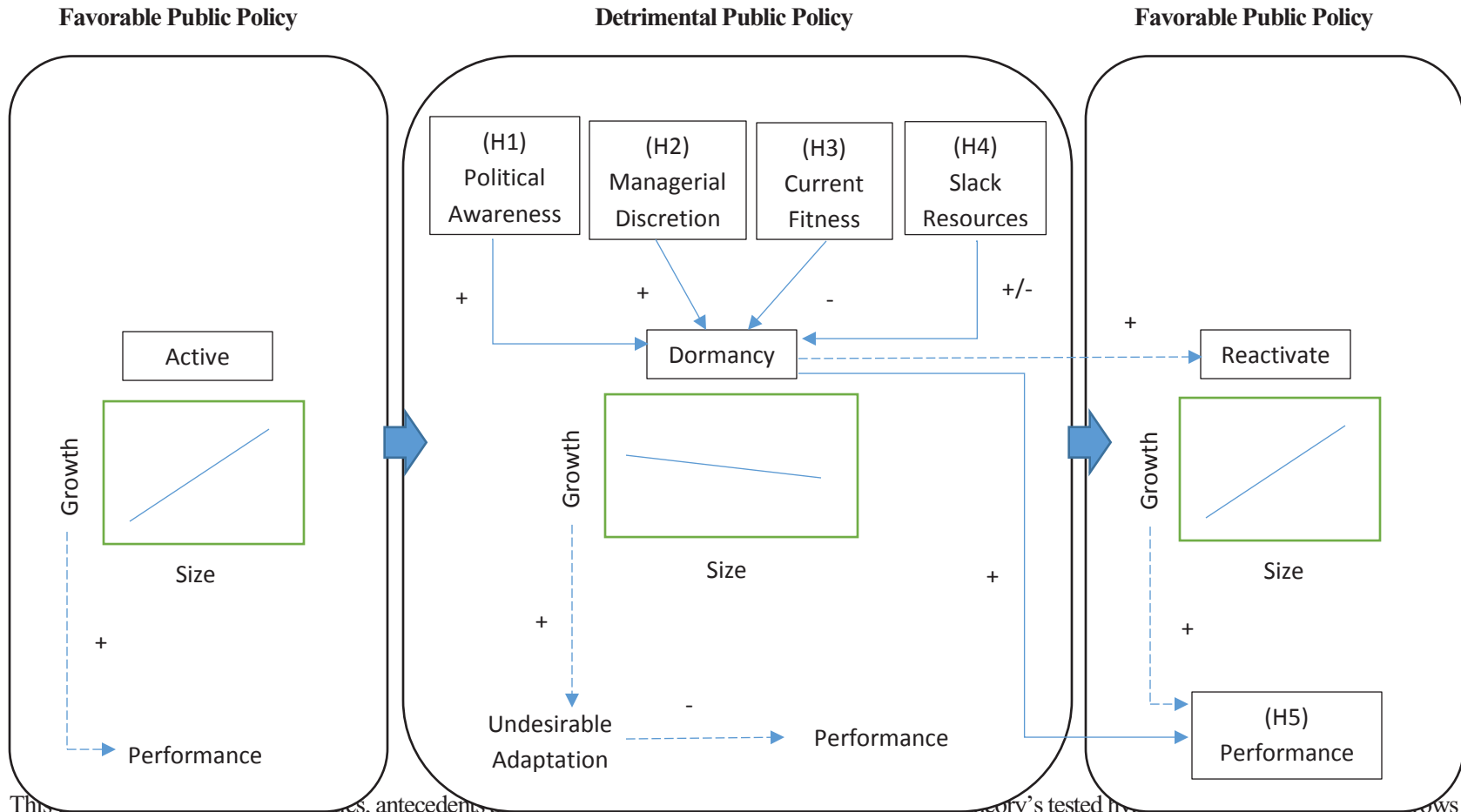
$$\text{Revival Rate} = (\text{Actual New Branches} - \text{Predicted New Branches}) / \text{Predicted New Branches}$$

“Actual New Branches” was measured as the number of new branches opened by the bank in a given year during the period of the favorable policy (1992-2003) and “Predicted New Branches” was estimated by regressing bank size (number of existing branches at t-1) on the number of new branches established by a bank during the period of the detrimental policy (1981-1991).

I then analyzed the impact of “Net Dormancy” on “Revival Rate” using a unconditional fixed effect Tobit model. As expected, “Net Dormancy” had a positive and significant effect on “Revival Rate”, indicating that organizations that remained dormant during the detrimental period revived their level of activity when the favorable policy resumed. These results are reported in Table 8.

FIGURE 1

A MODEL OF ORGANIZATIONAL DORMANCY



This figure illustrates the model's tested hypotheses, antecedents of organizational dormancy, and the underlying assumptions (some tested in additional analyses) are listed in dotted lines. The Block arrows between boxes represent temporal transition to different public policies.

FIGURE 2: TEMPORAL PATTERN OF BRANCH EXPANSION OF INDIAN BANKS, 1970-2003

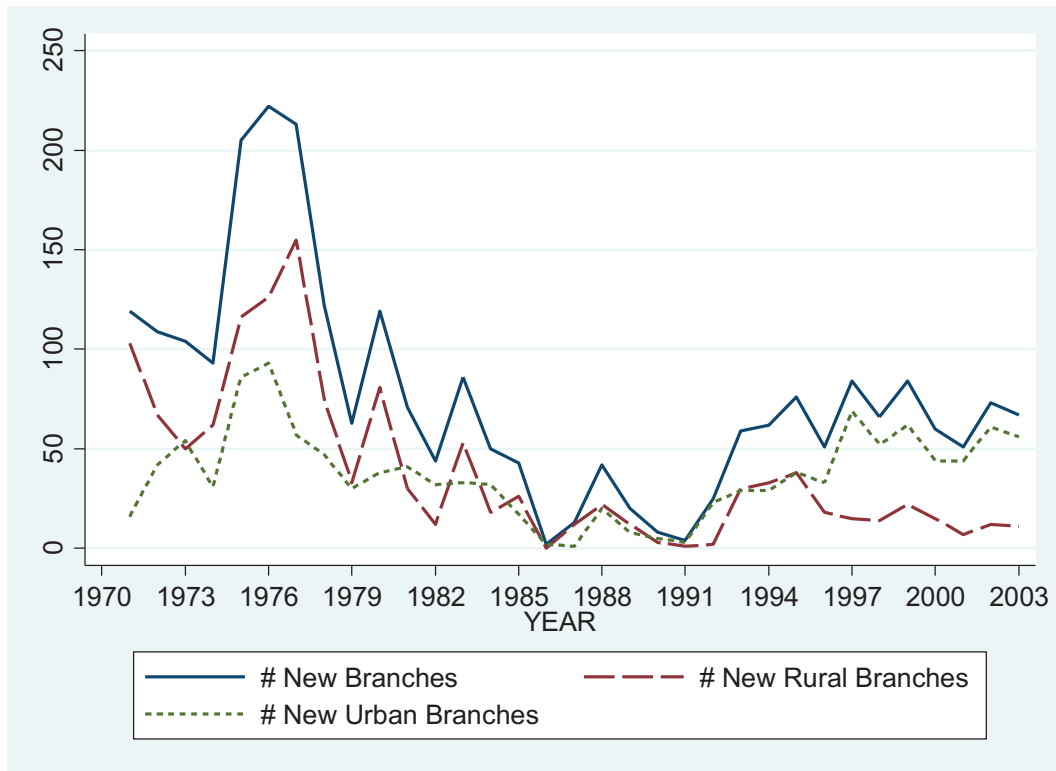


FIGURE 3: NONLINEAR EFFECT OF ORGANIZATIONAL SLACK ON DORMANCY

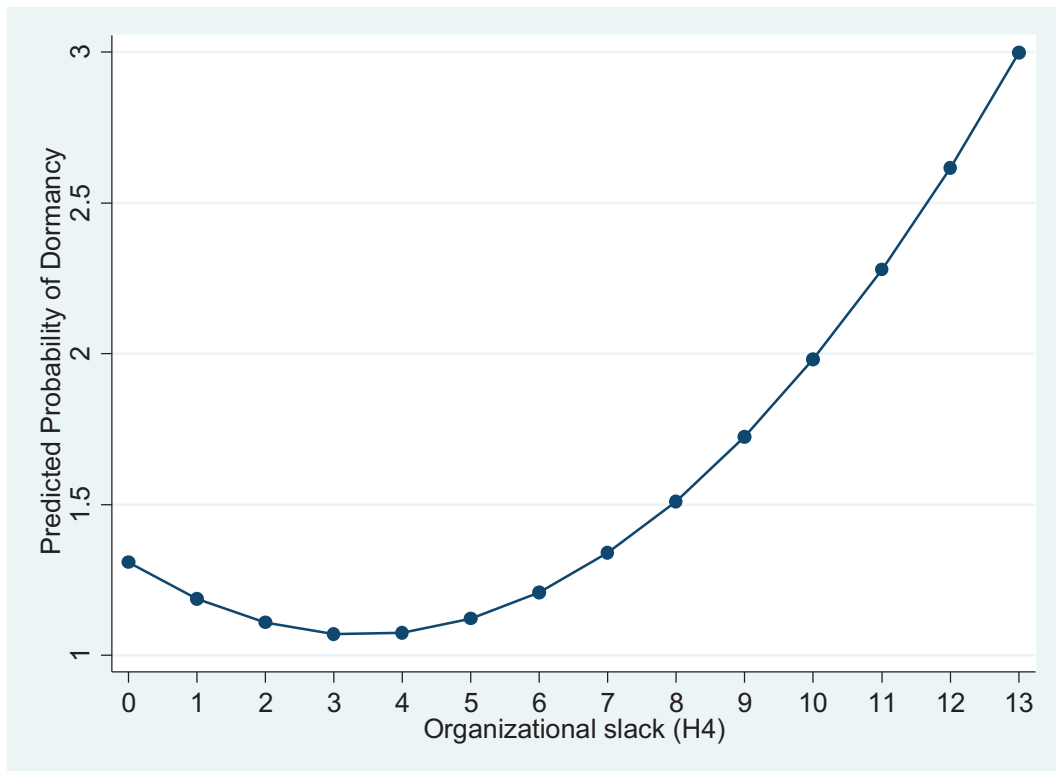


TABLE 5
Branch Expansion into Rural Areas to Conform to Detrimental Public Policy, 1981-2003

Covariates	Model 1	Model 2
Return on assets	-0.489** (0.15)	-0.227 (0.20)
Age	-0.004* (0.00)	-0.002 (0.00)
Size	-0.001** (0.00)	-0.001*** (0.00)
Ratio of deposits to total liabilities	-0.116* (0.06)	-0.104 (0.06)
Ratio of investments to advances	-0.000 (0.00)	-0.000 (0.00)
Political awareness	-0.001 (0.04)	-0.001 (0.04)
Exposure to political pluralism	0.061 (0.04)	0.043 (0.04)
Proportion of rural branches	0.556 (0.31)	0.562 (0.31)
Organizational slack	0.010** (0.00)	0.010** (0.00)
Detrimental Regulation		0.056* (0.03)
Constant	0.342*** (0.08)	0.198 (0.11)
R ²	0.116	0.121
• R ²		.005*

N = 763 firm years for 35 banks

Significance levels: * pd0.05; ** pd0.01; *** pd0.001 (all two-tailed tests)

TABLE 6**Effect of Conformity on Bank Performance, 1981-1990**

Covariates	Model 1	Model 2
Age	0.000 (0.00)	-0.000 (0.00)
Size	-0.000 (0.00)	-0.000 (0.00)
Ratio of deposits to total liabilities	-0.023 (0.01)	-0.024 (0.01)
Ratio of investments to advances	0.007 (0.01)	0.006 (0.01)
Political awareness	-0.007 (0.01)	-0.009 (0.01)
Exposure to political pluralism	0.175*** (0.01)	0.176*** (0.01)
Organizational slack	-0.000 (0.00)	0.000 (0.00)
Conformity		-0.009* (0.00)
Constant	-0.059** (0.02)	-0.049* (0.02)
R ²	0.866	0.869
• R ²		.003*

N = 310 firm years of 35 banks

Significance levels: * pd0.05; ** pd0.01; *** pd0.001 (all two-tailed tests)

TABLE 7

Effect of Net Dormancy on Bank Performance over Time, 1991-2004

Covariates	Model 1	Model 2	Model 3
Age	-0.000* (0.00)	-0.000** (0.00)	-0.000* (0.00)
Size	-0.000 (0.00)	-0.000 (0.00)	-0.000 (0.00)
Ratio of deposits to total liabilities	-0.027* (0.01)	-0.017 (0.01)	-0.017 (0.01)
Ratio of investments to advances	-0.000** (0.00)	-0.000** (0.00)	-0.000* (0.00)
Political awareness	0.019 (0.01)	0.019 (0.01)	0.018 (0.01)
Exposure to political pluralism	0.043*** (0.01)	0.040*** (0.01)	0.040*** (0.01)
Proportion of rural branches	-0.114 (0.18)	-0.113 (0.17)	-0.099 (0.17)
Organizational slack	0.003* (0.00)	0.005*** (0.00)	0.005*** (0.00)
Year	-0.005*** (0.00)	-0.005*** (0.00)	-0.008*** (0.00)
Net Dormancy		0.041*** (0.01)	-9.230*** (2.01)
Year X Net Dormancy			0.005*** (0.00)
Constant	9.566*** (1.23)	9.735*** (1.21)	16.587*** (1.90)
Adjusted R ²	0.37	0.39	0.42
• Adjusted R ²		0.02*	0.05*

N = 418 firm years for 35 banks; Fixed effects for origin states included

Significance levels: * pd.05; ** pd.01; *** pd.001 (All two tailed tests)

TABLE 8
Revival from Dormancy, 1991-2003

Covariates	Model 1	Model 2
Age	-0.04 (0.04)	-0.79*** (0.23)
Size	0.01 (0.05)	-0.00 (0.04)
Ratio of deposits to total liabilities	-7.00+ (4.05)	-8.40* (4.05)
Ratio of investments to advances	-1.17 (0.95)	-0.36 (0.93)
Political awareness	3.04 (2.49)	3.67 (2.46)
Exposure to political pluralism	-3.37 (2.64)	1.81 (3.00)
Proportion of rural branches	61.02 (42.62)	54.62 (42.02)
Organizational slack	1.76*** (0.52)	3.05*** (0.67)
Net Dormancy		84.17** (26.09)
Constant	-2.96 (6.26)	-21.66* (8.56)
χ^2	159.99	170.70
Log Likelihood	-508.46	-503.11
LR χ^2 Test		10.70**

N = 418 firm years for 35 banks; Fixed effects for origin states included

Significance levels: * p<.05; ** p<.01; *** p<.001 (All two tailed tests)