Agency, Firm Growth, and Managerial Turnover (R. Anderson, M. Bustamante, S. Guibaud)

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- Key features
  - Managerial turnover: Sleet & Yeltekin (2001), Spear & Wang (2005)
  - Agency and firm dynamics: Clementi and Hopenhayn (2006), DeMarzo & Fishman (2007)
- Baseline model: modification of DeMarzo & Fishman (2007), but growth induced by replacement

- Timing
    - cash flow realization, truthful report
    - growth opportunity arrival (truthful report)
    - replacement decision (growth decision)
    - managerial compensation
- Solving by backward induction

- Results
  - Replacement probability increases in growth opportunity
  - Possible entrenchment: no replacement after good performance
  - No severance (if growth opportunity arrival is observable)
  - Deferred compensation decreases in growth opportunity
  - Agency problems deteriorate growth
  - Externality of current contracts on the timing of future hires

- Extensions
    - growth opportunity is non-verifiable
        - severance to induce truthful reporting (high growth firms only)
    - growth possible without replacement
        - incumbent can grow the firm after good performance

- Testable predictions

    - High growth firms have higher managerial turnover

    - High growth firms use less deferred compensation

    - High growth firms should use higher severance (if growth opportunity arrival is not publicly observable)

COMMENTS:

- Growth opportunity as a creative destruction driven by replacement
- Infinite horizon extension
- High growth vs. low growth firms
- Jenter & Kanaan (2010): no RPE in CEO firing
- Implementation of optimal compensation
  - high growth $\Longrightarrow$ less deferred pay
- Role of moral hazard
- Managerial risk neutrality
- Initial promise after replacement is always $w_0\Phi$
- Old manager - another firm's innovator?