EXECUTIVE SUMMARY

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The High Cost of Accurate Knowledge?

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Abstract:

The knowledge economy is incredibly hungry for information. In their search for competitive advantage, companies are spending more money into collecting information about the world in which they operate. However, facts don't often speak for themselves. The authors have found that how accurate executives are about their competitive environments can be less important than the way they intrepret this information.

Keywords:

Protective accuracy, Interpretive orientation

Executive Summary:

Measuring Accuracy, Performance, and Change:

The initial step in determining whether someone's perception is accurate is to identify what that individual is trying to perceive. What are executives scanning the environment for? Such research suggests that most executives judge their industries along three dimensions: volatility, growth trends, and complexity.

Volatility:

This dimension measures the reliability of forecasts and the amount of risk associated with a strategic investment. It would seem to follow that companies that have a more accurate perception of their industry's volatility would have an advantage when it comes to creating strategic options.

Growth Trends:

This dimension demonstrates the quantity of resources available to companies in an industry. A CEO's perception of his industry's growth trend would determine how he would balance his company's growth trend would determine how he would balance his company's investments between growth and cost control. An accurate perception of industry growth would seem to lead to a competitive advantage.

Complexity:

This dimension relates to an industry's resources. Unlike growth, complexity refers to the distribution of resources. This dimension determines how interdependent a company's strategic moves are with those of its competitors. To measure the accuracy of managerial along these three industry dimensions, the authors used both survey and archival data.

Does Accuracy Pay?

Utilizing a number of statistical techniques such as regression analysis, the authors explored the relationships between organizational changes, the accuracy of manager' perceptions, and organizational performance. The authors had expected that initial investments in improving the accuracy of senior manager' perceptions would produce increasing returns for a while, then decline. The authors reasoned that early investments in accuracy would augment the quality and timeliness of executives' strategic moves, thus improving performance and facilitating change. Eventually, the returns would become negative as the search for greater accuracy consumed resources and distracted management from generating timely actions. Perhaps surprisingly, research showed that as accuracy decreased, performance got better. A result that seemed counterintuitive. The authors found positive correlations between overestimations of industry growth and profitability, between overestimations of volatility and sales performance and between overestimations of complexity and sales and profit outcomes. In other words, overstating these items leads to greater growth than underestimating them. The authors in their research found no significant correlation between prospective accuracy and the profit or sales that followed.

If Accuracy Doesn't Pay, Then What Does?

Having illustrated that accuracy does not guarantee competitive advantage, the authors turned their attention to the effects of executives' interpretive frameworks. Interpretive orientation can be compared along a number of different dimensions. For example, the degree to which events are interpreted as threats versus opportunities. For this study, the authors have chosen to compare orientations along two dimensions that seem to underlie the categories of threat and opportunity: high versus low controllability and positive versus negative expectations.

High versus Low Controllability.

Executives' attitudes towards situations depend on the degree to which they feel these situations are inside or outside their companies' control. Their sense of controllability derives from opinions about their firms; competencies and available resources. Conversely, that sense of control might encourage inactivity and decline, because executives may not recognize opportunities when they come knocking.

Positive Versus Negative Expectations.

A positive orientation implies enthusiasm about possibilities. Events are seen as opportunities rather than threats. As with controllability, the expectation orientation can play out in many ways. Top executives with a positive orientation may be more willing to take risks and consider new and creative solutions.

Those with negative might be more willing to assume risk because they feel they have less to lose. The authors obtained measures of control and expectations through survey questions. The quantitative findings on interpretive orientations are at least partially borne out in the authors case examples. Of course, the authors are suggesting that accuracy does not matter at all. A firm must have a good knowledge of the industry it operates in. What the authors question here is not the general value of perceptual accuracy but rather its importance to a company's top leadership as opposed to middle or junior managers. Research suggests that perceptual accuracy at the very top levels is actually a source of competitive disadvantage for some firms. Therein lies the paradox. On one hand, leaders should be positive about opportunities. Yet, they shouldn't be overly confident in their ability to control them.

In conclusion, a prudent balance of optimism and pessimism is probably best