DYNAMIC CAPABILITIES AND TOP MANAGEMENT COGNITIONS

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Environmental conditions affect the use of dynamic capabilities and this use is the outcome of managerial behavior that rests on psychological foundations. In this paper, we argue that to improve our understanding of how firms deploy dynamic capabilities we need to understand the interplay of environmental conditions (highly vs. moderately dynamic ones) and the specific decision-making approaches that top manager teams (TMTs) draw on when deploying dynamic capabilities (use of rational reasoning vs. heuristics). Building on extensive literature on heuristics-based decision-making, we argue that as environments become more dynamic, TMTs experience less accessibility to valid and accurate information, leading to decreased predictability of decision outcomes. Accordingly, in highly dynamic environments TMTs predominantly rely on a heuristics-based deployment of dynamic capabilities by ignoring much of the information available to them and focusing on specific cues with the goal of making decisions more quickly, frugally, and/or accurately when compared to drawing on more complex methods. We further argue that the use of a heuristics-based deployment of dynamic capabilities, in such conditions, is effective and enhances firm performance. The accuracy of such processes pertains to the trade-off between bias and variance. Heuristics-based approaches strike a balance between reducing error due to both bias and variance. This insight is in line with fundamental discussion of ecological rationality explaining that the use of heuristics is rational to the degree it matches the structure of the environment. This paper contributes to our understanding of the psychological foundations of dynamic capabilities through clarifying why and how heuristics assist in an effective capability deployment in highly dynamic environment. It also contributes towards offering a more unified explanation of the dynamic capabilities framework.