Firm Decentralization and Growth*

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Abstract

The economic consequences of changing the distribution of power within firms is a fundamental question, yet little is known of the longer-run growth effects of giving more autonomy to local managers. We match direct measures on decentralization of decision rights within firms to output and inputs in two complementary datasets: U.S. Census Bureau and international company accounts across 18 countries. In both datasets we show that decentralization from headquarters to plant managers is robustly correlated with growth over 15 years. We introduce a new IV strategy exploiting the decentralization tendencies of previous parent companies (a "donor firm" method) to show that the positive relationship between decentralization and growth appears causal. We find similar results using an alternative IV based on industry decentralization trends in culturally similar countries. We highlight two mechanisms for the positive effect of decentralization on growth. First, our results are strongest in older firms still controlled by the founder, suggesting some founders may inefficiently hoard power. Second, more decentralized plants perform better when faced by exogenous increases in business opportunities (market size shocks), suggesting they have greater agility. Overall, our results suggest a tendency in firms towards excess centralization.

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