The Dark Side of Promotion Tournaments: The Effect on Losing Competitors

Eric W. Chan
The University of Texas at Austin

John H. Evans III*
University of Pittsburgh

Duanping Hong
Kennesaw State University

Abstract
Firms commonly use promotion tournaments to motivate employee performance. While prior research has examined the incentive effects of such tournaments, we focus on certain additional consequences that arise following the end of promotion tournaments. More specifically, we investigate tournaments for promotion to CEO to explore the consequences in subsequent turnover and career outcomes for non-promoted VPs, whom we refer to as non-promoted executives (NPEs). A CEO promotion tournament could affect NPEs in two ways. First, when NPEs are passed over for promotion, their implicit, promotion-based incentives decline because their future prospects for advancement within the firm are reduced. We refer to this as the incentive effect. Second, the tournament has a sorting role that differentiates participates on their quality, which we refer to as the sorting effect. In our empirical analysis, we find that NPEs are generally more likely to subsequently leave their firms as compared to a group of control VPs from a sample of matched firms that do not have a CEO promotion. This holds for both NPEs who are strong competitors in the tournament and weak competitor NPEs. On the other hand, the job market assesses strong versus weak competitors differently. We find that strong NPEs are viewed more favorably by the job market than similar control VPs, while weak NPEs are viewed less favorably, suggesting that the incentive effect plays a more important role among strong NPEs while the sorting effect dominates in the cases of weak NPEs. We further find that both effects are stronger in firms that do not have an heir apparent prior to the promotion or have one but promote another executive. For firms that promote an heir apparent, we observe similar patterns on NPE turnover and career outcomes at the first stage of the CEO succession process when the firm promotes a VP to be the heir apparent. Overall, our results reveal a more complete picture for promotion tournaments at the top of the corporate hierarchy and their effects on NPEs.