Marris's Theory of The Managerial Enterprise

"In Corporate firms, there is structural division of ownership and management which allows managers to set goals which do not necessarily conform with those of the owners. The shareholders are the owners. Their utility function includes variables such as

profits,
size of output,
size of capital,
market share and
public image.

Marris's Theory of The Managerial Enterprise(contd.)

"

The Managers have other ideas. Their utility function includes variables such as

Salaries,

Job security,

Power and status.

Marris's Theory of The Managerial Enterprise(contd.)

- The owners want to maximise their utility while the managers attempt maximisation of their own utility.
- Both utilities do not necessarily clash, because the most of the variables of both the utilities, have a strong relationship with a single variable
- **i.e., size of the firm.**
- It is reasonable to assume that maximising the long-run growth of any indicator is equivalent to maximising the long-run growth rate of the others.

Marris's Theory of The Managerial Enterprise(contd.)

- Owners being interested in the growth of the firm want maximisation of the growth of the supply of capital, which is assumed to maximise the owner's utility.
- Managers wanting to maximise rate of growth of the firm rather than absolute size of the firm, believe that growth of demand for the products is an appropriate indicator of the growth of the firm.

- There are two constrains in the Marris's Model:
- 1. **The Managerial Team Constraint.**

  Since Management is a teamwork, hiring new managers does not expand managerial capaqcity immediately. New managers take time to get integrated in the team. Managerial tream constraint sets limits to both the rate of growth of demand and rate of growth of capital.
- 2. **The Job Security Constraint.** Managers want job security. Job security attained by pursuing a prudent financial policy which requires the three crucial financial ratios to be maintained at optimum levels.

Policy variables in Marris's balanced growth model are as follows:

- 1. The firm has the freedom to choose its financial policy, as it subjectively determines the three financial ratios, liquidity ratio, leverage/debt ratio and retention ratio.
- 2. The firm can decide its diversification rate, either by expanding the range of its products, or by merely effecting a change in the style of its existing range of products. OR it can adopt the two policies simultaneously.
- 3. Price is not a policy variable of the firm. It is a parameter. Price is taken as given by the oligopolistic structure of the market. Production costs are also taken as given.
- 4. The firm has the freedom to decide the level of it advertising and R&D. Since Price and Production Costs are given, increase in advt. & R&D, will imply lower profit margin and vice-versa.