

Transparency and Innovation in Organizations

Osamu Hayashida,^{*} Kimiyuki Morita,[†] and Takeharu Sogo^{‡§}

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Abstract

We study how transparency affects the incentives to innovate in a two-period model. By transparency, we mean that interim performance measures are observable within the organization just after the first period. In each period, an agent chooses either a new idea or a well-established idea and exerts effort to implement that idea (e.g., converting an idea into products or services). A key feature of the model is that the agent can acquire knowledge while exerting effort, which is partially wasted if the idea is switched with another one. Transparency promotes idea exploration by improving expected idea quality; however, it can be counter-productive if the output relies heavily on implementation effort rather than idea quality because transparency weakens the incentive for idea implementation. Perhaps surprisingly, we show that transparency can be further counter-productive if the acquired knowledge becomes less idea-specific, or if the interim performance measure becomes more precise.

^{*}Faculty of Business Administration, Osaka University of Economics, Japan, hayasida@osaka-ue.ac.jp

[†]School of Economics, Senshu University, Japan, kimiyuki1229@gmail.com

[‡]SKEMA Business School—Université Côte d'Azur, France, takeharu.sogo@skema.edu

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