

1-1-2005

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Philip C.F. Tsai

*National Sun Yat-sen University*

C. Rosa Yeh

*National Sun Yat-sen University*

Shu-Ling Wu

*National Sun Yat-sen University*

Ing-Chung Huang

*National Sun Yat-sen University*

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**Philip C.F. Tsai**

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**Ing-Cheng Huang**

*Institute of Human Resource Management*

*National Sun Yat-sen University*

*Kaohsiung, Taiwan, ROC*

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Philip C.F. Tsai  
C. Rosa Yeh  
Shu-Ling Wu  
Ing-Chung Huang

Institute of Human Resource Management  
National Sun Yat-sen University  
Kaohsiung, Taiwan, ROC

(Accepted by International Journal of Human Resource Management, November 2004)

## **Abstract**

Frooman's (1999) model of stakeholder influence strategy uses levels of resource dependence to determine the power of stakeholder influence. Our study provides initial empirical tests of his model applied in business downsizing. Data from 18 recently downsized firms in Taiwan, including 9 multi-national firms (MNC's), were plotted against the Frooman model. We found that resource-dependence along as Frooman theorized could not explain the influence strategies stakeholders (in this case the employees) took in response to firms' downsizing decisions. Further investigation revealed that the institutional factors had a significant effect on how firms structured their downsizing initiatives and hence changed the way the employees reacted to firm decisions. We proposed a new model using both resource-dependence and institutional legitimacy as determinants of stakeholder influence strategy and suggested relationships between these determinants and stakeholder actions. This proposed model has profound research implications for the strategic stakeholder theory, as well as practical implications for human resource management.

Key words: Stakeholder, Downsizing, Resource-dependence perspective, Institutional theory

## **Introduction**

Freeman (1984) first introduced the concept of stakeholder theory to the mainstream management theories. It has since become an integral part of the management literature (Donaldson & Preston, 1995). However, a lack of empirical evidence has limited the

application of stakeholder theory in a theoretical development stage. Frooman (1999) presented a theoretical framework of stakeholder influence strategy in the *Academy of Management Review*. Based on the resource-dependence theory, he proposed four strategic styles which stakeholders use to influence business decisions. His innovation is extremely helpful in explaining and predicting the strategies and actions firms and stakeholders adopt against each other in a conflict situation. Frooman's contribution is instrumental because this framework expanded beyond conceptual iteration and made empirical research of the stakeholder influence strategy theory possible.

Since the 80s downsizing has been a popular management strategy around the globe, a strategy that protects the interest of the enterprises at the cost of the well-beings of employees and their families (Mckee-Ryan & Kinicki, 2002). Under the conflict of interest, the internal stakeholders of a business, i.e., the employees, are bound to respond with resistant or disruptive strategy. At the same time, depending on the scope of downsizing, some external stakeholders such as the state, the media or some labor groups will also show their concern, escalating a business downsizing to a public event. How the internal stakeholder and the business react under the situation is an interesting issue worthy of further investigation. It also provides a perfect setting for an empirical test of the "stakeholder influence strategy theory".

Our research used a case study approach to provide empirical evidence to the stakeholder influence strategy perspective. Frooman's propositions were tested with data from 18 recently

downsized companies. Research and management implications were provided to further theoretical development of the perspective.

## **Theoretical Background**

### **Strategic stakeholder theory**

The stakeholder theory has become an indispensable part of the management literature (Donaldson & Preston, 1995). Frederick (1992) classified stakeholders into internal, external, key, and secondary ones, each carrying a different level of influence to the enterprise. When analyzing from the social network perspective, a firm does not deal with one stakeholder at a time, but multiple stakeholders simultaneously, with interdependent relationships among these stakeholders (Rowley, 1997). Consequently, the relationship between firms and their stakeholders are as complex as the ways to manage them. The premise of stakeholder theory is that firms are bound to have conflicts with their multiple stakeholders. The central issue of stakeholder research is thus how to minimize these conflicts.

Within the stream of stakeholder research, Frooman (1999) took the approach of deciphering stakeholder actions and developed his stakeholder influence strategy theory from a resource-dependence perspective. As Frooman theorized, the type of resource relationship between the firm and its stakeholder determines where the power lies in the exchange. The level of “resource dependence” depends on the attributes of a resource, such as the relative

magnitude of exchange in a resource relationship and the criticality of that resource. For example, if the firm depends on the stakeholder for a critical resource for survival, the stakeholder will have absolute power over the firm, and vice versa. Furthermore, the balance of power will determine the stakeholder's choice of influence strategy. Frooman quoted Willer, et al (1997: 573) in defining power as "the structurally determined potential for obtaining favored payoffs in relations where interests are opposed". An asymmetrical relationship occurs when one party has power over the other party in an exchange. This asymmetrical relationship provides opportunities for one party to gain control over the other party.

Two important features marked Frooman's discussion of stakeholder influence strategies: the way the stakeholders control resources, and the path the stakeholders take to manipulate the supply of resources. If a stakeholder owns resources that a firm needs, the stakeholder can control the firm by determining whether the firm gets the resources and whether the firm can use the resources in the way it wants. Frooman called these "resource control strategies", and differentiated between two types of resource control strategies: withholding and usage.

Withholding strategies are defined as those where the stakeholder discontinues the supply of a resource to a firm with the intention of making the firm change its action. Usage strategies, on the other hand, "are those in which the stakeholder continues to supply a resource, but with strings attached" (p. 197). For example, a strike is a withholding strategy carried out by employees; basing a continuation of supplies on a price increase or a change in contract deals

is a common usage strategy used by suppliers. Because these two strategies carry different costs to the stakeholder, cost consideration sometimes become key determinant in the choice of influence strategy.

Another important feature of Frooman's theory was the choice of "paths" a stakeholder takes to exert influence on the firm. Two path-related strategies were defined in his model: direct and indirect. Direct strategies are "those in which the stakeholder itself manipulates the flow of resources to the firm" (p. 198), and are often used when the resource relationship is a continuous one, such as those between a firm and its employees, or a supplier and its customers. Indirect strategies are "those in which the stakeholder works through an ally, by having the ally manipulate the flow of resources to the firm" (p.198). These allies can be called indirect stakeholders, but they often possess important resources to the firm which can be held hostage to sway firm decision. For example, employees often call upon the general public or the government as an indirect stakeholder to correct a firm's unethical employment practice.

Based on the balance of power in a resource relationship, Frooman presented the following four propositions for the four strategy types in his model of stakeholder influence strategy:

- 1. When the relationship is one of low interdependence, the stakeholder will choose an indirect withholding strategy to influence the firm.*
- 2. When the relationship is marked by firm power, the stakeholder will choose an indirect usage strategy to influence the firm.*

3. *When the relationship is marked by stakeholder power, the stakeholder will choose a direct withholding strategy to influence the firm.*
4. *When the relationship is one of high interdependence, the stakeholder will choose a direct usage strategy to influence the firm.*

*--Frooman, 1999, p. 202*

Frooman's model of stakeholder influence strategy was a significant step up in the direction of predicting stakeholder choice of action attempted to influence firm decision, and should have generated some research interests to test his propositions empirically. However, even Frooman himself had pointed out that the difficulty of carrying out such an empirical study lies not on the decision of who is dependent on whom, but on the estimation of the level and the scope of the dependence. That is probably why we were unable to find any empirical test of Frooman's model. We believe a test of his model is much needed and long over due. Moreover, as HRM researchers, we are particularly interested in the validation and application of the model in HR-related phenomena, for example, what transpires after a business decision to downsize. Is this model viable in explaining and predicting employee action as internal stakeholder influence strategy during a business downsizing? As downsizing remains a popular operational strategy, the jobs and the lives of thousands of employees are affected every day globally. It has become increasingly important for firms to predict and to manage how these employees react to a downsizing decision in order to minimize fatal damages to

employee relations and employee trust. We expect the process of validating Frooman's model in a downsizing scenario will shed much needed light on this issue.

### **Business downsizing**

Downsizing has become one of the perpetual trends in business world since the 80's (Mckee-Ryan & Kinicki, 2002, Landry, 2004). The merger and acquisition trend propelled by wide-spread globalization strategy, technical advances and economy of scale also leads businesses to downsizing (Hirschman, 2001). It is a popular and long-lasting business tactic (Fisher & White, 2000) which is also satirized as euphemism for a large-scale layoff (anonymous, 2001). Downsizing not only brings all the devastation of losing a job to an employee (Greenhalgh, Lawrence & Sutton, 1988), but also chaos to the employee's family, eventually affecting the entire society. Employees may suffer economical, physical, social, interpersonal, even psychological devastations during a business downsizing (Naumann et.al., 1995; Mckee-Ryan & Kinicki, 2002). Because of the magnitude of devastations, employees are bound to resist or even obstruct business decisions to downsize.

In the mean time, because of the stress and tension of unemployment in the society following a large scale downsizing, external groups such as the government or the community will exhibit their concerns or even condemn the employer for doing so. The external groups will check closely to see if the downsizing practice follows the laws and regulations, if the firm upholds its social responsibility, and whether the practice stands a test of business ethics. In

short, they want to know if the downsizing is “legitimate” (Yeh, 2000). Companies that are sensitive to external scrutiny will tend to evaluate their downsizing practices more carefully, taking a less drastic approach to avoid public attention.

#### **A-rational factors of downsizing—Influence of institution on firm behavior**

From a rational view, the amount of influence a stakeholder has upon a firm can be estimated from the degree of interdependence between the firm and the stakeholder in a resource relationship. However, we suspect some a-rational factors, such as those imposed by the institution, may have some bearings on the resource relationship. When organizational behaviors conform to the institution, firms gain institutional power. This institutional power may work against the stakeholder in a resource relationship, and hence change how the stakeholder selects its influence strategy.

Meyer and Rowan (1977) defined institutionalism as “the processes by which social processes, obligations, or actualities come to take on a rulelike status in social thought and actions”. (p. 341). Oliver (1997a) called these processes “the social construction of reality”. Institution reaches its highest point when individuals in a group accept a shared definition of reality (Scott, 1987). Legitimacy is the main concern of many institutionalists. To gain legitimacy, firms must operate under a framework approved by social norms and values, with appropriate structure and economic behavior. Numerous studies had supported that when firms display isomorphic behaviors that conform to social norms and expectations, they gain

legitimacy, resources and skills that are critical to firm survival and success. (Baum and Oliver, 1991; Carroll & Hanman, 1989; DiMaggio & Powell, 1983; Oliver, 1991; Scott, 1987; Oliver, 1997a, b) McKinley et. al. (2000) argued in their institutional downsizing theory that when firms adopt practices that conform to the prevailing culture and norms, it reduces uncertainty and ensures legitimacy. Therefore, when downsizing becomes a social convention, it is institutionalized into an ethically acceptable social reality that can be tolerated by the stakeholders. That is, when business behaves within social expectations (i.e., conform to social norms, isomorphic behaviors and ethical business conducts), it gains institutional legitimacy. The higher the legitimacy, the stronger the power to the firm and the weaker the stakeholder influence.

The implication of institution is that firms do not develop strategies simply by looking at the result of a rational evaluation. Accordingly, firms do not shape their downsizing practice simply by a rational analysis of resource dependence. Therefore, it is not wise for stakeholders to rely only on a rational assessment of mutual resource dependence to determine the strength of their power when selecting an influence strategy to counter firm's downsizing decision. We believe during a business downsizing, both the employer and the employees will choose a strategy based on an estimation of own power and the power of the counter party, similar to what Frooman had proposed in his stakeholder influence strategy model. However, we also believe that the strength of power is not determined solely by the level of mutual resource

dependence. We suspect that institutional legitimacy also plays an important role in predicting stakeholder choice of influence strategy because firms operate to fulfill not only economic objectives but also social objectives. Combining resource-dependence theory with institutional theory has also become a recent trend in management research; see Sherer & Lee (2002) or Abidin & Taylor (2002) for an example.

## **Research Methodology**

This research adopts a qualitative approach because of the complex cognition and human interaction involved in the event of a corporate downsizing. A qualitative approach is better at examining the uniqueness and the causes of HRM practices (Sherer & Leblebici, 2001).

### **Sampling**

We conducted empirical investigation on 18 Taiwanese business downsizing cases. We chose nine MNCs (Multinational Corporations) and nine Taiwanese indigenous companies to allow comparison of the stakeholder influence strategies among different country origins. Taiwan is an important emerging economy in the Asia Pacific region, ranking 15<sup>th</sup> in international trade annually. The World Economic Forum ranked Taiwan 5<sup>th</sup> in the 2003 Global Competitiveness Report, recognizing its significance in the global economic society. Its economic environment renders vitality and depth in international management research.

We targeted long-standing companies with a significant employee size and a recent

downsizing experience. Companies in both the service and the manufacturing industries were contacted in order to generalize research findings across industries. Of the companies which agreed to participate in the study only 18 fit the description of our target. Profiles of the 18 selected companies are presented in table 1. These companies were large and representative in each of their respective industries. The parent companies of our MNCs sample were well-known companies globally. All of these companies had performed large-scale downsizing<sup>1</sup> recently, which had a tremendous impact on the firms and the employees.

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Insert table 1 here.

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### **Data collection**

This research uses key informant method as its primary approach for data collection. To avoid reliability issue generally arises from collecting data from a single informant, we used multiple data sources when possible from both management representatives (firm) and labor representatives (stakeholder). Management representatives were higher level executives, while labor representatives were leaders of the unions or, when there was no union present, selective employees. Information provided from both sides was cross examined to ensure accuracy. Data were collected through the use of interviews and survey questionnaires. First, we conducted several exploratory focus group interviews of important actors during a business downsizing (i.e., members of the top management team, HR managers and union members) to uncover

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<sup>1</sup> According to Tomasko (1990), a cut in workforce between 5-15% can be defined as a large-scale downsizing

significant themes and events. Then, we designed a 45-item, semi-structured survey as our instrument for data collection and pilot tested it at one company to six participants.

At least four informants were sought in each case company to complete the survey. Once the surveys were completed, follow-up interviews were arranged to understand the background of the downsizing and the sequence of the events afterwards. Additional focus group interviews with union leaders were also conducted to collect information on how they found support from external stakeholders in a downsizing scenario.

Since there were multiple informants at each case company, we followed the procedure below to clean the data when differences were found among informants: 1) top-management perspective was used when the questions were related to corporate level strategy and policy; 2) HR manager perspective was used when HR management practices were the concern; 3) line manager perspective was used when the questions involved technical know-how's such as process re-engineering, work re-design, etc.; 4) as far as employee perceptions and sentiments were concerned, union perspective was used.

## **Analysis and Discussion**

Employees are key internal stakeholders during a business downsizing. In Frooman's 1999 framework on stakeholder influence strategy, he developed four strategy types based on the power derived from the level of resource-dependence between an organization and its stakeholders. Thus we began our analysis by assessing the balance of power between the case

companies and their employees in order to derive expected stakeholder influence strategy in Frooman's model. We then compared the expected strategy with actual strategy taken by stakeholders at each case company. The result of this comparison became the basis of our subsequent analysis and discussion of other potential determinants of stakeholder influence strategy. Of these determinants, institutional factors such as the legitimacy of firm decision were found most critical and were emphasized as such. An improved stakeholder influence strategy framework was proposed taking into consideration both the power of resource dependence and legitimacy of firm decision. This section presents the procedures and the results of our analysis as well as the discussions that lead to our proposed theoretical framework.

#### **Assessment of resource dependence between firm and stakeholder**

We measured a firm's dependence on its employees by assessing how much the employees possess core competencies of a firm. Conversely, external labor market demand for employees' competencies was the indicator of employee dependence on the firm. The more the employees possess firm required competencies, the more the firm depends on the employees for survival. The lower the external market demand for employees' competencies, the more the employees depend on the firm for living. These two factors greatly affect employees' resource capability and bargaining position, and hence are adequate determinants of power in a downsizing scenario. For instance, employees in case companies A, CT, H2, PH and S, with medium to

high proficiency level of firm-specific competencies and high opportunity in the external market, attained a superior bargaining position. These were situations of stakeholder power which gave employees more leverage to choose their influence strategy. In contrast, for those employees in CB and NY, whose firm-specific competencies and demands from external market were low, put themselves in a very weak bargaining position. These were clearly the situations of firm power. Employees in case companies B, F1, H1, M, and SJ, with low levels of firm-specific competencies and moderate opportunities in external market, had a weaker bargaining position and might be tempted to look outside their company. Table 2 summarizes where the employees stood on these two factors for each case company. We used a 7-point scale (0-6) to convert their standings to levels of dependence for subsequent analysis.

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Insert table 2 here.

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### **Expected stakeholder strategy based on Frooman's model**

To better visualize expected stakeholder strategy taken by the employees, the relative position of each case based on the level of dependence between a firm and its employees was plotted on a four-quadrant strategy matrix as specified in Frooman's theoretical model. As seen in figure 1, the *x* axis stands for the level of stakeholder dependence on the firm, while the *y* axis stands for the level of firm dependence on stakeholders.

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Insert figure 1 here.

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Figure 1 shows five companies (i.e., CT, A, H2, PH, S) resided in the "stakeholder power"

quadrant where the level of firm dependence on stakeholder was apparently higher than the level of stakeholder dependence on firm. Based on Frooman's model, the stakeholders of these firms, i.e., their employees, were expected to use direct withholding strategy to counter the firm's downsizing action. In contrast, two companies (i.e., CB, NY) fell under the "firm power" quadrant where stakeholder dependence on firm took precedence over firm dependence on stakeholder. According to Frooman, the stakeholders should have adopted an indirect usage strategy to influence the downsizing decision. Both the firm and the stakeholders of case company C were highly dependent on each other, and therefore the appropriate course of action taken by the stakeholders should have followed a direct usage strategy. On the opposite end, neither the firm nor the stakeholders of case company H1 were highly dependent on each other, and thus an indirect withholding strategy was expected.

The expected influence strategy of some case companies were not as clear cut as those mentioned above. As shown in figure 1, with a low stakeholder dependence on firm, and a medium firm dependence on stakeholders, the viable strategy for companies Y and P could have been either direct withholding or indirect withholding. In T1's case, with a medium stakeholder dependence on firm and a slightly larger firm dependence on stakeholders, the direct withholding or direct usage strategies were both reasonable. On the contrary, L, B, SJ, F1, and M companies were expected to adopt either of the two indirect strategies because of their medium stakeholder dependence on firm and lower firm dependence on stakeholders. We

cannot predict from Frooman's model what the stakeholders of case company TL should have acted to the firm's downsizing decision because both firm dependence on stakeholders and stakeholder dependence on firm were at a medium level, which put TL right at the center of the matrix.

### **Actual strategy by stakeholders**

Our research uncovered a completely different picture of the actual strategies taken by stakeholders at our case companies. Table 3 reveals how employees at these companies acted to influence firm decisions in the event of a downsizing. Except the employees at case company A, SJ, M and TL who seemed to have subjected themselves at the mercy of their firms, most employees had taken the direct usage strategy to negotiate with their employers. Some conducted these negotiations with strings attached (B, C, F1, H2, L, H1, NY, CB), some bargained with the added power of third-party mediators (PH, L, P, CB).

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Insert table 3 here.

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Contrasting the actual influence strategies taken by the employees of our case companies, we found very significant differences from the expected strategies we derived from Frooman's model (see figure 1). All the internal stakeholders at our case companies, with the exception of firm C, had chosen their strategies that were miles apart from what were expected during a downsizing event. In the cases of CT, H2, S, P, and PH, where the presence of a stakeholder power was strong, the employees had forgone a direct withholding strategy and instead

surrendered to a direct negotiation with strings attached. Cases P and PH even threw in the help of external stakeholders during the negotiation, adding an indirect dimension to their direct influencing strategy. Although the stakeholders had marginal power over the firms, cases T1 and Y were also resolved to a direct negotiation with strings attached. Interestingly, the “direct negotiation with strings attached” strategy applied to the cases H1, F1, and B where the internal stakeholders had relatively weaker power than the firms. Even the employees at cases L and CB, where firm powers were more dominant, negotiated directly with the firms on downsizing terms. To our surprise, employees at the stakeholder dominant case A and the neutral case TL took the same position as the weaker cases SJ and M--at the mercy of the firms. None of them displayed any collective effort to influence the firms’ decision and terms to downsize, and therefore could not be placed on any of the four quadrants using Frooman’s model. As shown in figure 2, deviations of the actual stakeholder strategies are drastic from the expected stakeholder strategies.

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Insert figure 2 here.

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### **Explanation of divergence between expected and actual stakeholder strategies**

To address the question of why there was such a divergence between the expected and the actual stakeholder strategies at our case companies, we looked for other determinants that might impact how the internal stakeholders reacted to a firm’s decision to downsize.

Stakeholders’ consideration of costs (Frooman, 1999) might have rationalized a move from the

direct withholding to the direct usage strategy, because a strike or a sabotage against an employer might incapacitate business operation causing lost revenues and profits which would translate into a lower employer ability to compensate the employees. A direct usage strategy gave the employees the opportunity to negotiate a better deal for laid-off employees without the social costs that might accrue to the employees and other external stakeholders due to confrontations of a direct withholding strategy. Therefore, it is explicable why a direct usage strategy is preferred by employees with dominant stakeholder power during a downsizing event.

However, when stakeholder power was weak, it seemed reasonable to assume that stakeholders could only adopt an indirect strategy as Frooman predicted, by inviting external stakeholders to influence the firm's decision, instead of negotiating directly with the firm using the "strings attached" approach like our case companies did. This huge deviation from Frooman's model spawned another level of analysis in our research. We looked into other factors that might provide a more adequate explanation to our findings. Two factors provided most useful clues to the situation: 1) a lack of external stakeholder power, and 2) high legitimacy of firm's downsizing decision.

### **Lack of external stakeholder power**

From our interviews, we found that most of our case companies had certain linkages to a variety of external stakeholders, forming a complex web of enterprise stakeholder network as

shown in figure 3. Of these external stakeholders, Union federation and the government labor department were two external stakeholders whom employees would most likely have sought help from. However, since these external stakeholders were tertiary to a firm's survival, they did not have enough stakeholder power to influence a firm when the firm had strong legitimacy for downsizing. In our study, except the state-owned case company CB whose external stakeholders could tap into the political resources of the ruling party to exert harsher pressure to the firm, external stakeholders in all our other cases could only do as much as expressing concerns and pleading for better severance packages or referral arrangement on behalf of the employees, as was the case in companies PH, L, and P when external stakeholders were involved in the negotiation.

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Insert figure 3 here.

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The comment made by the representatives from the Petro-chemical Union Federation in our focus group interviews was most descriptive.

*“... union federations and government labor officials are often sought by individual unions for assistance. ...The decision to bring in other social resources depends on how serious the matter is and availability of that resource. External resources are usually brought in one after another instead of altogether at the same time. However, the most fundamental strategy, and most effective too, is for employees to negotiate a resolution directly and internally with their employer, because external social*

*resources come with a cost. ... When a firm undergoes workforce reduction without violating any labor laws or regulations, then all that the federation can do is to try their best at helping the member union get a better severance deal for their employees.”*

It was clear from our analysis that external stakeholders in our cases did not have enough power to influence firm decisions because the resources of these external stakeholders were not critical to the firms. Moreover, these firms had worked within the legal lines to avoid any interference from government officials. When external stakeholders did not have enough power to influence the firm, the internal stakeholders (employees) would have to stand up on their own. Frooman had also posited that when employees were the internal stakeholders, it was better for the employees to adopt a direct negotiation strategy with the firm. However, when looking at the findings from the employers’ angle, one couldn’t help to wonder why firms tolerated the “direct negotiation with strings attached” strategy when their dependence on the employees was only moderate, and their actions were legitimate? It seemed using resource dependence perspective alone could not explain what happened at many case companies, especially NY, B, F1 and H1. A recurring theme in our interview data brought institutional factors to our attention.

### **Institutional Legitimacy**

We define institutional legitimacy as behaviors that comply with the social norms, that is, they are similar to those of the peer groups, and are within the boundaries of legal requirements,

business ethics and social expectations. A look at the downsizing practices at our case companies, we saw very clearly the effect of institutional factors at play. Not only the motives, actions and practices bore resemblance to one another, the strategy to buyoff stakeholders were also very similar. For instance, as presented in table 4, “stagnant or declining profitability”, “whole system organizational change”, “directive from a superior organization”, and “industry benchmark” were cited by most companies as key motives for downsizing. In terms of downsizing strategy, most firms took a slower and gradual course of action instead of a radical cutback. Even when more radical measures were necessary, firms would layoff employees in batches instead of all at once. Moreover, these workforce reduction actions were almost all tied to business reengineering processes or a whole organizational system change. Employee performance was the main factor for selecting targets.

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Insert table 4 here.

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All cases in our study had reduced their workforce in a way that complied totally with the law and regulations. Almost all provided layoff schemes superior to what the law and regulations had specified (see table 5). Why would companies do that? It could be that companies do these out of a strategic concern for the employees to ensure a win-win situation. But more possibly, companies were merely displaying institutionalized conducts that met social expectations at the time. The sample in our study was drawn in Taiwan, a Chinese society where Confucianism is still the predominant culture. Confucianism emphasizes a value

system which maintains social order and harmony. Organizations are required to follow a set of moral standards or ethical behaviors that conform to “jen-i” in order for the society to prosper and grow in the long term (Graham& Lam, 2003). “Jen”, or kindness, is to treat the others kindly, and “i”, or righteousness, is to act with righteous cause.

In a Confucian society, firms usually take up a paternal role to their employees, therefore it is a common practice to offer more monetary compensation to terminated employees. It is the ethical way, and the only way the society would allow. Although our sample included foreign companies and joint ventures, these companies tended to adopt similar practices to local companies. That is, they negotiated with employees with employees’ well-beings in mind and resolved any disagreement in a peaceful manner when downsizing. This might explain why, except cases A, M, TL, and SJ, all of our other cases were willing to engage in productive negotiation with their employees. Since the firm was open for negotiation, as the internal stakeholders, the employees were most certainly willing to take a higher power position and reacted to the firm’s decision to downsize with a direct usage strategy, regardless of what position their power had entitled them to. Although they could not stop the firm from downsizing because the firm had very legitimate reasons for doing so, they could acquire a better deal for employees through negotiation. To employees with less power in the company, their winning came from losing less.

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Insert table 5 here.

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An important external stakeholder in the downsizing matter, a county government official in charge of labor relations, described his view on how institution affected downsizing disputes:

*“The labor department can not help the employees reinstate their jobs if their employer acted in accordance with all legal guidelines, ... unless a powerful union is willing to challenge the legality of the downsizing. However, that is a very time-consuming ... and complicated way. Our position favors mediation whenever possible, asking the employer to offer better severance deals to employees. Our objective is to avoid direct confrontation or disputes. ... It is better to achieve a win-win resolution, since peace and harmony are what the society expects.”*

From the above analysis, we believe institutional factors helped shape firm’s decisions on how downsizing was carried out, and those decisions consequently affected how stakeholders reacted to the downsizing event. Because of this reciprocal influence process, a majority of stakeholders in our study found the results of the downsizing acceptable.

### **A new model of stakeholder influence strategy and propositions**

We have shown in the above discussion that resource dependence theory alone did not adequately predict stakeholder influence strategy in a business downsizing scenario.

Institutional legitimacy was another key variable. We adjusted Frooman’s model to include the dimension of institutional legitimacy and combined the two variables in a theoretical

framework as shown in figure 4. In this new model, we changed the  $x$  axis to indicate the level of legitimacy of firm decision, while  $y$  axis still represented the level of firm dependence on stakeholder. Four new propositions are developed from each quadrant of the new model to predict internal stakeholder influence strategy in a downsizing event. Our arguments for the predicted stakeholder influence strategy in each of the four quadrants follows.

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Insert figure 4 here.

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***Low legitimacy/low dependence quadrant:*** When a firm does not have a justifiable cause for downsizing, or adopts layoff practices which do not conform to social norms or legal requirements, its decision and subsequent actions to downsize constitute a low level of institutional legitimacy. These illegitimate actions, such as layoffs without advance notice, a reluctance to communicate with employees, or the use of dirty tricks to avoid severance pays (e.g., forcing employees to quit using inappropriate tactics such as relocating employees to remote areas or to unsuitable jobs against their wills), create strong negative emotions in employees, so much so that employees are likely to withhold their supply of labor to the employer. However, since the firm has a low dependence on the employees' labor, a direct withholding strategy will pose a higher cost to the employees than to the employer. Thus, a rational alternative for the employees in a weaker bargaining position is to ally with other stakeholders powerful enough to influence employer decision. For example, government labor department officials are often involved in illegitimate layoff cases to stop illegal downsizing

practices or to force employer compliance to labor laws and social norms.

**Proposition 1:** *When firm dependence on stakeholder is low, and the legitimacy of firm decision is low as well, the stakeholder will choose an indirect withholding strategy to influence the firm.*

**Low legitimacy/high dependence quadrant:** When the legitimacy of firm decision is low (for example, downsizing while the firm is still making money), but the firm is highly dependent on its stakeholder (for example, the firm needs to retain a large number of employees to run properly), the stakeholder will have more power over the firm. In this situation the stakeholder can take advantage of its own power and block the resources to the firm simply by a walkout or a strike. A rational firm will usually respect that power and adopt preventive measures to avoid provoking further employee resentment. Therefore a direct withholding strategy is the most effective stakeholder strategy when the stakeholder has more power.

**Proposition 2:** *When firm dependence on stakeholder is high, yet the legitimacy of firm decision is low, the stakeholder will choose a direct withholding strategy to influence the firm.*

**High legitimacy/low dependence quadrant:** When the legitimacy of firm decision is high, and the firm dependence on the stakeholder is low, the relationship between the firm and the stakeholder is marked by firm power. In the case a firm has very legitimate reasons to cut a workforce that is easily replaceable and does not break any laws or ethics in implementing it, there is hardly anything the employees can leverage on to counter firm decision. And since the

firm acts in accordance with the social rules, other stakeholders are in no position to interfere. This is the worst scenario for the employees. Therefore, under firm power, the stakeholder has no choice but to conform to firm decision. Other stakeholders such as social groups or government officials can help by showing their concerns for the employees' well-beings and that may be able to get the employees a slightly better severance deal. However, that will be entirely at the mercy of the firm. Therefore, when the exchange relationship is marked by firm power, the best the stakeholder can do is to use an indirect usage strategy.

**Proposition 3:** *When firm dependence on stakeholder is low, yet the legitimacy of firm decision is high, the stakeholder will choose an indirect usage strategy to influence the firm or conform to firm decision.*

**High legitimacy /high dependence quadrant:** When the legitimacy of firm decision is high, and the firm dependence on the stakeholder is high as well, there is a counterbalance of power between the firm and the stakeholder. In the case of a well-justified downsizing event, other stakeholders cannot find a good cause for their intervention, and since the employees possess power from the firm's dependence on them, neither are other stakeholders needed in the battle. In a counterbalanced relationship, it is rational for both parties to compromise and to share the cost of the final resolution. Firms are more likely to be vigilant and more willing to involve stakeholders in the downsizing decision to minimize the possibility of jeopardizing the trust, feelings and commitment of other existing employees. Thus a high-cost withholding strategy is

not favorable in this situation. The employees are more likely to continue supplying their labor while negotiating terms of the downsizing (such as a favorable buyout package) directly with the firm.

**Proposition 4:** *When firm dependence on stakeholder is high, and the legitimacy of firm decision is high as well, the stakeholder will choose a direct usage strategy to influence the firm.*

In addition to the above four propositions, we would also like to acknowledge the phenomenon of a strategy shift or a merge of different strategies due to the dynamic nature of strategy selection. For example, when the legitimacy of firm decision is low, the stakeholder is likely to use a withholding strategy (direct, indirect or both) first to force the firm into the negotiating room, then a usage strategy to close the deal. Take downsizing for instance, when a firm conducts illegitimate layoffs, it is common for employees to use one of two methods to force the management into negotiation: a strike or a threat by the labor department officials to close down business; both are withholding strategies. Once the management is willing to negotiate with the employees, the employees can then shift to a softer usage strategy to find a mutually acceptable resolution with their employer. Sometimes, external stakeholders such as politicians or government officials are brought in to do the initial negotiation on behalf of the employees before the firm communicates directly with these employees on final severance terms. Therefore, a static theory of stakeholder influence strategy like Frooman's and ours,

though may be helpful in predicting stakeholders' initial strategic attempt, may not fully encompass the actual actions as an event unfolds.

### **Initial test of the new model and propositions**

After the development of our new model, we conducted an initial test using datasets of our sample case companies presented earlier. We estimated the legitimacy of firm decision on downsizing on a scale of 0-6 from a few indicators available to us. These indicators included justifiable causes for downsizing, downsizing practices that conform to labor regulations, advance notice, severance packages that are superior to legal requirements, and availability of outplacement services. The first two indicators were considered the most important in estimating legitimacy of downsizing, companies that satisfied these two requirements were thus given the average score of 3. One extra point was added to the legitimacy score when an additional indicator was present at each case. Table 6 shows the result of our legitimacy estimates and the dependence estimates from table 2.

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Insert table 6 here.

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We then plotted the expected stakeholder strategies in our new model and compared those to the actual stakeholder strategies. (See figure 5.) Comparing figure 5 with figure 2, it was clear that our datasets fitted a lot better in the new model. Not only the actual strategies of all case companies now found their positions in the new model, the deviation of cases from model prediction was also significantly reduced. The initial evidence proved that our new model

offered a better prediction of stakeholder influence strategy at least in the downsizing scenario. Moreover, the deviated cases could be better explained in the new model. Except case company A, all the deviated cases follow the same pattern and move from a weaker indirect usage/conformity strategy to a better-positioned direct usage strategy. This was most likely due to a strategic shift in response to the firm's good will in involving the employees in the downsizing decision early on. A direct usage strategy was less costly and more effective to the stakeholders than an indirect strategy, therefore was adopted when the firm provided the opportunity. These deviations thus render partial evidence to our argument of a dynamic interplay when stakeholders select influence strategies.

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Insert figure 5 here.

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## **Conclusion and Implications**

### **Conclusion**

Our research uncovered another level of complexity in the choice of stakeholder influence strategy than what Frooman had proposed in 1999. Resource dependence between a firm and its stakeholders alone can not fully explain how stakeholders choose their influence strategy to counter firm decision. The other actor in the dispute, the firm, will not only consider rationally its dependence on the stakeholder, but will also need to conform to social norms and institutional rules, forcing it to provide better deals and opportunity for direct negotiation with

the stakeholders. When firms downsize with legitimacy, i.e., with justifiable cause and a severance package that adheres to ethical and legal rules, the stakeholders, internal or external, will not be able to stop the downsizing decision. The best they can do is to negotiate for fairness in implementation, reduction of workforce in a smaller scale and more favorable severance deals. Therefore, we believe institutional legitimacy is another important variable in predicting stakeholder influence strategy.

We did not find significant difference in the choice of stakeholder influence strategy between employees of MNC subsidiaries and those of local indigenous companies. An interesting finding was on the degree of attention between foreign companies and local companies on ethical business conduct. Foreign companies placed a high emphasis on business ethics that met social expectations. They were also the ones cared most about company image and social responsibility. MNC subsidiaries in Taiwan followed the local institutions strictly when carrying out their workforce reduction schemes. As the HR executive of one well-known banking MNC in our sample said: *“We follow the directive of our parent company in business operation strategies, but rules and norms of the local institutions are the principles to live by during implementation.”* We did not find the same degree of attention on social norms from joint ventures, local private enterprises and state-owned companies, although most of them still displayed a medium to high degree of efforts in conforming to institutional pressure. Only a few firms showed their disregard to institutional rules, for example, local private enterprise NY

and joint ventures SJ and M. Common characteristics of these companies included a low dependence on employees, radical downsizing strategies, unacceptable severance packages and a lack of employee communication or negotiation. These practices did not comply with the institutional environment and thus caused the most resentment and drastic measures from the stakeholders.

### **Research Implications**

We suggest that a direction for future research on stakeholder influence strategy is to combine resource dependence and institutional factors in a dynamic model that also takes firm strategy into consideration. In the previous discussion, we have shown that firms act under the influence of both resource dependence consideration and institutional pressure, while stakeholders react to firm actions. Thus a dynamic model will not only contribute to a more complete stakeholder influence strategy theory, it will also advance our knowledge in the areas of organizational change management and human resource management. Due to the sensitive nature of the downsizing topic and our strict sampling criteria, the sample size of this explorative study was limited. We suggest an empirical test of our four propositions with a larger sample size.

### **Practical Implications**

When firms and their stakeholders have a conflict of interest, firms must find a resolution based on their rational analysis of how much they rely on these stakeholders' resources, so

valuable resources are secured to create ultimate economic returns. Nonetheless, as part of a society, businesses must operate under the rules, values, and all other organizational and economic structures deemed socially correct, thus their decisions and actions are also abide by the norms, customs, traditions or prevailing cultures of the social institution (Oliver, 1997a; Mckinley, et.al., 2000). Therefore, management, MNC or local, should always attend to the demands of the local institutional environment when dealing with stakeholders. The same principle applies to stakeholders when choosing a stakeholder influence strategy. When social norms and expectations are taken into consideration, it is more likely to arrive at a win-win resolution that will ease the tension of a labor dispute created by business downsizing.

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**Table 1 Company profile of sample case companies**

	<b>Company Code</b>	<b>Equity Ownership</b>	<b>Industry Type</b>	<b>Industry segment</b>	<b>Age</b>	<b>Year Down-sized</b>	<b>No. of Employees Downsized</b>	<b>% Downsized</b>	<b>Change in Employee number</b>
1	<b>C</b>	Joint venture: 50% UK & USA	Mfg.	Petro-chemical	26	1997 ~2000	132	18.40	717→585
2	<b>Y</b>	Joint venture: 25% Japan	Mfg.	Auto-motive	49	1995 ~2002	813	27.07	3003→2190
3	<b>F1</b>	Joint venture: 35% Netherlands	Mfg.	Petro-chemical	28	1999 ~2002	100	32.90	328→220
4	<b>M</b>	Joint venture: 65% Netherlands & Thailand	Service	Retail	11	1999 ~2002	90	45	200→110(KHS)
5	<b>H2</b>	Joint venture: 10% Japan	Service	Auto-motive	55	2002	470	47.52	989→519
6	<b>SJ</b>	Joint venture: 49% Japan	Mfg.	Electronics	36	1998 ~2000	50	70	80→30
7	<b>B</b>	100% foreign capital : Germany	Mfg.	Petro-chemical	25	2000 ~2001	35	31.81	110→75
8	<b>A</b>	100% foreign capital: USA	Service	Finance	25	2002	51	8	572→613
9	<b>PH</b>	100% foreign capital: Netherlands	Mfg.	Information	36	2000 ~2002	340	13	2800→2002
10	<b>T1</b>	Local: private sector	Mfg.	Petro-chemical	12	2000	50	17.9	280→230
11	<b>L</b>	Local: private sector	Mfg.	Petro-chemical	26	1999 ~2002	30	9.37	320→290
12	<b>H1</b>	Local: Private sector	Mfg.	Information	19	2001 ~2002	1100	17.46	6300→5200
13	<b>S</b>	Local: Private sector	Mfg.	Information	19	2001	238	5.60	5000→4762
14	<b>P</b>	Local: Private sector	Mfg.	Electronics	2.5*	2002	300	16.60	1800→1500
15	<b>CT</b>	Local: State owned	Service	Telecom	6*	2000 ~2001	1651	18.8	8788→7137
16	<b>CB</b>	Local: State owned	Mfg.	Ship-building	30	2001	2280	45.37	5030→2729
17	<b>TL</b>	Local: Private sector ( 15% State ownership)	Mfg.	Petro-chemical	26	1986 ~1987	120	30	320→200
18	<b>NY</b>	Local: Private sector	Mfg.	Plastics	45	1998	67	98	80→1**

\*: This reflects company age after merger & acquisition; originally age was above 30 years.

\*\* : Plant relocated

**Table 2 Level of dependence between case companies and their employees**

Equity Ownership\ Company code																		
100% foreign			Joint venture						Local-private						State-owned			
Level of dependence	B	A	PH	SJ	C	Y	F1	M	H2	T1	L	H1	S	P	NY	TL	CT	CB
<i>Employee's firm-specific competencies</i>	<i>L</i>	<i>H</i>	<i>M</i>	<i>L</i>	<i>H</i>	<i>M</i>	<i>L</i>	<i>L</i>	<i>H</i>	<i>M</i>	<i>M</i>	<i>L</i>	<i>M</i>	<i>M</i>	<i>L</i>	<i>M</i>	<i>H</i>	<i>L</i>
Firm dependence on employees	2	4	3.5	2	4	3	2	2	4	3.5	2.5	2	3.5	3	1	3	4	2
<i>Demand for employees in external market</i>	<i>M</i>	<i>H</i>	<i>H</i>	<i>M</i>	<i>L</i>	<i>H</i>	<i>M</i>	<i>M</i>	<i>H</i>	<i>M</i>	<i>M</i>	<i>M</i>	<i>H</i>	<i>H</i>	<i>L</i>	<i>M</i>	<i>H</i>	<i>L</i>
Employees dependence on firm	3	2	2	3	4	2	3	3	2	3	3	2.5	2	2	5	3	1	4

L: low; M: medium; H: high

**Table 3 Actual stakeholder actions during downsizing at each case company**

Equity Ownership\ Company code																		
Stakeholder strategy	100% foreign			Joint venture						Local-private						State-owned		
	B	A	PH	SJ	C	Y	F1	M	H2	T1	L	H1	S	P	NY	TL	CT	CB
Direct usage	V		V		V	V	V		V	V	V	V	V	V	V		V	V
Indirect usage			V							V				V				V
No action (at mercy of the firm)		V*		V				V								V		
Direct withholding																		
Indirect withholding																		

\* Laid-off employees were entitled to internal selections to fill new positions.

**Table 4 Case company motives for downsizing**

Equity Ownership\ Company code																	
100% foreign			Joint venture					Local-private						State-owned			
B	A	PH	SJ	C	Y	F1	M	H2	T1	L	H1	S	P	NY	TL	CT	CB
Stagnant or declining profitability	V			V	V		V	V	V	V	V	V	V			V	V
New business model				V	V	V	V	V		V		V				V	V
Whole system change	V	V	V	V		V	V	V			V	V				V	V
Business process reengineering	V	V		V	V	V	V	V		V							V
CEO mission				V		V					V						
Merger, acquisition or relocation	V			V	V					V			V	V			
Directive from a superior organization	V	V	V	V	V		V	V	V	V			V	V	V		V
Industry benchmark			V	V		V				V	V	V			V		V
Downsizing as a business paradigm				V		V	V	V		V	V				V		V
Employees losing competitive advantage				V	V	V	V	V	V	V		V	V				V

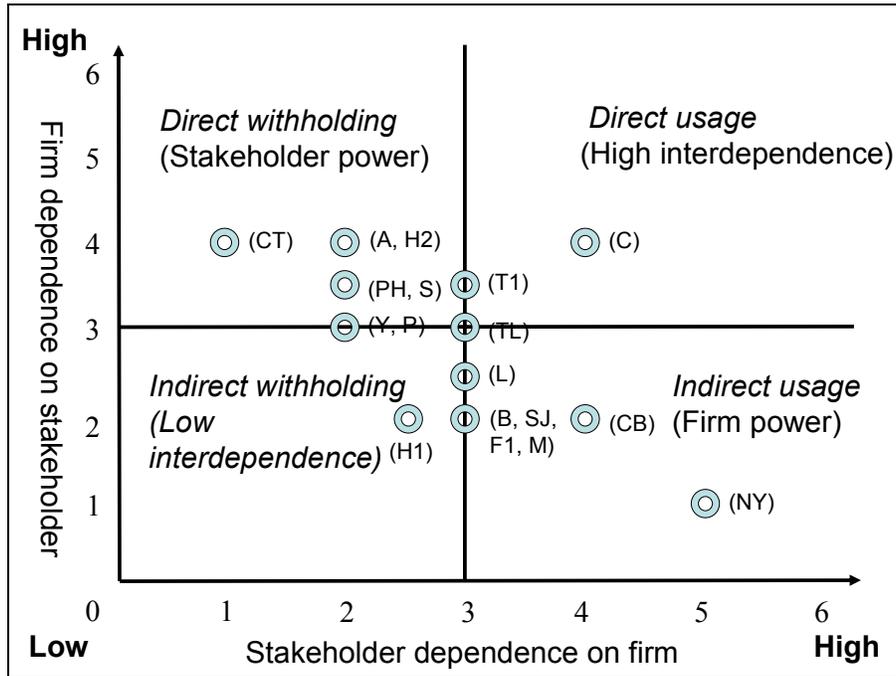
**Table 5 Downsizing practice and severance terms at each case company**

Equity Ownership\ Company code																		
	100% foreign			Joint venture						Local-private						State-owned		
Terms	B	A	PH	SJ	C	Y	F1	M	H2	T1	L	H1	S	P	NY	TL	CT	CB
Justifiable cause for downsizing	V	V	V	V	V	V	V	V	V	V	V	V	V	V	V	V	V	V
Practice conforms to labor regulations	V	V	V	V	V	V	V	V	V	V	V	V	V	V	V	V	V	V
Advance notice	V	V		V	V	V	V		V	V			V	V	V		V	V
Superior package to legal requirement	V	V	V	V	V	V	V		V	V	V			V		V	V	V
Outplacement services:																		
<input type="checkbox"/> Counseling	V	V	V		V	V	V		V	V	V	V	V				V	V
<input type="checkbox"/> Job finding/ venture assistance		V	V			V	V			V		V	V	V	V			V

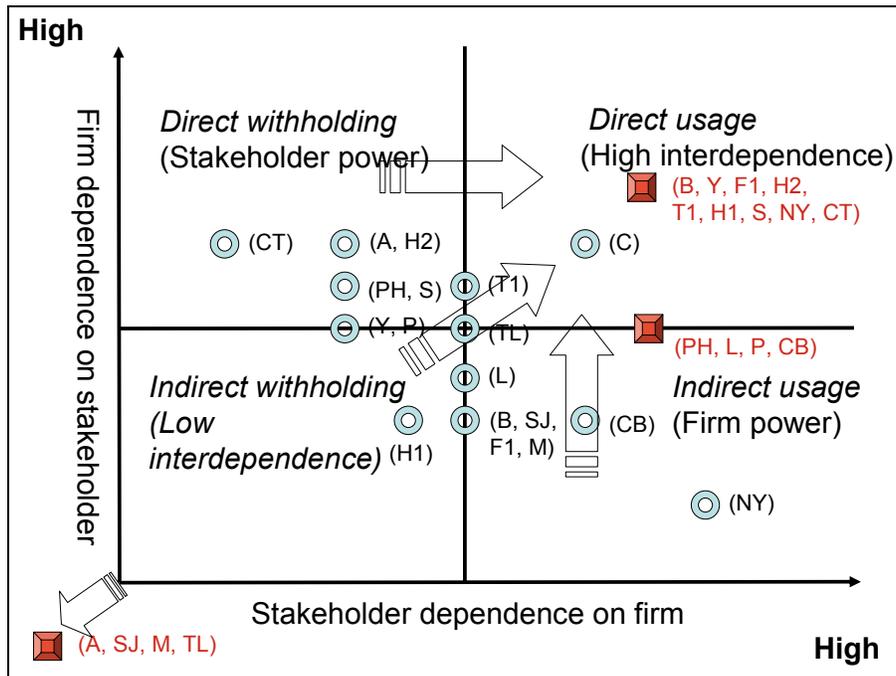
**Table 6 Levels of firm dependence and legitimacy of firm decision at each case company**

Equity Ownership\ Company code																		
	100% foreign			Joint venture						Local-private						State-owned		
	B	A	PH	SJ	C	Y	F1	M	H2	T1	L	H1	S	P	NY	TL	CT	CB
Firm dependence on stakeholder	2	4	3.5	2	4	3	2	2	4	3.5	2.5	2	3.5	3	1	3	4	2
Legitimacy of firm decision	5.5	6	5	5	5.5	6	6	3	5.5	6	5.5	5	5	6	4.5	4	5.5	6

**Figure 1** Expected stakeholder influence strategy at each case company



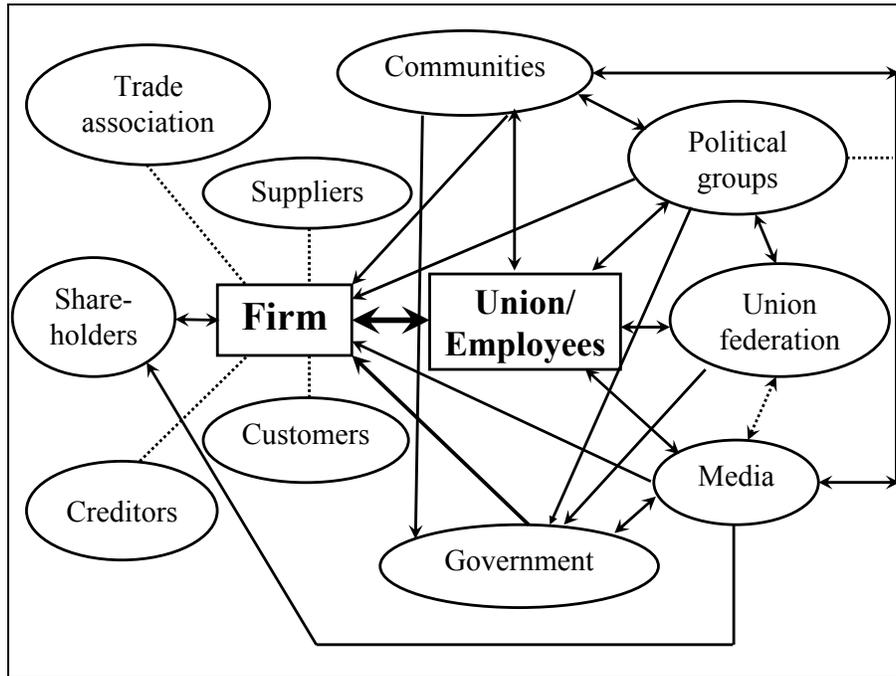
**Figure 2 Actual stakeholder influence strategy at each case company**



○ expected strategy

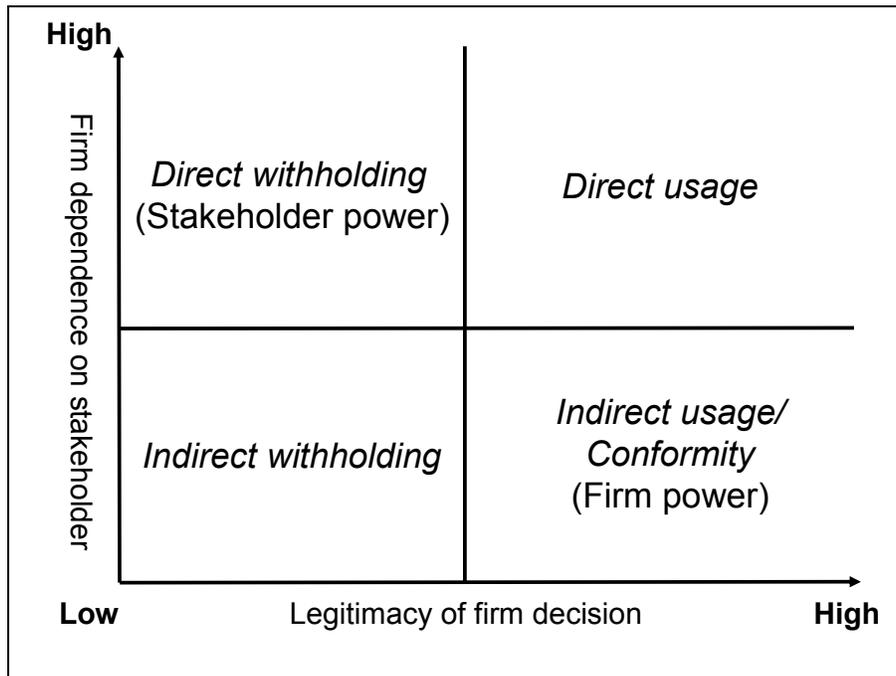
■ actual strategy

**Figure 3 An enterprise stakeholder network**

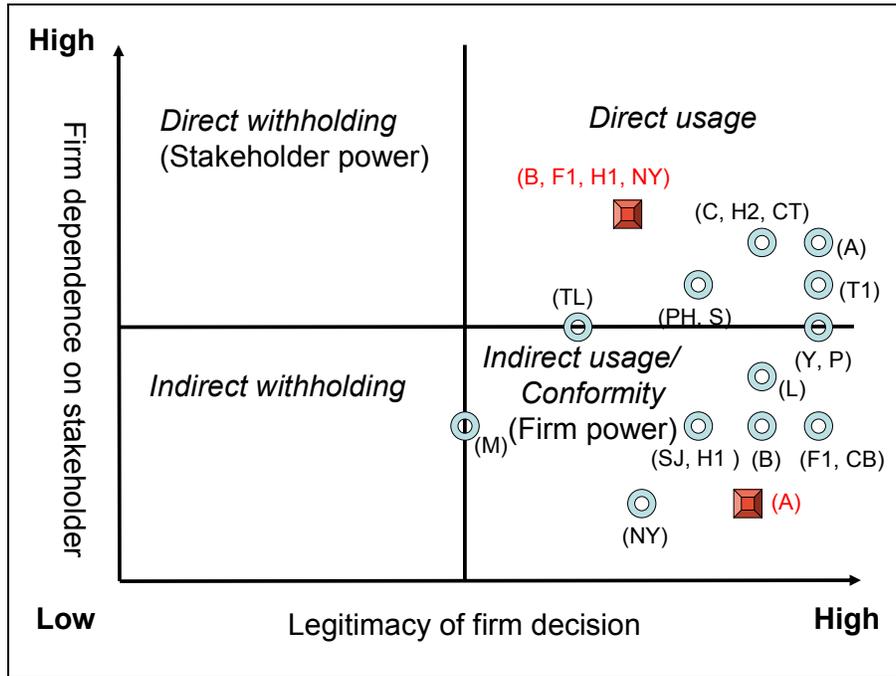


Source: Huang & Tsai, 2002

**Figure 4 A new model of stakeholder influence strategy**



**Figure 5 Comparison of actual stakeholder strategy with expected strategy in new model**



⊙ expected strategy

■ actual strategy