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The Journal of Socio-Economics 35 (2006) 142–150

The Journal of Socio-Economics

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Organizational portfolio theory and international not-for-profit organizations

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Abstract

The organizational portfolio theory is used to explain performance-driven organizational changes in international not-for-profit organizations. The forces that push international not-for-profit organizations to adapt are those that exacerbate the effect of the downward swing in organizational performance that results from misfit. On the other hand, the forces that retard adaptive change in these organizations are those that counteract the effect of the downward swing in organizational performance that results from misfit. Each of seven factors analyzed may push the international not-for-profit organizations to adapt or to not adapt, depending on their effect on organizational performance.

JEL classification: L30; F00

Keywords: Organizational portfolio theory; Organizational performance; International not-for-profit organizations

1. Introduction

Organizational portfolio theory represents a relatively new theory that treats the organization as a portfolio of causes of organizational performance (Donaldson, 1999, 2000). This theory is designed to explain the performance-driven organizational change at the firm level. Most international organizations in the area of economic development, monetary economics, international trade, human rights, as well as many other areas are either not-for-profit or not driven primarily by profit considerations. For the purposes of this paper and the theory developed herein we will call all the international non-profit membership organizations in which the members are nations (or regions) the international not-for-profit organizations. They all are constituted of member countries with very diverse interests. We believe, however, that with appropriate adjustments the

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doi:10.1016/j.socec.2005.12.008

organizational portfolio theory may be used to explain performance-driven organizational changes in international not-for-profit organizations.

Organizational portfolio theory begins with a premise that there are various internal and external causes that affect organizational performance.[1] Organizational performance, in turn, feeds back to drive organizational change such that the organization moves into fit with its situation. Organization theorists argue that organizational performance has to become low so that there is a crisis before it triggers adaptive organizational change. Adaptive organizational change will not occur if there is only a decline of organizational performance from the maximum level. This is because organizations have tendency to satisfice rather than maximize (Simon, 1976). There exists a satisficing level of performance, substantially below the maximum level, that the organization strives to maintain. The satisficing level is that level of performance that the managers of the organization consider to be satisfactory or acceptable. Organizations satisfice rather than maximize because of bounded rationality. In other words, there are limits on the decision-making capacity of managers given inadequacies, such as in their knowledge (March and Simon, 1958). Managers solve problems to restore performance so as to regain the satisficing level. Since the satisficing is a property of managerial decision making in general, it follows that adaptive organizational change of any kind should occur only when organizational performance falls below the satisficing level, because all adaptive organizational changes result from managerial decisions. Empirical research supports satisficing theory, in that low organizational performance is the trigger for adaptive organizational change in organizational strategy and structure (e.g., Cibin and Grant, 1996; Donaldson, 1994, 1987; Smith et al., 1990). Specifically, low levels of sales, profit, and earnings per share produce the needed adaptive structural change among large corporations (Donaldson, 1987).

A key question is then *why does the crisis or low performance of an organization occur*? The organizational portfolio theory borrows partially the answer from the contingency theory of organizations: due to misfit of the organization to its situation combining with other causes that depress organizational performance.[2] Moreover, each of these causes interacts with organizational misfit to determine the level of organizational performance. Variations of these causes over time define the performance fluctuations that are the leading forces of organizational change. These causes can reinforce misfit so that organizational performance is driven to the low value that triggers adaptive change, but also can nullify the effect on performance of misfit so that no change happens.

Another way of answering the above question is to consider that the causes of organizational performance form a portfolio, and each cause is termed a factor in the organizational portfolio. These organizational portfolio factors include causes of organizational performance inside

[1] Some will point out how the dynamic nature of the organizational portfolio theory may be drawn from the theory of the firm by Penrose (1980). While Penrose provided a sustained criticism of the static theory of the firm, she also constructed an elegant and serviceable framework for an alternative dynamic analysis of a firm, which can grow continuously at a finite rate. The organizational portfolio theory is similar to the extent that also provides a framework for a dynamic analysis. At the same time it is much more appropriate in the case of the not-for-profit organizations due to higher importance and relevancy of the non-economics, organizational and political factors for the survival and success of these organizations as compared to the traditional financial or cost consideration.

[2] The contingency theory of organizations holds that the organizational characteristics need to fit the level of the contingency variables of the organization (e.g., size, strategy, environmental uncertainty of the organization) for that organization to have high performance. Misfit leads to lower organizational performance than fit. Adaptive organizational change occurs when an organization moves by changing its characteristic from one that misfits the contingency to one that fits it (Donaldson, 1987, 2000; Hamilton and Shergill, 1992).