



Chapter 16.2  
Promotion practices

# Outline

- Problem and model assumptions
- Task allocation after failure
- Task allocation after success
- Initial allocation of a low-risk task
- Initial allocation of a high-risk task
- Summary

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- ▶ Expected salary:  $\Pi_M^2 = \pi_2 w_{FS} + (1 - \pi_2) w_{FF} - C_2$



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- ▶ Investment bank obtain the benefits  $V_i$  if successful
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- ▶ Investment bank obtain the benefits  $V_i$  if **successful**, pays the **wages**, and for the high-risk task loses **equity** if **not successful**
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- ▶ If allocated the low-risk task, the employee makes zero profits if he fails
- ▶ If he **succeeds**, he will be allocated the high-risk task in period 2 and obtains those **profits**, less the **costs** of effort in period 1
- ▶  $\Pi_M^L = \pi_1 (\pi_2 w_{SS} + (1 - \pi_2) w_{SF} - C_2) - C_1$



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- ▶ Profits are again  $\Pi_M^H = \pi_1 (\pi_2 w_{SS} + (1 - \pi_2) w_{SF} - C_2) - C_1$
- ▶ Optimal effort levels are given from  $\frac{\partial \Pi_M}{\partial \pi_1} = 0$  and  $\frac{\partial \Pi_M}{\partial \pi_2} = 0$

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- Problem and model assumptions
- Task allocation after failure
- Task allocation after success
- Initial allocation of a low-risk task
- Initial allocation of a high-risk task
- Summary

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