



AgEcon SEARCH
RESEARCH IN AGRICULTURAL & APPLIED ECONOMICS

The World's Largest Open Access Agricultural & Applied Economics Digital Library

This document is discoverable and free to researchers across the globe due to the work of AgEcon Search.

Help ensure our sustainability.

Give to AgEcon Search

AgEcon Search

<http://ageconsearch.umn.edu>

aesearch@umn.edu

*Papers downloaded from **AgEcon Search** may be used for non-commercial purposes and personal study only. No other use, including posting to another Internet site, is permitted without permission from the copyright owner (not AgEcon Search), or as allowed under the provisions of Fair Use, U.S. Copyright Act, Title 17 U.S.C.*

CEO duality, state shareholder and CEO turnover: Evidence from Vietnamese stock market

Quoc Trung Tran, Xuan Minh Nguyen, Tien Hoang Nguyen

Foreign Trade University, Vietnam

corresponding e-mail: tranquoc trung.cs2@ftu.edu.vn

address: 15, D5, Ward 25, Binh Thanh District, Ho Chi Minh City, Vietnam

The extant literature shows that the effects of CEO duality and state shareholder on the sensitivity of management turnover to firm performance are mixed. Using a sample of 1,260 firm-year observations from 226 firms listed in Vietnam from 2009 to 2015, we find supporting evidence for manager turnover mechanism. Interestingly, research results show that the negative relationship between firm performance and CEO turnover is weaker when CEOs simultaneously holds chairman positions. These findings imply that the separation of CEO and chairman positions is necessary to enhance corporate governance.

JEL Classifications: M12, G34

Keywords: CEO duality, state shareholder, CEO turnover, Vietnam

Citation: Tran Q.T., Nguyen X.M., Nguyen T.H., 2016. "CEO duality, state shareholder and CEO turnover: Evidence from Vietnamese stock market", *Business and Economic Horizons*, Vol. 12(3), pp.113-120, <http://dx.doi.org/10.15208/beh.2016.09>

Introduction

Management turnover has been an interesting topic in corporate governance. The separation of ownership and control causes agency problem between shareholders and managers (Jensen and Meckling, 1976). Consequently, management turnover is mechanism to enhance corporate governance. The extant literature shows that the negative relationship between firm performance and management turnover is empirically supported in both developed and developing stock markets. However, the effects of CEO duality and state shareholder on the sensitivity of management change to firm performance are mixed. Goyal and Park (2002) argue that the combination of CEO and chairman positions tends to weaken the performance-turnover mechanism and find supporting evidence of this hypothesis in the US market. Nevertheless, Rachpradit, Tang, and Ba Khang (2012) find that CEO duality is positively related to the sensitivity of management change to firm performance. Moreover, Kato and Long (2006) and Hu and Leung (2012) show opposite findings on the role of state shareholder in Chinese stock market.

We find that Vietnam is also a transitional economy in which the government holds shares of many listed firms. Like in other countries, the board of directors has the right to nominate, hire, pay, monitor and fire CEOs. Consequently, this study examines whether CEO duality and state shareholder affect the relationship between firm performance and CEO turnover. We use a research sample of 1,260 firm-year observations from 226 firms listed in Ho Chi Minh City Stock Exchange from 2009 to 2015. After controlling CEO age and firm characteristics, we find supporting evidence for manager turnover mechanism with a negative association between industry-adjusted profitability and CEO forced change. Remarkably, in line with agency theory, this association is weaker in firms

with single CEO and chairman position. There is no evidence for the impact of state ownership and state control on the sensitivity of CEO turnover to industry-adjusted profitability.

The remaining of this paper is as follows: Section 2 is literature review, Section 3 presents research model, Section 4 describes research data, Section 5 reports research findings and Section 6 is conclusion.

Literature review

Management turnover is a good mechanism to reduce agency costs of shareholders (Huand Leung, 2012). According to agency theory, managers tend to use firm resources for their own interest instead of maximizing shareholders' wealth since ownership and control are separated (Jensen and Meckling, 1976). Therefore, poor performance leads to management turnover if corporate governance is effective. Coughlan and Schmidt (1985) initially examine the relationship between management change and shareholders' interest and find that firms following management turnover policy can benefit shareholders. Weisbach (1988) investigating the relationship between management change and divestitures of acquired departments also find that management turnover results in reversal of poor performance. With the data of CEO turnover in the US from 1971 to 1994, Huson, Parrino, and Starks (2001) show that the negative relationship between firm performance and the probability of CEO turnover is significantly negative and stable during the research period. Supporting evidence of this relationship is found in many developed and developing stock markets including Australia (Suchard, Singh, and Barr, 2001), UK (Conyon and Florou, 2002; Franks, Mayer, and Renneboog, 2001), Denmark (Lausten, 2002), Italy (Brunello, Graziano, and Parigi, 2003), Japan (Abe, 1997), Finland (Maury, 2006), China (Firth, Fung, and Rui, 2006a) and Thailand (Rachpradit et al., 2012).

Moreover, this line of research is developed with several studies investigating the sensitivity of top management turnover to firm performance. Kang and Shivdasani (1995) show that the probability of top management turnover is more sensitive to earnings performance in firms with higher bank ties experience with a sample of 270 Japanese firms between 1985 and 1990. In addition, Mark L. DeFond and Park (1999) find a closer relationship between firm performance and CEO turnover in high competition industries. Especially, the impact of corporate governance on the association between firm performance and top management change is an interesting topic. Denis, Denis, and Sarin (1997) examine the relationship between ownership structure and the likelihood of top management change with a sample of 5,545 observations from 1,394 different firms listed in the US market over the period 1985 - 1988 and find that managerial ownership reduce the sensitivity of top executive turnover to stock price performance. Iqbal and French (2007) also find similar results with 260 firms in Standard and Poor's Research Insight database from 1991 to 1997. Mark L. Defond and Hung (2004) use data collected from 33 countries to investigate the role of investor protection as a means of corporate governance to identify and terminate poorly performing CEOs. They find that the relationship between poor performance and CEO change is much stronger in strong investor protection countries. Suchard et al. (2001), find that non-executive and independent directors reduce the likelihood of management turnover.

Interestingly, Goyal and Park (2002) argue that single CEO-Chairman is likely to affect negatively the effectiveness of monitoring mechanism by the board. They use a sample of 455 CEO turnovers and a control sample of 3239 observations from 823 firms without CEO change in the US market over the period 1992 - 1996. Their research results show that the sensitivity of CEO turnover to firm performance is weaker when the two titles are combined. However, Rachpradit et al. (2012) find an opposite evidence in Thai stock market.

Moreover, the mechanism of top management turnover is also examined in a transitional economy where there are many firms controlled by government. There are two opposite views on the effect of government control or ownership on governance of state-owned enterprises (SOEs). On the one hand, corporate governance in SOEs is less effective than in private firms since there is no individual owner who has strong incentives to monitor managers or government follows social, political and economic objectives at the same time. On the other hand, the government is an effective owner with strong incentives to apply corporate control methods and monitor managers more effectively (Huand Leung, 2012). Hence, government control can increase the sensitivity of management turnover to firm performance. Empirical evidence on this relationship is also mixed. Kato and Long (2006) investigate China's listed firms over the period from 1998 to 2002 and find that the impact of firm performance on CEO turnover is weaker for firms controlled by the government and those that have a relatively high state ownership. However, Hu and Leung (2012) find a stronger negative turnover-performance relationship with a research sample of 916 SOEs listed in Chinese stock market from 2001 to 2005.

This study investigates the effect of debatable governance measures including CEO duality, state ownership and state control on the relationship between firm performance and CEO turnover in Vietnamese stock market.

Research model

Following prior studies, we develop CEO turnover as a logit function of firm performance, interactive terms between firm performance and corporate governance measures and control variables. All of the independent variables are lagged one period.

$$\text{TURN}_t = \alpha + \beta_1 \text{ROA}_{t-1} + \beta_2 \text{DUAL}_{t-1} + \beta_3 \text{DUAL}_{t-1} \text{ROA}_{t-1} + \beta_4 \text{STATE}_{t-1} + \beta_5 \text{STATE}_{t-1} \text{ROA}_{t-1} + \beta_6 \text{AGE}_{t-1} + \beta_7 \text{LEV}_{t-1} + \beta_8 \text{SIZE}_{t-1} + \varepsilon \quad (1)$$

$$\text{TURN}_t = \alpha + \beta_1 \text{ROA}_{t-1} + \beta_2 \text{DUAL}_{t-1} + \beta_3 \text{DUAL}_{t-1} \text{ROA}_{t-1} + \beta_4 \text{D_STATE}_{t-1} + \beta_5 \text{D_STATE}_{t-1} \text{ROA}_{t-1} + \beta_6 \text{AGE}_{t-1} + \beta_7 \text{LEV}_{t-1} + \beta_8 \text{SIZE}_{t-1} + \varepsilon \quad (2)$$

Where:

CEO turnover (TURN_t) is equal to 1 if the current CEO does not the firm due to one in four reasons including retirement, change of ownership, health and the end of a temporary and 0 otherwise (Huand Leung, 2012).

Firm performance (ROA_{t-1}) is earnings before interest and taxes divided by total assets adjusted by the industry median at year $t-1$. Using EBIT is likely to reduce the effect of earnings manipulation by managers (Dah, Frye, and Hurst, 2014; Firth, Fung, and Rui, 2006b). Industry classification is based on super-sector of the Industry Classification Benchmark. We hypothesize that firm performance is negatively related to CEO turnover.

Corporate governance variables include CEO duality (DUAL_{t-1}), state ownership (STATE_{t-1}) and state control (D_STATE_{t-1}). DUAL_{t-1} is a dummy variable which takes 1 if the CEO simultaneously holds the chairman position at year $t-1$ and 0 otherwise. STATE_{t-1} is the proportion of shares held by state shareholder at year $t-1$. D_STATE_{t-1} is a dummy variable which is equal to 1 if state shareholder holds more than 50% total number of shares at year $t-1$ and 0 otherwise. As discussed in Section 2, the expected signs of these corporate governance variables and their interactions are as follows: DUAL_{t-1} (-), DUAL_{t-1}

$1*ROA_{t-1}$ (+), $STATE_{t-1}$ (+/-), $STATE_{t-1}*ROA_{t-1}$ (+/-), D_STATE_{t-1} (+/-), $D_STATE_{t-1}*ROA_{t-1}$ (+/-).

Control variables are CEO age (AGE_{t-1}), firm leverage (LEV_{t-1}) and firm size (SIZ_{t-1}). AGE_{t-1} is measured by the year t-1 minus the CEO's year of birth (Dah et al., 2014). CEO age is a proxy for experience (Ferris, Jagannathan, and Pritchard, 2003), hence we expect a negative relationship between CEO age and turnover. LEV_{t-1} is total liabilities divided by total assets. Gilson (1989) finds that the likelihood of management turnover is higher in financially distressed firms; therefore, firms with higher leverage tends experience higher CEO turnover. In addition, SIZ_{t-1} is log of total assets. Larger firms can find a substitution for their CEOs more easily hence they are more likely to change their CEOs. These control variables are winsorized at 5% to avoid the effect of outliers. Their expected signs are as follows: AGE_{t-1} (-), LEV_{t-1} (+) and SIZ_{t-1} (+).

Both equations (1) and (2) are applied pooled logit regression model clustered by firm for controlling within-firm correlated residuals. Moreover, they are added year dummies, industry dummies to control year and industry effects. Beside pooled regression, we also run random effects regression for the two equations as a robustness check.

Research data

To construct the research sample, we collect information on CEOs including turnover, duality, voting power and age from annual reports of firms listed in Ho Chi Minh City Stock Exchange over the period from 2009 to 2015 by hand. Accounting information is collected from the database of Tan Viet Securities Company (www.tvsi.com.vn) and cross-checked with the database of Stockbiz (www.stockbiz.vn). Then, firm-year observations meeting the following criteria are eliminated: (1) firms in financial industry including insurance, real estate and financial services and (2) observations with missing or incomplete information. The final research sample contains 1,260 firm-year observations that correspond to 226 firms with 58 CEO turnovers.

Panel A of Table 1 shows CEO turnover by industry. Construction and Materials have the largest number of CEO turnovers with 14 cases, followed by Basic Resources and Industrial Goods and Services with 10 cases for each. Both Automobiles and Parts and Retail experience only one case of CEO turnover during the research period. Moreover, Panel B illustrates CEO turnover by year. Annual number of CEO turnovers is small. The largest amount of turnovers is 11 in 2012 and the smallest is 3 in 2010. The other years experience from 7 to 10 cases of CEO turnover. Panel C of Table 1 shows descriptive statistics of both dependent and independent variables. Number of observations with CEO turnover only accounts for 5% in the research sample. The mean value of industry adjusted profitability is 0.01 which is near to zero. This implies that the research sample experience small selection bias. Firms with combined CEO and chairman constitutes about 36%% of the sample. In addition, state ownership is considerably high with the average proportion of 20.4% and the maximum value is 96.72%. CEO age is 48.85 on average.

Research results

Table 2 reports analysis results for both pooled and random effects regression models. In line with prior studies, we find a significant negative relationship between firm performance and the profitability of CEO turnover in Vietnamese stock market. This implies that firms listed in Vietnam also use turnover mechanism as a tool of corporate governance. Although CEO duality fails to affect CEO change significantly, its interactive terms with firm performance are negatively related to the likelihood of CEO turnover.

These findings are consistent with Goyal and Park (2002) and contrary to Rachpradit et al. (2012). Firms with combined CEO and chairman positions tend to have less effective monitoring systems and they experience lower sensitivity of firm performance to CEO turnover. Furthermore, we find no supporting evidence of the effects of both state ownership and state control on the sensitivity of firm performance to CEO turnover significantly. CEO age is negatively associated with CEO turnover. This can be explained that CEOs with more experience are less likely to be forced to leave their companies.

Conclusion

The extant literature shows that performance-turnover mechanism is effective in both developed and developing stock markets. However, the impact of CEO duality and state shareholder on this relationship is mixed. Using a sample of 1,260 firm-year observations from 226 firms listed in Vietnam - a transitional economy - from 2009 to 2015, we find supporting evidence for manager turnover mechanism. Interestingly, research results show that the negative relationship between firm performance and CEO turnover is weaker when CEOs simultaneously holds chairman positions. There is no supporting evidence for the relevance of state ownership and state control to this relationship. These findings imply that the separation of CEO and chairman positions is necessary to enhance corporate governance.

References

- Abe Y., 1997. "Chief Executive Turnover and Firm Performance in Japan", *Journal of the Japanese and International Economies*, Vol.11(1), pp.2-26.
- Brunello G., Graziano C., and Parigi B. M., 2003. "CEO turnover in insider-dominated boards: The Italian case", *Journal of Banking and Finance*, Vol.27(6), pp.1027-1051.
- Canyon M.J. and Florou A., 2002. "Top executive dismissal, ownership and corporate performance", *Accounting and Business Research*, Vol.32(4), pp.209-225.
- Coughlan A.T. and Schmidt R.M., 1985. "Executive compensation, management turnover, and firm performance. An empirical investigation", *Journal of Accounting and Economics*, Vol.7(1-3), pp.43-66.
- Dah M.A., Frye M.B., Hurst M., 2014. "Board changes and CEO turnover: The unanticipated effects of the Sarbanes–Oxley Act", *Journal of Banking and Finance*, Vol.41, pp.97-108.
- Defond M.L. and Hung M., 2004. "Investor protection and corporate governance: Evidence from worldwide CEO turnover", *Journal of Accounting Research*, Vol.42(2), pp.269-312.
- DeFond M.L., and Park, C. W., 1999. "The effect of competition on CEO turnover", *Journal of Accounting and Economics*, Vol.27(1), pp.35-56.
- Denis D.J., Denis D.K., Sarin A., 1997. "Ownership structure and top executive turnover", *Journal of Financial Economics*, Vol.45(2), pp.193-221.
- Ferris S.P., Jagannathan M., Pritchard A.C., 2003. "Too Busy to Mind the Business? Monitoring by Directors with Multiple Board Appointments", *The Journal of Finance*, Vol.58 (3), pp.1087-1112
- Firth M., Fung P.M.Y., Rui O.M., 2006a. "Corporate performance and CEO compensation in China", *Journal of Corporate Finance*, Vol.12(4), pp.693-714.
- Firth M., Fung P.M.Y., Rui, O.M., 2006b. "Firm Performance, Governance Structure, and Top Management Turnover in a Transitional Economy*", *Journal of Management Studies*, Vol.43 (6), pp.1289-1330.
- Franks J., Mayer C., Renneboog L., 2001. "Who disciplines management in poorly performing companies?", *Journal of Financial Intermediation*, Vol.10(3-4), pp.209-248.
- Gilson S.C., 1989. "Management turnover and financial distress", *Journal of Financial Economics*, Vol.25 (2), pp.241-262.

- Goyal V.K., Park C.W., 2002. "Board leadership structure and CEO turnover", *Journal of Corporate Finance*, Vol.8(1), pp.49-66.
- Hu F., Leung S.C.M., 2012. "Top management turnover, firm performance and government control: Evidence from China's listed state-owned enterprises", *The International Journal of Accounting*, Vol.47(2), pp.235-262.
- Huson, M.R., Parrino, R., and Starks, L.T., 2001. "Internal monitoring mechanisms and CEO turnover: A long-term perspective", *The Journal of Finance*, Vol.56(6), pp.2265-2297.
- Iqbal Z., French D.W., 2007. "Executive share ownership, trading behavior, and corporate control: Evidence from top management turnover during financial distress", *Journal of Economics and Business*, Vol.59(4), pp.298-312.
- Jensen M.C., and Meckling W.H., 1976. "Theory of the firm: Managerial behavior, agency costs and ownership structure", *Journal of Financial Economics*, Vol.3(4), pp.305-360.
- Kang J.-K. and Shivdasani A., 1995. "Firm performance, corporate governance, and top executive turnover in Japan", *Journal of Financial Economics*, Vol.38(1), pp.29-58.
- Kato T., Long C., 2006. "CEO turnover, firm performance, and enterprise reform in China: Evidence from micro data", *Journal of Comparative Economics*, Vol.34(4), pp.796-817.
- Lausten M., 2002. "CEO turnover, firm performance and corporate governance: empirical evidence on Danish firms", *International Journal of Industrial Organization*, Vol.20(3), pp.391-414.
- Maury B., 2006. "Corporate performance, corporate governance and top executive turnover in Finland", *European Financial Management*, Vol.12(2), pp.221-248.
- Rachpradit P., Tang J.C., Ba Khang D., 2012. "CEO turnover and firm performance, evidence from Thailand", *Corporate Governance: The international journal of business in society*, Vol.12(2), pp.164-178.
- Suchard J.-A., Singh M., Barr R., 2001. "The market effects of CEO turnover in Australian firms", *Pacific-Basin Finance Journal*, Vol.9(1), pp.1-27.
- Weisbach M.S., 1988. "Outside directors and CEO turnover", *Journal of Financial Economics*, Vol.20(C), pp.431-460.

Appendix

TABLE 1. SUMMARY OF STATISTICS

PANEL A. CEO TURNOVER BY INDUSTRY					
INDUSTRY	Count	Percent	Industry	Count	Percent
Construction and Materials	14	24.14	Utilities	3	5.17
Basic Resources	10	17.24	Personal and Household Goods	2	3.45
Industrial Goods and Services	10	17.24	Travel and Leisure	2	3.45
Chemicals	6	10.34	Automobiles and Parts	1	1.72
Health Care	5	8.62	Retail	1	1.72
Food and Beverage	4	6.9			

PANEL B. CEO TURNOVER BY YEAR					
YEAR	Count	Percent	Year	Count	Percent
2009	7	12.07	2013	8	13.79
2010	3	5.17	2014	10	17.24
2011	9	15.52	2015	10	17.24
2012	11	18.97			

PANEL C. DESCRIPTIVE STATISTICS					
VARIABLE	N	Mean	Std.	Min	Max
TURN _t	1,260	0.05	0.21	0.00	1.00
ROA _{t-1}	1,260	0.01	0.07	-0.10	0.17
DUAL _{t-1}	1,260	0.36	0.48	0.00	1.00
DUAL _{t-1} *ROA _{t-1}	1,260	0.00	0.04	-0.10	0.17
STATE _{t-1} (%)	1,260	20.40	24.65	0.00	96.72
STATE _{t-1} *ROA _{t-1}	1,260	0.36	2.27	-7.15	16.06
D_STATE _{t-1}	1,260	0.27	0.44	0.00	1.00
D_STATE _{t-1} *ROA _{t-1}	1,260	0.00	0.03	-0.10	0.17
AGE _{t-1}	1,260	48.85	7.35	23.00	71.00
LEV _{t-1}	1,260	0.47	0.21	0.11	0.80
SIZE _{t-1}	1,260	13.64	1.04	12.05	15.85

Note: TURN_t takes 1 if the current CEO does not the firm due to one in four reasons including retirement, change of ownership, health and the end of a temporary and 0 otherwise. ROA_{t-1} is earnings before interest and taxes divided by total assets adjusted by the industry median at year t-1. DUAL_{t-1} is a dummy variable which takes 1 if the CEO simultaneously holds the chairman position at year t-1 and 0 otherwise. STATE_{t-1} is the proportion of shares held by state shareholder at year t-1. D_STATE_{t-1} is a dummy variable which is equal to 1 if state shareholder holds more than 50% total number of shares at year t-1 and 0 otherwise. AGE_{t-1} is measured by the year t-1 minus the CEO's year of birth. CLEV_{t-1} is total liabilities divided by total assets. SIZE_{t-1} is log of total assets.

TABLE 2. LOGIT REGRESSION RESULTS

VARIABLE	EXPECTED SIGN	POOLED	RANDOM EFFECTS	POOLED	RANDOM EFFECTS
Intercept		-14.66*** (-6.67)	-0.08 (-0.03)	-15.06*** (-6.89)	0.06 (0.02)
ROA _{t-1}	-	-6.84** (-2.28)	-11.37** (-2.26)	-4.53* (-1.70)	-8.43* (-1.90)
DUAL _{t-1}	-	0.11 (0.29)	0.54 (1.35)	0.07 (0.18)	0.47 (1.17)
DUAL _{t-1} *ROA _{t-1}	+	8.88** (2.02)	11.50** (2.10)	8.73** (1.98)	10.69* (1.95)
STATE _{t-1}	+/-	0.01 (0.84)	0.01 (1.59)		
STATE _{t-1} *ROA _{t-1}	+/-	0.05 (0.72)	0.07 (0.70)		
D_STATE _{t-1}	+/-			0.16 (0.42)	0.30 (0.68)
D_STATE _{t-1} *ROA _{t-1}	+/-			-2.60 (-0.67)	-0.83 (-0.13)
AGE _{t-1}	+/-	-0.07*** (-3.71)	-0.10*** (-3.80)	-0.07*** (-3.83)	-0.10*** (-3.75)
LEV _{t-1}	+/-	0.55 (0.57)	-0.05 (-0.05)	0.56 (0.57)	-0.09 (-0.09)
SIZE _{t-1}	+	0.02 (0.12)	0.04 (0.19)	0.02 (0.15)	0.04 (0.20)
Wald χ^2 statistic		1,176.96***	20.11***	1,200.85***	18.86**
No. observations		1,260	1,260	1,260	1,260

Note: The dependent variable is CEO turnover (TURN_{it}) which takes 1 if the current CEO does not the firm due to one in four reasons including retirement, change of ownership, health and the end of a temporary and 0 otherwise. ROA_{t-1} is earnings before interest and taxes divided by total assets adjusted by the industry median at year t-1. DUAL_{t-1} is a dummy variable which takes 1 if the CEO simultaneously holds the chairman position at year t-1 and 0 otherwise. STATE_{t-1} is the proportion of shares held by state shareholder at year t-1. D_STATE_{t-1} is a dummy variable which is equal to 1 if state shareholder holds more than 50% total number of shares at year t-1 and 0 otherwise. AGE_{t-1} is measured by the year t-1 minus the CEO's year of birth. CLEV_{t-1} is total liabilities divided by total assets. SIZE_{t-1} is log of total assets. z-statistics are in parentheses. *** denotes significance at the 1% level. ** denotes significance at the 5% level. * denotes significance at the 10% level.