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Does Firm Performance Impact Top Executive Turnover ?

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Abstract

Using data from 1618 companies listed on National Stock Exchange (India) from 2001 to 2016, this paper examines the impact of financial performance on top executive turnover. The threat of turnover serves as a disciplining tool for top executives because turnover of top executives is a way to rectify the misfit between executives and company. We found that there is an inverse relationship between firm performance and top executive turnover. Further, we also found that firms having more leverage have a higher propensity to terminate their top executives. Other factors such as independence of board, regulation year exhibit a positive relationship with the likelihood of top executive turnover. The long run stock performance of companies post turnover exhibits improvement validating the improved management hypothesis proposed by earlier researchers.

I. Introduction

DESPITE A SIZEABLE AMOUNT of literature on turnover of executives in the developed economies, the emerging economies have received relatively less than their due attention. Gibson, 2003 points out the lack of academic research in the corporate governance domain in emerging economies in his study on top executive turnovers in eight emerging economies. While a number of studies have emphasized the existence of an inverse relationship between firm performance and executive turnover, the intensity of the relationship and time lag differs from country to country (Suchard, Singh and Borr, 2001). An emerging country is characterized by features not

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The regression results for post turnover performance reports a positive and statistically significant coefficient value for the intercept term for all the raw performance measures. The coefficient for intercept of industry adjusted performance measures is positive for most of the performance variables signifying an improvement in industry adjusted performance after top executive turnover. In order to test the influence of group affiliation of firms on top executive turnover, we've introduced a dummy variable for group affiliated firms where all business group affiliated firms takes a value 1 and 0 otherwise. The result from the introduction of dummy variable is also inconclusive. The result for raw performance variables show no impact of affiliation on subsequent performance, but when other control variables are introduced then for some performance variables (ROA, ROE and Tobin's q), affiliation becomes moderately significant for business group affiliated firms.

The results of long term stock performance measure show improvement in long term stock performance after top executive turnover. The results of our study have theoretical and practical implications for all the stakeholders in general and shareholders/investors in particular. According to the results obtained from this study, investors/shareholders can consider a decline in performance as a prelude to an impending top executive turnover. The inverse performance turnover relation is more pronounced in large firms and highly levered firms. The regulatory bodies should come up with provisions for enhanced scrutiny and more transparency in a bid to attract more people towards investing. The results would help portfolio managers in deciding which stocks to do away with when performance measures are in decline and later include after the turnover is executed because the long run stock performance improves after top executive turnover.

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