



**UNIVERSITI PUTRA MALAYSIA**

***IMPACT OF CEO TRANSITION ANNOUNCEMENT, CEO  
CHARACTERISTICS AND MODERATING EFFECT OF CEO  
TRANSITION PLAN ON SHARE PRICE OF MALAYSIAN COMPANIES***

**SHUBASINI SIVAPREGASAM**

**GSM 2021 1**



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By

**SHUBASINI SIVAPREGASAM**

**Thesis Submitted to the Putra Business School in Fulfilment of the  
Requirements for the Degree of Doctor of Philosophy**

**June 2020**

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Abstract of thesis presented to the Senate of Universiti Putra Malaysia in fulfilment of the requirement for the degree of Doctor of Philosophy

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**June 2020**

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The rate of Chief Executive Officer (CEO) succession or transition, especially CEO turnover in emerging economies, has increased lately and this has led to growing concerns and worries among investors over the safety, and more importantly, the profitability of their investment in the affected firms. This is especially important for firms with economic exposure to the Covid-19 pandemic as the situation would require the right person to maneuver the firm in the right direction. There have been some empirical studies on CEO succession, but most of such studies have been conducted in developed nations with findings that are largely inconsistent. In addition, studies on announcement effect of CEO succession on the share price are insufficient and biased towards announcement effect on CEO turnover. In view of these worries, this study examines the reaction of share price based on a revised classification of CEO planned succession announcement (Objective 1). It also looks at the CEO characteristics and the moderating effect of the CEO succession plan (CP) as important factors in the share price reaction (Objective 2 and 3).

This study is grounded in the theory of efficient market hypothesis (EMH), and examines the share price changes due to CEO turnover and appointment announcement using the standard abnormal return (AR) calculation. The share price reaction, which is referred to as cumulative average abnormal return (CAAR), is estimated using the Capital Asset Pricing Model (CAPM). Next, the impact of the CEO characteristics, which are age, origin, education, experience, stock ownership and gender, against CAAR, is examined using cross-sectional regression analysis. This analysis is conducted across the revised planned and unplanned announcement criteria. Using the similar regression analysis method, an analysis is made on the general announcement type of CEO turnover and appointment. Looking at announcement type separately, the moderating effect of CP on the relationship

between the CEO characteristics and the share price reaction is examined. This study uses secondary data from Bursa Malaysia for a period of 10 years, from 2007 to 2016.

The CAAR is observed to be significant and positive for planned CEO turnover and appointment announcement, indicating investors' confidence level with the firm increases with the establishment of a CP. In other words, when announcement of CEO turnover and appointment are made on the same day, it induces a positive reaction to the firm's share price.

As for the impact of CEO characteristics, significant results are found for different characteristics on different event windows. In planned CEO appointment and turnover announcement, origin, education and stock ownership variables are found to be significant. However, this reaction cannot be matched with the type of announcement because both the CEO appointment and turnover announcement occur on the same day. Meanwhile, for unplanned CEO appointment announcement, age, experience and stock ownership variables are significant; whereas for unplanned CEO turnover announcement, origin, education and gender variables are significant.

When the CP is moderated in the relationship between CEO characteristics and the share price, age, origin, experience and stock ownership variables are significant for announcement of CEO appointment. In general, when the share price is observed by the general classification of announcement. The CP significantly moderates age, experience and stock ownership for announcement of CEO appointment. The CP also moderates origin and education moderate for announcement of CEO turnover.

These findings highlight the importance of CP on firm value. It also emphasises the importance of CEO characteristics, even during his or her removal. The results of this study are expected to contribute to bridging the gaps in the literature on CEO succession by reclassifying announcement types while investigating CEO characteristics. Therefore, it will allow policymakers to re-examine current policies on CEO succession and establish an appropriate CEO succession policy, thus minimising repercussions caused by the sudden removal of a CEO.

**Keywords:** CEO succession, CEO succession plan, event study, signalling theory

Abstrak tesis yang dikemukakan kepada Senat Universiti Putra Malaysia sebagai memenuhi keperluan untuk ijazah Doktor Falsafah

**IMPAK PENGUMUMAN PENGGANTIAN KETUA PEGAWAI  
EKSEKUTIF (CEO), CIRI-CIRI CEO DAN KESAN MODERASI PELAN  
PENGGANTIAN CEO TERHADAP HARGA SAHAM SYARIKAT-  
SYARIKAT DI MALAYSIA**

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Kadar penggantian atau peralihan Ketua Pegawai Ekskutf (CEO), terutamanya pertukaran CEO dalam ekonomi baru telah meningkat sejak kebelakangan ini dan telah membawa kepada kebimbangan dan kerisauan di kalangan para pelabur terhadap kesejahteraan pelabur dan yang lebih penting, adalah mengenai keuntungan pelaburan mereka dalam firma-firma yang terjejas. Ini penting terutamanya untuk firma yang terkesan secara ekonomi kepada wabak pandemik Covid-19 memandangkan situasi ini memerlukan seseorang yang sesuai untuk menerajui firma. Terdapat beberapa kajian empirikal mengenai penggantian CEO, tetapi kebanyakan kajian sedemikian dijalankan di negara-negara maju dengan penemuan yang tidak konsisten. Tambahan pula, kesan pengumuman penggantian CEO ke atas harga saham adalah kurang dan memihak kepada kesan pengumuman pertukaran CEO. Berdasarkan situasi tersebut, kajian ini adalah untuk meneliti reaksi harga saham berdasarkan klasifikasi pengumuman CEO terancang yang telah dimurnikan (Objektif 1). Kajian ini juga meneliti ciri-ciri CEO dan kesan moderasi pelan penggantian CEO sebagai faktor utama dalam reaksi saham (Objektif 2 dan 3).

Kajian ini adalah berasaskan ramalan hipotesis pasaran cekap (Efficient Market Hypothesis-EMH) dan akan menyemak perubahan harga saham disebabkan pengumuman pertukaran CEO dan pelantikan CEO menggunakan kaedah standard pengiraan pulangan luar biasa (abnormal return –AR). Reaksi saham, yang dikenali sebagai purata pulangan abnormal kumulatif (cumulative average abnormal return-CAAR) dikira menggunakan model penentuan harga aset modal (capital asset pricing model-CAPM). Seterusnya, impak ciri-ciri CEO, iaitu umur, asal-usul, pendidikan, pengalaman, pegangan saham dan jantina dikaji menggunakan analisis keratan lintang (cross sectional). Analisa ini dilaksanakan ke atas pengumuman CEO

terancang dan tidak terancang yang telah disemak semula. Menggunakan kajian keratan lintang yang sama, satu analisa dibuat ke atas pengumuman pertukaran dan pelantikan CEO yang umum. Melihat pengumuman secara berasingan, kesan moderasi pelan penggantian CEO ke atas hubungan antara ciri-ciri CEO dan harga saham diteliti. Kajian ini menggunakan data sekunder dari Bursa Malaysia untuk tempoh 10 tahun, dari 2007 hingga 2016.

CAAR yang didapati positif dan signifikan untuk pengumuman pertukaran dan pelantikan CEO terancang, menunjukkan keyakinan pelabur ke atas firma adalah meningkat dengan pengwujudan pelan penggantian CEO. Dalam erti kata lain, apabila pengumuman pertukaran dan pelantikan CEO berlaku pada hari yang sama, ia mendorong reaksi positif ke atas saham firma.

Untuk impak ciri-ciri CEO, keputusan signifikan diperolehi untuk ciri yang berlainan pada tempoh peristiwa yang berlainan. Dalam pengumuman pertukaran dan pelantikan CEO terancang, pemboleh ubah asal-usul, pendidikan dan pemilikan saham adalah signifikan. Namun, reaksi ini tidak dapat di padankan dengan jenis pengumuman kerana kedua-dua pengumuman berlaku pada hari yang sama. Sementara itu, untuk pengumuman pelantikan CEO tidak terancang, pemboleh ubah umur, pengalaman dan pemilikan saham didapati signifikan, sementara bagi pengumuman pertukaran CEO tidak terancang, pemboleh ubah asal-usul, pendidikan dan jantina adalah signifikan.

Apabila pelan penggantian CEO dimoderasikan dalam hubungan antara ciri-ciri CEO dan harga saham, pemboleh ubah umur, asal-usul, pengalaman dan pemilikan saham adalah signifikan untuk pengumuman pelantikan CEO terancang. Secara umumnya, apabila saham diteliti berdasarkan klasifikasi umum, pelan penggantian CEO memoderasi secara signifikan ke atas pemboleh ubah umur, pengalaman dan pemilikan saham bagi pengumuman pelantikan. Pelan penggantian CEO juga memoderasi secara signifikan pemboleh ubah asal-usul dan pendidikan untuk pengumuman pertukaran CEO.

Penemuan ini menunjukkan kepentingan pelan penggantian CEO dilaksana ke atas nilai firma. Ia juga memberi penekanan ke atas kepentingan ciri-ciri CEO, walaupun semasa pertukaran CEO. Hasil daripada kajian ini dijangka menyumbang untuk merapatkan jurang dalam literasi penggantian CEO dengan mengkлас jenis pengumuman disamping mengkaji ciri-ciri CEO. Sehubungan ini, ia membolehkan penggubal dasar untuk menyemak semula dasar semasa mengenai penggantian CEO, mewujudkan dasar penggantian CEO yang sesuai, dan dengan itu meminimumkan kesan yang disebabkan oleh pertukaran CEO secara mengejut.

Kata Kunci: Penggantian CEO, Pelan Penggantian CEO, hipotesis pasaran cekap, teori signal

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Last, I would like to extend my sincere thanks to all my friends for believing in me.



I certify that a Thesis Examination Committee has met on 26th June 2020 to conduct the final examination of Shubasini Sivapregasam on her thesis entitled “Impact of CEO Transition Announcement, CEO Characteristics and Moderating Effect of CEO Transition Plan on Share Price of Malaysian Companies” in accordance with the Universities and University Colleges Act 1971 and the Constitution of the Universiti Putra Malaysia [P.U.(A) 106] 15 March 1998. The Committee recommends that the student be awarded the degree of Doctor of Philosophy.

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## LIST OF ABBREVIATIONS

AAR	Average Abnormal Return
AR	Abnormal Return
ACCIM	Associated Chinese Chambers of Commerce & Industry
ASX	Australian Stock Exchange
BOD	Board of Directors
BRIC	Brazil, Russia, India, and China
CAAR	Cumulative Average Abnormal Return
CAPM	Capital Asset Pricing Model
CCM	Capital Malaysia
CEO	Chief Executive Officer
CP	CEO Succession Plan
EDU	Education
EMH	Efficient Market Hypothesis
EPS	Earnings per Share
EXP	Prior CEO Experience
GEN	Gender
IP	Industrial Product
Khazanah	Khazanah Nasional Berhad
LEV	Leverage
MCCG	Malaysian Code of Corporate Governance
MM	Market Model
MOF Inc	Ministry of Finance Incorporated
MSCI	Morgan Stanley Capital International

MSWG	Minority Shareholder Watch Group
ORG	Origin
PwC	Price Waterhouse Cooper
ROA	Return on Asset
ROE	Return on Equity
R&D	Research and Developemen
SIZE	Size
SO	Stock Ownership
SP	Share price
S1	Step 1
S2	Step 2
S3	Step 3
TS	Trading and Services
US	United States of America
9MP	Ninth Malaysia Plan



# CHAPTER 1

## INTRODUCTION

### 1.1 Overview on CEO Succession

In the past, the theory of efficient market hypothesis (EMH) has been widely used in many empirical studies to explain announcement effects of corporate events, such as Chief Executive Officer (CEO) succession. According to the EMH, a market is said to be efficient if all information is already reflected in the share price (Fama, 1970). Ideally however, a firm's share price must react to new information and this has the ability to increase the future wealth of the firm (Fama, Fisher, Jensen, & Roll, 1969). This is because on the basis of insider knowledge, the firm takes advantage of the exclusive new information from the announcement on change of CEO to increase firm wealth (Spence, 1973). This presupposes that although all information is already reflected in the share price, not all interested investors have the information at the same time. This has made the EMH assumption on efficient market highly contentious, leaving investors with many investment decisional dilemmas.

Nevertheless, an investor's decision to buy, hold, or sell a share is influenced by a number of elements, including but not limited to motives, knowledge, experience, feeling, and other cognitive, emotional and social influences (Redhead, 2009). To take positive advantage of these elements, firms base their decision on the signalling theory to release new information to the market so as to influence an investor's decision. Under this theory, this study attempts to explain how a firm uses announcement on change of CEO to control the share price movement. This study focuses on the share price movement because it is the aspect of the firm that shows an immediate effect from any information released by the firm. Furthermore, changes in the share prices are also aspects of the firm that are associated with an investor's confidence level in a firm. Further, the share price of a firm is sensitive to information relating to changes in corporate structure and key pillars of strength of an organisation.

The pillars of strength of many successful firms are underpinned by three elements: a talented CEO; a diverse board of directors (Board); and good corporate governance (Garrat, 2011). The present study focuses on one of the pillars, i.e., the CEO, in terms of its announcement effect on the share price. The CEO is appointed by members of the Board, to oversee the firm's daily activities; while members of the Board themselves are appointed by shareholders who own the firm to oversee the long-term overall performance and legal compliances. Other than the appointment of a CEO and overseeing of the running of the firm, the Board also establishes the firm's long-term business plan in line with its objectives. The Board, the CEO, and the shareholders of the firm are guided by corporate governance. Thus, corporate governance strengthens the relationship among the shareholders, the CEO, and the Board. Corporate Governance also improves firm performance (Bhatt & Bhatt, 2017). The role of these parties is vital for corporate success, but that of the CEO



seems to be prominent due to the general perception of the CEO as being the driver of the organisation. The perception of the role of a new CEO in an organisation has changed markedly in recent times to such an extent that it is invariably reflected in the instability of the share price.

It should however be noted that the issue of CEO succession over the years has received attention from academicians and consultants. Although the investigation on CEO succession has been excessively done since the 1950s, the focus on CEO succession only emerged in the 1980s (Mehrabani & Mohamad, 2011). CEO succession is a continuous process of change of leadership that comprises both the events of CEO turnover and CEO appointment. More often, the appointment of a new CEO is more crucial to a firm than his or her removal. A new CEO has an impact on a firm's sustainability and future growth. Despite that, most studies on CEO succession have focused on CEO turnover. This has left a gap in related literature on CEO appointment which the present study fills.

### **1.1.1 Global Trend**

The focus on CEO turnover event has increased in parallel with the increase in CEO turnover rate globally. Table 1.1 reports an increasing trend of CEO turnover globally (PWC, 2018) over a period of 19 years. The percentage of CEO turnover globally increased by about 4.6% to about 17.5% (Column 1) in the year 2018, compared to 12.9% (Column 1) in the year 2000.

Similarly, during the same period, planned CEO turnover rate for all region except for the United State of America (US) and Canada shows an increasing trend. The highest CEO turnover rate in the year 2018 was in Western Europe and in other mature economies; it is 19.8% (Column 3), with an increase of 9.6% from 10.2% (Column 3) in the year 2000 and 19.7% (Column 4) with an increase of 9.7% from 10.0% (Column 4) in the year 2000. However, the percentage change is more significant for BRIC (Brazil, Russia, India, and China) and other emerging economies, where CEO turnover rate for BRIC increased by 13.5% from 4.0% (Column 5) in the year 2015 to 17.5% (Column 5) in the year 2018. Meanwhile, other emerging economies show an increase by 14.8% from 1.8% (Column 6) in the year 2000 to 16.6% (Column 6) in the year 2018. Only data for the US/Canada show a declining trend at 3.2% from 17.9% (Column 2) in the year 2000 to 14.7% (Column 2) in the year 2018.

**Table 1.1 : Overview of CEO Turnover Rate by Region from 2000 to 2018**

<b>Year</b>	<b>Globally (%)</b>	<b>US/Canada (%)</b>	<b>Western Europe (%)</b>	<b>Other Mature Economies (%)</b>	<b>BRIC (%)</b>	<b>Other Emerging Economies (%)</b>
	<b>(1)</b>	<b>(2)</b>	<b>(3)</b>	<b>(4)</b>	<b>(5)</b>	<b>(6)</b>
2000	12.90	17.90	10.20	10.00	4.00	1.80
2001	10.90	13.40	8.50	11.40	1.70	1.20
2002	10.80	10.90	11.60	9.80	18.30	2.90
2003	9.80	10.10	10.10	11.00	2.90	1.90
2004	14.70	12.80	16.50	14.60	23.90	13.10
2005	15.40	16.00	15.20	16.60	4.70	8.90
2006	14.40	15.40	16.10	12.40	14.20	7.60
2007	13.80	12.70	16.50	11.50	4.30	7.30
2008	14.40	15.00	16.50	16.60	9.80	9.60
2009	14.30	12.70	15.20	17.60	11.50	11.40
2010	11.60	11.40	8.70	13.70	10.80	15.90
2011	14.20	13.60	13.70	16.60	13.80	11.30
2012	15.00	14.30	14.70	15.70	15.10	16.30
2013	14.40	13.20	12.90	15.20	18.80	13.40
2014	14.30	13.20	14.30	14.70	15.30	15.90
2015	16.60	14.30	17.90	17.90	19.10	16.70
2016	14.90	14.20	15.30	15.10	15.70	13.60
2017	14.60	13.20	14.50	14.20	17.70	14.30
2018	17.50	14.70	19.80	19.70	17.50	16.60

**Note:** The data is derived from 2,500 largest firms globally divided by region: US/Canada, Western Europe (Austria, Belgium, Denmark, Finland, France, Germany, Guernsey, Ireland, Italy, Jersey, Luxembourg, Netherlands, Norway, Portugal, Spain, Sweden, Switzerland, and the United Kingdom); other mature economies (Argentina, Australia, Bahrain, Chile, Czech Republic, Hong Kong, Hungary, Japan, New Zealand, Poland, and Korea), BRIC (Brazil, Russia, India, and China) and other emerging economies (Egypt, Kazakhstan, Mexico, Nigeria, South Africa, Turkey, and Vietnam). Malaysia is mentioned as part of the other emerging economies in the year 2000 to 2017, however, it was removed in the year 2018.

**Source:** PWC (2018)

**Table 1.2 : Summary of Planned and Forced CEO Turnover Rate by Region from 2000 to 2018**

Year	Globally		US/Canada		Western Europe		Other Mature Economies		BRIC		Other Emerging Economies	
	Planned Turnover (%)	Forced Turnover (%)	Planned Turnover (%)	Forced Turnover (%)	Planned Turnover (%)	Forced Turnover (%)	Planned Turnover (%)	Forced Turnover (%)	Planned Turnover (%)	Forced Turnover (%)	Planned Turnover (%)	Forced Turnover (%)
	(1)	(2)	(1)	(2)	(1)	(2)	(1)	(2)	(1)	(2)	(1)	(2)
2000	6.40	3.40	8.20	5.40	3.5	2.60	7.8	1.20	4.00	0.00	0.00	1.80
2001	6.00	2.40	6.80	2.80	3.00	3.90	9.80	0.40	1.70	0.00	1.20	0.00
2002	5.00	4.40	5.10	4.20	5.60	4.40	3.70	4.80	8.30	10.00	2.90	0.00
2003	5.30	3.20	5.30	3.30	3.20	5.00	8.70	1.60	0.00	1.50	0.90	0.90
2004	7.70	4.50	6.40	3.60	7.30	6.50	9.10	3.50	19.50	3.50	4.00	8.10
2005	9.20	3.60	9.20	3.60	7.80	4.80	11.70	3.00	2.80	0.00	5.40	1.80
2006	6.60	4.60	6.20	4.60	5.60	5.70	8.20	3.70	5.80	7.50	3.80	3.80
2007	6.80	4.20	7.20	4.50	8.90	5.50	7.10	4.20	3.00	1.00	3.30	4.00
2008	7.20	5.10	7.00	4.30	8.10	5.70	8.70	7.00	4.40	3.80	6.10	3.50
2009	9.10	3.40	9.30	1.40	7.80	4.90	11.60	5.30	7.60	3.00	9.00	2.40
2010	7.70	2.20	6.40	2.00	6.00	1.50	10.70	1.50	6.90	3.20	10.60	4.30
2011	9.80	2.20	9.30	1.60	9.70	2.40	11.40	3.10	10.00	2.50	9.20	0.40
2012	10.80	2.80	9.00	2.70	10.60	3.30	12.90	2.40	10.10	2.90	13.30	2.50
2013	10.10	2.60	9.10	1.70	6.70	4.10	11.70	2.30	14.20	3.50	10.40	2.20
2014	11.20	1.90	9.80	1.50	10.00	3.00	12.00	1.80	12.90	1.80	14.90	1.00
2015	10.90	3.00	7.70	2.20	10.30	5.20	14.20	2.40	13.40	3.10	13.10	2.50
2016	10.30	2.40	8.70	2.10	8.70	3.70	10.80	3.20	13.50	1.60	11.70	0.60
2017	9.90	2.80	8.10	2.00	9.50	3.00	9.60	3.70	13.20	3.00	11.20	2.50
2018	12.00	3.60	8.30	2.90	11.10	5.80	15.60	3.40	14.50	2.30	12.90	3.70

**Note:** This table is derived from 2,500 largest firms globally divided by region: US/Canada, Western Europe (Austria, Belgium, Denmark, Finland, France, Germany, Guernsey, Ireland, Italy, Jersey, Luxembourg, Netherlands, Norway, Portugal, Spain, Sweden, Switzerland, and the United Kingdom); other mature economies (Argentina, Australia, Bahrain, Chile, Czech Republic, Hong Kong, Hungary, Japan, New Zealand, Poland, and Korea), BRIC (Brazil, Russia, India, and China) and other emerging economies (Egypt, Kazakhstan, Mexico, Nigeria, South Africa, Turkey, and Vietnam). Malaysia is mentioned under the other emerging market in the year 2017 but removed in the year 2018.

**Source:** PWC (2018)

Table 1.2 highlights planned and forced CEO turnover rate by region from 2000 to 2018. For planned CEO turnover rate, the highest CEO turnover rate of 15.6% (Column 1) is in other mature economies in the year 2018; while 14.5% (Column 1) is for BRIC in the same year. The change in percentage points is also higher for BRIC and other mature economies. However, the highest percentage change of 12.9% is for other emerging economies from zero (Column 1) in the year 2000 to 12.9% (Column 1) in the year 2018. For forced CEO turnover, even though the percentage is lower compared to planned CEO turnover, most of the regions show an increasing trend, except for the US/Canada region, which shows a drop of 2.5% from 5.4% (Column 2) in the year 2000 to 2.9% in the year 2018 (Column 2). The decline in CEO turnover rate in the US/Canada region could be the result of the government's decision to acknowledge the importance of CEO succession planning and the impact of the sudden removal of a CEO on a firm's day-to-day business operations.

In recent times, the effect of the coronavirus pandemic globally has highlighted the critical need for CEO succession planning, especially for countries that have been badly hit (Cheng, Groysberg, & Heal, 2020). From Table 1-3, the survey result of 5,000 the Board on the decision to have CEO succession planning is presented for all countries by region. In total, about 53% (Column 1) of the firms do not have contingent planning for CEO succession, 41% (Column 2) do not discuss CEO succession, and 54% (Column 3) do not have an effective planning process for CEO succession.

Table 1.3, three regions that do not have any contingent planning to establish CEO succession plan (CP) are Asia with 64% (Column 1), Middle East with 69% (Column 1), and Central/South America with 72% (Column 1). Two regions that do not regularly discuss CEO succession are Asia with 73% (Column 2) and Middle East with 76% (Column 2). However, on the question of not regularly discussing CEO succession, Australia/New Zealand and North America have a lower percentage of 23% (Column 2) and 29% (Column 2), respectively. Lower percentage means that the two regions do discuss CEO succession planning regularly.

**Table 1.3 : Survey on Succession Planning for all Countries by Region**

Countries by Region	No Contingent Planning for CEO Succession (%)	No Regular Discussion on CEO Succession (%)	No Effective Plan for CEO Succession (%)
	(1)	(2)	(3)
Africa	55	34	48
Asia	64	73	68
Australia/ New Zealand	56	23	52
Central/South America	72	49	54
Eastern Europe/Russia	60	43	81
Middle East	69	76	73
North America	45	29	47
Western Europe	59	48	59
Total	53	41	54

**Note:** The table is derived from a survey 5,000 boards of directors globally based on countries affected by on the coronavirus as at 21 April 2020

**Source:** Cheng *et al.* (2020)

The US Security and Exchange Commission requires all listed firms to disclose the CP in their corporate governance framework. On 29 October 2009, this Commission ruled that firms should no longer use Rule 14a-8(i) (7) to avoid submission of a CP. Following this decision, firms in the US began to include CP in their proxy statement, giving assurance to the investors of their commitment towards establishing a proper succession plan (Ferris & O'Brien, 2010). Similarly, in Australia, the Australian Stock Exchange (ASX) Corporate Governance Council (2014) gives major importance to CP by requiring the Board to establish a nomination committee to oversee CEO succession planning as per the corporate governance principles and recommendations (Recommendation 2.1). In Table 1-3 also, regions that do not have an effective plan for CEO succession are mainly Eastern Europe/Russia and Middle East, with the highest percentages of 81% (Column 3) and 73% (Column 3), respectively.

### 1.1.2 CEO Succession in Malaysia

In Malaysia, 76% of firms are family-owned businesses (Economist, 2015). For family-owned firms, selection of the CEO is conditioned by 'family power, family generation, directors' independence, shareholder protection, and past firm performance' (Ansari, Goergen, & Mira, 2014). A report by Pricewaterhouse Coopers (PwC) (2016) highlights that 69% of family-owned firms in Malaysia have next-generation family members working for the firm, but only 15% have a robust and documented succession plan. In another report by the Associated Chinese Chambers of Commerce & Industry (ACCCIM) Family Business Survey of 2018, only 13% of the family-owned firms have a robust and documented succession plan, while 63% of the respondents claimed to have established an informal plan or are thinking about it but have not documented it, and the remaining 24% of the respondents do not think about it as a priority (ACCCIM, 2019). These figures in Malaysia are far lower in comparison to the global survey.



Based on the Minority Shareholder Watch Group (MSWG), only one-fifth of the top 100 firms listed on Bursa Malaysia in the year 2016 have adopted a proper CEO succession policy (MSWG, 2017). Although the Malaysian government, through the Putrajaya Committee for Government Linked Companies (GLC) High Performance, has launched the green book (Enhancing Board Effectiveness) under the GLC Transformation Programme, to address among others, CP and the issue of CEO sudden removal, the document does not address the need for proper adoption of a CEO succession policy and succession plan by way of making it compulsory (Khazanah, 2006). Rather, it is only a guideline and only applicable to GLCs<sup>1</sup>.

In addition to the green book, the Ministry of Finance has issued a guideline for the Board appointed by the Ministry of Finance Incorporated (MOF Inc.), among others, to recommend CP to the Board. In planned CEO succession, selection of the CEO is based on skills and experiences that are matched with current performance, competitive landscape and aspirations of the firm (Khazanah, 2006). The selection process is based on three categories of the CEO succession model: 'Relay race', 'Horse race' and 'Greyhound race'. The 'Relay' and 'Horse' race models are based on internal candidates, while the 'Greyhound' race model is based on selection from both internal and external candidates. In the Relay race model, the candidate is identified by the Board and groomed by the current CEO, while for the Horse race model, several identified candidates compete and the Board selects the candidate who is perceived as fit for the position. The third model, Greyhound race, is similar to the Horse race model but the candidate is selected from a pool of talented individuals from both internal and external sources. However, this model is only applicable in critical situations, such as when there is a leadership gap or when the firm needs different leadership styles to transform the firm's performance. To ensure the CEO is accountable for all decisions made while in position, the appointment of the CEO is on a contractual basis and includes a provision to measure CEO's performance based on achievement of Key Performance Indicators (KPI), where the KPIs of the CEO are matched with the KPIs of the firm (Khazanah, 2006).

However, this guideline is limited only for MOF Inc. companies. Failure to establish a CP will delay the CEO's selection process, which can lead to business risks (Ferris & O'brien, 2010), as well as inherent court battles, especially in family-owned businesses (Lopez, 2017). Therefore, the Board has a major responsibility in selecting the right CEO who matches current performance and objectives of the firm as well as the competitive surroundings (Khazanah, 2006).

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<sup>1</sup>GLCs are companies that have a primary commercial objective and which are owned by government linked investment companies (which include MOF Inc companies, such as Telekom Malaysia Bhd, Tenaga Nasional Bhd, Khazanah Nasional Bhd), Employees Provident Fund, Lembaga Tabung Haji, Armed Forces Fund Board, Retirement Fund (Inc) and Permodalan Nasional Bhd).

### 1.1.3 Redefining CEO Succession Event

In the past, CEO succession was mainly referred to as CEO turnover. Warner, Watts, & Wruck (1988) classified CEO succession as an event that occurs due to “redesignation, retirement, no reason, control change, death, and poor performance, taking other positions, policy difference, health, getting fired, and others”.

Farrell & Whidbee (2003) and Allgood & Farrell (2000) defined CEO succession as an event that occurs “voluntarily” or “by force”. This definition is driven by the EMH which emphasises on the timing of the release of information. This implies that whether events occur voluntarily or forcefully, the time it occurs is of importance and it is expected to result in a more significant reaction.

According to Farrell & Whidbee (2003) and Allgood & Farrell (2000), voluntary events occur due to “retirement, normal management succession, death, or illness, or those involving CEO’s departure for a prestigious position elsewhere, meanwhile, forced removal occurs due to resignations, pressure from the board of directors, pressure from outside block-holders, pressure from bank lenders, policy or personality disagreements, demotion, being fired, scandal, poor performance, bankruptcy, and reorganisation”.

In terms of planned succession, Lambertides (2009) classified CEO succession as an “initiated” event. An initiated event by the CEO is similar to the voluntary event, while an initiated event by the Board is a forced event. However, some of the classifications under voluntary event occur unexpectedly, and are beyond the control of the CEO. On this basis, Rhim, Peluchette, & Song (2006) reclassified CEO succession as “anticipated” or “unanticipated”. The anticipated classification includes events, such as retirement, while unanticipated classification includes events caused by death, health, poor performance of a firm, legal problems, forced resignation, and other personal reasons of the predecessor, merger/acquisition-related, and restructuring/reorganisation of a firm.

In Malaysia, Ishak & Latif (2012) classified CEO succession as turnover and successor’s selection. However, it is unclear if the successor’s origin is representing CEO appointment announcement or if announcement of CEO turnover and successor is occurring on the same day from the same firm. When CEO succession is not clearly defined, findings are always biased towards CEO appointment; more so when the finding is based on the appointment of an outsider due to forced removal (Hassan, Jaffar, & Rosly, 2016; Ishak, Ismail, & Abdullah, 2013; Charitou, Patis, & Vlittis, 2010; Ishak, 2010; Cools & Prags, 2007).

Thus, for this study, CEO succession is classified as a process of change of CEO, which includes both CEO appointment and turnover. The CEO succession event is classified as: (1) planned; and (2) unplanned. The planned CEO succession announcement is when CEO appointment and turnover announcement occur on the

same day. This succession definition is based on the firm's CP. This plan is a strategic document that is established by the Board for the selection of the CEO, which most likely induces same-day smooth CEO succession. Meanwhile, unplanned succession is appointment and removal of the CEO that happens on a different day, either forced/anticipated or voluntarily/initiated. Henceforth, planned succession announcement event refers to unplanned CEO turnover and unplanned CEO appointment announcement.

## **1.2 Statement of Research Problem**

In a recent finding by Kato & Honjo (2020), CEO succession influences sales growth in new firms. The unplanned CEO turnover reduces shareholder returns by 13% compared to 0.5% for planned CEO turnover (PwC, 2015). Without proper succession planning, firms will not be prepared to address complex business problems, unexpected executive departure, and the geopolitical demands of the global market (LeCounte, Prieto, & Phipps, 2017). Moreover, firms that do not have a contingency plan, cannot discuss the CP regularly and lack of such a plan creates leadership instability (Cheng et al., 2020). Failure to institute a CP is viewed as a business risk, which subsequently will have an impact on firm performance (Gehrke, 2019 and Ferris & O'Brien, 2010). In family-owned businesses, failure to document a succession plan can cause inheritance litigations upon the death of the founder (Lopez, 2017). The result of poor succession planning will lead to poor firm performance (Charan, 2005), which subsequently will lead to higher turnover (Ismail, Ahmad, Sarun, & Mahjom, 2020), and corporate instability because the successor usually will change the firm's strategy (Hassan et al., 2016).

Based on finding ACCCIM (2019) and MWSG (2017), most of the firms in Malaysia is still reluctant to acknowledge CP. A firm's negligence occurs probably because the government has given less emphasis on having a CEO succession policy or introduced such policy measures in the Malaysia Code of Corporate Governance (MCCG). Even though the government has highlighted this policy measure under the GLC Transformation Programme, it may be a mere guideline for GLCs and is not mandatory.

In recent times, the incidence of CEO turnover in Malaysian listed firms has increased similar to global trends and this has exacerbated investors' apathy to the extent that it may likely lead to disinvestment. Some of the prominent exit news are the sudden death of YTL CEO in the year 2017 (Lopez, 2017); resignation of two Malaysian Airline System Berhad CEOs in the years 2016 and 2017 (Tay, 2016; Yunus, 2017) and the Telekom Malaysia Berhad. CEO in the year 2018 (Zainul, 2018); as well as suspension of FGV Holdings Berhad. CEO in the year 2018 following the investigation of the firm's financial loss (The Star, 2018). Moreover, the recent political change in Malaysia has led to a sudden exit of CEOs from both private and statutory bodies. This negative news on removal of CEO has impacted the firms' share prices. Most often, it is during a crisis that succession planning is given importance. Santora (2020) defined it as emergency succession planning. A



CP could reduce the impact of such sudden news of a CEO's removal on the share price and build investors' confidence in the firm, in particular, and the economy, at large.

In reviewing earlier shortfalls on CP, it is found that most empirical findings have focused on developed nations, with very few on emerging markets, for which the results have been both inconclusive and largely contradictory. For instance, different countries have different regulations and policy measures that may have a different impact on a CEO's influence on a firm, and this could result in the inconsistency (Rose, 2018). A developed nation is considered ahead of other countries when it comes to implementing policy measures regarding corporate governance, in particular, the succession plan. Thus, it would be inappropriate to generalise findings from a developed nation to the emerging economies, most of which are politically, economically, and culturally diverse.

Also, very few studies have looked into the impact of CEO succession policy on share price. More often, studies on CEO succession have been conducted within the ambit of management rather than finance, with high usage of management theories, especially the upper echelon theory, to analyse CEO characteristics.

The announcement impact on CEO succession policy could be more properly observed when CEO appointment and turnover announcement occur on the same event day, because simultaneous announcements generate positive reaction to share price (Cools & Praag, 2007; Hassan et al., 2016; Charitou et al., 2010). CEO succession is a process of change of leadership, involving both appointment and turnover of a CEO. However, most firms have failed to establish a CP, and therefore, the appointment of a new CEO is often delayed. Past findings have viewed CEO succession separately, as either CEO appointment or CEO turnover, with more emphasis given to CEO turnover. Moreover, past definitions of CEO succession are unclear, which may result in discrepancy in the finding. Therefore, in this study, CEO succession is defined as change of leadership that includes both the events of removal and appointment of CEO, with reclassification as "planned CEO succession" and "unplanned CEO succession". Planned succession is for firms that have a CP and CEO appointment and turnover announcement occurring on the same event day; while unplanned CEO succession is for firms that do not have a CP.

In view of the above, it is safer to argue that there are a number of gaps in extant literature in the relationship between CP and firm value. While studies on CEO appointment announcement have focused on demographic factors, such as age, origin, experience, education and gender, most academicians and consulting firms are trying to bridge the gap in the relationship between CEO turnover announcement and firm value. The announcement of CEO turnover is viewed as more relevant than CEO appointment as news of a CEO's departure is typically unexpected, and thus, has a different implication on a firm based on the reason for departure.

By examining the effect of CEO appointment and turnover announcement occurring on the same day on the share price, and the effect of CEO characteristics on the share price as well as the moderating role of CP in the relationship between CEO characteristics and share price, new knowledge is expected to be added to this field to narrow or bridge the identified gaps in literature.

### **1.3 Research Questions**

Based on the issues highlighted in this study, the following research questions are raised to find a solution to the problem this study seeks to resolve:

- i. What is the effect of planned and unplanned CEO appointment and turnover announcement on the share price?
- ii. Do CEO characteristics (age, origin, education, experience, stock ownership, and gender) have a significant effect on the share price reaction upon planned and unplanned CEO appointment and turnover announcement?
- iii. Does the CP moderate the relationship between the characteristics of the CEO (age, origin, education, experience, stock ownership, and gender) and the share price reaction upon planned and unplanned CEO appointment and turnover announcement?

### **1.4 Objectives of the Study**

In general, the main objective of the study is to examine the effect of planned and unplanned CEO appointment and turnover announcement based on the new reclassification of the announcement. This study also looks at the influence of CEO characteristics on the share price reaction and how succession plan can influence CEO demographics and the share price reaction. Specifically, these are the following objectives:

- i. To examine the effect of planned and unplanned CEO appointment and turnover announcement on the share price;
- ii. To investigate if CEO characteristics (age, origin, education, experience, stock ownership and gender) have a significant effect on the share price reaction upon planned and unplanned CEO appointment and turnover announcement; and
- iii. To examine if the CP moderates the relationship between CEO characteristics (age, origin, education, experience, stock ownership, and gender) and the share price reaction upon planned and unplanned CEO appointment and turnover announcement.

Meeting the above objectives will provide useful information with regards to the impact of CEO appointment and turnover announcement on the share price, especially for firms that have an established CP.

## **1.5 The Significance of the Study**

Studies on CEO succession have often been viewed from the human resource management planning angle and less from finance and governance perspectives as most studies have had a high tendency to use the upper echelon theory to relate the impact of CEO characteristics on firm performance. The upper echelon theory explains the connection between a firm's strategic decisions and the characteristics of top management, for example, age, tenure, education and experience.

More often, research on finance is fragmented by types of announcement and other additional materials that are argued to have been responsible for ambiguity in past empirical findings. However, this research provides a holistic view, in that it reviews the impact of CEO succession announcement simultaneously and individually by CEO appointment and turnover announcement.

Next, this thesis explores the impact of CEO succession announcement based on planned and unplanned succession. The breakdown by planned and unplanned succession contributes towards identifying another dimension of succession description. Specifically, the study investigates planned CEO succession announcement (appointment and turnover) that happens on the same day, but separately for unplanned succession. Therefore, the study enables stakeholders to look further into the actual impact of CP on firm value.

The results will likely lead to better leadership planning for the firm in ensuring sustainable growth. The findings can contribute to better policy formulation and a more targeted policy approach to CEO succession policies and the need to establish CP as part of the governance structure.

## 1.6 Chapter Summary

This chapter provides an introductory overview of the key issues of the study. Firstly, the researcher discusses the background to the study. It has been reported that most studies on CEO succession are fragmented and examined separately by types of announcement. While the appointment of a CEO could have long-term effects on a firm, the removal of a CEO is likely to have an immediate effect on the firm. The chapter also provides justification for the conduct of this study based on the problems identified, to include but not limited to, past empirical findings on CEO succession which are typically too broad, ambiguous and inconsistent. The inconsistency is probably due to a number of factors, including differences of country demographics and unclear definition of CEO succession. Furthermore, the chapter raises research questions and objectives to drive and guide this investigation. There is among others, issues such as review of the trend of the CEO succession nationally and globally. In the last section of the chapter, the significance of the findings of this study are mentioned, including those who will benefit, such as policy-makers, investors, the academia as well as the research community. The next chapter elaborates on the theories and empirical findings as well as develops the conceptual framework based on the hypothesis.

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