

Influence of the Company Performance and Ownership Structure on CEO Turnover: the Evidence of Slovenia

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The goal of the article is to research relation between CEO turnover, company performance ownership structure concentration and change. The empirical evidence presented in the article is based on the sample of 211 Slovenian companies in period 1998-2002. As expected the relation between CEO turnover and company performance is inverse. Ownership concentration is not an efficient corporate governance mechanism. Opposite change in the ownership structure influence on the management turnover in the poorly performing companies.

Key words: CEO turnover, ownership structure, ownership concentration, ownership change corporate governance, agency theory

Vpliv poslovanja podjetij in lastniške strukture na zamenjavo predsednika uprave: Primer Slovenije

Cilj članka je raziskati relacijo med zamenjavo predsednika uprave in uspešnostjo poslovanja podjetij, lastniško strukturo, koncentracijo lastništva ter zamenjavo lastništva. Za empirično testiranje hipotez je bil uporabljen vzorec od 211 slovenskih podjetij v obdobju 1998-2002. Kot pričakovano rezultati so pokazali, da je relacija med zamenjavo predsednika uprave in poslovanjem podjetij inverzna. Koncentracija lastništva ni učinkovit mehanizem vladanja podjetjem. Nasprotno zamenjava lastniške strukture vpliva na zamenjavo predsednikov uprav v podjetjih, ki slabo poslujejo.

Ključne besede: zamenjava predsednika uprave, lastniška struktura, koncentracija lastništva, zamenjava lastništva, vladanje podjetjem, teorija agenta

1 Introduction

The separation of ownership and control is a phenomenon that can explain the incidence of CEO turnover. Due to the separation managers become the administrators of the shareholders' wealth. In the process, both parties – managers and owners – want to maximise their interests, therefore expropriation of the CEO position is not rare. One powerful weapon in the hands of owners in this situation is the threat of CEO dismissal. Therefore, relation between company performance and management turnover is expected to be inverse (Warner et. al, 1988; Weisbach, 1988; Jensen and Murphy, 1990; Murphy and Zimmerman, 1993; Denis and Denis, 1995; Lausten, 2000; Brunello et.al, 2000; Kaplan, 1994 a,b; Kiang and Shivadasani, 1995; Renneboog, 2000 etc.). In order to practice this threat an owner can use different corporate governance mechanisms.

One of the internal corporate governance mechanisms that can be used are ownership structure, concentration and change. Denis et al. (1997) believed that the possibility of executive managers' turnover is positively related to the presence of external owners. On the contrary, Jensen (1993) claimed that managerial shareholding helps align

the interests of shareholders and managers (principals and agents). Berle and Means (1932) claimed that controlling block holders are more efficient monitors of a company's performance than a large number of shareholders. So, the probability of turnover in poorly performing companies in the case of concentrated ownership is higher and opposite. An ownership change is usually connected with management turnover. In these cases, there is a higher probability that the management turnover is not connected with the poor performance of the company but is instead caused by an ownership change (hostile or friendly takeover). Empirical researches (Holderness and Sheeham, 1985; Barclay and Holderness, 1991) have shown that the probability of management turnover is higher after a company has been taken over by a new owner.

Research results on the sample of Slovenian companies showed that external owners (funds and other companies) are not better principals than insider owners (employees and managers). Further, ownership concentration is not identified as an efficient corporate governance mechanism. Therefore, concentration does not improve the efficiency of monitoring control. Opposite ownership change is an efficient corporate governance mechanism used for disciplining poorly performing managers.

The rest of the paper proceeds as follows. The next section briefly describes empirical evidence on turnover performance relation, followed by the findings and conclusions of the existing literature regarding the influence of the ownership structure, concentration and change on CEO turnover. Influence of management and company characteristics on management turnover is presented in section four. Data and methodology used are described in the section fifth. The sixth section is dedicated to the description of ownership structure and its change in Slovenia and CEO characteristics and turnover rates. The results of the probit regression model researching the influence of the ownership structure, concentration and change on management turnover are presented in the section seventh. Discussion on policy implications and conclusions are presented in the section eight.

2 Performance-turnover relation

The sensitivity of top management turnover to firm performance is usually interpreted as an indication that the shareholders hold the CEO responsible for poor corporate performance and that they dismiss an underperforming CEO in order to increase the corporate value. It is commonly reported in the empirical studies that a poor corporate performance is associated with CEO turnover.

Most of the empirical evidence in developed countries on turnover-performance confirms inverse relation between two variables, meaning that shareholders are replacing poor performing managers (Warner *et al.*, 1988; Weisbach, 1988; Jensen and Murphy, 1990; Marphy and Zimmerman, 1993; Denis and Denis, 1995; Lausten, 2000; Brunello *et al.*, 2000; Kaplan, 1994 a,b; Kiang and Shivadasani, 1995; Renneboog, 2000 *etc.*).

Empirical evidence in transition countries is scarce. Few studies research the turnover – performance relation and confirm that relation is negative. Gibson (2003) empirically examines the link between management turnover and firm performance in eight emerging markets and concludes that there is a significant negative relationship between management turnover and companies performance. Aivazian *et al.* (2005) reported an inverse relationship between management turnover and companies' performance on a sample of incorporated Chinese SOEs (state-owned enterprises). For a sample of Russian companies, REB Monitoring (2003) found that the replacement of top executives is more likely to occur in poorly performing companies. Eriksson (2005) also provided evidence on management turnover in the Czech and Slovak Republics. He found a significant and negative relationship between management turnover and companies' performance levels. Frydman, Hessel and Rapaczynski (2000) claim that management turnover among Czech, Hungarian and Polish companies affected with the company revenue growth. The companies in which new managers were appointed had higher growth rates. Fidermuc and Fidermuc (2006) analyzed management replacement after the privatization in Czech Republic. Authors showed that company performance improved after appointing the new manager. On a sample

of large Ukrainian companies, Warzynski (2001) found that management turnover did not effect a change in productivity in state-owned enterprises but had a small and positive effect in privatised companies.

3 Ownership characteristics as a corporate governance mechanism controlling management turnover

Three ownership characteristics influence on CEO turnover: ownership identity, ownership concentration and ownership change.

Theoretical and empirical evidence researching relation between **ownership identity** and CEO turnover mainly focus on the proportion of insiders and outsiders owners. Concerning Jensen's hypothesis on the convergence of interest, managerial shareholding helps align the interests of shareholders and managers (principals and agents). With regard to this hypothesis, as the proportion of managerial equity grows the company's performance improves as well (Jensen, 1993). De Angelo and De Angelo (1985) also found that it is reasonable for owners to motivate the managers to invest in the company and share their faith with other company shareholders. On the other side, managerial ownership lowers the probability of replacing management which becomes a problem if poor managers are appointed. Further, managerial ownership can inhibit the external control market, reduce the effectiveness of internal control and reduce the probability of receiving a takeover bid. Therefore, managerial ownership can be referred to as good if there is a successful manager in the position and 'too much of a good thing' if poor performing managers are appointed.

Evidence of the influence of managerial ownership on the turnover-performance relationship is mostly limited to US practice. On a sample of American companies, Weisbach (1988) did not find evidence that having a top executive shareholding reduces the probability of turnover. Morck *et al.* (1988) claimed that boards with significant managerial ownership are more likely to behave in the interests of shareholders due to the fact they are owners. On the other hand, Denis *et al.* (1997) found that management turnover is significantly less sensitive to performance when managers hold 5 to 25 percent of ownership shares than when directors hold less than 5 percent of the shares, meaning there is lower possibility of a poor performing manager being replaced if they hold higher ownership shares in the company. Mikelson and Partch (1996) also found a negative relationship between management turnover and management ownership of a company. UK practice shows that managerial ownership reduces the probability of management turnover (Dahya, 1988; Dedman, 2003; Conyon and Florou, 2002).

Parrino *et al.* (2003) and Denis *et al.* (1997) focus on institutional investors and their influence on CEO turnover and found that institutional investors positively affects the probability of top executive turnover due to poor performance.

Brunello *et al.* (2003) on the sample of Italian companies

found that presence of the CEO as a controlling shareholder increases the sensitivity of turnover to performance. Voplin (2002) drew a different conclusion on a sample of Italian companies. In Russia, inside ownership exerts a negative impact on management turnover probability while outside ownership has a positive one (REB Monitoring, 2003). In the case of Danish companies Lausten (2002) proved that family ownership can cause poor corporate governance. On the contrary, the presence of foreign and other domestic companies raise the probability of a poorly performing manager's turnover. Ronneboog (2000) found that neither large institutional investors (banks, investment funds and insurance companies) nor holding companies seem to be involved in active corporate monitoring. In contrast, management replacement is influenced by large industrial investors and blocks held by families, however not significantly. Kang and Shivdasani (1995) in a case of Japanese companies indicated that the relationship between turnover and performance is significantly stronger for a firm tied to a main bank or a member of a keiretsu. On the other hand, Kaplan (1994a) did not confirm that banks or large block holders increase the probability of a Japanese management turnover in the case of a poor performance.

Concentrated ownership should provide efficient management control, the maximisation of shareholders' interests and the availability of external sources for financing the company (Shleifer and Vishny, 1997). Bearle and Means (1932) claim that controlling block holders are more efficient monitors of a company's performance than a large number of minority stockholders. So the probability of turnover should be higher in the case of concentrated ownership. However, little empirical evidence confirms this hypothesis. For instance, the Belgian corporate governance system is characterised by high ownership concentration yet Renneboog (2000) showed there is scant evidence about the corporate control role of large shareholders. As expected, empirical evidence from the UK and the US does not support this hypothesis (Franks *et al.*, 2001; Ronneboog and Trojanowski, 2003; Denis and Denis, 1995; Franks and Mayers, 2001). Opposite Voplin (2002) on a sample of Italian companies recorded a more sensitive turnover-performance relationship due to ownership concentration.

An ownership change is usually connected with management turnover especially in the case of poorly performing company (Holderness *et al.*, 1985; Barclay *et al.*, 1991; Franks *et al.*, 2001; Wayne and Megan, 1997; Mikkelsen and Partch, 1997). The same evidence can be recorded in developing countries (REB Monitoring, 2003; Gibson, 2003).

4 Management and company characteristics

Besides the stated corporate governance mechanisms, management and company characteristics' impact on the probability of management turnover will be tested. Within

management's characteristics, management tenure and age have mostly been used in the empirical studies so far (Kaplan, 1994 a,b; Franks *et al.*, 2001; Kang and Shivdasani, 1995; Lausten, 2001; Gibson, 2003; Suchard *et al.*, 2001; Brunello *et al.*, 2003). It is shown that older management with a higher tenure has a greater probability of being replaced.

Company size is the mostly used measure for testing the influence of company characteristics on management turnover (Conyon and Nicolitsas, 1998; Cosh and Hughes, 1997; Lausten, 2002; Suchard *et al.* 2001; Eriksson, 2005; Zhou, 2000; Warner *et al.*, 1988). Empirical evidence is inconsistent when explaining the influence of company size on management turnover. Some research has found that the probability of management turnover in larger companies, while others claim the opposite. This hypothesis will be tested in the case of Slovenia.

Last but not least, financial leverage can influence management turnover (Hart, 1995; Hotchkiss, 1995; Franks *et al.*, 2001; Renneboog, 2000). Creditors' power to influence the business decisions of the company arises from the many controllers' rights belonging to them when the company does not fulfil all of its responsibilities. High business risk and low liquidity raise the probability of a company going into bankruptcy, which ultimately leads to management turnover. Whether higher financial leverage increases the probability of management turnover in Slovenian companies will also be investigated in this article.

5 Hypothesis, data and methodology

Hypotheses tested within this article are listed below:

- H.1: The relationship between CEO turnover and company performance is expected to be inverse.*
- H.2: A higher proportion of ownership controlled by outsiders (funds and other companies) increases the probability of a management turnover in poorly performing companies.*
- H.3: Outsiders as controlling shareholders increase the probability of a management turnover in poorly performing companies.*
- H.4: An ownership change positively influences a management turnover in poorly performing companies.*
- H.5: Older and management board members with higher tenure decrease the probability of CEO turnover.*
- H.6: Company size influences the probability of CEO turnover.*
- H.7: The higher the financial leverage the higher the probability of a CEO turnover.*

In order to test influence of the corporate governance mechanisms and company performance on management turnover, primary and secondary data sources were used.

Primary data used for this research were collected within quantitative research performed by the Institute for South-East Europe (ISEE)¹. The research took place in the period from May to September 2003. The first step within

¹ The research was conducted within the project 'Regional Think Tank Partnership Project' and was financed by the IRIS.

the research was the preparation of the questionnaire, which was addressed to Slovenian firms. The questionnaire was composed of five parts: corporate governance system characteristics; management characteristics; companies' core competences; financing issues; and research and development. For the purpose of the analysis presented in this paper the questions from the first two parts addressed in the questionnaire, namely corporate governance system and management characteristics, were used. The questionnaire was mailed to 623 Slovenian companies. 211 questionnaires were returned. The high response rate of 34 percent was the result of a few months' work. The main database is structured as an unbalanced panel dataset collected from the questionnaires addressed to the firms.² Data were collected for the period 1998-2002.

Secondary data sources on financial data. Financial reports were available from the Agency of the Republic of Slovenia for Public Legal Records and Related Services. The Agency keeps records for all joint-stock and limited companies that are not financial institutions. There are approximately 37,000 legal entities in the Agency's register. Financial reports consist of balance sheets and income statements as well as information on a company's main activity, main office location, number of employees etc. Those data were used to compose a second database containing balance sheet and income statement data for the 211 firms in our sample, namely companies that co-operated in the research.

Most companies (81 percent) in the sample are registered as joint-stock companies. The interviewed companies represented 19.5 percent of the sales and assets of all Slovenian companies and employed 20.1 percent of all employees in 2002. The average number of employees in the companies in the sample varies through the years from 458 to 496 (the standard deviations are very high). If companies are classified with regard to the classification recommended by the Companies Act from 1993, the sample was composed of 10.7 percent of small companies³, 75.8 percent of medium-sized companies⁴ and 13.5 percent of large companies⁵. Financial indicators showed that, on average, total company sales grew from 7.2 to 11.5 percent on the yearly level. The return on assets (ROA) in the observed period was between 9.4 and 11 percent, while the return on equity (ROE) was between 4.1 and 5.3 percent. The companies in the sample had a debt-to-assets ratio of around 40 percent.

To examine the impact of company performance and corporate governance mechanisms on management turnover, the Logit, Probit or Tobit regression models have been employed in most of the empirical studies conducted so far. To examine the impact of the company performance and ownership characteristics on CEO turnover in Slovenia, a Probit regression model was employed:

$$P(\text{CEO turnover}) = f(\beta_1 + \beta_2 X_{(\text{Performance measures variables})} + \beta_3 X_{(\text{Ownership identity, ownership concentration, ownership change})} + \beta_4 X_{(\text{Management characteristics variables})} + \beta_5 X_{(\text{Company characteristic variable and Financial leverage})} + \varepsilon$$

In order to test the relationship between turnover and performance two accounting measures of performance were used. Market measures of performance were not used since all companies in the sample were not listed⁶ on the Ljubljana Stock Exchange. Current (in year t) and lagged performance values (in year $t-1$ and $t-2$) were used in the regression analysis. All performance measures were available for the period 1998-2002. The first measure of performance used is *sales growth*. The second measure of performance used in the regression is return on assets (ROA)⁷. The both performance measures were adjusted for the industry average⁸.

Data on owners' identity were collected within the primary research. For regression analysis, state and investment fund ownership shares were combined within one variable: ownership of funds, domestic and foreign companies' shares in one variable: company ownership and employees and management ownership shares in one variable: internal ownership. The reference group was the ownership shares of bank, state and minority shareholders. Ownership share data were used to form dummy variables representing the ownership concentration in the hands of a specific group of owners. Namely, the dummy variable took the value of 1 if a specific owner holds controlling shareholdings in the company (an ownership share higher than 50 percent) and 0 if it does not. Dummy variables were also used for ownership change. If the tracked ownership change was 10 percent or higher then dummies variables took the value of 1, and the value of 0 otherwise. I took 10 percent as a threshold value due to the fact that an owner gains substantial power in a company's decision-making process if he increases his ownership share by 10 or more percent (an increase in shareholding for example by 1 or

² The panel is unbalanced, there are some missing values for different reasons (e.g. the company was established after 1998), so the actual number of observations differs from analysis to analysis.

³ A small company has: average number of employees up to 50; average annual income up to SIT 200 million (EUR 834,585) and average assets value up to SIT 100 million (EUR 417,292).

⁴ Medium company has: average number of employees from 51 to 250, average annual income from SIT 200 million (EUR 834,585) up to SIT 800 million (EUR 3.34 million) and an average value of assets from SIT 100 million (EUR 417,292) to SIT 400 million (EUR 1.67 million).

⁵ Large companies are companies which have at least two criteria higher than those companies classified as medium sized (more than 251 employees, average annual income higher than SIT 800 million (EUR 3.34 million) and an average value of assets higher than SIT 400 million (EUR 1.67 million).

⁶ 42 out of 211 companies from the sample are not listed on the Ljubljana Stock Exchange.

⁷ ROA is defined as the ratio between EBIT related to firm total assets.

⁸ Newly created performance measures represent company performance plus the difference in company performance and the industry average (for example, $DTSt_i + (DTSt_i - DTSt)$). Using industry-adjusted variables company performance was adjusted for the industry average. For example, if the whole industry performed poorly, by adjusting company performance for industry average, the company results would be improved. Industry-adjusted variables for testing turnover performance relationship were also used by Dahya *et al.* (2002); Kang and Shivdasani (1995); Denis and Denis (1995); Renneboog (2000); Brunello *et al.* (2003).

2 percent does not increase the owner's decision-making power substantially). In order to relate ownership identity, concentration and change with company performance an additional set of variables was created. Namely, ownership characteristic variables were interacted with performance measures: total sales growth and return on assets (values at moment t).

6 Ownership structure in Slovenia

Privatisation gave an important role to the insiders (employees and managers) and funds (state and investment) in the process of governing Slovenian companies. However, the ownership structure changed after the privatisation and is still in the process of transformation. Data on the ownership structure in Slovenian companies were collected during quantitative research for the period 1998-2003. In the observed period on a sample of 211 companies the most important individual owners were domestic and foreign companies, employees⁹ and investment funds controlling on average 22.9 20.1 and 15.4 percent of the ownership, respectively. State funds owned on average 12.4 percent of the shares, while banks held on average 1.7 percent. Management¹⁰ and minority shareholders held on average approximately the same ownership shares, amounting to 3 percent. The trends show an increase in the average ownership shares in the hands of domestic and foreign non-financial companies. On the contrary, the average ownership shares controlled by state funds, investment funds and employees are decreasing¹¹ (Table 1).

The results point to the conclusion that employees' and state funds' ownership 'created' during and after privatisation has been spilling over into the hands of managers and non-financial domestic companies. Ribnikar (1995) believed that the ownership share of employees is decreasing due to the short-term orientation of employees as owners. 'Employees will be prepared to sell shares at the moment, when they will receive more for it, than they had paid' (Ribnikar, 1995). Many authors claim that the reduction of the ownership controlled by state funds is highly important. Simoneti *et al.* (2005) claimed that the artificially made state funds were the transitional owners of the companies' shares and they showed themselves to be good sellers of their ownership to 'final' owners. Pahor *et al.* (2003) reported that the transformation of state and investment funds is highly important for achieving a normal market-oriented economy with a reduced political influence on business. Domadenik (2003) shared their opinion. Based on the above, it is expected that state funds will continue to decrease their ownership and thus the state's influence on the economy. The trend of increasing ownership held by other domestic non-financial companies will continue, while it is to be expected that foreign companies will raise their ownership in the future.

Ownership concentration in Slovenian companies remained low and in 1998 half of the firms listed on the Ljubljana Stock Exchange did not have an owner holding more than 20 percent of the voting rights, while the concentration of ownership and control was slightly higher in the case of non-listed companies (Gregorič, 2003). The trends showing the increasing concentration of ownership among Slovenian companies. Based on data obtained from the official Shareholders' Register kept and updated by the Central Clearing Securities Corporation, the largest owner (C1) in 211 companies in the 1998-01 period had an average share of 35 percent, the second largest owner has 14 and the third 8 percent, while the top five owners (C5) had on average 61 percent of the ownership shares (Knežević Cvelbar, 2006).

7 CEO turnover rates in Slovenia

The average CEO turnover rate, calculated on a sample of 211 Slovenian companies in the 1998-02 period was 5.97 percent. The CEO turnover rate is calculated as the percentage of changed CEOs in the total number of observations from the sample. This figure is lower than that recorded in developed countries. For example, the CEO turnover rate in the US varies from 18.3 percent (Warner *et al.*, 1988) to 7.8 percent (Weisbach, 1988), in the UK between 13.6 percent (Franks *et al.*, 2001) and 7.71 percent (Dahya *et al.*, 2002) etc.

Table 2 reveals that the CEO turnover rate in Slovenia differs over the observed period. An analysis of variance showed significant differences between the turnover rates in 2001 and 2002 in comparison to other observed years. CEO turnover rates in 2001 and 2002 moved closer to the developed countries' average and amounted to 9.5 and 8.5 percent, respectively. On the other side, CEO turnover rates in the 1997-2000 period were significantly lower and on average amounted to 3 to 4 percent. It is hard to explain why the CEO turnover rates were lower in 1997-2000 than after 2000. The changing ownership structure could be one reason. Namely, after privatisation the artificial owners were gradually replaced with more active ones. The replacement or even retirement of the 'old boys' who came into their positions after privatisation might be an additional reason for the higher turnover rates in 2001 and 2002. Another reason for the higher turnover rates recorded after 2000 could be the change of four-year mandate for CEOs taking up their positions in 1996 (after privatisation). The main limitation of the results presented here is that the data do not distinguish the reason for turnover. Therefore, the reported CEO turnover rate could be biased upwards due to the fact that unforced turnovers are included in the reported turnover rate. As presented in the table 2 below on average, the Slovenian CEO has held their position for 6.7 years and on average CEO has

⁹ This group includes: employees, former employees, retired persons and their relatives.

¹⁰ This group includes: managers – top, middle, low managers.

¹¹ These findings support the research results of Prašnikar *et al.* (2000), Gregorič and Prašnikar (2002), Damijan *et al.* (2003) and Simoneti and Gregorič (2004).

Table 1: Ownership structure in Slovenian companies in the 1998-2003 period (mean and standard deviation (SD) value

Year	Mean	SD	State fund ownership	Investment fund ownership	Bank ownership	Domestic companies' ownership	Foreign companies' ownership	Employees' ownership	Management ownership	Minority owners	Other
1998	18.3***	(16.3)	14.8	14.8	1.3	13.8***	3.5	27.5***	2.2**	2.5	7.1
			(16.9)	(16.9)	(5.2)	(27.2)	(12.3)	(21.3)	(5.9)	(7.2)	(19)
1999	16.7***	(15.6)	15.7	15.7	1.6	16.9***	3.3	24.2***	2.1**	2.7	7.9
			(18.4)	(18.4)	(5.1)	(29.2)	(13.9)	(19.9)	(5.8)	(9.9)	(17.3)
2000	13.2***	(15.7)	16.2	16.2	1.6	21.8***	4.3	20.4***	2.1**	3.4	7.1
			(19.7)	(19.7)	(6.9)	(30.4)	(17.3)	(17.9)	(9.6)	(9.5)	(18.4)
2001	11.2***	(13.5)	15	15	2.2	25.0***	5.7	17.1***	3.1**	2.8	8.7
			(22)	(22)	(6.1)	(31.2)	(21.7)	(19.4)	(10.9)	(9.3)	(15.3)
2002	8.5***	(12.4)	15.8	15.8	1.9	28.8***	7.0	16.5***	4.0**	3.1	6.3
			(21.9)	(21.9)	(6.2)	(32)	(21.4)	(19.9)	(11.3)	(9.6)	(15.5)
2003	7.3***	(15.6)	15.1	15.1	1.9	30.6***	6.7	16.4***	4.3**	3.2	6.3
			(19.3)	(19.3)	(5.8)	(29.9)	(17)	(20.4)	(8.8)	(8.8)	(17.3)
1998-2003	12.4***	(15.4)	15.4	15.4	1.7	22.9***	5.1	20.1***	3.0**	2.9	7.2
			(2.2)	(2.2)	(12.7)	(21.6)	(2.2)	(2.2)	(7.0)	(18.2)	(9.6)

Source: questionnaire data and own calculations

** differences between the groups significant at the 5% level (One-way Anova; Duncan method)

*** differences between the groups significant at the 1% level (One-way Anova; Duncan method)

Table 2: CEO turnover rates and characteristics in the 1997-2002 period

Year	CEO turnover rate (%)	CEO tenure	CEO years in company ***	CEO age
1997	4.3** (2.0)	4.6*** (6)	9.0*** (9.7)	46.0*** (7.1)
1998	3.3** (1.7)	5.2*** (6.3)	9.7*** (10.0)	46.0*** (6.7)
1999	4.3** (2.0)	5.9*** (6.6)	10.4*** (10.3)	47.0*** (7.4)
2000	4.3** (2.0)	6.6*** (6.9)	11.1*** (10.6)	48.0*** (7.6)
2001	9.5** (2.9)	7.3*** (7.1)	11.8*** (10.9)	48.8*** (7.7)
2002	8.5** (2.8)	8.2*** (7.3)	12.7*** (11)	49.2*** (7.5)
1998-2002	5.9 (2.3)	6.7 (6.9)	11.2 (10.6)	47.9 (7.5)

Source: questionnaire data and own calculations

** differences between the groups were significant at the 5% level (One-way Anova; Method: Duncan)

*** differences between the groups were significant at the 1% level (One-way Anova; Method: Duncan)

been working for 11 years in the company. The last CEO characteristic observed was the CEO's age. On average, the Slovenian CEO is 48 years old.

8 Results

The first question is whether a turnover is related to a poor company performance. The article investigate whether disciplining takes place at an early stage (rapidly after a sales growth decrease) or later when a company has been generating low or negative sales growth rates for a few years. The inclusion of lagged performance up to two years after a turnover allows me to investigate the reaction time of Management Board restructuring.

As shown in Table 3 in the case of non-financial Slovenian companies there is a negative and significant relationship between CEO turnover and both performance measures. A significant and negative relationship was recorded between current sales growth and CEO turnover, while a significant and negative relationship was recorded between CEO turnover and the lagged return on assets. Both total sales growth and industry-adjusted sales growth rates showed there is a higher probability of a CEO being replaced if the sales volume drops in the current year. On the contrary, there is a higher probability of the CEO being replaced if ROA and industry-adjusted ROA were negative two years before the turnover. Therefore, the evidence presented in Table 3 **fails to reject hypothesis H1** and shows that the poorer the performance the higher is the probability of a CEO turnover.

The Probit regression presented in Table 3 also investigates whether the ownership structure plays a performance-induced disciplining role. Regression results showed that all of the ownership categories seem to be involved in disciplinary actions against the CEO when performance is poor. Variables explaining the interactions between company performance (sales growth) and the owners' identity were negative and significant. On the other side, variables representing the interaction between ownership shares and ROA were negative but not significant¹². Based on these results hypothesis **H.2** stating that management turnover due to poor performance falls along with increasing ownership shares of insiders **has to be rejected**. The results point out that insiders are just as good as monitors as outsiders.

High leverage encourages management to generate sufficient funds to service the debt. Therefore, a high debt-assets ratio is expected to reduce management's discretion and call for more intensive creditor monitoring. Management turnover is expected to be positively correlated with high financial leverage. On the sample of Slovenian non-financial companies **hypothesis H7 thus has to be rejected**. The relationship between the debt-to-assets ratio and CEO turnover is significant and negative, meaning that a higher debt-to-assets ratio decreases the probability of a CEO turnover. This result can be explained by the fact that banks are crediting successful companies (Knežević Cvelbar, 2006)¹³. The next determinate included in the regression is company size. Regression results showed that the size of the company does not affect CEO turnover in Slovenia, therefore **hypothesis H.6 can be rejected**.

¹² An exception was the negative relationship recorded between CEO turnover and ownership shares in the hands of insiders, meaning there is a higher probability of the CEO being replaced if an ownership share in the hands of insider owners' increases and the company is recording a negative return on assets.

¹³ Knežević Cvelbar (2006) performed Factor and Cluster analysis. Companies were divided in three groups. Results showed that companies that belong to the group of »the most successful companies« had higher debt to assets ratio. This result could be explained with the fact that Slovenian banks have restrictive bank policies.

The last group of independent variables included in the Probit regression model are management characteristics. CEO characteristics could not be included in the model since data on CEO turnover are truncated variables based on CEO tenure, meaning that we collected data on current CEO characteristics. Instead, CEO characteristics, board members' tenure, age and turnover were incorporated in the model. As presented in Table 3, all Management Board members' characteristics variables are significant. The regression results showed that the longer Management Board

members have held their position and the older they are there is a lower probability of a CEO turnover. This result can be explained by the fact that companies frequently appoint an insider as a new CEO. A dummy variable representing the other board members turnover was included in the models. The results showed a positive relationship between CEO turnover and Management Board member turnover. This result may indicate that the Supervisory Board usually gives its trust in the whole Management Board and replacing one of the board members raises the probability of replacing the others.

Table 3: Probit regression on CEO turnover – ownership identity

VARIABLE	TOTAL SALES GROWTH (DTS)		RETURN ON ASSETS (ROA)		INDUSTRY-ADJUSTED DTS		INDUSTRY-ADJUSTED ROA	
	Par. est	P > z	Par. est	P > z	Par. est	P > z	Par. est	P > z
Obs. N.	392		504		392		514	
1. Intercept	-0.263	0.793	0.4644	0.511	-0.1313	0.894	0.1649	0.811
Performance								
2. Performance t	-6.202**	0.034	2.4713	0.344	-2.7034**	0.026	-0.8633	0.583
3. Performance t-1	-0.120	0.805	-0.5832	0.474	0.0866	0.728	-0.3382	0.413
4. Performance t-2	-0.142	0.738	-1.4079*	0.059	-0.0226	0.917	-0.6422*	0.085
Ownership identity (%)								
5. Funds	0.007	0.358	0.0023	0.708	0.0064	0.374	0.0008	0.888
6. Other companies	0.005	0.468	0.0006	0.899	0.0046	0.479	0.0008	0.865
7. Internal	-0.006	0.539	-0.0127	0.103	-0.0059	0.522	-0.0078	0.289
Interaction between ownership share (%) and performance at t								
8. Funds	-0.085**	0.019	0.0347	0.617	-0.0757**	0.013	0.0124	0.736
9. Other companies	-0.091**	0.021	0.0293	0.336	-0.0791**	0.019	0.0090	0.594
10. Internal	-0.155***	0.001	-0.0806***	0.000	-0.1456***	0.000	0.0107	0.814
Financial Leverage								
11.DA	-1.106**	0.043	-1.1353***	0.010	-1.0192**	0.050	-0.8463**	0.053
Firm characteristic								
12. Employee num	0.000	0.781	-0.0001	0.560	0.0001	0.599	-0.0001	0.536
Management characteristics								
13. MBM tenure	-0.108***	0.000	-0.0748***	0.001	-0.1085***	0.000	-0.0733***	0.001
14. MBM age	-0.031***	0.007	-0.0293***	0.004	-0.0306***	0.008	-0.0275***	0.005
15. MBM turnover	0.324*	0.100	0.3523**	0.041	0.3080	0.131	0.3936**	0.017
Prob> chi2	0.0000		0.0000		0.0000		0.0001	
Pseudo R ²	0.2999		0.1905		0.3029		0.1855	

* coefficients statistically significant at the 10% level;

** coefficients statistically significant at the 5% level;

*** coefficients statistically significant at the 1% level.

Source: questionnaire data and own calculations

In line with the theory, large shareholdings controlled by a single owner should improve monitoring and reduce agency costs. On the sample of Slovenian non-financial companies' **hypothesis H.3 was rejected**. The regression results indicate that in successful companies in which other companies hold controlling shareholdings the probability of replacing the CEO is significantly higher than if internal owners have controlling shareholdings. On the contrary, the probability of CEO turnover in poorly performing companies in which funds are controlling owners is not significantly greater compared to companies controlled by

internal owners. This would mean that poor performance and the existence of a controlling outsider owner do not increase the probability of a CEO turnover. These results indicate that ownership concentration does not improve the efficiency of the corporate governance system. Other independent variables had the same influence on CEO turnover as in the previous regression (Table 4).

Increasing the ownership shares in the hands of a specific owner could boost the probability of a management turnover. Regression results testing how ownership changes influence CEO turnover in Slovenia are presented

Table 4: Probit regression on CEO turnover – ownership concentration

VARIABLE	TOTAL SALES GROWTH (DTS)		RETURN ON ASSETS (ROA)		INDUSTRY-ADJUSTED DTS		INDUSTRY-ADJUSTED ROA	
	Par. est	P > z	Par. est	P > z	Par. est	P > z	Par. est	P > z
Obs. N.	386		505		385		504	
Performance								
1. Intercept	0.0944	0.876	0.0646	0.900	-0.0085	0.989	-0.1575	0.754
2. Performance t	-3.1817***	0.004	-2.1285	0.217	-1.5076***	0.003	-0.2559	0.555
3. Performance t-1	0.2446	0.637	-0.7399	0.364	0.1354	0.595	-0.3790	0.345
4. Performance t-2	-0.2585	0.574	-1.4782**	0.047	-0.1038	0.644	-0.7379**	0.052
Ownership concentration dummy								
5. Funds	0.2576	0.411	0.2401	0.394	0.3565	0.250	0.4306	0.112
6. Companies	0.2490	0.382	0.3026	0.207	0.3770	0.178	0.4761**	0.052
Interaction between ownership concentration dummy and performance at t								
7. Funds	1.6277	0.248	4.1129	0.321	0.8256	0.217	1.8693	0.366
8. Companies	2.4230*	0.079	2.1156	0.285	1.1713*	0.073	6.1991*	0.060
Financial Leverage								
9.DA	-0.7865	0.111	-0.8286**	0.052	-0.8152*	0.098	-0.8846**	0.039
Firm characteristic								
10. Employee num	-0.0004	0.134	-0.0003*	0.100	-0.0004	0.121	-0.0003	0.166
Management characteristics								
11. MBM tenure	-0.0940***	0.000	-0.0735***	0.001	-0.0933***	0.000	-0.0773***	0.001
12. MBM age	-0.0279***	0.008	-0.0254***	0.009	-0.0284***	0.007	-0.0253***	0.011
13. MBM turnover	0.3663**	0.051	0.4150**	0.014	0.3734**	0.048	0.4026***	0.020
Prob> chi2	0.0000		0.0000		0.0000		0.0000	
Pseudo R²	0.2540		0.1962		0.2495		0.1996	

* coefficients statistically significant at the 10% level;

** coefficients statistically significant at the 5% level;

*** coefficients statistically significant at the 1% level.

Source: questionnaire data and own calculations

in Table 5. An increase in ownership controlled by funds and other companies are defined as dummy variables, while an increase of insider ownership is defined as a reference variable. Results of the Probit regression indicate that an ownership change does not significantly increase the probability of a CEO turnover. Variables representing the interaction between an ownership change and current performance were also included in the model. The results showed there is a higher probability that a CEO will be replaced if other companies increased their ownership shares (by 10 percent or more) in poorly performing companies (sales growth is decreasing) than where internal owners were to increase their ownership holdings. On the contrary, there is no significant difference in the probability of a CEO turnover if funds increase their ownership shares. These results indicate that the probability of a CEO turnover in poorly performing companies will rise if other companies increase their ownership shares. Therefore, **hypothesis H.4 cannot be rejected** if other companies are increasing their ownership share. These results indicate that managers in successful companies have a higher probability of remaining in their position when other companies increase their ownership shares (Table 5).

9 Conclusions

The Slovenian corporate governance system is closer to the insider than the outside corporate governance model (Gregorič, 2003). A relatively low ownership concentration (the largest shareholder controls 35 percent of ownership shares), the increasing ownership shares in the hands of non-financial domestic companies and managers, decreasing ownership held by employees, gradual selling off of the ownership controlled by state funds, the low level of interference of foreign non-financial companies are just some of the characteristics of the Slovenian corporate governance system (Gregorič, 2003; Prašnikar and Gregorič, 2002; Domadenik, 2003; Pahor, 2003; Knežević Cvelbar, 2006).

Research results showed that external owners (funds and other companies) are not better principals than insider owners (employees and managers). The results did not prove that insiders, employees and managers are protecting CEOs interest when performance is poor. It appears that funds, other companies and insiders are involved in disciplinary action against the CEO when performance is poor. Ownership concentration

Table 5: Probit regression on CEO turnover – ownership change

	TOTAL SALES GROWTH (DTS)		RETURN ON ASSETS (ROA)		INDUSTRY-ADJUSTED DTS		INDUSTRY-ADJUSTED ROA	
	Par. est	P > z	Par. est	P > z	Par. est	P > z	Par. est	P > z
Obs. N.	384		487		384		487	
Performance								
1. Intercept	0.4463	0.488	0.4137	0.510	0.4044	0.522	0.2887	0.606
2. Performance t	-0.7554	0.187	-0.1762	0.790	-0.3464	0.209	-0.0102	0.975
3. Performance t-1	0.1812	0.693	-0.9663	0.191	0.1084	0.622	-0.4088	0.280
4. Performance t-2	-0.6554	0.145	-1.8030**	0.026	-0.2982	0.179	-0.8327**	0.044
Ownership change dummy								
5. Funds	-0.0538	0.921	-0.7634	0.279	-0.2226	0.679	-0.4116	0.412
6. Companies	-0.2652	0.415	0.1871	0.435	-0.5843*	0.094	0.1516	0.503
Interaction between ownership change dummy and performance at t								
7. Funds	-3.5674	0.176	1.4751	0.112	-1.5595	0.237	7.1189	0.111
8. Companies	-7.5267***	0.000	-1.0746	0.594	-3.4593***	0.000	-0.3702	0.705
Supervisory Board composition (dummy) and size								
9. SB size	0.0593	0.296	0.0321	0.541	0.0548	0.335	0.0257	0.626
10. SB external	0.632**	0.013	0.5447**	0.017	0.5902**	0.020	0.5228**	0.021
Financial Leverage								
11.DA	-0.8781*	0.082	-0.8458*	0.057	-0.9273*	0.064	-0.8440*	0.059
Firm characteristic								
12. Employee num	-0.0001*	0.060	-0.0004*	0.084	-0.0004*	0.070	-0.0003	0.125
Management characteristics								
13. MBM tenure	-0.0885***	0.000	-0.0936***	0.000	-0.0916***	0.000	-0.0943***	0.000
14. MBM age	-0.0349***	0.003	-0.0277***	0.008	-0.0328***	0.003	-0.0282***	0.008
15. MBM turnover	0.2694	0.184	0.4213**	0.025	0.2722	0.174	0.4247**	0.021
Prob> chi2	0.0000		0.0000		0.0000		0.0000	
Pseudo R²	0.2884		0.2210		0.2790		0.2140	

* coefficients statistically significant at the 10% level;

** coefficients statistically significant at the 5% level ;

*** coefficients statistically significant at the 1% level.

Source: questionnaire data and own calculations

was not identified as an efficient corporate governance mechanism. Regression results indicate that ownership concentration increase the probability of a CEO turnover, however it does not discipline poorly performing CEOs. Therefore, concentration does not improve the efficiency of monitoring control. This might be the case since ownership concentration is lower in Slovenia in comparison with other continental European countries and the largest owners do not have a controlling ownership share. Ownership change is an efficient corporate governance mechanism used for disciplining poorly performing CEOs. The research results showed in companies that recorded poor performance, an increase of ownership (by 10 percent or more) in the hands of other companies increases the probability of CEO turnover. These results point out that the increasing of ownership shares controlled by other companies plays a disciplining role in the process of CEO turnover.

There is a higher probability of a board member turnover if the CEO is replaced. This can lead to the conclusion that a management board member's career is linked to that of the CEO. A significant and negative relationship was recorded when relating CEO turnover to board member age and tenure, indicating there is a lower probability of the CEO being replaced if board members are older and have held their position longer. This may lead to the conclusion that CEOs in Slovenian companies are being replaced by insiders.

Financial leverage has a negative relationship with CEO turnover, indicating that the CEO in those companies with a lower debt-to-assets ratio has a higher probability of being replaced. This result is an indication that Slovenian banks are financing more successful companies (Knežević Cvelbar, 2006).

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