Powerful CEOs in uncertain times: survival of the fittest

Jiaqi (Jacky) Zheng, PhD Candidate in Finance, University of Oxford   Jiaqi.Zheng.DPHIL@said.oxford.edu

Motivation

How much power should a CEO have?
➤ Conventional concerns about managerial entrenchment
➤ However, uncertain times often see a rise in strong leadership

Data and sample

➤ Uncertainty measured by *Stock volatility* (and alternatives) on the industry-year level
➤ CEO power measured by *Dual CEO* (and alternatives) on the firm-year level
➤ Panel data: 2,732 US public firms between 1999 and 2020
➤ 900 forced CEO turnovers; CEO duality among 54% firm-years

Research question: Are powerful CEOs more desirable and more effective in uncertain times?
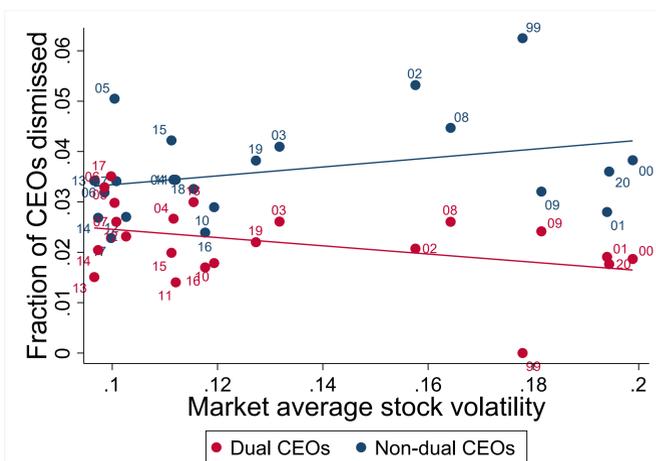
Uncertainty and CEO dismissals

Dependent variable =	Forced turnover dummy	
Uncertainty	0.060	
	(0.14)	
CEO power	0.005	-0.000
	(0.01)	(0.00)
CEO power × Uncertainty	-0.104***	-0.095***
	(0.04)	(0.03)
Year FE & Industry FE	Yes	No
Year-Industry FE	No	Yes
Controls	Yes	Yes
Obs	32033	32033

➤ Powerful CEOs experience significantly fewer forced turnovers as uncertainty increases
➤ Uncertainty ↑ one SD → dismissal rate(powerful CEO) ↓ 0.57% (for comparison, the average rate is 2.31%)

Two rival theories of CEO turnover

Managerial entrenchment theory: entrenched CEOs influence their own turnover decisions
➤ Replacing powerful CEOs is especially costly in uncertain times, so they become (even more) entrenched
➤ Powerful CEOs are associated with both worse performance and increased compensation

Optimal dismissal theory: the board makes efficient turnover decisions
➤ Firms optimally retain more powerful CEOs for their effectiveness
➤ Powerful CEOs are associated with neither worse performance nor increased compensation

Dependent variable =	Q	
Uncertainty	1.930*	3.641**
	(1.12)	(1.46)
CEO power	0.010	-0.037
	(0.07)	(0.06)
CEO power × Uncertainty	0.412	0.767
	(0.55)	(0.49)
Year FE & Firm FE	Yes	Yes
Controls	No	Yes
Obs	28569	28569

➤ Powerful CEOs are not associated with worse performance when uncertainty is higher
➤ Similar results if measuring performance by *ROA* or *Sales growth*

Dependent variable =	Ln(compensation)	
Uncertainty	-0.118	0.778
	(0.58)	(1.01)
CEO power	0.148***	0.118***
	(0.04)	(0.04)
CEO power × Uncertainty	-0.406	-0.453*
	(0.25)	(0.23)
Year FE & Firm FE	Yes	Yes
Controls	No	Yes
Obs	25432	25432

➤ Powerful CEOs' compensation does not increase with uncertainty

Dependent variable =	Cumulative return Feb 20th to Mar 20th			
Year =	2020		2019	
CEO power	0.030***	0.028***	-0.007	-0.006
	(0.01)	(0.01)	(0.00)	(0.00)
Firm Size		0.009**		0.001
		(0.00)		(0.00)
Constant	-0.411***	-0.417***	-0.015***	-0.016
	(0.01)	(0.05)	(0.00)	(0.02)
Controls	No	Yes	No	Yes
Obs	1427	1424	1539	1537

➤ Firms with powerful CEOs are more resilient to the COVID-19 shock
➤ No such result from the placebo test

Two potential mechanisms for powerful CEOs' effectiveness in uncertain times:

(better information sharing with the board)   (faster responses)

Conclusion

In uncertain times, powerful CEOs are more effective and optimally more likely to be retained.

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