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Do characteristics of CEO and Chairman influence Government-Linked Companies performance?

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Abstract

Chairman is the leader of the board, responsibile to ensure that board is effective, communicate with the shareholders and a good relationship between board. While the Chief Executive Officer (CEO) plays a major role in managing and ensuring the business operations. This study examines the characteristics of CEO and Chairman of Government Linked Companies (GLCs) in Malaysia with firm performance using a sample of 80 companies for the period 2005-2009. This study finds that there are positive relationship among chairman's age, ethnicity, firm size and firm age, when regressed on Return on Assets (ROA). In terms of CEO characteristics, there are negative relationship for professional qualification, CEO age, firm age with ROA. In sum, it can be concluded that factors such as age, ethnicity, professional qualification, firm size and firm age do influence firm performance.

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Keywords: Government-linked companies; CEO; Chairman; Malaysia;

1. Introduction

On May 14, 2010 the first high-profile removal of the head of a GLC was reported in all Malaysian press. The Sime Darby Bhd's group chief executive officer (CEO), Dato' Ahmad Zubir Murshid was asked to take a leave of absence before the expiry of his contract on Nov 26, 2010. The Sime Darby chairman, Tun Musa Hitam comments that Zubir's leaving was in connection with the cost overruns amounting of RM964 million that the group's energy and utilities division had suffered in carrying out projects in Qatar and the Bakun hydro-electric dam (The Star, May 14). As in Sime Darby case, it seems that top management (both the CEO and supposedly the Chairman) has a significant influence on firm performance. Thus, it is interesting to study whether CEO/Chairman characteristics have some impacts on firm performance on a wider perspective. This is in line with views from the resource dependency theory (RDT) that proposes directors are appointed based on specific skills and experience (see empirical works on RDT in Terjesen, Sealy & Singh, 2009 on women on boards; Jackling & Johl, 2009 on board meeting; Singh, 2007 on ethnicity on board and Chen, Dyball & Wright, 2009 on diversifications). In terms of contribution of the study, this study provides avenues on the current CEO/Chairman characteristics' selection in

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Malaysian market. This work also provides evidence on the importance of CEO/Chairman characteristics' in enhancing the firm performance.

2. Literature review and hypotheses development

Given the high responsibility and commitment by the stakeholders, Chairman and CEO need to ensure firm performance is leading towards the company objectives. Thus, to be a Chairman or CEO for company, an individual needs to possess certain criteria and qualities and these fit with the resource dependency theory. The attributes considered in this study are education level, professional qualification, age, gender, and ethnicity.

2.1 Education level

A professional CEO with a higher educational background provide a valuable human capital to the company. A higher educational background such as the post-graduate level will increase the value of individual's human capital (Phan & Hoon, 1995) or as having a higher cognitive ability, higher capacity for decision processing, higher tolerance for ambiguity and propensity or receptivity to innovation which equip them with an effective solution for a complex decision making task (Bantel & Jackson 1989). As a result, CEOs with high education qualification are less likely to experience turnover as their turnover portray a loss to a company (Thomas et al., 1991; Ou-Yan & Shuang-Shii, 2007) as the CEO serves some functional backgrounds (as argued in Pfeffer & Salancik, 1978) which include problem definition, information procession and strategic choices (Rajagopalan & Dafta, 1996).Therefore, we hypothesize that:

H_1: CEO/Chairman of GLCs with higher educational level has better performance than CEO/Chairman with lower educational level.

2.2 Professional qualification

The revised Malaysian Code on Corporate Governance (2012) stresses that nominating commitees should consider recruiting directors that have skills, experience and qualifications. Directors' expertise such as in accounting, financing, consulting and law supports managers in making decisions especially in specific business settings (Brockbank, Ulrich & Beatty, 1999; Zajac & Stearns, 1997; Guner et al., 2007), and become more effective strategic business partners (Lawler & Mohrman, 2003; Anderson & Reeb, 2004). Professional appointees received a stronger stock market reaction (Defond, Hann & Hu, 2005; Hillman, Cannella, & Paetzold, 2000) and provide better monitoring (Erickson et al., 2005). Today's professional managers are more likely to move between firms as and when their expertise is required by all firms (Hayes & Abernathy, 1980). Based on the above arguments, we hypothesize that:

H_2: CEO/Chairman of GLCs with professional qualification has better performance than CEO/Chairman with no professional qualification.

2.3 CEO/Chairman age

Brockmann and Simmonds (1997) argues that managerial success is positively correlated with age as older executives also tend to be more risk averse than younger executives (Carlsson & Karlsson, 1970). However, the Companies Act 1965 in Malaysia prohibits the appointment of a person of or over the age of 70 years as a director of a public company or subsidiary of a public company. For listed companies, the CEOs need to retire at least once in every three years but they are eligible for re-election. Based on the arguments, it is hypothesized that:

H_3: GLCs with older CEO/Chairman has better performance than younger CEO/Chairman.

2.4 Gender

Women lack industry experience and they concentrate on less profitable sectors (Loscocco et al., 1991; Alowaihan, 2004) and as such creates a barrier to business (Fischer et al., (1993). Women also employ fewer employees, and have smaller annual sales than their male counterparts (Shim & Eestlick, 1998). Women business owners are found to undercapitalise their firms, typically investing approximately only one third of the capital used by men (Shaw et al., 2009). Therefore, we hypothesize that:

H_4: GLCs with male CEO/Chairman has better performance than female CEO/Chairman.

2.5 Ethnicity

Hofstede (1991) suggests that the two main ethnic groups (Malay and Chinese) are both low on masculinity but high on power distance. The Malays have high uncertainty avoidance which is reflected their uneasiness in dealing with ambiguities and uncertainty. They encourage collectivism, but at the same time they are more secretive which implies low disclosure. In contrast, the Chinese are rated as low uncertainty avoidance, individualistic, willing to accept new challenges and willing to take a greater risk (Haniffa & Cooke, 2002). However, majority of GLCs are headed by Malay leaders, thus we hypothesize that:

H_5: Malay CEO/Chairman of GLCs has better performance than Chinese CEO/Chairman.

3. Research methodology

3.1 Sample size

This study utilised using the secondary data over the period of 2005 to 2009 (5 years). A list of GLCs was obtained from the website http://www.pcg.gov.my. Data on CEO/Chairman profile such as professional qualification, education level, age, gender and ethnicity were hand-collected using the annual reports. ROA data was gathered from Thomson Financial Datastream Advance.

3.3 Research model and measurement

$$PERF_{it} = b_0 + b_1EDUC_{it} + b_2PROF_{it} + b_3AGE_{it} + b_4GENDER_{it} + b_5ETHNIC_{it} + b_6DEBT_{it} + b_7FAGE_{it} + b_8FSIZE_{it} + e_{it}$$

3.4 Model specification

The dependent variable ROA is the ratio of accounting earnings before interest and taxes to the book value of assets. The use of ROA as a performance measure is more preferable than other accounting measures (ROE, EPS) because the operating income used to calculate ROA is not influenced by special charges and also less susceptible to manipulation by managers (Bushman & Smith, 2001). For CEO/Chairman attributes such as education level, professional qualification, age, gender and ethnicity were measured using dummy (0,1). The control variables were debt, firm age and firm size. Debt is the book value of long-term debt divided by total assets. Firm age is the number of years since incorporation. Firm size is the natural log of book value over total assets.

3. Findings and discussions

Based on Table 1, results reveal that majority of Chairman (69.4%) and CEO (66%) do possess a degree qualification. 21.4% of the Chairman are professionally qualified, and 22.1% CEOs are professionally qualified. Even though the number is still low but the professional qualification adds credibility to a person and he is referred to as ‘expert’ in his area. Chairman of 51-70 years amounted to 66.4%, with the youngest at the aged of 31 and the eldest at 61 years. For the CEO, the percentage is 66.2% for CEO of 51-70 years with minimum age of 31 and eldest at 64 years. GLCs do have more male Chairman (77.6%) and CEO (85.5%) as compared to female Chairman (22.4%) and CEO (14.5%). Majority of Chairman for GLCs (74.1%) are Malays, followed by 19.7% Chinese and 6.2% of foreign Chairman. For the CEO, GLCs comprise 73.3% Malays, 12.5% Chinese and 14.2% foreign CEO.

Table 1: Percentage for CEO and Chairman characteristics

		%	%
		Chairman	CEO
EDUC	With degree	69.4	66.0
	Without degree	30.6	34.0
PROF	With professional qualification	21.4	22.1
	Without professional qualification	78.6	77.9
AGE	30-50 years old	33.6	8.2
	51-70 years old	66.4	66.2
	71 and above years old	-	25.6
GENDER	Male	77.6	85.5
	Female	22.4	14.5
ETHNİC	Malay	74.1	73.3
	Chinese	19.7	12.5
	Indian	-	-
	Foreigner	6.2	14.2

With reference to Table 2 (Panel A), there is a positive relationship between Chairman age and firm performance (ROA). Older chairman has higher level of experience (Carlsson & Karlsson, 1970) and maybe risk averse (Brockmann & Simmonds,1997). Arguably, such chairman of the board could provide a check and balance to the management team led by the CEO. Ethnicity also shows a positive relationship with the firm performance. The Malay Chairman was found to be associated higher firm performance. The Malays have high uncertainty avoidance which is reflected their uneasiness in dealing with ambiguities and uncertainty. They encourage collectivism, but at the same time they are more secretive which implies low disclosure.

Table 2: Regression analysis for Chairman and CEO characterisctics and firm performance

	Panel A: Chairman				Panel B: CEO			
	Coef.	**Std. error**	**t**	**P> t**	**Coef.**	**Std. error**	**t**	**P> t**
Education	-.0122486	.0230027	-0.53	0.595	.0163826	.0296835	0.55	0.582
Professional	.0379732	.020653	1.84	0.067	-.0977519	.0188359	-5.19	0.000
Age	.0050623	.001023	4.95	0.000	-.0046773	.0012834	-3.64	0.000
Gender	.0143014	.0635742	0.22	0.822	-.0565514	.0694529	-0.81	0.416
Ethnic	.0724295	.0161829	4.48	0.000	.0745046	.009686	7.69	0.000
Debt	3.42e-10	5.40e-10	0.63	0.528	-3.98e-10	5.10e-10	-0.78	0.436
Firm age	.0010888	.0005576	1.95	0.052	.0007424	.0004816	1.54	0.125
Firm size	-7.66e-10	2.86e-10	-2.68	0.008	-4.85e-11	2.52e-10	-0.19	0.847
Constants	-.3344344	.0827479	-4.04	0.000	.2590354	.0972686	2.66	0.008
Prob > F	0.0000				0.0000			
R-squared	0.1569				0.3168			
Adj R^2	0.1286				0.2904			

In contrast, the Chinese are rated as low uncertainty avoidance, individualistic, willing to accept new challenges and willing to take a greater risk (Haniffa & Cooke, 2002). İn terms of firm age, matured companies that operate in the market do contribute to better firm value, and small size companies do perform better as compared to large companies. For Table 2 (Panel B), there is a significant negative relationship between professional qualification of the CEO and CEO age with firm performance which is quite baffling. Younger CEOs perform better perhaps due that younger CEO tend to be more energetic, aggresive in action taking and willing to take the risk. İn terms of ethnicity, this factor do add up the firm performance. Whilst, education and gender (for both Chairman and CEO) do not have any effect on performance.

4. Conclusion

The study finds some evidence the experience of the older chairman and the aggresiveness of the younger CEO work as a better combination to achieving higher firm performance rather than having both older chairman and CEO or younger chairman and CEO although this speculation needs more careful future studies. The result on ethnicity although seems preliminary, still is indicative enough to suggest that major ethnic would be appointed on successful GLCs as it also a part of the New Economic Policy (NEP) initiatives set up by the ruling party. Although the study is limited to GLCs and its matched pair, it could be argued that the government selects companies that could reach public at large to be under its stable as it would have more direct and indirect impacts on government policies and could be generalized to similar state-business mechanism which is familiar in Asian region.

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