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Original Article

Antecedent and Consequences from CEO Turnover Rate in Indonesia

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Abstract *- This study aims to explore the antecedent factors of CEO turnover rates in Indonesia and their impact on the performance of companies listed on the Indonesia Stock Exchange. The originality of this study was to use the political connection as one of the antecedents to measure the consequences of CEO turnover in influencing company performance. Very little research in Indonesia or in ASEAN countries uses CEO turnover as a mediating variable in measuring the relationship between political connection and company performance. This study uses partial least square analysis to test all research hypotheses. Research data in the form of secondary data taken from financial statements and annual reports of companies listed on the Indonesia Stock Exchange from the period 2012 to 2017. The results showed that political connection and family ownership had a significant effect on CEO turnover rates. In addition, political connection, family ownership, and CEO turnover have a significant effect on company performance. The mediating effect of the CEO turnover rate is able to strengthen the significant influence of political connection and family ownership on company performance.*

Keywords *- CEO turnover rates, Company performance, Political connection*

I. INTRODUCTION

Indonesia adheres to corporate governance that is a two-tier system. In this system, there are two separate tasks, namely the supervisory board and the executive board. The supervisory board consists of independent non-executive directors. At the same time, the board of directors consists of company operational executives such as the president director, finance director, operational director, and so on. The President Director (CEO) plays an important role in determining the direction, vision, and mission of a company. But it is not uncommon for director changes in a company. In the past few decades, issues regarding CEO turnover have often been published. CEO turnover is believed to affect company performance. Morck, Yeung, & Yu (2000) state that it is normal for companies to change the leadership of a CEO. The company needs a new concept in an effort to improve corporate performance and competitiveness. CEO turnover may be due to a decrease in company performance if it keeps retaining the current CEO. The CEO turnover indicates that there will be changes in the management of the company by implementing new procedures or regulations and policy changes that are expected to improve company performance.

Research on CEO turnover has been carried out by academics and practitioners from various countries. Lindrianasari & Hartono (2011) examined the relationship between accounting performance and the CEO turnover rate. The results showed that deteriorating accounting performance triggered a high level of CEO turnover in Indonesian companies. Murphy & Zimmerman (1993) conducted a study to find out what caused the company's CEO to be replaced. Researchers use the company's financial performance factors (such as return on asset, return on equity, and Tobin's Q) before and after the CEO is replaced. The results showed that poor corporate financial performance forced the CEO turnover of the companies that were used as research samples.

One factor that deserves attention for research in Indonesia about company performance is the factor of political connections. There are many literature reviews that examine the importance of political connection factors in influencing company performance. The Indonesian economy is strongly influenced by political conditions, so companies that are active in Indonesia must have strong political connections to develop their business (Fisman, 2001). Political connections play an important role in prospering the company and also the country, but also become the main trigger for the country's economic downturn (for example, the 1997-1998 monetary crisis that brought down Indonesia). Political connections can bring in foreign investment. Unfortunately, investment funds are not used to make productive investments. Weak economic fundamentals were the main trigger for Indonesia's bankruptcy in the era of the 1997-1998 crisis (Fisman, 2001).

Pfeffer & Salancik (1978), in their theory, revealed that political connections help companies obtain customer contract guarantees and counteract various uncertain possibilities that often arise so that they can increase the value of the company. You & Du (2012), in their research, stated that CEOs in China who have political connections are able to maintain their director's position from pressure or call to withdraw from other shareholders. Even though the company's performance was deteriorating, the CEO with a political background was still able to obtain high enough trust because he was believed to be able to get the company out of trouble thanks to the political connections that the director had.

This research was designed with the aim to examine the CEO turnover rate, which is one of the important elements in the function of corporate governance. The novelty of this research is to link political connection variables with CEO turnover rates. Many previous studies directly examined the influence of political connections on company performance or the effect of CEO turnover on company performance. There is still very little research in Indonesia or in ASEAN countries that conducts research on the effect of political connection variables on CEO turnover rates.

In addition to political connections, this study will also analyze the influence of family ownership on CEO turnover rates in Indonesia. Family ownership is often an important factor in CEO turnover decisions. Families that have an influence on the management and supervision of the company create agency conflicts. Family members who are leaders of the company will be difficult to be replaced (Bammens, Voordeckers, & Van Gils, 2011). Not all studies show the positive side of family ownership in minimizing the level of CEO turnover. Aguilera & Crespi-Cladera (2012) prove that family ownership is not good enough in corporate governance because dominating families tend to carry out activities that benefit their own families. The level of CEO turnover will be high that occurs in these family companies. The diversity of the results from previous research makes it quite interesting to be re-examined using data from Indonesia.

II. RESEARCH FRAMEWORK AND HYPOTHESIS DEVELOPMENT

According to Adhikari *et al*. (2006), leaders who have a political connection will gain greater trust from shareholders to lead the company in the long term. Piotroski *et al*. (2010) analyzed the relationship of political events in China to the rate of change of company directors. The researcher concluded that directors who have political connections proved to be able to deal with a series of domestic political events and were able to boost the overall performance of the company. The results of the study concluded that CEOs with strong political experience have a corporate leadership period that tends to be longer than companies led by CEOs who have no political background.

H_1: Political connections have a significant effect on CEO turnover rates.

The research conducted by Aguilera & Crespi-Cladera (2012) aims to analyze the effects of owner-family control on the issue of the company's CEO turnover and the position of minority shareholders in the company. The results of the study concluded that family ownership also played a role in reducing the sensitivity of CEO turnover rates. Research on the influence of family ownership on CEO turnover rates was also carried out by Chua *et al.* (2012), but researchers did not find a significant relationship between family ownership variables with CEO turnover rates. Craig *et al*. (2013) concluded that involvement, ownership, and family culture tended to reduce the company's CEO turnover.

H_2: Family ownership has a significant effect on CEO turnover rates.

Krause & Semadeni (2014) analyzed the influence of the independence of the board of commissioners in maintaining company performance. The researcher concluded that The level of independence of the board of commissioners would decrease if the old CEO who is replaced fills certain positions within the board of commissioners. The CEO turnover rate (which was accompanied by the appointment of the old CEO in the board of commissioner leadership structure) would lead to an increase in the overall performance of the company. Research on the relationship between CEO turnover rates and company performance was also carried out by Jenter & Kanaan (2015). The results of the study show that CEO turnover and company performance are interrelated.

H_3: CEO turnover rate has a significant effect on company performance.

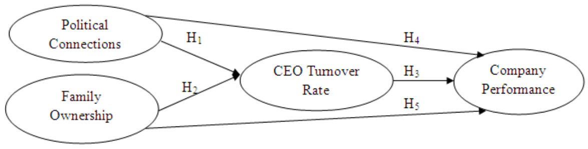
Research on the influence of political connections on corporate performance has been carried out by academics in various countries. Du & Girma (2010) conducted a study to determine the effect of political connections on company performance. The results of the study show that political connections play a role in increasing company growth and increasing the probability of companies in China maintaining their business existence.

H_4: Political connections have a significant effect on company performance.

Shyu (2011) conducted a study to examine the effect of family ownership on the performance of companies in Taiwan. The results showed that family ownership with a portion of ownership below 30% had a significantly positive relationship to company performance that was measured by ROA and Tobin's Q. But if family ownership rose above 30%, the company's performance would tend to decrease because entrenchment potential was expected to increase with increasing family ownership. Penelitian The research conducted by Aloulou (2018) uses family involvement and ownership as a variable that moderates the relationship between entrepreneurial orientation and the performance of the family company. The results of the study indicate that family ownership is significantly positively related to company performance.

H_5: Family ownership has a significant effect on company performance.

From the basis of the theoretical review, this study proposes nine hypotheses shown in Figure 1 below as a conceptual research framework:



I.

III. RESEARCH METHODOLOGY

This research can be categorized as quantitative research based on the method of data collection. Based on the type, this research is classified as hypothesis-testing research, which is a comparative causal test because it involves several independent variables in testing its effect on the dependent variable. This research includes explanatory research, which aims to explain the influence between variables through testing hypotheses based on collected data samples. Data samples were collected by purposive sampling, which are all companies listed on the Indonesia Stock Exchange from the year 2012 to 2017, and selected companies must have data that will be used in measuring the research variables. The definition of operational variables used to measure research variables was adopted from several previous studies. Company performance uses the formula in the research of Rachpradit *et al*. (2012); CEO turnover using the formula in the study of Setiawan, Phua, & Chee (2017); political connection using the formula in the research of You & Du (2012); family ownership adopted the formula in the research of Taras *et al*. (2018). After all the research data are collected, then this study uses SPSS 21.0 to analyze descriptive statistics and using variant-based Structural Equation Model with data processing using Smart PLS software to design structural models, measurement models, estimate models, test hypotheses, and goodness of fit tests including the mediation analysis.

IV. RESULTS AND DISCUSSION

Descriptive statistics of this study show that 52.9% of companies listed on the Indonesia Stock Exchange from 2012 to 2017 were indicated to have a political connection relationship. The results of the descriptive statistics also show that the CEO turnover rate in Indonesian companies was 15.3% of the research data sample. Descriptive statistical results for other variables are shown in table 1 below:

Table 1 Statistic Descriptive

Variables	*N*	*Minimum*	*Maximum*	*Mean*	*Std*
Family ownership	2580	0,0000	0,97204	0,09310089	0,21083
Company performance	2580	-3,93324	2,19203	0,02538024	0,17825

The results of processing using Smart PLS show the value of the outer model with the convergent validity technique with good results because all loading factors have values above 0.70, so the variables used will not be eliminated from the research model. The results of the outer model with discriminant validity techniques also indicate that each latent variable already has good discriminant validity. This is because each cross-loading value of each indicator of a latent variable has the largest cross-loading value (value 1.000000) compared to other cross-loading values for other latent variables. The results of the last outer model with the composite reliability technique also show a construct that has a high level of reliability because the composite reliability value in this study has a value above 0.70 and the value of AVE above 0.50.

Structural model testing shows that the R-Square value for the CEO turnover variable is 0.091. This means that 9.1% of the CEO turnover rate can be explained and influenced by political connection and family ownership. The remaining 90.9% is explained and influenced by other variables not found in this study. The structural model testing also shows that the value of R-Square for the company performance variable is 0.126. This means that 12.6% of the company's performance variables are able to be explained and influenced by political connection, family ownership, and CEO turnover rate. The remaining 87.4% is explained and influenced by other variables not found in this study. The hypothesis test results (Table 2 below) further concluded that all hypotheses were accepted in this study.

Table 2 Hypothesis Test Results

No	Hypothesis	Path Coefficient	T-Value	Decision
H_1	Political connection → CEO turnover rate	0.069234	3.556127	Accepted
H_2	Family ownership → CEO turnover rate	-0.050862	2.839130	Accepted
H_3	CEO turnover rate → Company performance	-0.232204	11.721005	Accepted
H_4	Political connection → Company performance	-0.054095	3.549819	Accepted
H_5	Family ownership → Company performance	0.082505	3.884783	Accepted

The table above shows that political connections have a significant positive effect on CEO turnover (t-value above 1.96). This means that the stronger the political connection within the company, the higher the level of CEO turnover in the company. According to You & Du (2012), government-owned companies that have a strong political connection are proven to often make CEO turnover if the CEO does not achieve the expected performance. The table above shows the higher level of family ownership in the company, the lower the level of CEO turnover in the company. Companies whose dominant shares are owned by families tend to rarely make CEO turnover because the CEO is most likely also a member of the owner's family. Although the CEO does not achieve the expected performance, the owner's family will still retain "his own people" in the company's leadership. The table above shows that companies that often make CEO turnover result in lower company performance. CEO turnover signifies the start of a new leadership era. New leaders have their own ideas and strategies for running the company. The organization as a whole must adopt a new strategy; this can result in a decrease in company performance. The above results show that companies with strong political connections are proven to reduce company performance. Political connection is indeed able to bring certain benefits to the company, but if it is not properly utilized, it will even harm the company. For example, company leaders who are less capable are appointed to lead companies based on close relations because of political interests and not based on merit. Things like this tend to harm the company as a whole. The table above shows that companies with large family ownership are proven to increase company performance. The family of company owners tends to work seriously in running their family business because reputation is also at stake.

This study also analyses the effect of CEO turnover in mediating the influence of political connections and family ownership on company performance. The test results concluded that the CEO turnover rate variable was able to strengthen the negative influence of political connections and the positive influence of family ownership on company performance.

V. CONCLUSION

This study examines two antecedents that influence CEO turnover and the consequences of CEO turnover rates on company performance. The results of the study concluded that antecedent factors such as political connections and family ownership were able to influence significantly the case of CEO turnover rates in companies listed on the Indonesia Stock Exchange. The high level of CEO turnover also has consequences for the decline in the company's financial performance (ROA). The antecedents of political connection and family ownership both are proved to have a significant effect on the financial performance of the company. CEO turnover rates are also proven to be able to mediate the influence of political connections (strengthen negative influences) and family ownership (strengthen positive influence) on company performance.

This research also contributes to the development of strategic management knowledge. The main originality of this research is to test the CEO turnover rate in mediating the influence of political connections on company performance which is rarely examined in studies in Indonesia and the ASEAN region specifically. This research is expected to contribute and add to the literature on cases of CEO turnover in Indonesia. This study is also able to provide empirical evidence about the consequences of CEO turnover in influencing company performance. This can have practical implications for decision-makers (Board of Directors) in Indonesian companies. Companies that often change their CEO positions are proven empirically to cause a decline in company performance. The position of a CEO is recommended to be maintained at least in accordance with the period of service (unless extreme things occur which make the CEO must be replaced suddenly and tend to be "forced"). The higher the political connection the CEO has is proven to increase the probability of CEO replacement. This research suggests that the CEO should not prioritize using his or her political connections in running the company's business. The results showed that the stronger the political connection of a CEO actually increased the case of CEO turnover itself. This study has a number of limitations. Future studies are expected to be able to expand the measurement of CEO turnover (at least disclose the reasons for voluntary and non-voluntary CEO turnover) and the performance of companies that are not only limited to financial performance factors. The company's non-financial performance factors are also worth considering in future research. Further research is also expected to be able to explore more data relating to political connections and family ownership, which are basically very difficult to collect those data.

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