THE EFFECT OF ANNOUNCEMENT OF CHIEF EXECUTIVE OFFICERS CHANGES ON STOCK RETURNS OF FIRMS LISTED AT NAIROBI SECURITIES EXCHANGE

BY

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DECLARATION

This research project proposal is my original work and has not been presented for award of any degree in any University.

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This research project proposal has been submitted for examination with my approval as University of Nairobi supervisor.

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DEDICATION

This research project is dedicated to my family and friends for their support throughout our course.

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LIST OF ABBREVIATIONS

CEO Chief Executive Officer

CMA Capital Market Authority

NSE Nairobi Securities Exchange

SPSS Social Programme for Social Sciences

ABSTRACT

The study sought to analyse the effects of announcement of top management changes on share prices with focus to selected firms listed on Nairobi Securities Exchange. The specific objectives of the study were to find out the impact of share price performance at the date of announcement of a CEO change, to determine the impact of share price performance for the three years subsequent to the change in CEO, to established whether the reaction of the stock market to internal versus external successors differs and to assess whether the stated reason for the CEO change has an impact on the stock market reaction at the date of the announcement. The study was of great benefit to the management of listed companies in the NSE, the stakeholders including policy makers, the future researchers and to the existing body of literature concerning effects of announcement of top management changes on share prices. The study adopted, Agency Theory, Stewardship Theory, Stakeholder Theory and Resource Dependency Theory to assist in understanding the announcement of top management changes on share prices. Descriptive research design was used. Target population in the study included selected companies listed at the Nairobi Securities Exchange. The study selected only firms that have changed their top management in the period between 2009 and 2015. The study sought to determine the announcement of changes in top management on the shares price before and after the exit of the CEOs. The study used secondary sources of data. Data collected was analysed using quantitative and qualitative method. A Standard event study methodology model was used to determine the announcement of top management changes on share prices with focus to selected firms listed on Nairobi Securities Exchange. The research observed a statistically significant negative impact on share prices at the date of announcement of CEO turnover, but this was negated by statistically significant positive returns when looking at the day prior to the announcement. No statistically significant results were observed for internal versus external CEO replacement. Forced CEO turnover had a negative effect on share price performance when compare to voluntary turnover, but this was not statistically significant. No significant results were observed for the seven years' post the appointment of the new CEO. The conclusion of the research is that the impact of CEO turnover is not significant at announcement date or over time.

CHAPTER ONE

INTRODUCTION

1.1 Background of the Study

A change in executive leadership is a significant event in the life of a firm. The top management ability, preferences, and ultimate decisions affect the firm through the projects the firm selects, its financial policy, and the corporate culture. To the extent that these characteristics and the resulting decisions differ across individuals, Chief Executive Officers (CEO) changes can alter the course of the firm and its performance Suchard et al, (2001). Recognizing that top management is not restricted to one individual raises the possibility that competition between top managers is an important force affecting management turnover. For example, there are cases in which the chairman/CEO tries to oust the president, and vice versa) Thus, while other empirical work on turnover emphasizes the role of the board of directors. The board is not the only force disciplining top managers. Since block holders can be directors or serve as top managers, the forces of managerial competition, board monitoring, and block ownership seem interrelated (Sundaram & Inkpen, 2004)

Although top managers' contribution to firm value is not directly observable, stock returns are a potential source of information. In an efficient market, however, stock return is a noisy measure of management performance. The return reflects only the unexpected component of top management performance and is influenced by a variety of exogenous factors. Given the noise in stock returns, alternative sources of information, such as earnings reports could provide measures more closely associated with management

performance. Some measures could incorporate information not reflected in stock returns (Weisbach 2008).

1.1.1 Chief Executive Officers Changes

CEOs changes occur for different reasons, and differ in their prior relation with prior share performance. Some could follow good performance, and others could have no relation to prior performance. In either case, inclusion of such changes biases tests against finding an inverse relation between share performance and top management changes. To address this potential problem, several types of management changes are studied using information on the details of observed management Changes (Padilla, 2000).

Termination of top manager's employment is more likely to be a response to poor management performance than are management changes in general. Few management changes ate described as terminations in press announcements. As discussed later, however, it is possible to identify those cases in which the management change involves a top manager's leaving the firm and in which he is most likely to have been forced out as a consequence of poor performance (Worrell et al 2005).

Replacement of a team member or an addition to the management team can be made either by promoting a current lower-level manager or by hiring from outside the firm. Hiring an outsider involves potential costs not borne by the firm with an insider. For example, the outside appointment can adversely affect insiders' incentives. If insiders

revise downward their probability of achieving a top management position, their motivation to perform is reduced Lazear and Rosen (2001). In addition, to function effectively the outsider will have to acquire firm-specific human capital. Given the hypothesized costs, an outsider appointment must involve substantial benefits. These benefits are likely to be greater in situations where management performance is poor. A caveat is that some outsider appointments occur as part of a firm expansion into new areas in which the firm has no specific human capital. If such firm expansion occurs after the firm has done relatively well, the predicted inverse relation between share performance and outsider appointments is reduced (Weisbach, 2008).

Change of the CEO is another factor that can affect the share prices. Previous work on turnover and performance focuses solely on CEO changes. CEO changes are probably also linked to performance. In addition, it is useful to distinguish important from unimportant CEO changes (Huson et al 2004). For example, Vancil (2007) argues that many CEO changes are part of the normal succession process; it is common for the chairman and CEO to pass the CEO title to the president, s. This kind of CEO change is not included as a management change because it does not involve a change in the group of individuals comprising top management. Title changes alone are less likely to be related to poor performance, and excluding them should enhance the ability to detect a relation between stock price performance and subsequent management changes.

The analysis by Black-Scholes (2002) shows that all types of changes in executive leadership result (on average) in equity volatility increases. The most significant increase

is associated with forced turnover, and for this type of departure, he found no significant difference between inside and outside successions. For voluntary departures, volatility increases are greater for outside than for inside succession. Furthermore, the effects are long-lived; He found statistically significant increases in volatility up to two years after the event. Taken together, these findings support the strategy and ability hypotheses, reject the scapegoat hypothesis, and are consistent with signals of firm value becoming more informative as market participants learn about the new CEO. As additional confirmation, found that stock-price sensitivity to the unexpected component of quarterly earnings announcements increases following a turnover.

1.1.2 Stock Returns

Stock returns reaction at announcement of a management change can indicate whether the capital market considers the event significant. However, predictions about the sign of the abnormal stock price effect at announcement are not precise even if the change is a response to poor performance, in shareholders' interests, and unanticipated. One reason is that announcement of a change can convey other information (Furtado and Karan, 2000).

The extent of management's poor performance was not previously known to the market. Then abnormal stock return at announcement is the sum of two components. One is an information component that is negative if the change signals worse management performance than anticipated. The second is a real component that is positive if the change is in shareholders' interest. A positive net effect is expected only if the real component is larger in absolute value than the information component. Although each

component is unobservable, it is possible to examine whether, on average, the sum of firm's information and real components is equal to zero. This is equivalent to testing for shifts in the mean of the cross-sectional distribution of abnormal returns. These tests can fail to detect a mean stock price response to announcement if some firms have a positive response and others a negative response such that the average response is zero. To address this possibility, tests for shifts in the variance of excess returns are also employed, and indicate whether a stock price effect exists, regardless of its sign. Such tests are widely *used* in the accounting literature (Beaver2008).

1.1.3 Chief Executive Officers Changes and Stock Returns

If poor performance leads to a management change, negative stock performance should be present before this event for a sample of observed changes. Examination of pre-event abnormal performance thus provides a useful check on the prediction results. However, examining pre-event stock price behaviour for a sample of observed management changes does not address some important issues directly (Friedman and Singh 2009)

Corporate senior management play an important role in determining the future success of their organisation. In forecasting future earnings of a firm and determining an expected return on investment, the investment community is therefore concerned with the composition of this management team. Any change in the set of individuals holding the senior positions of Chief Executive Officer, Managing Director, Chairman of the Board and Chief Financial Officer or Finance Director is expected to be considered a major event for the company and to lead to a reassessment of the firm's potential earnings

stream by investors. The market reaction to changes in payout policies is of critical importance in determining corporate payout dynamics. Over the years, the literature on payout policy has produced many hypotheses to explain payout rationale. The Dividend Signalling Hypothesis asserts that a dividend increase is a signal of unexpected positive and persistent higher future earnings; the Free-Cash-Flow (FCF) Hypothesis states that a dividend increase reduces the agency problems between shareholders and top management; The Maturity Hypothesis maintains that a dividend increase is an indication of entering a mature life-cycle stage of low systematic risk; Finally, the Catering Hypothesis argues that managers are catering to investors by increasing dividends during times when dividend paying stocks are in high demand and therefore rewarded with a return premium.

One is precisely how the probability of a management change depends on the level of stock price performance, and the relevant measure of performance. A related issue is whether stock price performance is a good predictor of a management change. In contrast, prediction procedures used examine these issues explicitly, with potential gains from exploiting information on firms that do not experience a management change (Denis and Denis, 2010).

1.1.4 Listed Companies in Nairobi Securities Exchange

In Kenya, sixty one companies are listed in the Nairobi Securities Exchange (NSE), which is the only securities exchange firm in the country (Nairobi Securities Exchange, 2014). Listed companies fall into two main segments, that is, the main market segment

and the alternative investment market segment. The Nairobi Securities Exchange classified these companies into ten sectors. These are; agricultural, commercial and services, telecommunication and technology, automobiles and accessories, banking, insurance, investment, manufacturing and allied, construction and allied, energy and petroleum (NSE, 2014). The Nairobi Stock Exchange marked the first day of automated trading in government bonds through the Automated Trading System (ATS) in November 2009. The automated trading in government bonds marked a significant step in the efforts by the NSE and CBK towards creating depth in the capital markets by providing the necessary liquidity. In December 2009, NSE marked a milestone by uploading all government bonds on the Automated trading System (ATS). Also in 2009, NSE launched the Complaints Handling Unit (CHU) SMS System to make it easier for investors and the general public to forward any queries or complaints to NSE

In July 2011, the Nairobi Stock Exchange Limited changed its name to the Nairobi Securities Exchange Limited. The change of name reflected the strategic plan of the Nairobi Securities Exchange to evolve into a full service securities exchange which supports trading, clearing and settlement of equities, debt, derivatives and other associated instruments. In October 2011, the Broker Back Office commenced operations. The system has the capability to facilitate internet trading which improved the integrity of the Exchange trading systems and facilitates greater access to our securities market. In November 2011 the FTSE NSE Kenya 15 and FTSE NSE Kenya 25 Indices were launched. The launch of the indices was the result of an extensive market consultation process with local asset owners and fund managers and reflects the growing interest in

new domestic investment and diversification opportunities in the East African region. As of March 2012, the Nairobi Securities Exchange became a member of the Financial Information Services Division (FISD) of the Software and Information Industry Association (SIIA).

1.2 Research Problem

Stock price reactions to announcements of change in management have been investigated by many researchers. There are different methods of changing the firm management. According to economic theory internal control mechanisms are effective if there are more changes of CEO in poorly performing firms than in firms whose performance is good. Moreover improvements can be observed in firms' performance after CEOs changes (Black-Scholes 2002).

Despite evidences that changes of firm management affect the performance shares prices of the firm negatively, studies find different findings. Based on the managerial turnover data from the US stock market, Furtado and Rozeff (2007) found increases in stock prices due to the event, but from a statistical point of view this result was insignificant. Unlike Furtado and Rozeff (2007),Worell, Davidson, and Glascock (2013) documented a statistically significant price increase of 2.3%. A very interesting work is that of Weisbach (2008), who reported that, on the one hand, there is no price impact if the managerial resignation takes place in a company whose board is dominated by executive directors. On the other hand, there is a significant positive stock price reaction if the majority of the board consists of external, independent directors. Nevertheless, Khanna

and Poulsen (2005) examined whether management turnover leads to improvement in firms' performance. They argued that removing poorly performing managers is an important step toward maximizing shareholder wealth.

A management board must identify poor management and attract superior replacement managers. This is the main criterion of the effectiveness of internal monitoring. However a negative correlation between prior stock price trends and managements turnover may coexist with effective internal board monitoring. Khanna and Poulsen supply two alternative explanations. The first one is that managers of poorly performing companies may voluntarily resign in order to avoid shareholder lawsuits. The second one is that company boards may replace the managers of poorly performing firms even if those managers are not responsible for the bad financial situation of a company. Under neither of these two scenarios would a change in management necessarily be expected to induce improvements in performance share prices (Behn et al, 2006).

In Kenya, many companies has changed their CEOs, including Safaricom, Kenya Data Net Works, Kenya Commercial bank, Barclays bank to mention but a few. The effects of each change in top management on share prices have not been document. It is not clear if the changes in top management by the Kenyan firms listed in the Nairobi Securities Exchange has any impact on the share prices. This study will therefore seek to investigate this aspect and answer the following questions; what are the impacts of share price performance at the date of announcement of a top management change?, the impact on share price performance for the three years subsequent to the change in CEO?, Whether

the reaction of the stock market to internal versus external successors differs? And whether the stated reason for the CEO change has an impact on the stock market reaction at the date of the announcement?

1.3 Objective of the Study

The objective of the study is to determine the effect of announcement of CEOs changes on stock returns of listed firms at the Nairobi Securities Exchange

1.4 Value of the Study

The management of listed companies in the NSE will benefit from the study as they will be able to understand their effects on share prices thus offering their leadership towards improvement and avoiding exit gap that would drop the share prices. This will help the shareholders, board of directors and the chairman of such as a firm to come up with corporate governance policies that guide the firm management towards achieving the intended growth in share prices through subjecting the management and organisational employee to a culture of firm governance and responsibility. The study shall further enable the management of the listed companies to adhere to the CMA principles of governance practices which shall keep the firm off from firm failures and penalization which might come through forced ejection of the top management or otherwise.

This research will help the stakeholders including policy makers into understanding the importance of top management in the growth of the firm share prices, their impact on exit of the firm leadership realm and methods that should applied during top management

retirement to avoid drop in share prices. Kenya has a history of collapsed firms; situation that can be attributed to lack of proper top management leadership by the management and directors of such companies. The study will offer suggestions, recommendations and findings on effects of resignation, eviction or retirement of such top management to ensure the firm remains in the same share price health as it were before the exit of such top management officials or even improved share price.

This study will be of help to the future researchers who will be interested in the same topic of effects of announcement of top management changes on share prices. This will provide them with valuable insight in the subject under study and will allow them to plan the areas that require more attention and those are yet to be researched. The study will add to the existing body of literature, concerning effects of announcement of top management changes on share prices. The study will therefore provide an additional literature to the libraries, journals and provide more information to the knowledge gap on top management changes on share prices.

CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

The main purpose of this literature review is to analyse the effects of announcement of CEOS changes on share returns with focus to selected firms listed on Nairobi Securities Exchange. The chapter covers introduction of the literature, review of theories, review of empirical studies, conceptual framework and chapter summary.

2.2 Theoretical Review

Neuman (2006) defines a theory as a system of interconnected ideas that condense and organize knowledge about the world. The agency theory and the stewardship theory are the main theories underlying the concept announcement of top management changes in the listed firms in the Nairobi Securities Exchange and the impact they have on the share prices relates to these theories.

2.2.1 Agency Theory

Agency theory is defined as the relationship between the principals, such as shareholders and agents such as the company executives and managers. In this theory, shareholders who are the owners or principals of the company, hires the agents to perform work. Principals delegate the running of business to the directors or managers, who are the shareholder's agents (Clarke, 2004). Agency theory suggests that employees or managers in organizations can be self-interested hence affecting the share prices of the company. The agency theory shareholders expect the agents to act and make decisions in the

principal's interest. On the contrary, the agent may not necessarily make decisions in the best interests of the principals (Padilla, 2000).

The agent may be succumbed to self-interest, opportunistic behaviour and falling short of congruence between the aspirations of the principal and the agent's pursuits. Even the understanding of risk defers in its approach. Although with such setbacks, agency theory was introduced basically as a separation of ownership and control (Bhimani, 2008). The agents are controlled by principal-made rules, with the aim of maximizing shareholders value. Hence, a more individualistic view is applied in this theory (Clarke, 2004). Indeed, agency theory can be employed to explore the relationship between the ownership and management structure and the effects it has on the share prices of the listed firm. However, where there is a separation, the agency model can be applied to align the goals of the management with that of the owners. The model of an employee portrayed in the agency theory is more of a self-interested, individualistic and are bounded rationality where rewards and punishments seem to take priority (Jensen & Meckling, 2006).

2.2.2 Stewardship Theory

A steward is defined by Davis, Schoorman & Donaldson (1997) as one who protects and maximizes shareholders wealth through increasing share prices, because by so doing, the steward's utility functions are maximized. In this perspective, stewards are company executives and managers working for the shareholders, protects and make profits for the shareholders. Stewardship theory stresses not on the perspective of individualism, but rather on the role of top management being as stewards, integrating their goals as part of

the organization. The stewardship perspective suggests that stewards are satisfied and motivated when organizational success is attained. It stresses on the position of employees or executives to act more autonomously so that the shareholders' returns are maximized. Indeed, this can minimize the costs aimed at monitoring and controlling behaviours.

Daly et al. (2002) argued that in order to protect their reputations as decision makers in organizations, executives and directors are inclined to operate the firm to maximize organizational growth and financial growth as well as shareholders' profits. In this sense, it is believed that the share prices can directly impact perceptions of their individual growth. Moreover, stewardship theory suggests the announcement of top management changes due to specific reason that relate to their leadership might affect the share prices in the firm. It was evident that there would be better safeguarding of the interest of the shareholders.

2.2.3 Stakeholder Theory

Wheeler et al, (2002) argued that stakeholder theory was derived from a combination of the sociological and organizational disciplines. Stakeholder theory can be defined as any group or individual who can affect or is affected by the achievement of the organization's objectives.

Stakeholder theorists suggest that managers in organizations have a network of relationships to serve – this include the suppliers, employees and business partners. And

it was argued that this group of network is important other than owner-manager-employee relationship as in agency theory. On the other end, Sundaram & Inkpen (2004) contend that stakeholder theory attempts to address the group of stakeholders deserving and requiring management's attention.

2.2.4 Resource Dependency Theory

Whilst, the stakeholder theory focuses on relationships with many groups for individual benefits, resource dependency theory concentrates on the role of board directors in providing access to resources needed by the firm. Hillman, Canella and Paetzold (2000) contend that resource dependency theory focuses on the role that directors play in providing or securing essential resources to an organization through their linkages to the external environment.

Johnson et al, (1996) concurs that resource dependency theorists provide focus on the appointment of representatives of independent organizations as a means for gaining access in resources critical to firm success and increasing share prices. For example, outside directors who are partners to a law firm provide legal advice, either in board meetings or in private communication with the firm executives that may otherwise be more costly for the firm to secure. It has been argued that the provision of resources enhances organizational functioning, firm's growth and its survival (Daily et al, 2002). According to Hillman, Canella and Paetzold (2000) that directors bring resources to the firm, such as information, skills, access to key constituents such as suppliers, buyers, public policy makers, social groups as well as legitimacy.

2.3 Determinants of Stock Returns

The turnover event of a CEO occurs in varying circumstances and is caused by any of a number of factors. Turnover is possible as a result of dismissal, voluntary exit, death, or retirement due to either age or ill-health (Huson et al (2004), Denis and Denis (2010), Behn, Dawley, Riley & Yang (2006), Rhim et al (2006)).The experience of the firm prior to the CEO turnover event also varies. Wagner, Pfeffer and O'Reilly (2004) assert that firms with performance that is either exceptionally high or exceptionally poor are more likely to experience turnover of the highest ranked executive. Previous studies suggest that poor firm performance is positively correlated with the likelihood of CEO turnover (Wagner et al, 2004). Huson et al (2004) find that the likelihood of turnover is higher in poor performing firms. This is supported by Bonnier and Bruner (2008), who find that excess returns are significantly positive at the announcement of a change in senior management in a poorly performing firm.

This is consistent with the view that a change in management in a poorly performing firm represents gains to shareholders. For a Board of Directors, deposing a CEO presents the dilemma that doing so too soon might prevent a potential recovery, and waiting too long may make a poor situation worse (Lublin, 2007). There is evidence that the likelihood of executive turnover increases in a distressed firm. Daily and Dalton (2010) refer to studies showing that 45% of companies that had filed for bankruptcy had experienced CEO changes in the 5 years prior to filing, compared to 19% of the control group studied. These results are consistent with Furtado and Karan (2000) who find that CEO's are more

likely to be removed after poor firm performance or in the case of firms close to bankruptcy.

Khanna and Poulsen (2010), however, compare the stock market's reaction to announcements of managerial turnover in failing firms to that of turnover in firms that are not failing. The results are not found to be significantly different. The market reaction to managerial turnover is found to be significant and negative for both the financially distressed group studied and the control group, adding to the inconsistency of the results of previous studies. In a study of US companies filing for Chapter 11 bankruptcy, for the period October 1979 and September 2008, it is found that 55% of firms have replaced their CEO 2 years prior to filing, by the time a plan of reorganisation is proposed (Hotchkiss, 2010). 70% of firms had replaced the CEO by the time the reorganisation plan was implemented after filing for bankruptcy. The legislative environment in the United States of America provides for existing management to remain in office after the firm has declared bankruptcy Khanna and Poulsen (2010).

This is supported by the courts and suggests that the failure of the firm is outside of the manager's control, and blaming the manager is scapegoating. Much is argued against this view. Furtado and Karan (2000) assert that further research is needed to establish whether turnover in these situations is 'scapegoating' or whether the senior managers are trulyresponsible for poor performance. In the study, Hotchkiss (2010) finds that the continued involvement of the pre-bankruptcy management after the event is strongly associated with poor post-bankruptcy performance. This suggests that a change in

management in these firms improved firm performance. The stock market reaction at the date of announcement of CEO turnover.

2.4 Empirical Review

Bonnier and Bruner (2008) argue that the conflicting results of previous study on the effect of CEO turnover on firm performance reflect the information effect and the real effect of the announcement of management change. The information effect would potentially be negative if the announcement of the removal of a senior executive suggests that the organization was experiencing more difficulty than was thought by the market. A positive real effect is the actual positive effect of a change made in shareholders' interests. The individual magnitudes of these two effects in each circumstance of management change would lead to differing results for each incident of management change.

In support of Bonnier and Bruner's (2008) argument regarding the information effect, Furtado and Karan (2000) consider an important aspect of CEO turnover announcements to be the signal received by the market. CEOs are privy to information not publicly available and a turnover in these ranks may send a message about the firm's current or future status. Furtado and Karan (2000) state that the market may respond positively, negatively or not at all to the signals received. There are different explanations for the stock market effect on the day of the announcement of the change in a firm's CEO (Suchard et al, 2001). The negative reaction could be as a result of the adverse short-term effect of a new CEO. This adverse effect is caused by the distraction to the core business

of the firm, the new CEO's period of adjustment and possible restructuring of the management team (Suchard et al, 2001).

It is also possible that the negative effect of the announcement is as a result of the additional information it provides to the market. If the market had been unaware of the significance of the level of difficulty experienced by the firm, the announcement of a change in management may signal to the market that the firm is in more trouble than was thought and that the performance of the firm is likely to be worse than expected (Khanna and Poulson, 2002). This additional information will then be reflected in an adjusted share price for the firm (Fama, 2001). A positive market effect could be attributed to the hypothesis that the Board of Directors of the company are perceived by the market as having behaved in such a way to enhance shareholder wealth (Suchard et al, 2001).

A study of the impact of CEO turnover on the financial performance of an organization assumes that the CEO has influence over the company's decisions. Finkelstein and Boyd (2011) find that high levels of discretion given to CEO's by the Boards of Directors increases their ability to directly influence firm performance. Central to Finkelstein and Boyd's managerial discretion concept is the idea that strategic leadership, especially as embodied in the role of the CEO is pivotal to the success of the firm. Higher managerial discretion and the associated increased riskiness of the CEO role, leads to greater potential impact of the CEO on the firm.

A positive impact on firm performance of a change to CEO requires that the Board of Directors has the ability to recognize and attract a superior successor (Denis and Denis, 2010). Studies conducted on the results of these replacements are not consistent (Huson et al, 2004).CEO turnover affects initial stock price levels, as well as subsequent firm performance. Rhim et al (2006) find that the stock market reacts more favourably in cases where the CEO turnover was not anticipated by the market. It can be argued that anticipated events are already priced in to the current share price of the affected company (Fama, 2001).

Friedman and Singh (2009) find that stockholders react positively if prior firm performance is poor, and the succession was initiated by the Board or the CEO, and if the prior firm performance was good, the stock price reaction is negative. An unanticipated death of a CEO results in a reduction in company share price (Behn et al, 2006), as do delays in the announcement of a replacement of a CEO in the case of CEO death. This implies that the market places value on succession planning, as this would reduce uncertainty, and also implies that the role of CEO is perceived to add value. Huson et al (2004) find that prior to the replacement of a CEO deterioration in performance was experienced, with improvement subsequent to the replacement of the CEO, implying an increase in managerial quality and operational performance.

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are already priced in to the current share price of the affected company (Fama, 2001). Friedman and Singh (2009) find that stockholders react positively if prior firm performance is poor, and the succession was initiated by the Board or the CEO, and if the prior firm performance was good, the stock price reaction is negative. An unanticipated death of a CEO results in a reduction in company share price (Behn et al, 2006), as do delays in the announcement of a replacement of a CEO in the case of CEO death. This implies that the market places value on succession planning, as this would reduce uncertainty, and also implies that the role of CEO is perceived to add value. Huson et al (2004) find that prior to the replacement of a CEO, a deterioration in CEO performance was experienced, with improvement subsequent to the replacement of the CEO, implying an increase in managerial quality and operational performance.

Although Suchard et al (2001) find a short-term negative reaction to the announcement of a CEO change, the long-term effect of a change in CEO is perceived to be positive, assuming the CEO is competent and can improve firm performance over time. Where the news of a CEO change results in a negative market reaction, it is where the short-term negative effect is perceived by the market as outweighing the long-term positive effect. Theory surrounding CEO succession is not clear and predictions of stock price reactions to turnover events are not unambiguous (Huson et al, 2004). It is argued that, if the incoming manager is expected to be superior to the outgoing manager, the stock price may be expected to improve. If, however, the replacement of a CEO is as a result of previous poor management decisions, this could result in a reduction in the stock price, if the market had previously been unaware of the extent of this poor decision making. Stock

price reactions at the time of an announcement reflect the expected outcomes of the turnover, but the actual outcomes are only known with time (Huson et al, 2004).

Much work has been conducted on whether internal or external successors to departing CEOs are more effective (Dalton and Kesner, 2006). An insider appointment can be considered a maintenance strategy, while an external appointment is considered a more fundamental change to the priorities and operations of the organization. Swartz and Menon (2002) concur that insider succession is believed to signal a maintenance approach to the running of the organization, where external replacement suggests radical changes may occur within the organization. It is found by Rhim et al (2006) that for some measures of performance, CEO turnover yielded positive results when the CEO was replaced by an insider. It was established that for turnovers that were normal retirements or retirements due to ill-health, the successor was more likely to be an internal candidate.

The majority of firms studied stated a preference for an internal replacement. Worrell et al (2005) find, however, that in the case of CEO firings, an outside replacement yielded an immediate positive stock price reaction, with an internal replacement resulting in little reaction. In the case of CEO death, the announcement of an outside replacement results in a reduction in equity value (Behn et al, 2006).

Davidson et al (2002) find that stockholder reaction to an outside replacement is more favorable than an insider, and that this is more significant if the replacement arises from a related industry. This is interpreted as being a factor of a replacement from within the

industry being expected to bring about change more quickly. An outsider is expected to have a fresh approach, but may have no knowledge of the firm or industry, and may take time before making required changes. Huson et al (2004) also find a positive stockholder response to outside successors. Earlier study conducted by Dalton and Kesner (2002) found that prior poor firm performance did not lead to an external successor. Outside successors appeared only in the midrange of firm results. This suggests that in cases of extreme performance, either positive or negative, an internal appointment may be considered to be less risky.

Davidson et al (2000) find insider succession associated with increased firm performance. This is consistent with the argument that insider succession is less disruptive and is less likely to result in poorer firm performance. The later study conducted by Kahnn and Poulsen (2010), however, found no significant difference in reaction was observed between the announcements made regarding an internal or external replacement.

Per Fee and Hadlock (2004), the probability of turnover of the top 5 executives of an organization following CEO dismissal is greater than when the CEO does not leave. This is evident more so in firms where the successor CEO is an outsider. This suggests a team nature to management departures. The results of prior research have been inconsistent when examining the effect of internal versus external CEO replacement, even when the effect of pre-succession firm performance has been controlled for (Dalton and Kesner, 2006). This can be explained as the market interpreting the turnover signals differently (Bonnier and Bruner, 2008).

The effect on stock price of CEO turnover varies for different causes of turnover. Denis and Denis (2010) find that in cases of normal retirement, there is no decline in firm performance prior to the announcement of the change, where performance is measured by operating income to total assets. A subsequent increase in performance was observed over the three-year period studied.

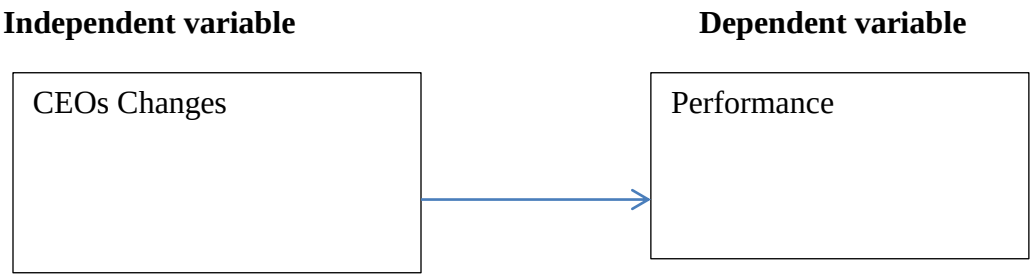
Friedman and Singh (2009), find that the stock price reacts negatively to a CEO change as a result of disability. Worrell et al (2005) find that in the case of CEO firings, the market responded positively to an announcement where a permanent replacement was also announced. Announcements of firings without additional information were found to cause no response in the market. Previous studies have indicated that most CEO successions take place with the successor having been identified well in advance, and the proposed successor is then groomed into the position (Canella and Shen, 2001). In their later study, Shen and Cannella (2002) find that many CEO's are reluctant to step down, and unplanned poorly handled CEO successions have a negative impact on CEO wealth. Per Davidson, Nemec and Worrell (2001), part of the succession plan results in a successful CEO being promoted to the Chairman of the Board. The reaction of the market in this case is likely to differ from instances of forced removal.

2.5 Conceptual Framework

Conceptual framework, according to researcher Saunders (2007) are structured from a set of broad ideas and theories that help a researcher to properly identify the problem they are looking at, frame their questions and find suitable literature. According to Young

(2009), conceptual framework is a diagrammatical representation that shows the relationship between dependent variable and independent variables. In this study, the conceptual framework will look at the effect of the announcement of CEOs changes on the performance of listed firms at NSE. The independent variable is the announcement of CEOs changes while the dependent variable is the performance.

Figure 2.1: Conceptual framework



2.6 Summary of Literature Review

Prior research on the effect of managerial succession on firm performance has been mixed, and per Davidson et al (2000) there exist three main contradictory views that have emerged. The first is that managerial succession improves operational performance and hence organisational performance. This is termed the 'common sense' viewpoint. The second view is the 'vicious circle'. Here the replacement of senior management causes tension and disruption, and reduces firm performance. The third viewpoint is that a change in leadership does not affect firm performance, suggesting that the leader is relatively unimportant. This is termed the 'ritual scapegoating' argument. The study conducted by Davidson et al (2000) showed that the stock market generally responded

favourably to the announcement of executive succession, suggesting the 'common sense' viewpoint.

However, it is argued that if these results were taken on their own, the more turnover events a firm experiences, the greater the stock price return of the corporation would be expected to be. Methodological differences including different types of organisations, different time periods and different statistical measures all contribute to the lack of consistency in the results of studies investigating the effect of executive succession on firm performance (Davidson et al, 2000). The market views different types of succession announcements differently. (Davidson et al, 2000), and these reactions are reflected in the firm's share price (Fama, 2001). This study will focus on the Kenyan environment, and will examine the market effects of a change in CEO in this environment. The study will attempt to provide further insight into the discussion around CEO succession, focussing on its effect on the share price listed on the Nairobi Securities Exchange.

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

This chapter explains the methodology the researcher used when collecting data, research design, and selection of the target population, sampling design, and data collection instruments and data presentation methods.

3.2 Research Design

The study used descriptive research design. According to Mugenda and Mugenda (2003) descriptive research design is a scientific method which involves observing and describing the behaviour of a subject without influencing it in any way. Descriptive research is often used as a pre-cursor to quantitative research designs, the general overview giving some valuable pointers as to what variables are worth testing quantitatively.

The reason for using this research design is to describe the effects of announcement of CEOs changes on share prices with focus to selected firms listed on Nairobi Securities Exchange. Research designs help researchers to lay out their research questions, methodologies, implementation procedures, and data collection and analysis for the conduct of a research project. In this study, the researcher used quantitative research design, which includes the descriptive research design. The study intends to describe the major variables associated with announcement of CEOs changes on stock returns.

3.3 Population

Target population in the study included selected companies listed at the Nairobi Securities Exchange. The study will select only firms that have changed their CEOs in the period between 2009 and 2015. The study determined the effect of announcement of changes on the shares price before and after the exit of the CEOs. Firms in the Nairobi securities Exchange are grouped as; agricultural, commercial and services, telecommunication and technology, automobiles and accessories, banking, insurance, investment, manufacturing and allied, construction and allied, energy and petroleum and growth enterprise market segment. There were 64 companies listed in the Nairobi Securities Exchange as at 31st December 2015.

3.4 Data Collection

The study used secondary sources of information and data to ensure the information used is up-to-date and relevant. Secondary data is any information that has been collected or researched recently. Sources of secondary data included the internet, libraries, company reports, newspaper among others. The data collected is useful as it allows the researcher to see the prevailing thoughts about his/her area of study (Patton, 2002).

3.5 Data Analysis

Data collected and analysed using quantitative and qualitative method, which improves the validity and reliability of the research study. The data was then presented using various statistical methods such as tables and figures. Quantitative data was analysed through the use of descriptive statistics. The effects of announcement of top management

changes on share prices with focus to selected firms listed on Nairobi Securities Exchange was examined with the help of Statistical Package for Social Science (SPSS 21) and specific statistical methods such as Multiple Linear regression and Factorial analysis. Multiple regressions was used establish how a set of independent variables explains a proportion of the variance of a dependent variable to a significant level through significance test. It was also used to explain the relative predictive importance of independent variables by comparing the beta weights.

3.5.1 Analytical Model

Event study methodology was used in the study. An Event study is a statistical method to assess the impact of an event on the value of a firm. As the event methodology can be used to elicit the effects of any type of event on the direction and magnitude of stock price changes, it is very versatile (Kothari et al, 2004). In order for the sample not to be skewed by illiquid shares, a proxy test of liquidity will be used. A period of 21 trading days was created around the announcement date. This consisted of the date of the announcement and the 10 trading days before and 10 trading days after the announcement. The announcement date relates to either the announcement of an impending CEO departure, or a new CEO appointment date. Actual daily returns will be calculated each share for each company in the data set using the following formula;

$R_{it} = \log [P_{it}/P_{it}-1]$

Where:

R_{it} = the actual share price return for security i for day t; and

P_{it} = the share price of security i at the end of day t.

Expected daily returns was then estimated for each share using the Market Model approach, in order to take both market trends and the company's systemic risk into account (Firer et al, 2004). To control for market risk and sector specific returns, sector-specific company betas was calculated for companies with turnover events. The calculation was performed over a seven year period (2009-2015), for the five years ending at the date of turnover announcement.

3.5.2 Test of Significance

T-tests can be used to determine whether there is a significant difference between two sets of means. Therefore t-tests using SPSS statistical program would be employed in this study. Conducting the t-tests requires that the normality of the data is not violated. The P-values of results of the multiple regression analysis was used to test for significance of the relationship between variables. The significance level of 0.05 (5%) was used to test for significance where any P-value of less than 0.05 shall indicate a significant relationship.

CHAPTER FOUR

DATA ANALYSIS, RESULTS AND DISCUSSION

4.1 Introduction

This chapter involved analysis of data collected and discussion of the results obtained. The study targeted all listed companies in the NSE that had an announcement of change of top management in the year between periods 2009 to2015. However, in order to fulfil the requirement of obtaining company data on announcement of change of top management and its effects on share prices, all companies that were not consistently listed between 2009 to 2015 were eliminated. Thus only thirty one (31) companies were consistently listed from 2009-2015 (NSE, 2015). The study went further to eliminate all the companies that had not announced the change of top management between that span of time. Finally the study ended with Eight (8) companies that had announced the change of their top management between 2009 and 2014.

4.2 Descriptive Analysis

Table 4.1*:* Summary Data

Sample Size	**8**
Reasons for CEO departure	
Voluntary – retirement	1
Voluntary - pursue opportunity outside the company	4
Voluntary - remain linked to the company	2
Forced removal	1
Internal versus External CEO replacement	
Internal	4
External	3
Status of companies 3 years after CEO change	
Delisted	0
Liquidated	0
Merger	0
Name change	0
Unchanged	8

Eight (8) companies experienced a CEO change in the 6 year period, which translates into 11.1% of all NSE listed companies experiencing this change during the years, studied. There were therefore 5 turnover events which announced both a CEO departure

and the replacement of the CEO. The announcement of the new CEO was made on the same day as the departure announcement in 3 cases, as shown in Table 4.2.

Table 4.2: Delays between departure announcements and the corresponding replacement announcement

No. of observations	Average delay(days)	Percentage internal replacement	Percentage external replacement
3	0	68%	33%
2	18.8	20%	80%

The Average Abnormal Returns (AARs) shown in Table 4.3 below were calculated as per paragraph analytical model. No significance testing was done on the Average Abnormal Returns, but a discussion of the AARs provides greater insight into the Cumulative Average Abnormal Returns.

Table 4.3 shows the Average Abnormal Returns for each day of the 11-day event window. This window commences 5 days before the announcement date, with the announcement date being reflected as D0 in Table 4.3. The event window ends on D+5 which is 5 days after the event date, or announcement date. Data is presented for two event windows, the first where D0 is the announcement date of the impending departure of the incumbent CEO, and the second where D0 is the date of announcement of the details of the new or replacement CEO.

Table 4.3: Average Abnormal Returns for the 11-day event window [-5,+5]

Panel A	**AARs at announcement date of CEO departure**				
Sample size 8					
	AAR	**Median AR**	**Number of positive ARs**	**Percentage of positive ARs**	**t-stat**
D-5	-0.080	-0.288	26	46%	-0.01
D-4	1.002	-0.083	25	44%	0.88
D-3	-0.324	0.158	30	53%	-0.53
D-2	-1.013	-0.112	26	46%	-1.35
D-1	1.354	0.115	34	60%	2.06**
D0	-1.481	0.006	29	51%	-1.84*
D+1	0.459	0.425	35	61%	0.82
D+2	0.332	0.058	32	56%	0.95
Panel BAARs at announcement date of new CEO					
Sample size 8					
	AAR	**Median AR**	**Number of positive ARs**	**Percentage of positive ARs**	**t-stat**
D-5	-0.988	-0.288	26	46%	-1.00
D-4	0.488	-0.083	25	44%	0.50
D-3	0.234	0.483	34	60%	0.40
D-2	0.053	-0.093	26	46%	0.15
D-1	0.465	0.130	33	58%	1.22
D0	-0.991	0.006	29	51%	-1.21
D+1	1.038	0.801	38	68%	1.80*
D+2	-2.589	0.056	31	54%	-0.91
D+3	3.496	-0.083	28	49%	1.01
D+4	-0.118	-0.340	26	46%	-0.16
D+5	1.666	0.838	38	68%	1.86*

* Statistically significant at the 10% level

** Statistically significant at the 5% level

4.3 Multi-Factor Analysis

There were 4 turnover events where the date of announcement of the departure of the CEO was the same as the date of announcement of the new CEO appointment. These turnover announcement dates allow for the analysis of the market when all the information related to a turnover event occurs on the same day. The reaction is therefore a combination of the market's response both to the information provided about the outgoing CEO, as well as the reaction to the new CEO information. Table 4.4 reflects the results for this sample set, providing greater insight into the market reactions to the four classifications of announcements, as described above.

Table 4.4: Cumulative Abnormal Returns where Date of announcement of the Departure and the new Appointment occur on the same day

Event window [0]						
Category	**Number of events**	**CAR**	**ACAR**	**Median**	**Standard Deviation**	**CAR**
VI	1	-8.406	-0.365	CAR	2.132	
FI	1	-4.196	-0.599	0.006	3.889	
VE	1	-3.200	-0.246	-0.339	4.890	
FE	1	-49.809	-24.904	0.223	20.811	
Event window [-1;+1]						
Category	**Number of events**	**CAR**	**ACAR**	**Median CAR**	**Standard Deviation**	**CAR**
VI	1	6.155	0.268	0.882	5.916	
FI	1	10.639	1.520	0.885	5.260	
VE	1	29.066	2.236	2.383	8.564	
FE	1	-58.362	-29.181	-29.181	11.800	
Event window [-3,+3]						
Category	**Number of events**	**CAR**	**ACAR**	**Median CAR**	**Standard Deviation**	**CAR**
VI	1	-8.515	-0.328	-0.846	6.848	
FI	1	6.181	0.882	2.858	6.588	
VE	1	86.486	5.884	6.685	10.989	
FE	1	-90.135	-45.068	-45.068	25.208	
Event window [-5,+5]						
Category	**Number of events**	**CAR**	**ACAR**	**Median CAR**	**Standard Deviation**	**CAR**
VI	1	30.883	1.338	-0.256	12.284	
FI	1	-16.019	-2.288	-1.582	4.552	
VE	1	100.84	8.858	9.998	18.282	
FE	1	2.484	1.242	1.242	29.503	

Data surrounding CEO turnover events occurring in the five calendar year period from 2009 to 2014 were gathered from the NSE Company announcement. Detailed information about each turnover event was sourced from financial press reports at the time of the events. This included information surrounding the exit of the old CEO even

and the appointment of the replacement CEO. This data was then used to establish event date around which share price performance could be measured. Details of share prices around the event dates were sourced through Capital market Authority and NSE share prices. In total, there were 8 turnover events during the period. Using the data categorisation and analysis processes referred to in at a categorization and analytical model above, the data was converted into smaller judgemental samples. These samples were used to test the research results.

According to the analysis, it's found that the Cumulative Abnormal Returns for announcements where the details of both the departure of the old CEO and the appointment of the new CEO are announced on the same day. For all four categories, the market reaction to the event on the announcement day [0] is negative. For the three day event window [-1,+1], the market responded positively to all three categories of announcement , except forced removal with an external replacement. For this VE category, the market reaction on the day of the announcement was negative.

The longer 8-day event window [-3,+3] showed a negative market reaction to the VI and FE categories, and a positive reaction to the FI and VE categories. The 11-day event window, [-5,+5] showed a positive market reaction to all categories except the If category.. The announcement reactions are most negative to the FE announcements, but are also more negative for the FI announcements than the voluntary ones. The most positive reactions occur for VE announcements, with VI being more positive than FI.

4.3.1 The Impact of CEO Turnover

Hypothesis 1 relates to the impact of CEO turnover at the date of announcement. The sample size used in testing this hypothesis has been derived using the analytical model methodology.

Table 4.5: Average Cumulative Abnormal Returns

Event window (days)	**ACAR**	**Median CAR**	**Standard Deviation CAR**	**t-stat**
Sample size	8			
[0]	-1.481*	0.006	6.388	-1.840
[-1,+1]	0.342	1.121	8.844	0.300
[-3,+3]	-1.282	0.445	13.800	0.498
[-5,+5]	0.955	-1.821	15.080	0.488

4.3.2 The Impact of CEO Turnover post the Turnover event

The result relates to the impact of CEO turnover for the five years post the turnover event. The sample size that results is 5 turnover events and the data relating to the results is contained in Table 4.6.

Table 4.6*:* Impact of CEO turnover for the five years post the turnover event

Event window (days)	**ACAR**	**Median CAR**	**Standard Deviation CAR**	**t-stat**
Sample size	5			
[0,3]	95.883	19.914	632.230	0.802

4.3.3 CEO Replacement for Internal or External Successors

The results relates to the impact of CEO turnover at the date of announcement of the CEO replacement for internal or external successors. The sample size used in testing this hypothesis has been derived using the analytical model in chapter three. The sample size that results is 5 turnover events.

Table 4.7: Cumulative Average Abnormal Returns Internal Replacement (I) External Replacement (E)

Event window (days)	**ACAR**	**Median CAR**	**Standard Deviation CAR**	**ACAR**	**Median CAR**	**Standard Deviation CAR**	**t-stat**
[0]	-0.293	-0.043	2.425	-2.101	0.146	9.515	0.884
[-1,+1]	0.513	0.882	5.411	0.508	6.845	21.433	0.002
[-3,+3]	0.224	-0.132	6.368	4.090	0.146	9.515	-0.824
[-5,+5]	0.045	-1.123	10.450	8.089	6.845	21.433	-1.886*

CEO Turnover for Different Reasons

The results relates to the impact of CEO turnover at the date of announcement of the CEO turnover for different reasons of turnover. The sample size used in the study has been derived using analytical model in chapter three.

Table 4.8: Cumulative Average Abnormal Returns Voluntary Turnover (V) Forced Turnover (F)

Event window (days)	ACAR	Median CAR	Standard Deviation CAR	ACAR	Median CAR	Standard Deviation CAR	t-stat
[0]	-0.548	0.203	3.636	-4.932	-2.109	11.831	1.288
[-1,+1]	1.065	1.121	6.868	-2.368	0.882	22.018	0.834
[-3,+3]	0.516	0.445	10.289	-8.985	-2.109	11.831	1.299
[-5,+5]	1.688	-1.821	14.045	-1.891	0.882	22.018	0.596

4.4 Interpretation of Findings

The analysis according to Table 4.3 shows the Average Abnormal Returns (AARs) achieved by the firms with CEO turnover events in the 5 calendar years studied. These AARs represent the average extent to which actual returns over the 11-day event window differed from that expected. The AARs for the 11-day event window at the announcement date of the departure of the CEO fluctuate between positive and negative

for the days studied. 52.6% of all abnormal returns (ARs) over the event window are positive.

A statistically positive AAR of 2.06% is observed on D-1, being the day before the announcement. This is statistically significant at the 5% level. As seen in Table 4.3, the AAR observed on D_0, or the day of the departure announcement date, is a statistically significant -1.84%. This is significant at the 10% level. Combining the AARs on D-1 and D0 gives a total AAR return for the two days of 0.32%, or a small positive reaction to the announcement of the departure. The AARs observed on days D+1 and D+2 are also positive, 0.82 and 0.95 respectively, but are not statistically significant.

Table 4.3 also shows the AARs for the 11-day event window around the date of announcement of the new CEO. It was found that positive AARs are observed for8 of the 11 days, with an average of 53.3% of all abnormal returns (ARs) over the 11 days being positive. For the AARs around the announcement of the new CEO, two statistically significant AARs were found at the 10% significance level. The day after the announcement date has a significant positive AAR of 1.80, and D+5 have a significant positive AAR of 1.86%. A negative AAR of -1.21% is observed on D0, but this is not statistically significant. In their comparison of ten event studies of the effect on shareholder wealth of CEO turnover, Furtodo and Karan (1989) find that the results of the studies at the date of the turnover were inconclusive. Six of the studies observed positive abnormal returns at the announcement date, three of which were statistically

significant. Of the four studies observing negative abnormal returns, one result was at a significant level.

Table 4.5 shows that a negative Average Cumulative Abnormal Return (ACAR) of -1.481% was observed for the 1-day, [0], event window. This is significant at the 10% level. The market therefore reacts negatively to the announcement of a change in CEO at the announcement date. For this event window, there is sufficient evidence to reject hypothesis 1 at the 10% significance level.

This is in direct contrast with Suchard et al (2001). In their study of Australian firms, they find a positive but insignificant effect on the day of announcement of the CEO change. Suchard et al (2001) do, however, observe a significant negative response the day after the announcement, suggesting a lagged effect where the information flows to the market after it is disseminated through the stock exchange. The study found a positive ACAR of 0.342% for the 5-day event window, [-1,+1], suggesting a small positive reaction in total when the market has had a day to adjust to the announcement.

Bonnier and Bruner (1989) find significantly positive excess returns in response to the announcement of CEO change, but consider only firms which had underperformed prior to the change. In this research, a smaller negative ACAR of -1.282 was observed for the 8-day event window, and a positive ACAR for the 11-day event window of 0.955. In their study, Suchard et al (2001) also found a negative abnormal return for the 8-day event window. These abnormal returns were not statistically significant.In this study a

significant negative reaction was observed on the announcement day. This must be interpreted in the light of the longer event windows, however, as it is possible that the negative reaction on the official announcement date is a correction of the significant positive reaction observed the day before the announcement, as shown in Table 4.3, suggesting a leaking of information before the announcement is officially made.

Table 4.6 indicated that ACARs of the share price of a company experiencing CEO turnover over of the five years' post the new CEO appointment is not significantly different from zero, the study found that ACAR for the period from the effective date of commencement of employment of the new CEO to three years post this date. This translates into the accumulation of 850 daily Average Abnormal Returns per company in the judgmental sample of 8 companies. The ACAR observed is positive, 95.883, but this is not a statistically significant result. Huson et al (2004) find negative abnormal returns for the 5 years after the turnover event of -0.61%, but this is not statistically significant. Rhim et al (2006) find improvements in various measures of operating performance in the five years post the turnover event, but did not observe a significant improvement in equity measures of performance over the three year period.

There is thus insufficient evidence to reject the hypothesis that the Average Abnormal Returns experienced for the five years post appointment of the new CEO are significantly different from zero. It can therefore not be concluded that the change in CEO resulted in significantly higher returns for the three years after the new CEO takes office.

The analysis on table 4.8 indicated that Average Cumulative Abnormal Returns (ACARs) experienced at the announcement date of the replacement CEO when the CEO is from inside the firm is not significantly different from the ACARs experienced when the replacement CEO is from outside the firm, the study found that the ACARs for the four event windows studied. For the 11-day event window, the ACAR for the case of external replacement is 8.089% over the window, and the ACAR for internal replacement is 0.045%. This result is statistically significant at the 10% level, and demonstrates that the positive Abnormal Returns experienced over this window for external replacement are significantly higher than those for internal replacement. This can be compared to Bonnier and Bruner (1989) who find positive abnormal returns of 5.4% for external CEO replacement. For the event windows [0], [-1,+1] and [-3,+3], no significant results are observed. There is therefore not sufficient evidence over these event windows to conclude that the returns experienced for internal versus external CEO replacement are significantly different. Furtado and Karan (1989) also find no significant relationship between share price performance and the origin of the successor.

Previous studies have also found significant results in the comparison of internal versus external CEO replacement. Rhim et al (2006) find that the market responds more favourably for internal CEO succession than for an external CEO. This is in contrast with Bonnier and Bruner (1989) referred to earlier in this paragraph, as well as with Davidson et al (2002) and Huson et al (2004). For the event window [-1,0], Davidson et al (2002) find a positive CAR of 1.5311%, which is significant at the 1% level, and suggests a positive market reaction to outsider succession. These results are line with Huson et al

(2004) who find a significantly positive market reaction for external CEO replacement. In this research, for the 11-day event window, there is sufficient evidence at the 10% significance level to reject the argument that the returns for internal and external replacement are not significantly different. For the shorter 3-day and 8-day event windows, a positive reaction to external replacement compared to internal replacement is observed, although not statistically significant. In summary, the market reacts more positively to external CEO replacement than to internal replacement, when measured by share price returns, and this reaction is statistically significant over the 11-day event window.

The Average Cumulative Abnormal Returns (ACARs) experienced at the announcement date of the CEO departure for a firm that experiences CEO departure is not significantly for voluntary or forced reasons of CEO departure, the study found that the ACARs for the four event windows studied. The ACAR for the date of announcement of voluntary CEO departure, [0], shows a negative ACAR of -0.548.

The other three event windows have positive ACARs when the turnover is voluntary. In all cases of forced turnover, the ACARs are negative, suggesting a negative response from the market to the turnover event. Friedman and Singh (1989) find negative reaction to CEO turnaround in forced turnovers, but no reaction for retirements. Positive reactions were found for voluntary CEO turnover, and these were more significant in cases of poor firm performance prior to the turnover event. Worrell et al (1993) found a negative reaction to forced CEO turnover announcements, but a positive reaction if a replacement

CEO was announced at the same time as the departure announcement. Dennis and Dennis (1995) find positive abnormal returns for both forced resignations and normal retirements, although these are not statistically significant. The difference in the observed abnormal return between the two groups is, however, statistically significant. None of the results in this study are statistically significant. There is therefore insufficient evidence to suggest that there is a difference in share price return at announcement date when the turnover is voluntary compared to when it is forced.

CHAPTER FIVE

SUMMARY, CONCLUSION AND RECOMMENDATIONS

5.1 Introduction

In this chapter, the summary of findings, conclusion, recommendations, and limitation of the study and areas of further study will be established.

5.2 Summary

According to the analysis, it's found that the Cumulative Abnormal Returns for announcements where the details of both the departure of the old CEO and the appointment of the new CEO are announced on the same day. For all four categories, the market reaction to the event on the announcement day [0] is negative. For the three day event window [-1,+1], the market responded positively to all three categories of announcement , except forced removal with an external replacement. For this VE category, the market reaction on the day of the announcement was negative.

The longer 8-day event window [-3,+3] showed a negative market reaction to the VI and FE categories, and a positive reaction to the FI and VE categories. The 11-day event window, [-5,+5] showed a positive market reaction to all categories except the If category.. The announcement reactions are most negative to the FE announcements, but are also more negative for the FI announcements than the voluntary ones. The most positive reactions occur for VE announcements, with VI being more positive than FI.

5.3 Conclusion

This study found 8 instances of CEO change in the years 2009 to 2013, translating into 11.48% of NSE listed companies experiencing a turnover event in the five years. Bonnier and Bruner (1988) discuss the information effect the and real effect of CEO turnovers, and these effects have been tested in this research. This study has found that the announcement of a CEO change has a significant negative effect on share prices on the day of the announcement. There is a significant positive movement in share prices the day before the announcement, which suggests the market has received the information about the impending turnover event prior to the date of official announcement through NSE. It would appear that the reaction on the day of the announcement is a market correction of the previous day's positive reaction.

The effect of the announcement on share price performance is, however, not significant when considered over the 3-day, 8-day and 11-day event windows. This suggests that the information effect around the announcement date of a CEO change has no permanent impact on the share price performance of the company experiencing the turnover.

The announcement date for the new CEO yields significantly positive share price performance on the day after the announcement [D+1] as well as five days later [D+5]. The study also found that the share price performance is significantly more positive at announcement date for external CEO replacement compared to internal replacement. The effect on share price performance of external CEO replacement for the 11-day event window was found to be significantly positive. For the 3-day and 5-day event window,

the share prices of those companies with external replacement performed better than those for internal replacement, though not significantly. The information effect in this instance is positive. No significant difference in share price performance was observed for voluntary versus forced turnover. For all event windows studied, however, the ACARs were negative for forced CEO removal, suggesting a negative market response to the firing of a CEO. The market responded positively to voluntary turnover for three of the event windows, with a small negative ACAR for event window [0]. The ACARs observed for voluntary turnover were small in magnitude, however, and not significant.

Forced CEO turnover elicits a negative share price reaction, but voluntary turnover does not have an effect on performance. It is thought that the high number of turnover events experienced by listed companies has potentially given rise to a market which responds only slightly to 'normal' turnover events. Of the 8 CEO turnovers observed, only 2 resulted in the new CEO retaining the position for a period of at least three years from the date of commencing employment in the new role. The measurement of the real effect of the CEO change was performed on this sample.

The ACAR observed for this sample over the five years after the new CEO takes office was positive, but not statistically significant. The CEO changes did not destroy value on average, but did not provide a significantly better performance than the market as a whole.

In summary, companies generally experienced a small positive information effect, or reaction, to CEO turnover events. These events then led to a small, but insignificant positive real effect over the five year period, although this was observed on a small sample size.

The information effect of the announcements of CEO changes when both the departure and replacement announcements are made at the same time was measured. The results were different for each event window, but a pattern of ACARs was observed. The sample size in total was eight, so there are concerns about the significance of the results, but an initial model can be constructed to assist in understanding the information effect, and to provide a framework for future research to test, perhaps over longer periods, with larger sample sizes.

Forced CEO removals cause uneasiness in the market, and the announcement date shows more negative share price performance. Where this turnover event is followed by an internal replacement, the market information received may be that the organization has made a mistake in the past, but is intending to return back to its core strategy, and is thus going 'Back to basics'. Forced removals, however, which are followed by an external CEO replacement result in negative information effect. The unplanned removal and the appointment of an unknown external CEO may signal that the organization is in crisis, at worst, but results in much uncertainty at best. For shareholders, this is 'Foreign territory', and the share price performance is most negative for this type of turnover. This study contributes to the debate of the impact that CEOs and the turnover of this senior

executive in particular, in the Kenyan context. It aids in the facilitation of the conversation around the importance of this office in an organization.

5.4 Recommendations for Policy

This research has found that, although the Chief Executive Officer of the organization is a key function for the Nairobi Securities listed companies, there is far more that drives company performance. Established organizations have many experienced skills which have the potential to make the organization a success, potentially independently of the Chief Executive Officer, as seen by the insignificant long term positive impact made by the CEO turnovers, and the small percentage of CEOs who lasted a period of at least five years in office.

Recommendations for Boards of Directors would be to choose the CEO with care, but also not neglect the rest of the organizational executives and management. Organizations are complex structures, and making a single executive appointment, while very important, is not the entire function of the Board in facilitating in the success of the organization.

If CEO tenures remain relatively short, the impact made by the CEO on the organization will remain limited, and an excellent CEO may not have time to bring about changes to the organization which would be beneficial to all stakeholders. Steps should be taken to enhance the likelihood of retaining high quality CEOs for longer periods of time.

5.5 Limitations of Study

The research was conducted using a single measure of financial performance, being performance as reflected in a company's share price. This provided a limited assessment of organizational performance as expressed by Venkatraman and Ramanujam (1985). The results of the study cannot be generalized to accounting or other organizational measures of performance. The research was concerned only with the financial impact of a change in top management level such as CEOs.

It examined only the effect of a single historical event, and did not examine the personal characteristics of a CEO that may bring about a positive or negative change in financial performance. The study can therefore not be used to assess the likely effect of an incoming or outgoing CEO on financial performance, based on the CEO's individual characteristics.

The research was concerned with the impact of an event which had already taken place. It was not an analysis of the factors leading to the CEO change, and cannot be used as a predictor of the likelihood of a change in CEO. The period of CEO change measured was over a five-year period, and may therefore not be generalized to all CEO changes over time. Only listed companies were included in the study, making it difficult for the findings to be generalized to non-listed organizations.

The sample size for the long-run event study was relatively small. For long-run event studies, the methodology used to calculate expected returns becomes more important.

This research used a single method of calculating such returns. Other methodologies, for example the Fama and French (1992) three-factor model may have yielded different results. Mordant and Muller (2003) also extended this model to allow for the Kenyan environment, allowing for the influence of resource sectors, and a study using this methodology might yield different results for the long-run study.

5.6 Suggestions for Further Research

This research was concerned with the post-turnover experience of a NSE listed companies. It has not attempted to research the factors which precede CEO turnover. An interesting area of future study would be to examine pre-turnover characteristics of the firm.

Two possible areas of research within this category would be the pre-turnover financial performance of the firm, as this would be expected to predict CEO turnover, particularly in cases of poor firm performance. Study could also be conducted into Board composition and a possible association between independent Boards of Directors – or Boards with a majority of external directors – and CEO turnover.

Further research could also be conducted into firm performance for CEOs with different tenures. Out of the 8 turnover events studied in this research, only 1 of the CEOs remained for a three year period, either as a result of the new CEO being replaced or the firm delisting. Study could be conducted to compare the firm performance for companies with single long tenure CEOs to those with multiple short tenure senior executives.

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APPENDICES

APPENDIX I: COMPANIES LISTED IN NAIROBI SECURITIES EXCHANGE

AS AT 31 DEC 2015

AGRICULTURAL

Eaagads Ltd

Kapchorua Tea Co. Ltd

Kakuzi

Limuru Tea Co. Ltd

Rea Vipingo Plantations Ltd

Sasini Ltd

Williamson Tea Kenya Ltd

COMMERCIAL AND SERVICES

Express Ltd

Kenya Airways Ltd

Nation Media Group

Standard Group Ltd

TPS Eastern Africa (Serena) Ltd

Scangroup Ltd

Uchumi Supermarket Ltd

Hutchings Biemer Ltd

Longhorn Kenya Ltd

TELECOMMUNICATIONAND TECHNOLOGY

Safaricom Ltd

AUTOMOBILES AND ACCESSORIES

Car and General (K) Ltd

CMC Holdings Ltd

Sameer Africa Ltd

Marshalls (E.A.) Ltd

BANKING

Barclays Bank Ltd

CFC Stanbic Holdings Ltd

I&M Holdings Ltd

Diamond Trust Bank Kenya Ltd

Housing Finance Co Ltd

Kenya Commercial Bank Ltd

National Bank of Kenya Ltd

NIC Bank Ltd

Standard Chartered Bank Ltd

Equity Bank Ltd

The Co-operative Bank of Kenya Ltd

Source: www.nse.co.ke

INSURANCE

Jubilee Holdings Ltd

Pan Africa Insurance Holdings Ltd

Kenya Re-Insurance Corporation Ltd

Liberty Kenya Holdings Ltd

British-American Investments Company (Kenya) Ltd

CIC Insurance Group Ltd

INVESTMENT

Olympia Capital Holdings ltd

Centum Investment Co Ltd

Trans-Century Ltd

MANUFACTURING AND ALLIED

B.O.C Kenya Ltd

British American Tobacco Kenya Ltd

Carbacid Investments Ltd

East African Breweries Ltd

Mumias Sugar Co. Ltd

Unga Group Ltd

Eveready East Africa Ltd

Kenya Orchards Ltd

A.Baumann CO Ltd

CONSTRUCTION AND ALLIED

Athi River Mining

Bamburi Cement Ltd

Crown Berger Ltd

E.A.Cables Ltd

E.A.Portland Cement Ltd

ENERGY AND PETROLEUM

KenolKobil Ltd

Total Kenya Ltd

KenGen Ltd

Kenya Power & Lighting Co Ltd

Umeme Ltd

GROWTH ENTERPRISE MARKET SEGMENT

Home Afrika Ltd

APPENDIX 2: COMPANIES THAT HAVE CHANGED THEIR TOP MANAGEMENT

COMPANIES	REASON FOR RESIGNATION	DTAE OF RESIGNATION
CMC MOTORS	Voluntary – retirement	**28/3/2011**
BARCLAYS BANK	Voluntary - pursue opportunity outside the company	**1/2/013**
KCB	Voluntary - pursue opportunity outside the company	**1/1/2013**
KENYA POWER	Voluntary - pursue opportunity outside the company	**1/8/2013**
CENTUM INVESTIMENT	Voluntary - pursue opportunity outside the company	**1/8/2010**
EABL	Voluntary - remain linked to the company	**1/8/1012**
MUMIAS SUGAR	Voluntary - pursue opportunity outside the company	**20/8/2012**
SAFARICOM	Voluntary - remain linked to the company	**1/11/1010**