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Impact of CEO Duality on Financial Performance: A Study with Special Reference to Selected Listed Companies in BSE

Binoy Chacko*, Gireesh Kumar G.S.**

Abstract

This study examines the relationship between the CEO duality and the financial performance of BSE listed companies in India. To accomplish this, data were sourced from the websites of 50 selected companies'. Simple random sampling is used for selecting sample unit and the study mainly depend on secondary data from published sources. CEO duality in a financial year (Annual report 2014) is taken as independent variable and Return on Asset, Earnings Per Share, Calculated ROA and Current Ratio were taken as dependent variables. It is found that there exists a negative relation between CEO duality and ROA and Calculated ROA but no significant relationship with other variables considered for the study.

Keywords: CEO Duality; Financial Performance; Board Composition; Corporate Governance.

Introduction

Economic development of a country mainly depends on industrial growth and development. Industrial development needs well performed organizations and less growth of sick and other unviable units. Long term growth of any organization primarily depends on its good corporate governance mechanism. Good corporate governance is essential for companies to access domestic as well as global capital at competitive rates. Corporate governance has received the special attention of various stakeholders after the revelation of a number of corporate scandals such as financial scams of Enron, WorldCom and Satyam in India. These incidences emphasized the need of improved corporate governance and led the way towards more legislation in India and all over the world. Corporate governance deals with the rights and responsibilities of a company's management, its board, shareholders and various stakeholders such as employees and customers. Corporate governance affects the investment decisions of the company. Therefore, good corporate governance is necessary to make a sound investment decision which, in turn, helps firms to prosper in the domestic as well as in the global market. It is concerned with the proper implementation of policies and procedures by a company to satisfy its related parties including shareholders, employees, customers, suppliers, regulatory authorities and the community at large.

The Organization for Economic Corporation and Development [O.E.C.D] (1999) original definition reads: "Corporate governance specifies the distribution of rights and responsibilities among different participants in the corporation, such as the board, managers, shareholders and other stakeholders, and spells out the rules and procedures for making decisions on corporate affairs. By doing this, it also provides the structure through which the company objectives are set, and the means of attaining those objectives and monitoring performance." Financial system plays a very important role in the economic life of the nation. The board of directors of a company is obliged to monitor the activities of management on behalf of shareholders and other stakeholders. It is

Author's Affiliation: *Assistant Professor, St. Thomas College, Arunapuram, Pala, Kerala 686574. **Associate Professor, PG and Research, Department of Commerce, Nirmala College, Muvattupuzha, Kerala-685 661 (On Deputation as Director, Centre for Continuing Education Kerala).

Reprint's Request: Gireesh Kumar G.S., Associate Professor, PG and Research, Department of Commerce, Nirmala College, Muvattupuzha, Kerala-68 661.
E-mail: gireeshkartha@yahoo.coms

assumed that board performance of its monitoring duties is influenced by factors such as board composition and quality, size of board, duality of chief executive officer, number of board meetings etc.

The overall health of an economy is closely related to the effectiveness of the financial system in that economy. We cannot imagine any business / industrial activity in an economy without the involvement of efficient banking and financial services. Indian banking and financialindustry, has always played a key role in preventing the economic disasters in our economy.

Statement of the Problem

Often members of Board of directors have been largely criticized for the decline in shareholders' wealth and corporate failure.They have been in the spotlight for the fraud cases that had resulted in the failure of major corporations, such as Enron, WorldCom Global Crossing and Satyam computers in India. Some ofthe reasons stated for these corporate failures are the lack of vigilance by the board of directors,the inappropriate board composition etc. As a result, various corporate governance reforms have specificallyemphasized on appropriate changes to be made to the board of directors in terms of its composition, structureand ownership configuration and in India Securities and Exchange Board of India (SEBI) introduced clause 49 of listing agreement Therefore, the study is a humble attempt to understand the association of CEO duality-one of the essentials of board composition on financial performance of companies listed in BSE.

Research Question

The study attempts to address the research question "Is there any significant relation between the CEO duality and the financial performance of the listed companies in India?"

Research Objectives

The review of literature revealed that corporate governance has been studied from different angles. The present study therefore focuses on an important aspect of corporate governance i.e. CEO duality. The study attempts to understand the relationship of financial performance and CEO duality of companies listed in Bombay Stock Exchange (BSE).

Research Hypothesis

H_0:- There is a no significant relationship between CEO duality and organizational performance.

H_1:- There is a significant relationship between CEO duality and organizational performance.

Methodology

Since this study is on the board meeting of listed companies in India, population of the study is made up of companies listed on the Bombay Stock Exchange (BSE). A sample of 50 listed companies for the financial year 2013-2014 was used for detailed study and analysis. For the purpose of the study data has been collected through secondary sources. The sampling technique adopted for the purpose is simple random sampling for selecting industries (banking and finance) and sample units.

Descriptive statistics, one sample t-test and Spearman rank correlation coefficient test are used for data analysis. Statistical software SPSS used to analyze data.

Review of Literature

Adegbemi B.O Onakoya et al. conducted a study on the topic "Corporate Governance and Bank Performance: A Pooled Study of Selected Banks in Nigeria" among a sample of six selected banks listed on Nigerian Stock Exchange and the researcher observed that corporate governance have been on the low side and have impacted negatively on bank performance. The study therefore contends that strategic training for board members and senior bank managers should be embarked or improved upon, especially on courses that promote corporate governance and banking ethics.

"Corporate Governance and Firms' Financial Performance" is a study conducted by Sekhar Muni Amba among 39 companies listed in Bahrain bourse in the Kingdom of Bahrain and the study revealed that corporate governance variables do influence firms' performance. CEO duality, proportion of non-executive directors and leverage had negative influence and board member as chair of audit committee, proportion of institutional ownership had positive influence on firms' financial performance.

Lal C. Chugh et al (2009) on their research "Corporate governance and firm performance:

evidence from India" among 41 companies listed in NSE in India and found that there is a positive relationship between larger boards and financial performance. The study also found a negative relationship between autonomous board and financial performance and the researches did not found any relationship between CEO duality and financial performance.

Matama Rogers (2008) conducted a study on the topic "Corporate governance and financial performance of selected commercial banks in Uganda" among 4 banks covering 388 sample respondents and found that Corporate Governance predicts 34.5 % of the variance in the general financial performance of Commercial banks in Uganda and the significant contributors to financial performance include openness and reliability. Openness and Reliability are measures of trust. The study also found that credit risk as a measure of disclosure has a negative relationship with financial performance.

Zahid Irshad Younas et al. (2010) conducted a study on the topic "Effect of firm performance on corporate governance a panel data analysis" among a sample of 52 firms listed on Karachi Stock Exchange from manufacturing sector of Pakistan over the period of 2006-2009 with an objective to investigate the impact of prior year firm's performance on subsequent year firm's corporate governance mechanism. Their results revealed that prior year firm's performance has positive relationship with board size but negative relationship with audit expenditure. Furthermore, any change in prior year firm's performance causes change in CEO duality.

Mamta Brahmbhatt, et al. (2012) conducted a study on the topic "An empirical investigation of corporate governance scenario in public vs private banks in India" among two banks each from public and private sector banks over the period of 2008-2011. The study found an existence of ambiguity in correlation between compliance of corporate governance parameters and net profit. Clause 49 as per SEBI rule was not been able to provide numerical value of importance to each parameter as it is debatable issue over years. Primary research revealed the importance of different parameters set from the perspective of investors and financial advisors.

Jatinder Kaur (2014) conducted a study on the topic "Corporate Governance and Financial performance: A Case of Indian Banking Industry" was an attempt to examine the relationship between corporate governance and the performance of Indian banks. Based on the regression results, it was found that different committees constituted by the banks are significantly related with their performance.

Sumaira Aslam, et al. (2012) conducted a study on the topic " Relating Corporate Governance with Market Valuation and Organisational performance : An Empirical Study on KSE Pakistan" with an objective to empirically test the impact of corporate governance measures on organizational performance of listed companies at 100-index of Karachi stock exchange (KSE) and the result revealed that there was a positive and significant relationship between organizational performance and corporate governance practices and there was positive and very significant relationship between company Valuation and corporate governance and the results are consistent with organizational theory and Agency theory of corporate Governance.

Data Analysis

The Table 1 shows the descriptive statistics of dependent and independent variables of our sample companies.

The Table 1 explains that the range of the CEO duality in BSE listed companies is 1, (Minimum 0 and Maximum 1), standard deviation is 0.505, and the Median is 1, the above descriptive statistics table also shows that the CEO duality has the mean equal to 0.52 and has the standard deviation of 0.505. Skewness of the data is -0.083(standard value of normal distribution is "0") and the Kurtosis is- 2.078 (standard value of normal distribution is "3") both value of the CEO duality variable shows that the data is approximately normally distributed. The following Figure1 explains our analysis:

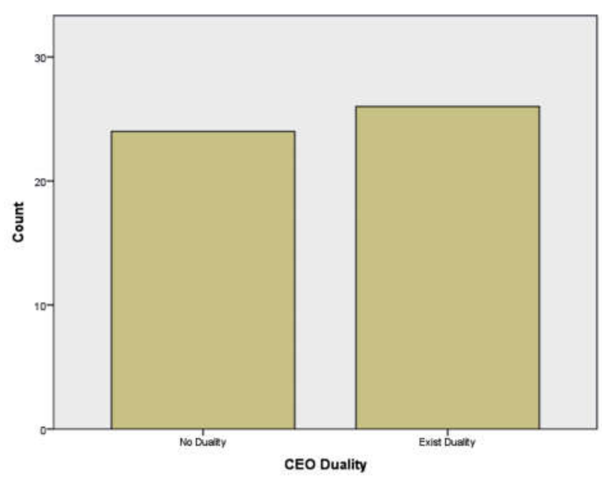

Fig. 1: Shows the data distribution approximately give any normal distribution pattern.

Table 1: The descriptive statistics of dependent/ independent variables used for the study

		CEO Duality	Return on Asset	Earning Per Share	Calculated ROA	Current Ratio
N	Valid	50	50	50	50	50
	Missing	0	0	0	0	0
Mean		.52	-1.097109806	42.35540	.662665904	1.8318
Std. Error of Mean		.071	2.4477799305	7.340521	3.1103572532	.38050
Median		1.00	.645000000	26.46000	.625296459	.9204
Mode		1	.2900000	-.270[a]	-120.4092219[a]	.50[a]
Std. Deviation		.505	17.3084178773	51.905319	21.9935470566	2.69057
Variance		.255	299.581	2694.162	483.716	7.239
Skewness		-.083	-6.952	1.971	-1.876	3.495
Std. Error of Skewness		.337	.337	.337	.337	.337
Kurtosis		-2.078	48.888	4.137	25.732	12.945
Std. Error of Kurtosis		.662	.662	.662	.662	.662
Range		1	127.9041200	244.190	215.2003475	14.27
Minimum		0	-120.4041200	-.270	-120.4092219	.50
Maximum		1	7.5000000	243.920	94.7911256	14.77
Sum		26	-54.8554903	2117.770	33.1332952	91.59

The Table 1 exhibits that the range of the Return on Asset in BSE listed companies is 127.9041200, (Minimum -120.4041200 and Maximum 7.5000000), standard deviation is 17.3084178773, and the Median is .645000000, the above descriptive statistics table also shows that the Return on Asset has the mean equal to -1.097109806 and has the standard deviation of 17.3084178773. Skewness of the data is -6.952 (standard value of normal distribution is "0") and the Kurtosis is 48.888 (standard value of normal distribution is "3") both value of the Return on Asset variable shows that the data is not normally distributed. The following Figure 2 further explain our analysis;

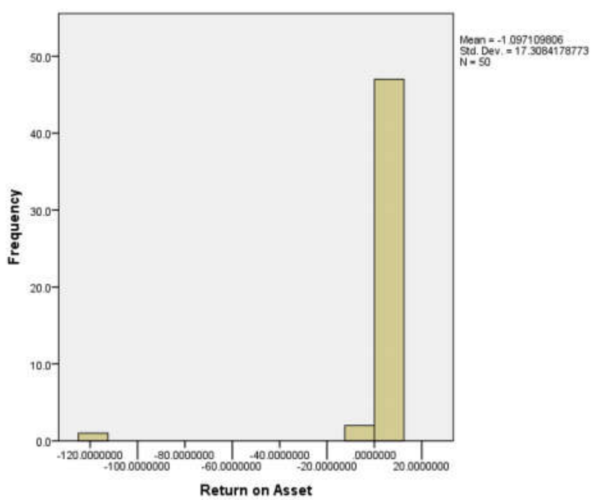

Fig. 2: Shows the data distribution is not normally distributed.

The Table 1 explains that the range of the Earning Per Share in BSE listed companies is 244.190,(Minimum -.270 and Maximum 243.920) standard deviation is 51.905319, and the Median is 26.46000, the above descriptive statistics table also shows that the Earning Per Share has the mean equal to 42.35540 and has the standard deviation of 51.905319. Skewness of the data is 1.971 (standard value of normal distribution is "0") and the Kurtosis is 4.137 (standard value of normal distribution is "3") both value of the Earning per Share variable shows that the data is not normally distributed. The following Figure 3 further explain our analysis;

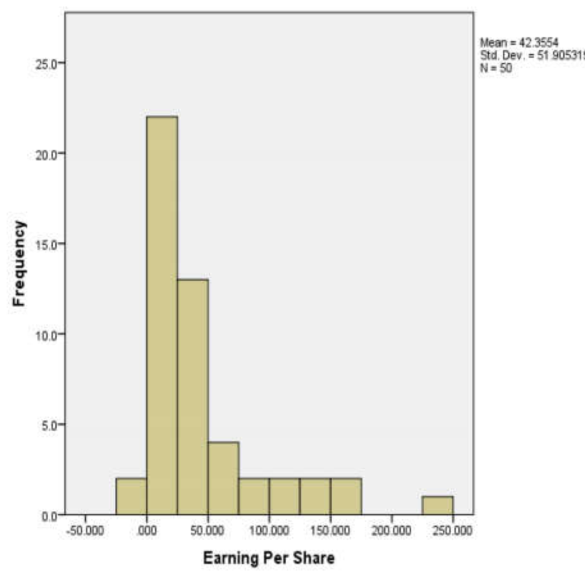

Fig. 3: Shows the data distribution is not normally distributed.

The Table 1 explains that the range of the Calculated ROA in BSE listed companies is 215.2003475, (Minimum -120.4092219 and Maximum 94.7911256) standard deviation is 21.9935470566, and the Median is .625296459, the above descriptive statistics table also shows that the Calculated ROA has the mean equal to .662665904 and has the standard deviation of 21.9935470566. Skewness of the data is -1.876 (standard value of normal distribution is "0") and the Kurtosis is 25.732 (standard value of normal distribution is "3") both value of the Calculated ROA variable shows that the data is not normally distributed. The following Figure 4 further explains our analysis;

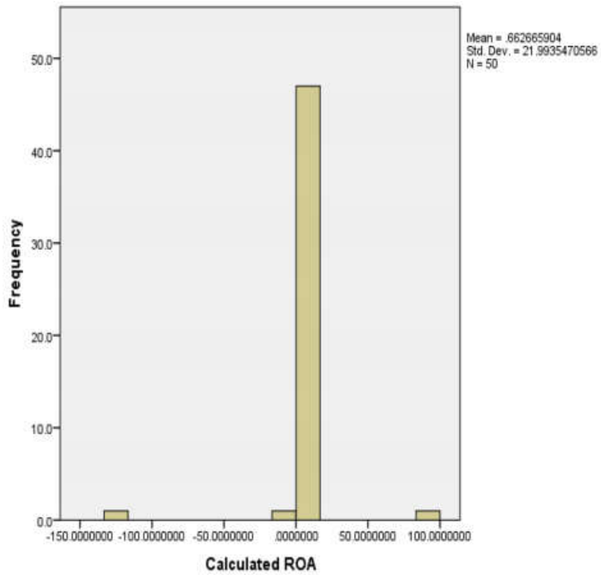

Fig. 4: The above diagram shows the data distribution is not normally distributed.

The Table 1 explains that the range of the Current Ratio in BSE listed companies is 14.27, (Minimum .50 and Maximum 14.77) standard deviation is 2.69057, and the Median is 0.9204, the above descriptive statistics table also shows that the Current Ratio has the mean equal to 1.8318 and has the standard deviation of 2.69057. Skewness of the data is 3.495 (standard value of normal distribution is "0") and the Kurtosis is 12.945 (standard value of normal distribution is "3") both value of the Current Ratio variable shows that the data is not normally distributed. The following Figure 5 further explain our analysis;

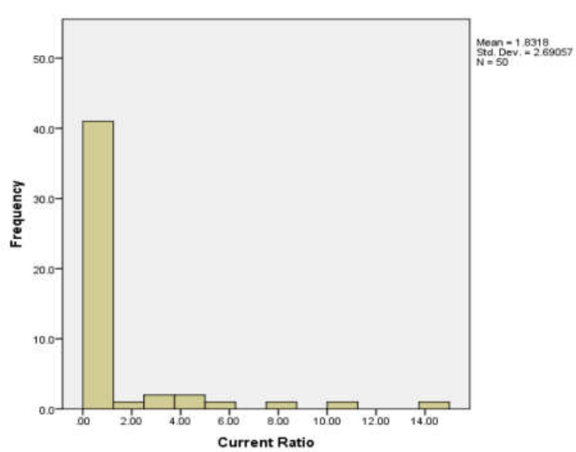

Fig. 5: Shows the data distribution is not normally distributed.

Relation between CEO Duality and Financial Performance

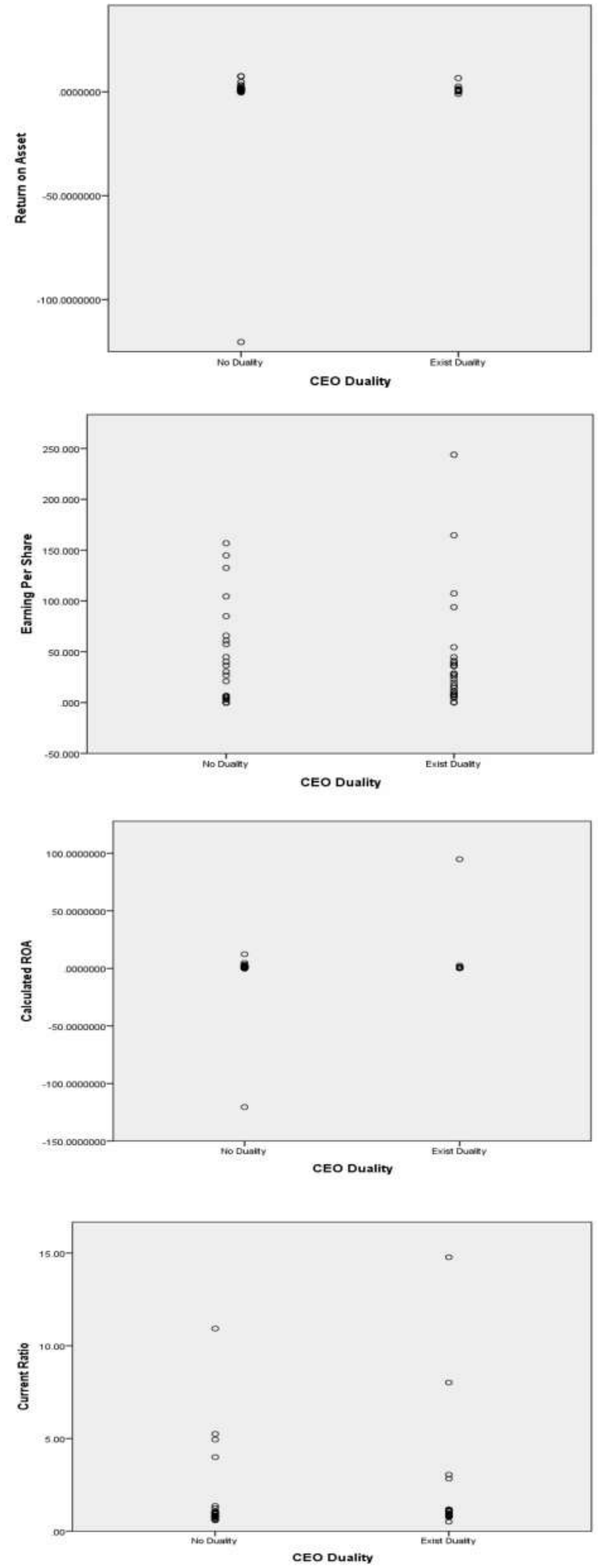

Fig. 6: Showing the association between CEO duality and financial performance variables.

The Figure 6 showing the association between CEO duality and financial performance variables (Return on Asset, Earning per Share, Calculated ROA and Current Ratio). The R2 (coefficient of determination) value for relation between CEO duality and return on asset is 0.115, for CEO duality and earning per share is 0.22, for CEO duality and calculated ROA is 0.170 and for CEO duality and current ratio is 0.015, which states the level of strength for this linear relation.

Further, we applied Spearman rank correlation coefficient test on the values of both variables calculated for our sample of 50 companies. For the relation between CEO duality and return on assets we found the following results of Spearman correlation test.

Table 2: The Spearman correlation test for CEO duality and Return on Asset

			CEO Duality	Return on Asset
Spearman's rho	CEO Duality	Correlation Coefficient	1.000	-.377**
		Sig. (2-tailed)	.	.007
		N	50	50
	Return on Asset	Correlation Coefficient	-.377**	1.000
		Sig. (2-tailed)	.007	.
		N	50	50

**. Correlation is significant at the 0.01 level (2-tailed).

As we can see from the correlation results that there is a significant negative relation between CEO duality and the return on asset, the significance level of our Spearman correlation coefficient test is 0.007 which is below the standard level of 0.05. So we can say this relation as significance. Hence the null hypothesis can be rejected, which states that there is no significant relation between CEO duality and the return on asset, and accept the alternative hypothesis that there exist a significant relationship between CEO duality and the return on asset.

Now we are presenting the research results for the Spearman rank correlation coefficient test for the relation between CEO duality and Calculated ROA of the sample companies.

Table 3: The Spearman correlation test for CEO duality and Earing Per Share.

			CEO Duality	Earning Per Share
Spearman's rho	CEO Duality	Correlation Coefficient	1.000	.022
		Sig. (2-tailed)	.	.878
		N	50	50
	Earning Per Share	Correlation Coefficient	.022	1.000
		Sig. (2-tailed)	.878	.
		N	50	50

Table 4: The Spearman correlation test for CEO duality and Calculated ROA

			CEO Duality	Calculated ROA
Spearman's rho	CEO Duality	Correlation Coefficient	1.000	-.352*
		Sig. (2-tailed)	.	.012
		N	50	50
	Calculated ROA	Correlation Coefficient	-.352*	1.000
		Sig. (2-tailed)	.012	.
		N	50	50

*. Correlation is significant at the 0.05 level (2-tailed).

As we can see from the correlation results that there is a weak positive relation between CEO duality and earning per share, the significance level of our Spearman correlation coefficient test is 0.878 which is beyond the standard level of 0.05. So we cannot say this relation as significance. Hence the null hypothesis cannot be rejected, which states that there is no significant relation between CEO duality and earning per share of the company.

Now we are presenting the research results for the Spearman rank correlation coefficient test for the relation between CEO duality and Calculated ROA of the sample companies

Correlation results show that there is a significant negative relation between CEO duality and the Calculated ROA, the significance level of our Spearman correlation coefficient test is 0.012 which is below the standard level of 0.05. So we can say this relation as significance. Hence the null hypothesis can be rejected, which states that there is no significant relation between CEO duality and the Calculated ROA, and accept the alternative hypothesis that there exist a significant relationship between CEO duality and the Calculated ROA.

The research results for the Spearman rank correlation coefficient test for the relation between CEO duality and current ratio of the sample companies is exhibited in the following Table 5.

Table 5: The Spearman correlation test for CEO duality and Current Ratio

			CEO Duality	Current Ratio
Spearman's rho	CEO Duality	Correlation Coefficient	1.000	.044
		Sig. (2-tailed)	.	.760
		N	50	50
	Current Ratio	Correlation Coefficient	.044	1.000
		Sig. (2-tailed)	.760	.
		N	50	50

As we can see from the correlation results that there is a weak positive relation between the number of CEO duality and current ratio, the significance level of our Spearman correlation coefficient test is 0.760 which is beyond the standard level of 0.05. So we cannot say this relation as significance. Hence the null hypothesis cannot be rejected, which states that there is no significant relation between CEO duality and current ratio of the company.

Summary of Findings and Conclusions

The below Table 6 gives a clear idea about our research findings:

Table 6: Association between Variables

Independent Variable: CEO Duality	Hypothesis	
Dependent Variables	Null: H0	Alternative: H1
Return on Asset	Rejected	Accepted
Earnings per Share	Accepted	Rejected
Calculated ROA	Rejected	Accepted
Current Ratio	Accepted	Rejected

According to the Spearman rank correlation coefficient test for the CEO duality as independent variable, all the null hypothesis are accepted except Return on Asset and Calculated ROA dependent variables. It means there exists a significant relation between CEO duality with Return on Asset and CEO duality with Calculated ROA.

Conclusion and Scope for Further Research

This part will answer the research question and summarize the crux of the study. This empirical research work examines the inter-relationship between CEO duality and financial performance of the BSE listed companies. The purpose of this research was to analyze the relationship between the CEO duality with the financial performance of the company listed in BSE.

Analysis on the relationship between CEO duality and firm's performance measures, it is found that there is no significant relationship between CEO duality with earning per share and current ratio. But the other two financial performance variable such as Return on Asset and calculated ROA show a significant relationship with CEO duality. There exists a significant negative relationship between CEO duality and Return on Asset and calculated ROA. It means that if Chairman and CEO are same, firms Return on Asset and calculated ROA decreases and vice versa.

Due to time constraint, we focused on impact of CEO duality on the financial performance of the BSE listed companies of India for one year i.e. 2014, which is a short period of time to analyze the comprehensive and complex data on impact of board composition on the financial performance. It is recommended that the researchers should extend this study for more than one year so that they can get more comprehensive results. This study focused on the impact of CEO duality on financial performance of the firm. Several other variables of corporate governance such as audit committee, disclosure practices etc. which should be considered by the researchers while analyzing the corporate governance with financial performance of the companies.

So, any prospective researcher should consider other myriad factors of corporate governance while analyzing the firm performance so that the study could be more meaningful and accurate.

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