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Does Chief Executive Officer Succession Affect Firms Financial Performance in Nigeria?

Stephen A. Ojeka[1]*, Dorcas T. Adetula[2], Dick O. Mukoro[3], Oyintinane P. Kpokpo[4]

[1]Department of Accounting, Covenant University, Ota, Ogun State, Nigeria, [2]Department of Accounting, Covenant University, Ota, Ogun State, Nigeria, [3]Department of Accounting, Covenant University, Ota, Ogun State, Nigeria, [4]Department of Accounting, Covenant University, Ota, Ogun State, Nigeria. *Email: stephen.ojeka@covenantuniversity.edu.ng

ABSTRACT

This study examined empirically the impact of Chief Executive Officer (CEO) succession on the financial performance of firms listed on the Nigerian stock exchange. For the purpose of this research, secondary data was used and the instruments of data collection were financial statements. A matched-paired t-test was used in testing the hypothesis. The overall results show that using return on asset, return on equity, return on capital employed and Tobin's Q as a measure of performance; companies that experienced forced CEO turnovers had disrupted performances and therefore experienced decreased performance following CEO succession. The results also show a significant decline in the performance of companies that had insider successors. However, the study found increase performance in firms where the CEO voluntarily resigns and an outsider took over as the CEO. As CEO succession has a significant impact on subsequent performance of Nigerian firms, this study therefore recommends that board should have well-structured succession plans that would define what exactly is the goal of the firms and the type of successor required to fit in. In addition the apparent successors should be assessed based on the proficiencies needed to achieve high financial and organizational performance and the capabilities and profile necessary to undertake the role of the CEO should be properly defined. This should include a narrative explanation of the required skill, competencies, attitudes, knowledge and other important abilities required for a standard performance.

Keywords: Chief Executive Officer Succession, Financial Performance, Nigerian Stock Exchange, Firms and Competencies
JEL Classifications: E44, G1

1. INTRODUCTION

Chief Executive Officer (CEO) (hereafter refers to as CEOs) succession events are considered to be very vital occurrences in the corporate life which as a result determines the performance or otherwise of a business enterprise. It is of utmost importance because the going concern of the business relies significantly on who succeeds the CEO. CEO succession makes available an avenue for evaluating the effectiveness and efficiency of a leader in determining a firms' wealth. Davidson et al. (2006) identified leadership as being an important component of a successful corporate governance mechanism, which can improve the performance of a firm.

The CEO is the individual saddled with the responsibility of setting organizational plans, goals, objectives, organizational structures and performances. As a result of this, the central concept and framework of the business in any organizational setting emanates from the CEO. An interesting view was expressed by Dalton and Kesner (1985) that "many financial periodicals, including Business Week, Forbes, Fortune and the Wall Street Journal, confirms that experts agree that CEOs will be the individuals responsible and to blame for setting organisational technique, structure, setting and efficiency and because CEOs considerably influence their particular organisations, any changes from the CEO situation will considerably affect investors" perceptions, thus affecting the longer term of this firm.

Due to the importance of these highly ranked managerial positions, a top management change represents a major event in the history of any company Costa 2013.

Therefore, the replacement of such a manager is of extreme importance and has its effects on the going concern of the organization.

As noted by Morten et al. (2012), CEOs have an economically and statistically large effect on profitability, revenue, and investment outcomes. Firms underperform when their chief executives are hospitalized but otherwise exhibit similar performance relative to other firms. The results of an investigation carried out by Morten et al. (2012) indicated that a 10 days hospital stay reduces firm operating profitability by 4%. In the words of Rhim et al. (2006), it was posited that top executives with leadership roles largely influences the firm's strategy, design, performance and corporate culture.

However, Dauda (2013) posited that the biggest challenge for most organizations in Nigeria is how to effect a well-designed change of leadership without disrupting the organizational continuity. The transition from one CEO to another is a critical moment in a company's history because a smooth transition is essential to maintain the confidence of investors, business partners, customer and employees, and provides the incoming CEO with a solid platform from which to move the company forward (Russell, 2014).

Prior studies have revealed mixed findings about the impact of CEO, management, and leadership successions in firms pursuing high performance. Most of the studies have centred on the developed countries but none to the best of the researchers' have considered how CEOs succession impact on the financial performance of listed firms in Nigeria. Therefore, the focal point of this research is therefore to investigate the manner, in which CEO succession affects the financial performance of selected listed firms in Nigeria. In addition, this paper would also attempt to examine whether the nature of the CEO's turnover or the origin of the CEO can be connected to the post-succession financial performance of the firms listed in the Nigeria stock exchange (NSE). The major objectives of this paper is to determine how outsider successor; inside successor; forced CEO turnover and voluntary CEO turnover affect the post-succession financial performs of listed firms in Nigeria.

The rest of the paper is divided into 5 parts. The 2nd part looked at the literatures and hypotheses development and third section discussed the research methods part 4 discusses the analysis and implications of findings while part 5 is the conclusion and recommendations.

However, for the purpose of achieving the above state objectives, the following hypotheses have been stated in the null:

H_0: A forced CEO turnover does not negatively affect the post-succession financial performance of firms in Nigeria.

H_0: There is no significant impact of insider succession on firms' post-succession financial performance.

H_0: Voluntary CEO Turnover does not affect the post-succession financial performance of firms in Nigeria.

H_0: There is no significant impact of outsider succession on firms post-succession financial performance.

2. LITERATURE REVIEWS

2.1. CEO Succession

Since the Sarbanes-Oxley Act in 2002, the planning process for an executive officers' succession has become a vital issue in the area of corporate governance ever. This act ensured that, in the event of having difficulty with one employee, the company will not have a threatened going concern and will remain fully functional. This creates tremendous value for shareholders. The concept of CEO succession has been described in various ways by different bodies and organisations.

In Nigeria, there is no uniform definition to the concept of CEO succession. CEO succession can be identified as the process by which a corporate board ensures that its organization is able to maintain sustenance of excellence in CEO leadership over time, with changes from one leader to the next. According to Animashaun and Oyeneyin (2002), succession in legal terminology is the passing of property to persons upon the death of the owner of the property.

In organizational theory, succession is the process of transferring management control from one generation of leaders to the next generation including the dynamics before, during and after the actual transition as cited by Shepherd and Zacharakis, (2000). Nigeria has witnessed different forms of CEO succession. While many have increased the performance of the firms in term of profitability, brands, goodwill and productivity level, many have eroded what the company initially stood for and shareholders' wealth. The dynamics of CEO succession globally and especially in Nigeria comes with its intrigues and politics which necessitate an empirical review now that many firms (as a result of global liquidity) are either merging or acquiring one another and how this can improve the wealth of the owners and the value it create.

2.2. CEO Succession and Post-succession Financial Performance

In a research carried out by Ishak et al. (2013), the examination indicates that on average, the post-succession performance of firms improves to some extent after the occurrence of CEO succession. This position was supported by Graffin et al. (2011) that succession happens when an organization or a firm makes a declaration concerning the appointment of a new CEO. Also, Helfat and Bailey (2005) recommended that members of the board expect that a newly appointed leader will make changes and will impose a mandate for improving the organization's policies. In other words, they assume that a newly elected CEO would establish policies and schemes that will improve the post-succession performance of the organization.

For example, Chaimahawong and Sakulsriprasert (2013) in their finding which was aimed at examining the important factors that affects the succession processes in businesses and the post succession era of Thai family firms, recognises several stages of effects and categorize them into four factors. The factors include: The financial factors, the context factors, the personal factor and the intra-family relationship factor. The structural equation model was used to evaluate the grades of impacts these factors have on the succession process of Thai family firms. According to Chaimahawong and Sakulsriprasert (2013), the outcome of the research work, indicated that the relationship between succession process and the post-succession performance is positive and affects post succession performance at a very high degree. What this means is that, the better the succession process, the better the post-succession performance and vice versa.

According to Banning (2013), companies often discharge their CEOs when the financial performance of the company weakens. The research was focused on evaluating the reason CEO replacement affects the financial performance of firms. They also maintained that new CEO's have the potential of initiating highly favourable negotiations on contracts with high benefits.

2.3. Outsider Successors and Post-succession Financial Performance

Chung and Luo, (2012) in a recent research paper evaluated the impact leadership succession has on the performance of firms in economies that are emerging. Their argument is based on the origin of the successor and firms performance. The researchers according to their findings suggested that outside successors improves the firm's profitability due to the fast growing changes and large scale in the developing markets. Nonetheless, the outsider efficiency is minimized in family owned businesses but in non-family owned businesses, outsider successors are amplified because the ways in which the outsider successor facilitates resource acquisition is perceived by many to be legitimate. This study was supported by evaluating Taiwanese listed firms between 1996 and 2005.

This was corroborated by Mooney et al. (2014) that when considering the replacement of a CEO, the board of directors seek for knowledgeable and upright personalities to front-run organizations over a long period of time.

2.4. Insider Successors and Post-succession Financial Performance

The succession of a leader is a central event in the life of any business organization. What this view tries to buttress is that the new manager would have significant impact on firm performance (Hambrick and Mason, 1984). The selection of an internal successor capitalizes on the significance of continuity. According to Chung et al. (1987), insiders possess great knowledge of the firm and their established social networks. The existence of an internal candidate provide for smooth transition stability due to the fact that they are well informed and have taken part in the development of corporate strategies. Employees also have a sense of commitment when there is an avenue for staff rising up the ranks to attain top management positions.

2.5. Forced CEO Turnover and Post-succession Financial Performance

On the basis of turnover type, Ishak et al. (2013) on CEO succession, find that in scenarios involving forced turnovers (FTOs), the individual chosen to succeed the CEO is most likely to be an outsider and in cases of voluntary turnovers (VTOs), insiders are more likely to be chosen as successors. In the words of Weisbach (1988), a forced CEO turnover can be defined as a turnover that results from reasons other than customary retirements. On the other hand, recognizing FTOs is troublesome since openly accessible sources don't recognize them accordingly. Hence, former poor performance is taken as an intermediary that triggers a forced CEO turnover.

For the most part, forced CEO turnovers are isolated into two sorts. It includes: CEO-initiated turnover and board initiated turnover. According to Furtado and Karan (1990), markets react differently to turnovers initiated by company boards compared to turnovers initiated by CEO's. In the event that the board launches the evacuation of the CEO, it is officeholder on the board as it arranges the evacuation of the CEO to plan for the arrangement of the acting CEO. For coherence purpose, the arrangement of the Acting CEO ought to be synchronized with the declaration of the evacuation of a CEO.

2.6. Voluntary CEO Turnover and Post-succession Financial Performance

According to Maury, (2006), VTO can be defined as the change of CEO that occurs as a result of retirement between the age of 54 and 55, loss of life or illness, or the CEO replacement which occurs due to mergers and takeovers. VTO is usually a planned occurrence and therefore has no significant effect on the share price movement of a firm. A very good illustration of a planned CEO change is the accustomed retirement whereby an announcement is made by the CEO regarding his intention to retire at a future date. As the change is foreseen, the successor has of now been decided and prepped inside the firm.

According to Rhim et al. (2006), since the market is mindful of the foreseen substitution of the CEO, it does not essentially respond to the declaration of the approaching CEO. Denis and Denis (1995) however demonstrate that ordinary retirement is not identified with lower execution preceding administration change and that a little change in execution generally takes after such a succession. Salas (2010) nonetheless discovers that the stock value response is firmly positive if the senior official's residency surpasses 10 years, a marker of administrative entrenchment. In the occasion of a voluntary flight, the CEO will make an announcement of his intention before a consequent take-off. Normally, a deliberate take-off does not give sufficient lead time to the quest for a lasting substitution to be finished in time before the flight of the officeholder. Unless the intentional flight emerges on the event of a retirement, an acting CEO is normally presupposed amid such moves. In this condition, the Board would have sufficient time to meet to consider the arrangement of the acting CEO and the arrangements for the pursuit to discover a changeless substitution. In delegating an acting CEO, the board may need to consider whether it wants to choose somebody who won't be a possibility for the changeless part.

3. RESEARCH METHODS

This paper focused on the listed firms in Nigeria because whatever affects these firms has a spiral effect on the economy. In addition, investors and other stakeholders must be carried along and be abreast of any changes that might want to take place in the organization in order to protect their investment interests. Therefore, the population of this study consists of all the companies listed on the NSE. There are 193 companies listed on the NSE. The sample size consists of all companies listed on the NSE that experienced CEO succession between 2009 and 2013. The breakdown of the sectors are: Agriculture (5), Conglomerates (6), Construction/real estate (10), Consumer goods (28), Financial services (58), Health care (11), ICT (10), Industrial goods (24), Natural resources (5), Oil and gas (14), Services (22). However after omitting companies with incomplete financial statements, companies that experienced CEO succession more than once, 11 CEO succession events were realized. A match paired t-test was used to carry out examination on the differences in mean and median of firm performance before and after CEO successions.

3.1. Model Specification

In order to examine the relationship between CEO Succession and firms financial performance, a linear regression model equation was used. The two constructs involved includes CEO succession and firms financial performance. The regression equation can be computed as

$$Y = \beta_0+\beta X_1+\mu_{it} \tag{1}$$

Explicitly, equation 1 can be defined as;

$$\text{Firms financial performance} = f\,(\text{CEO Succession}) + C \tag{2}$$

In a regression form, the model specification becomes:

$$ROE = \beta_0+\beta_1 FTO+\beta_2 VTO+\beta_3 INSDR+\beta_4 OUTSDR \tag{3}$$

$$ROCE = \beta_0+\beta_1 FTO+\beta_2 VTO+\beta_3 INSDR+\beta_4 OUTSDR \tag{4}$$

$$TOBIN'S\ Q = \beta_0+\beta_1 FTO+\beta_2 VTO+\beta_3 INSDR+\beta_4 OUTSDR \tag{5}$$

$$ROA = \beta_0+\beta_1 FTO+\beta_2 VTO+\beta_3 INSDR+\beta_4 OUSTDR \tag{6}$$

Where:

ROE = The amount of net income returned as a percentage of shareholders equity.

ROCE = A financial ratio that measures a company's profitability and the efficiency with which its capital is employed.

Tobin's Q = A ratio that measures the combined market value of all the companies on the stock market to their replacement costs.

ROA = An indicator of how profitable a company is relative to its total assets.

FTO = Forced turnover (that is 1 If the CEO was replaced forcefully and 0 otherwise).

VTO = Voluntary turnover (if the CEO was voluntarily succeeded).

INSDR = Insider (that is 1 if the successor is from within the firm and 0 otherwise).

OUTSDR = Outsider (if the successor is outside the firm).

μ = Error term, which captures other explanatory variables not explicitly included in the model.

4. RESEARCH FINDINGS AND ANALYSIS OF RESULT

This section of the study looked at the analyses of results and presentations. The hypothesis stated was tested and analysed using descriptive statistics and paired sample t-test.

The Table 1 shows the result of the descriptive statistics with return on assets (ROA) having the highest mean and the Tobin's Q having the lowest. It also captures the mean for successor origin and turnover types.

In the Table 2, it could be deduced using FTO (Forced CEO Turnover), as the explanatory variables and ROA; return on equity (ROE); return on capital employed (ROCE) and Tobin's Q as the dependable variable, showed that there is a mean difference between the pre and post succession result. For example, while the pre mean for ROA shows 0.002 that of the post mean shows −0.003. Also while the pre mean using ROE shows 0.020, the post mean reveals −0.739. Furthermore, the pre mean ROCE was 0.021 and post mean was −0.006. Also, while the Tobin's Q pre mean displayed 0.011, the post mean result showed 0.008. The results were all significant at 1%, 5% and 10% respectively.

The implication of these results is that, the impact and the effect of Forced CEO Turnover on ROA, ROE, ROCE and Tobin's Q in a post-performance of a firm is negative. This means, when a CEO is forced out of the system, there is likelihood of uncertainties that make the stakeholder begin to re-consider their investments plan. In the same light, the system might not have prepared the incoming CEO adequately for the job at least in the first few months. This position lends credence to the vicious cycle theory which describes a negative relationship between senior leader succession and subsequent organizational performance. The negative relationship exists because the departure of a senior leader is believed to cause disruption to a struggling organization. The disruption leads to poorer performance, leading to removal of another senior leader, thus repeating the vicious cycle. FTOs are usually as a result of poor pre-succession performances and past performance has a significant and adverse consequence on shareholders reaction. It is therefore asserted that a forced CEO turnover negatively affect the post-succession financial performance of firms in Nigeria.

In terms of VTO (Voluntary CEO Turnover), the mean ROA is 0.008 and in the post succession era, the mean ROA is −0.000. By using ROE as a measure of performance, the result shows that the mean ROE increases in the post succession phase. In the pre succession phase, the mean ROE is 0.072 and in the post succession era, the mean ROE is 0.114. More so, as regard to ROCE as a measure of performance, the result shows that the mean increases in the post succession phase. In the pre succession

Table 1: Descriptive statistics for all the sampled companies

Variable	OBS	Mean±SD	MIN	MAX
ROA	53	0.0051679±0.0953164	−0.4416	0.1944
ROE	53	−0.1384509±20.040752	−14.6606	0.8995
ROCE	53	0.1559321±0.3515831	−0.3373	2.402
Tobin's Q	53	0.0289041±0.0342433	0	0.160626
Successor origin	53	0.8113208±0.3949977	0	1
Turnover type	53	0.3584906±0.4841463	0	1

Researcher's survey, ROA: Return on assets, ROE: Return on equity, ROCE: Return on capital employed, SD: Standard deviation

Table 2: Results of the paired sample t-test

Variables	ROA			ROE			ROCE			Tobin's Q		
	Pre	Post	Significant	Pre	Post	Significant	Pre	Post	Significant	Pre	Post	Significant
FTO	0.002	−0.003	0.000***	0.020	−0.739	0.000***	0.021	−0.006	1.00*	0.011	0.008	0.000***
VTO	0.008	−0.000	0.000***	0.072	0.114	0.000***	0.070	0.164	0.000***	0.016	0.018	1.00*
INSIDR	0.017	0.012	1.00*	0.05	−0.27	0.000***	0.060	0.049	0.000***	0.013	0.012	0.000***
OUTSDR	−0.04	−0.06	0.000***	0.051	0.150	1.00*	0.026	0.333	1.00*	0.018	0.020	0.000***

Researchers' computation, Significant level at 1%*** and 10%* respectively, ROA: Return on assets, ROE: Return on equity, ROCE: Return on capital employed, FTO: Forced turnover, VTO: Voluntary turnover

phase, the mean ROCE is 0.070 and in the post succession era, while post the mean showed 164. Also, the Tobin's Q result showed that the pre mean stood at 0.016 while in the post succession era, the mean increased to 0.018. All the results are valid at 1%; 5% and 10% level of significance.

The implication of these results could be that since the outgoing CEO already know that it would be leaving makes it incumbent on it to start preparing its successors and exposing it to the rudiments of the business. The CEO might want to live a landmark by priding itself a successful person when the incoming CEO takes the firm to the next level. This assertion lend credence to the common sense theory notion popularised by Guest (1962); Ishak et al. (2013) which suggests that new leaders can cause positive changes in organizations and which would result in the post-succession performance especially when an ineffective CEO is replaced. A VTO is usually planned and since it is planned, the successors have already been trained within the firm and such planned retirements represent smooth transitions.

In terms of insider successor, the table demonstrated that, using INSIDR (insider succession), as the explanatory variables and ROA; ROE; ROCE and Tobin's Q as the dependable variable, there is a mean difference between the pre and post succession result. While the pre mean using ROA showed 0.17, the post mean was 0.012. The result of the ROE as a dependent variable showed the pre mean to be 0.05 while the post mean was −0.27. Using ROCE, the pre mean stood at 0.060 while the post mean showed 0.049. In the same vein, using the Tobin's Q, the pre mean was 0.013 while the post mean was reduced to 0.012.

The implication of the result is that, inside successors are usually relaxed since they have always been part of the system and some of the decisions that previous CEO took. The required changes necessary to boost the firm's performance may be lacking. The above results have been supported by prior researchers who argued that inside successors are slow in recognising how urgent the current challenges are and pursue old strategies that no longer have proper effects. Lauterbach (1999) posited that an inside selection deteriorates post succession performance.

In terms of OUTSDR (CEO outside successor), the mean ROA stood at −0.04 while the post mean was −0.06. For ROE, the pre mean was 0.051 and the post mean 0.150. In the pre succession phase using ROCE, the mean was 0.026 while the post mean was 0.333. Lastly, the pre mean for Tobin's Q was 0.018 while the post mean was 0.020.

The increase in performance after CEO succession using Tobin's Q as a measure has been supported by several researchers. According to Ishak et al. (2013), the stock market reacts more positively if the new CEO is an outsider and comes from an industry related to the firms' operations. In supporting this position, Karaevli (2007) also posited that external CEOs enhance the performance of underperforming firms. This is so because it is assumed that outside CEOs bring new ideas and strategies to the table and take more drastic actions to achieve success. For an outsider to be chosen as a CEO, the candidate must have been seen to have an outstanding track record that is superior to other outside or inside candidates. According to the outsider succession theory, the outside successor is more prone to produce new thoughts and convictions into the association. This expands the different qualities of deduction and thoughts at the top level of the association, considering more prominent choice making self-governance to the successor.

5. CONCLUSION AND RECOMMENDATIONS

The core objective of this research is to examine how CEO succession affects the subsequent financial performance of Nigerian listed firms. From the table above, it was clearly demonstrated that only the CEO VTO and Outside CEO Successor improve the performance of firms. However, it was demonstrated in the contrary that insider CEO successor and CEO FTO impact negatively on the financial performance of the firms (considering all the financial performance indicators considered) especially in Nigeria. This implies that a well-structured CEO succession plan which ought to serve as an aid to a smooth CEO transition is lacking among Nigerian listed companies. The grooming process of apparent successors should be an act that should start even before the need arises. Training of apparent successors should begin early rather than wait until the CEO position is vacant.

In addition, Nigerian firms should carry out their activities having in mind those emergency situations in which the CEO may be forced to vacate the position due to poor performance be nip in the bud. The position of the CEO is so sensitive that investors want to know who calls the shot in an organization. The CEO determines the directions and coordinates strategic investment decisions that could either make or destroy the system hence, the reaction of the market. The CEO successor should be a person with capacity to drive the system and the people at work. The leadership style must command the attention of all and sundry within and outside the system.

As a result of the above, it is therefore recommends that, the board of directors recognize key roles that require a well-structured succession plan. This would involve, identifying the organizational positions that would require a structured succession plan. It is very important for a well-structure plan to aid the smooth transition into the new CEO's tenure. Also, there should be a formal documentation of every detailed plan to ensure easy referencing. Included in this documentation should be any form of adjustment that might occur along the planning and execution process.

In addition, the apparent successors should be assessed based on the proficiencies needed to achieve high financial and organizational performance. Lastly, the capabilities and profile necessary to undertake the role of the CEO should be properly defined. It should include a narrative explanation of the required skill, competencies, attitudes, knowledge and other important abilities required for a standard performance.

The benefits inherent in this research work are vast and this can be carefully considered in the findings and most importantly, when the issue of CEO succession/leadership to the success of any firm is taken into consideration. However, just like other studies, there are limitations that make it imperative to draw inference with caution. These limitations are considered as opportunities for further studies. First, the research was centred on identifying the impact CEO succession on the subsequent performance of listed firms in Nigeria, further studies, researches can be carried out on Nigerian Universities and even government parastatals. Secondly, the research focused on the impact of CEO succession on the financial performance of listed firms in Nigeria. Further researches can look at the impact of CEO succession on the market performance of listed firms. The scope could also be widened to include other countries in Africa.

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