

# Knowledge ICOI

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## Conference Paper

# Functions, Age, Education, Tenure of CEO, and Employee Commitment Toward Firm Performance

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## Abstract

To be effective, a company needs the role of leadership. Leadership is a challenging combination of technical, organizational, and political knowledge, managerial competence, political savvy, organizational vision, as well as communication and interpersonal relationship skills. The present research explored among Chief Executive Officer (CEO) functions, employee commitment, and economic factor toward firm performance. Using the Best CEO list from 2009–2016 taken from Swa Magazine in Indonesia, the top 36 performing public-listed companies were chosen. This study used quantitative methods with linear regression by SPSS. CEO index has a negatively significant effect on Return on Asset (ROA), while pioneer index and commitment have a positively significant effect on ROA. Age, tenure and CEO education have no positive impact on ROA.

**Keywords:** leadership, CEO, financial performance, staff commitment

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## 1. Introduction

Companies face challenges in many ways. Changes are rapidly happen in societies, markets, customers, competition, and technology. Companies need to adapt and establish their values, as well as develop new strategies and even new ways of operating. Their success is based on many factors. CEOs play a vital role in bringing organizational success. They have to break down organizational visions to mission and strategic. They will not be able to work as a single player for mobilizing all the people within the companies.

Team is a basic unit for companies. When change is increasingly complex and quick, then companies are no longer able to rely on individual member to complete a certain task. Instead, it needs the efforts from all teams. Cooperating effectively and having trust on each other will be important elements to gain success [1].

Team effectiveness depends on the leadership of the team leader. When team members trust their leader, they will be willing to take risk to achieve their goal

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<sup>1</sup> because they believe that their own rights and interests are taken into account [2]. The ability to influence his team to be more satisfied, committed and in return be willing to increase productivity is based on leadership styles [3].

To be effective, a company needs the role of leadership. Leadership is a challenging combination of technical, organizational, and political knowledge, managerial competence, political savvy, organizational vision, as well as communication and interpersonal relationship skills. <sup>7</sup> Leadership and management are two distinctive and complementary systems of action <sup>7</sup> [4]. Management is about coping with complexity while leadership is about coping with changes. Companies deal with complexity by planning and budgeting. Management develops the capacity to achieve its plan by organizing and staffing. Management ensures plan accomplishment by controlling and problem solving.

There are four roles of leadership according to Covey (2002). The first is path finding, that is, creating a vision that connects what customers are passionate to get to what we are passionate to give. The second is aligning, and <sup>11</sup> creating a technically elegant system to work. The third is empowering, that <sup>11</sup> releasing the talent, energy, and contribution of people. The last is modeling that building trust with others.

Different types of leaders are considered successful in different types of situations. Based on previous research, there is no evidence for the existence of universal traits, personalities, or even behaviors that can be linked to leader effectiveness. The effectiveness of a leader in a particular situation depends on how well the leader personality, abilities and behaviors match the situation in which the leader works. The types of situations could be stressful, and how they engage their team and make decisions in facing these situations will be a key to success [6].

Roles of CEO are important to the firm success. This research would like to explore which functions of CEO that would impact on firm performance. Based on the situations, this research tried to explore the effects of CEO index, pioneer, age, tenure, and educational index of CEO and employee commitment on firm performance.

## 2. Literature Review

There are a lot of fruitful research on CEO by a number of researchers. They explored this topic from various aspects. These researchers found out <sup>4</sup> that leadership has a positive significant influence on company performance [7–10]. The influence could be either direct impact or indirect impact through employee commitment.

The factors of organizational success related to CEO function would be broad arrays. It could have a domino effect regarding how the leadership style would impact the company operations through its employees. It involves work system that CEO would inspire employees to work hard and feel satisfied [7, 8, 11].

When turbulence situation occurs, success requires innovation. In other words, a company needs to seek creative ways to handle the turbulence situation. Innovation will lead to customer satisfaction and, in turn, customer satisfaction will lead to satisfying financial performance [8, 12].

People wonder whether being successful leaders is affected by their education or whether it is innate. Many MBA schools are created to produce good CEO and being very famous. According to Warren Buffet, one of the most famous investors, the answer is no [13]. Shareholder when seeking for CEO tends to choose someone who will add values to the company. Educational background is public information that could be gathered and used as consideration based on alumni and education system history track. However, other researchers found out the other side of a coin. They said that CEO education has no relationship with company performance [13, 14]. There is no different performance between CEOs from business schools and others.

The behavior of CEO to handle situation is based on many factors. Based on learning theory, the more you spend, the better you are. There is premise that CEOs with long tenure are better than those with shorter one. CEOs with long tenure tend to have more experience to cope with situations. CEOs who have dealt with good and bad economy tend to be more reliable to handle such situations. In addition, in common situation people would be mature in certain age. Tenure and age would be seen as a positive factor to adjust and resolve turbulence within a company. In fact, some research findings showed that there are pros and cons toward it. Harvard Business Review conducted a study entitled 'The Best-Performing CEOs in the World'. In this study, they found that the definition of long term tenure is at least three years [15]. Arbogast & Mirabella (2014) stated that there is a strong relationship between CEO age and company performance, but there is no relationship between CEO tenure and company performance. The summary of these research findings is shown in Table 1.

Based on these research findings, we propose mapping of research. Financial performance will be influenced by the skill of CEO, represented by index of CEO. CEO age will influence financial performance based on the premise that more mature CEO will be wiser. Based on the learning experience, there is a premise that CEO with longer tenure tend to perform better thus affecting financial performance. CEO with higher education will impact financial performance. To be excellence, CEO needs to be pioneer. All the

TABLE 1: Summary of research findings.

Khan, Ha <sup>14</sup> z, Rizvi, Hasnain, & Mariam (2012)	Employee's organizational commitment strongly mediates the impact of leadership style on organizational performance.
Feuss, Harmon, Wirtenberg, & Wides (2004)	Leadership behavior and organization factors mirroring high-involvement work systems are strongly associated not only with employee and customer satisfaction, but also with important business outcomes, such as service quality, cost, and financial performance.
Arbogast & Mirabella, (2014)	There is a strong relationship between a company's change in revenue and CEO Age. Tenure and education have no relationship with company's change in revenue.
Gottesman & Morey (2010)	There is no significant evidence that the type or selectivity of the education of the CEO is related to the firm's financial performance.
Shen & Chen (2007)	Leadership has a positive effect on team trust and team performance. Team trust also has a positive effect on team performance.
Tjiang & Devie (2016)	There is a positive effect of leadership style on innovation, and innovation on customer satisfaction, and customer satisfaction on financial performance. There is a negative effect between innovation and financial performance.
Ramadhany (2017)	Leadership style has a positive effect on staff performance.
Krisnadi & Tarigan (2016)	Leadership style has a positive effect on financial performance. Leadership style also has a positive effect on manager attitude. Manager attitude also has a positive effect on financial performance.

efforts of CEO need support from employees, represented by commitment index. The research mapping is shown in Figure 1.

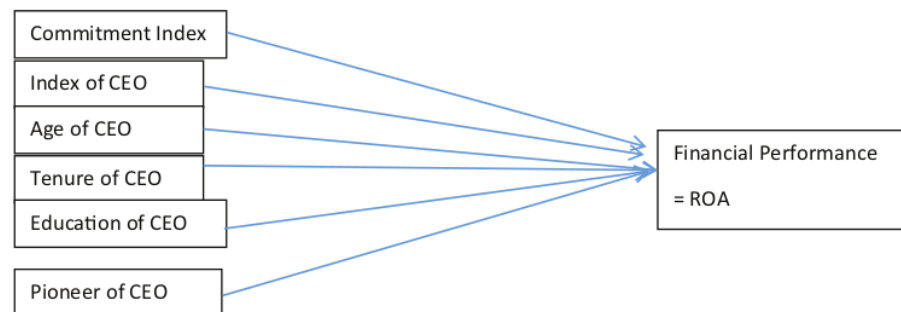


Figure 1: Mapping of research.

### 3. Methods

The data were collected from the Best CEO list from 2009–2016 from Swa Magazine in Indonesia. Return on Asset data were collected from the Investor Magazine from 2009–2017. By using the best performers, the issues of a company strength and likelihood of

success were intended to be controlled. There were 95 Best CEOs. Purposive sampling was used based on the criteria that CEO should come from public listed companies. This resulted in 40 CEOs. However, four of them did not have pioneer index so they were taken out. Table 1 shows the final 36 CEOs.

TABLE 2: Data collection.

Year	The Best CEO	Public Company	Complete Data
2009	22	11	7
2010	27	10	10
2011	10	5	5
2012 (no event)	–	–	–
2013	10	4	4
2014	10	4	4
2015 (no event)	–	–	–
2016	16	6	6
Total	95	40	36

Source: Swa Magazine 2009–2016 [16–21].

Almost every year, Swa Magazine conducts the best CEO selection. The committee selects thirty CEOs to be surveyed and interviewed. The result is index value on pioneer, alignment, empowerment and role model. Those indexes are then summarized as CEO index. In terms of employees, there is survey on commitment and motivation. These two indexes comprise employee index. The range of index is between 0–100. The data collected on CEOs were the number of years the CEO worked for their companies (tenure), CEOs age and CEO education. The data were taken from many sources but mainly from Bloomberg.com and other online articles.

The use of data ranging from 2009–2016 allowed for a time period when economy faced upside down. First there was period of recession in 2008 whose effect would be seen in 2009 and continued to grow until 2016. Return on Asset of companies was chosen as an indicator of financial performance. The analysis used quantitative methods with linear regression by SPSS. Classical assumption test was conducted before running the SPSS program. Based on the mapping, we proposed the following hypotheses:

- H1 = The index of CEO has an impact on ROA
- H2 = The commitment of CEO has an impact on ROA
- H3 = The pioneer of CEO has an impact on ROA
- H4 = The age of CEO has an impact on ROA
- H5 = The tenure of CEO has an impact on ROA
- H6 = The educational index of staff has an impact on ROA

## 4. Results

All the data were analyzed using SPSS 23.0. We performed linear regression with  $\alpha = 5\%$  on the model. The model can explain 45.2% that ROA is influenced positively by the age of CEO, tenure of CEO, education of CEO, pioneer of CEO, and commitment index, while index of CEO negatively influences ROA. The model is not significant because 31.5% is higher than  $\alpha = 5\%$  as shown in Table 2.

TABLE 3: Model summary.

Item	Value
R	0.452
R Square	0.204
F	1.242
Significant	0.315

We examine the result by looking on independent variables. It can be inferred that index of CEO and commitment have a significant effect on ROA at  $\alpha = 5\%$ , but the index of CEO has a negative coefficient. The pioneer index has a positively significant effect on ROA at  $\alpha = 10\%$ . The age of CEO, tenure of CEO, and education background do not have significant effect on ROA at  $\alpha = 5\%$  as seen in Table 3.

TABLE 4: Coefficients.

Model	Coefficients	T	Significance
Constant	-1.306	-0.789	0.437
CEO	-1.892	-2.489	0.019*
Commitment	0.892	2.041	0.050*
Pioneer	1.279	1.958	0.060*
Age	0.027	0.143	0.887
Tenure	0.001	0.048	0.962
Education	0.007	0.212	0.834

Based on the findings, the study showed a significant relationship between CEO and ROA but in negative relationship, thus hypothesis H1 is rejected. Commitment has a significant relationship with ROA, so that hypothesis H2 is accepted. Pioneer has a significant relationship with ROA, so that hypothesis H3 is accepted. Age, tenure, and education do not have any significant relationship with ROA, thus hypotheses H4, H5, and H6 are rejected.

Stepwise regression was employed to determine how the model would be if it only included significant variables. We excluded age, tenure, and education of CEO. We performed regression on index of CEO, pioneer of CEO, and commitment on ROA to



see better picture. The model can explain 45% that ROA is influenced negatively by index of CEO, but influenced positively by pioneer of CEO and commitment index. Other variables may influence ROA by 65%. The model is significant at  $\alpha = 10\%$ . CEO index has a negatively significant effect on ROA, while pioneer index and commitment have a positively significant effect on ROA. The result can be seen in Table 4.

TABLE 5: Model summary.

Item	Value
R	0.450
R Square	0.203
F	2.711
Significant	0.061

TABLE 6: Coefficients.

Model	Coefficients	T	Significance
Constant	-1.309	-0.993	0.328
CEO	-1.870	-2.633	0.013
Commitment	0.876	2.142	0.040
Pioneer	1.297	2.170	0.038

Based on Kolmogorov-Smirnov test, the result of the variables is normal while based on collinearity test, the result of variables has VIF value below 10. It can be concluded that there is no collinearity as seen in Table 6.

TABLE 7: Classic assumption test.

Variables	Kolmogorov-Smirnov	Collinearity (VIF result)
CEO	Normal	7.61
Commitment	Normal	3.60
Pioneer	Normal	4.23

## 5. Discussion

The result that CEO index has a negative impact on ROA (H1 hypothesis) is different with those of Ramadhany (2017) and Krisnadi & Tarigan (2016). They found that CEO has a positive effect on financial performance. Negative effect may occur because CEO as an agent, who would like more compensation while company perform better. On the other side, CEO functions are complex situation that may not solely be based on one criterion. Company performance may result from national or global economic situation too.



Commitment index has a positive impact on ROA (H2 hypothesis). Staff commitment may lead company to perform better. They become more productive and contribute to financial performance. Staffs are committed to work for the best interest of company. They understand the role and goal of the company, so they put effort to achieve it. Commitment will lead to high performance of the company. This result is in line with those of Feuss, Harmon, Wirtenberg, & Wides (2004) and Khan, Hafeez, Rizvi, Hasnain, & Mariam (2012).

Pioneer index has a positive impact on ROA (H3 hypothesis). Company needs to be creative to be pioneer in the business to survive. Creative companies will produce products or services that could differentiate them with other competitors. CEO should always seek creativity to be the pioneer of product or service. Distinct products will have a positive impact on customer value that will lead to company performance. The result is in line with that of Tjiang & Devie (2016).

Age has no positive impact on ROA (H4 hypothesis). Arbogast & Mirabella (2014) stated that there is a strong negative relationship between CEO age and financial performance. They concluded that older CEO would be less productive. Our findings revealed no relationship between age and ROA. It could be that every age has a competitive advantage compared with each other. Older CEOs may be seen as having more knowledge and wisdom. Younger ones may have the advantage in terms of risk taking, better understanding about new world, and less time to make decisions so that company will keep updated within the competition.

Tenure has no relationship with ROA (H5 hypothesis). The reason could be that CEOs with longer tenure may feel that they are in their comfort zone. A study by Lublin (2010) showed that CEOs who underperform in the first three years would exit the market. Stockholders use the first three years to see the performance. The world is so volatile, changes are unavoidable. Companies need fresh mind and this might be the reason for not having long tenure anymore. The result that there is no relationship between CEO tenure and company performance is supported by Arbogast and Mirabella (2014).

CEO education has no positive impact on ROA (H6 hypothesis). The educational background of CEO is not linked to company performance. This result is supported by Gottesman and Morey (2010) and Arbogast and Mirabella (2014). They found out that there is no different performance between companies led by MBA or non-MBA. The no difference performance because there is time different between CEO completion of the degree and the gained position as CEO. The benefits of education may diminish because of time lag.

## 6. Conclusion

CEO index has a negative impact on ROA, while commitment index and pioneer index have a positive impact on ROA. CEO is an agent that would not be away from vested interest and he has various skills to support his performance that may result in the success of company. To be successful, company needs to be different from others, and pioneer skill is highly needed in a competitive world. Commitment is a long process in keeping the trusts from staffs in order to achieve visions. Similar research could explore more by adding more companies or years or other variables (such as growth or GDP) so that the result could be fruitful.

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