IDEAS

CEO TURNOVER

POLITICS OF THE REVOLVING DOOR

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CEOs who are sacked because of their poor performance may make the headlines but bad results are a minor factor behind the turnover of top executives.

STAFF TURNOVER • RETIREMENT • MERGERS

Contrary to popular wisdom, bad results are not the main reason that the managing directors of large companies lose their jobs. Although poor performance makes them more vulnerable to being sacked, other factors have to be considered in order to understand the dismissal of CEOs, such as the power they wield within the organization, the availability of alternative candidates and the board's expectations and loyalty.

In fact, CEOs most frequently lose their jobs as a result of mergers and acquisitions, through planned succession or because they retire, as is shown in the "Study of CEO Turnover in Spain's Major Listed Companies (2001-2010)," that I carried out along with the researchers **Salvador Plaza** and **Lourdes Susaeta**.

According to this research, 47 percent of Spain's listed companies have changed their CEO once or more than once during the period covered by the study, above all in 2009 and 2010, and in particular in the real estate, finance and energy sectors. However, there has been hardly any turnover in the leisure and hotel sector.

What leads a board of directors to dismiss their top executive? What are the factors underlying a CEO's departure? This study maps the causes of CEO turnover in Spanish listed companies. The reasons may be endogenous, in which case the executive may exercise a certain influence, if he or she has a capital investment, or is involved in recruitment of directors or compensation. If the reasons are exogenous such as, for example, age, the type of industry or the size of the company, these are factors over which the executive will have less influence.

FLUCTUATING TURNOVER

After studying the changes in 184 companies over a 10-year period (2001-2010), we discovered that more than half (53 percent) of companies kept their managing director in the job during the entire period and almost a third (33 percent) only changed the top executive once during this period. Only 10 percent changed their CEO twice and just under 4 percent had three or more CEOs during this period. This means that barely 14 percent of companies account for the majority of the 123 dismissals recorded during that decade.

Curiously, the trend was reversed during the last few years studied. While 2009 was the most active of the decade, with 15 percent of dismissals, 2010 was much quieter and only produced 6 percent of the total CEO turnover.

Understanding the circumstances that have led large Spanish compa-

WHEN THE REPUTATION OF THE COMPANY OR INDIVIDUALS IS AT STAKE, THE REAL REASON FOR DISMISSAL IS OFTEN NOT GIVEN.

nies to dismiss the top executive is of interest not only to academics interested in corporate governance, but also to politicians, business people, consultants and anyone who wants to understand the workings of Spain's power structure.

This study is based on reasons given for dismissal as published in the media and other complementary sources of information such as corporate governance reports from each of the companies studied. This, however, has its limitations. On the one hand, because there may be more than one reason for the dismissal, and on the other, because companies don't always make public the real reason for dismissing someone.

For example, when the reputation of the company or people involved in the dismissal is at stake, they usually offer "generic" explanations, such as personal reasons or some type of illness. At other times, part of the CEO's severance terms may include maintaining the appearance that he or she has resigned for personal reasons rather than attribute it to the board of directors.

REASONS FOR DISMISSAL

The principal cause of CEO turnover is mergers and acquisitions (29 percent), especially those that result from hostile takeovers. When a company is bought or absorbed by another, the stronger of the two always imposes its management team.

Then there is natural turnover, which represents almost a third of the total. This includes planned successions (19 percent) and retirement (11 percent). It makes sense that turnover through retirement should be high given that a CEO is at the summit of his or her professional life, having arrived at a point where they are able to put their experience to use after a long and fruitful career.

By planned succession we mean the process through which the CEO, along with the company's board of directors, plans their departure in advance and chooses a successor with the potential and skills necessary to take on the job. This can be done through adopting a relay succession strategy, seeking an heir apparent or through staging a "horse race."

It is interesting to note that in almost two out of every 10 cases, CEO departure has occurred through planned succession. This may be a positive result of improved management and the reforms introduced based on recommendations in the code on good governance.

On the other hand, 23 percent of dismissals are directly related to the managing director's successful or poor performance. In 9 percent of cases, a job well done translates into taking on a more prestigious position at another company, while 7 percent have been fired on the grounds of poor results, the same percentage as those leaving because of disagreements about management policy.

In other cases, personal or health reasons are given for the CEO's departure (8 percent) and to a lesser extent, death (3 percent) and scandal (3 percent). Finally, it should be pointed out that only 2 percent of companies offer no public explanation for the dismissal.

IS AGE AN ISSUE?

Age itself need not be grounds for dismissal, always assuming the CEO maintains his or her abilities and is capable of carrying out their work normally. However, some companies include contract clauses that set an upper age limit for executives. For example, the BBVA bank has established an age limit of 70 for executives. Clearly this has strategic implications that have not yet been studied.

According to our study, the average age of a CEO on departing their post is 62 but there is a variation of 11 years on this figure, in that we have found directors who have stayed on till the age of 90 and others who have left at barely 40.

On the other hand, data on the age of incoming CEOs is more homogenous. Around 30 percent take up the position aged between 50 and 55, although the average age of an incoming managing director is slightly higher (56).

BANKING AND THE REAL ESTATE SECTOR

The sectors that have seen the highest turnover are financial services and real estate, with 23 percent, followed by consumer goods (19 percent), the basic materials sector, industry and construction (18 percent). The service industry is in fourth position at 16 percent. The sectors with the lowest turnover are energy (13 percent) and technology and telecommunications (around 9 percent).

It's noticeable that in the real estate sector dismissals peaked in 2006, coinciding with a significant surge in mergers and acquisitions which shows how the impact of buying and selling real estate agencies played a significant role a year before the crisis hit.

SHORTER MANDATES FOR CEOS

The study reveals that CEOs face shorter and more intense mandates. It remains to be seen whether this phenomenon represents a passing fashion or a more fundamental change and whether this increased turnover has been triggered by a higher degree of activism on the part of shareholders.

In Spain, managing directors spend an average of nine years in the job. However, there are significant variations, depending on the sector in which the company is operating. There are CEOs who have stayed on for 43 years and others whose presence in the organization has been little more than the blink of an eye.

It is surprising that 26 percent of CEOs have been in the job for less than two years. The reason for this is the same as for the turnover of executives in general: mergers and acquisitions, planned successions and moving on to more prestigious jobs. It should be highlighted that some of these brief mandates relate to CEOs in transition, that is to say, executives who are bridging the gap between a CEO who is departing through planned succession and the new appointment, while the company seeks the ideal candidate.

In sectors such as consumer goods, basic materials, industry and construction or financial services and real estate, the managing director's mandate is on average usually longer than nine years. On the other hand, in more dynamic sectors, such as technology and telecommunications, oil and energy and consumer services, CEOs usually have shorter mandates of between five and eight years.

Finally, it's worth noting that CEOs who have managed to stay in the job the longest, leave their positions through death, for personal reasons or illness, or through retirement.

As we have pointed out, poor results are a relatively minor cause of the dismissal of CEOs in Spanish listed companies, representing only 7 percent of cases. However, these dismissals often attract a lot of media attention, as do those concerning scandal, creating the impression that these are much more frequent motives for dismissal than they really are when, as this study shows, the most common reasons are mergers and acquisitions, a planned succession, retirement or moving on to a more prestigious position.

THE AVERAGE RETIREMENT AGE IS 62 BUT WE HAVE FOUND DIRECTORS WHO HAVE STAYED ON UNTIL THE AGE OF 90 AND OTHERS WHO QUIT AT 40.