Do CEOs overpower blockholders and governance mechanisms in CEO turnover?

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Keywords: CEO turnover, CEO power, corporate governance, firm performance

Word count: 9,417 words, excluding references.

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Abstract

Although corporate governance practices and shareholder protection have improved over time, CEO turnover remains an opaque process in China. I used the longest panel data from 2002 to 2022 to investigate CEO power channels through structural, ownership, and prestige power on CEO turnover in the presence of blockholders in China. Generalized estimating equations are used to examine each channel of CEO powers against the same power by the directors and shareholders, and overall effects. The predicted CEO turnover is then used to investigate the impacts of CEO turnover and similar power channels on firm performance. I find CEO ownership power dominates ultimate blockholders and shareholder directors in deterring CEO turnover. Different levels of ultimate ownership concentration of State-Owned Enterprises (SOEs) and Individuals have varying effects on turnover. In addition, CEO prestige through external directorships also prevents their departure. Both power channels positively affect firm performance in the post-turnover period. CEO structural power through CEO-Chairman duality has a weak effect and is not robust. There are important implications for the use of corporate governance and equity-based incentive plans. Governance mechanisms are endogenous, and their combined effects can vary in different ownership settings. Moreover, power channels can be endogenous, which affects the effectiveness of equity-based incentive plans. CEOs who hold shares face the dual role of being top executive and minority shareholders in the presence of blockholders, which affects strategic decisions and firm performance.

Introduction

China has undergone significant economic and regulatory reforms that affect the CEO and executive labor markets, including corporate governance, state-owned enterprises, executive compensation regulations, and anti-corruption campaigns. Compared to the West, CEO turnover in China is linked to restrictive factors such as blockholders (Chen et al., 2016; Shen & Lin, 2009), CEO's political and external connections (He et al., 2017; You & Du, 2012), CEO power (Zhang et al., 2011), executive compensation (He & Fang, 2016; He et al., 2017), firms' financial and social performance (Chang & Wong, 2009; Gao et al., 2017; Lee et al., 2012; Qin & Yang, 2022), and workforce diversity (Kim et al., 2021; Ma, 2022). However, CEO turnover events are often opaque and catch investors and broader markets by surprise, such as the recent mysterious disappearance of China Renaissance Holdings' founder-CEO, Bao Fan[1], before his departure and the sudden change in the role of the former CEO of Alibaba Group Holding Ltd., Daniel Zhang[2]. These cases show that even powerful CEOs face challenges in sustaining their incumbency. This strongly suggests that CEO turnover is a process in which strong influence is in place in unique Chinese institutional settings (Chen et al., 2016) and the developing managerial labor market (He et al., 2017). Spanning over various regulatory reforms and guidelines, I examine CEO turnover using the longest sample period, 2002-2022 to answer the following questions: Do CEO powers vary in different ownership structure settings and corporate governance mechanisms? Do the same factors affect firm performance after a turnover?

[1] See Hoskins, P (2024, February 2). "Bao Fan: Missing China billionaire banker resigns from all roles", The BBC, https://www.bbc.com/news/business-68177941.
[2] See Zhang, J (2023, September 11). "Alibaba's ex-CEO quits as Jack Ma's lieutenants take helm", The Financial Review, https://www.afr.com/companies/retail/alibaba-s-ex-ceo-quits-as-jack-ma-s-lieutenants-take-helm-20230911-p5e3st.

I address several limitations of previous studies of CEO power and turnover. First, I use the longest panel data that capture the effect of corporate governance and shareholder protection regulatory developments in China as opposed to a short limited sample, such as a sample of 1997-2006 focusing on forced turnover by Pi and Lowe (2011) and a sample from to 2005-2009 by Zhang et al. (2014). Furthermore, previous studies examine governance mechanisms and nominal ownership variables simultaneously but do not identify the effects of specific ultimate ownership settings (González et al., 2015; Zhang et al., 2011; Zhang et al., 2014). To address this, I create unique settings using ultimate shareholding concentration and types of blockholders to test the effects of CEO power. Many studies examine CEO power on firm performance by controlling for CEO turnover events (Ting, 2013) or financial performance affecting CEO turnover, incorporating CEO power and characteristics (Chijoke-Mgbame et al., 2023; Gao et al., 2017; He & Fang, 2016; Qin & Yang, 2022; Srivastav et al., 2017). Instead, I examine the power factors that affect CEO turnover, and use the predicted value to address the endogeneity between turnover and firm performance.

The empirical literature identifies various factors that determine CEO turnover in the West, such as firm- and industry-level performance prior to turnover (Eisfeldt & Kuhnen, 2013; Gao et al., 2012), labor market conditions (Liu, 2014; Mobbs, 2013), board structure and leadership (Goyal & Park, 2002), ownership structure (Brunello et al., 2003), firm risk (Qin & Yang, 2022), corporate diversification (Berger & Ofek, 1999), investor disagreement (Huang et al., 2020), and market control activities (Lel & Miller, 2015). To study CEO turnover in China, I employ complementary theories to identify the power channels, namely Agency Theory and Resource Dependency Theory, considering the unique Chinese institutional settings through CEO ownership, the CEO's influence on the board of directors, and the CEO's external network.

Agency Theory is relevant to examining governance mechanisms and effectiveness following share structure and corporate governance reform and development in China (Liao et al., 2014; Qian, 1995; Tenev & Zhang, 2002). Resource Dependency Theory complements this because network-based transactions and connections at the market, firm, and individual levels affect resource access and optimization (Luo & Hassan, 2009; Steinfeld, 2004; Yen & Abosag, 2016). However, blockholders from different backgrounds dominate the institutional environment (Chen et al., 2016; Liu et al., 2015), differentiating the Chinese market from the dispersed ownership landscape in the west. Given this unique setting, I investigated and compared the influence of principals and agents on CEO turnover through three distinct channels. The first is prescriptive governance mechanisms in terms of board structure. The second is equity-based executive incentives and shareholder activism through ownership structure. Third, resource-based external networks of directors and CEOs exist.

I collected data on board structure, shareholding, outside directorships, CEO turnover, and financial performance from the CSMAR database for the period 2002-2022 to construct panel data. The percentage of firms with CEO turnovers ranged from 12% to 19%, with an average of 15%. The most-cited reasons for CEO departure were reappointment (35.3%) and position change (22.7%). This undermines the significance of previous studies that focused on forced turnover (Chang & Wong, 2009; Pi & Lowe, 2011). Furthermore, it can be argued that the reasons were opaque to the public eye, as in the case of Bao Fan, who cited health and family reasons for his departure. The CEO power measures were selected to reflect three distinctive channels: structural power (Finkelstein, 1992; van Essen et al., 2015), ownership power (Fabisik et al., 2021; Jensen & Meckling, 1976), and prestige power (Luo & Cheng, 2015). To examine the power channels of CEOs in the presence of modern governance mechanisms and

blockholders, I include corporate governance structure measures, shareholding by blockholders and directors, and the percentage of co-opted directors and directors' external roles. To explain the effects on CEO turnover, I follow Pi and Lowe (2011) and use generalized estimating equations (GEE) with a logit link function and first-order auto-regression working correlation matrix to analyze longitudinal panel data with binomial outcomes. Lagged explanatory variables were used to address endogeneity (He & Fang, 2016). I then generate a predicted CEO turnover variable to explain firm performance and test the robustness across models using the Generalized Method of Moments, Difference-in-Difference, and fixed- and random-effects methods.

Overall, the results show the extent of changes in CEO power in different ownership settings. CEO shareholding is a robust power channel in the presence of blockholders and shareholder directors, implying that CEO ownership power is significant in deterring turnover. This power also affects firm performance in a two-stage regression analysis that addresses endogeneity. On the other hand, the effect of ultimate ownership concentration on CEO turnover varies according to the level of concentration and type of blockholders, namely, State-Owned-Enterprises (SOEs) and individuals. CEOs' salaries were also found to affect turnover. The next significant channel that affects CEO turnover is CEOs' prestige power through the number of external directorships. The effect is robust and significant across different models in the presence of ownership and governance mechanisms. The more external connections CEOs have, the less likely they are to leave their firms. Co-opted directors negatively impact CEO turnover, but their effects are neither robust nor significant. CEOs' structural power through CEO-Chair duality is negatively related to turnover; however, this effect is weakened by other power channels. Overall, board structure and other characteristics do not affect CEO turnovers. Firm performance declines in the post-turnover period, but the predicted CEO turnover variable does not show any

effect, implying that other factors affect performance after a CEO leaves the firm. CEO shareholding and lagged performance are robust in positively affecting firm performance, whereas board size has a negative effect. Furthermore, early regulatory reforms in corporate governance in 2001-2005 significantly and positively affected firm performance, whereas the later reform of equity-based executive incentive plans in 2016 had a negative effect. The results show that CEO turnover and firm performance are affected by different sets of factors, after controlling for endogeneity.

I provide several important insights into the issues of CEO turnover and governance mechanisms surrounding this strategic decision. First, there is potential endogeneity between governance mechanisms and strategic decisions that are governed. For example, governance structure and composition are affected by ownership structure, while equity is used to align CEOs' interests with shareholders, which in turn grants CEOs ownership power to affect governance effectiveness and strategic outcomes such as CEO turnover. Second, the use of equity-based incentive plans for executive compensation is complicated in the presence of blockholders. In this situation, CEOs play dual roles in leading executive decision-making and safeguarding minority interests against dominating shareholders. These conflicting objectives affect CEOs' objectives of staying at or leaving a firm, which in turn influences firm performance. Third, governance mechanisms and their effects are endogenous, as are the CEOs' power channels. More importantly, CEO turnover is affected by the powerplay between principals and agents. Therefore, it is important to examine the endogenous relationships between firm actors and the channels through which power play is transmitted in future research.

This paper is structured as follows. Section 2 discusses the literature review and hypothesis development. Section 3 presents the study methodology. Section 4 presents the results and a discussion is presented in the following section. Section 6 concludes.

Literature Review and Hypothesis Development

The framework of the related theories underpins the influence of CEOs on turnover. First, Agency Theory postulates that shareholders, as capital providers, monitor managerial actions and prevent shirking to safeguard financial welfare (Jensen & Meckling, 1976). Shareholders can execute their roles either by being blockholders (Bae et al., 2012; Isakov & Weisskopf, 2014), or by appointing a board of directors in a dispersed ownership structure (Desender et al., 2013; Hillman & Dalziel, 2003). The latter comes with more agency costs associated with the contractual mechanisms of monitoring and bonding between the principal and the agents (Singh & Davidson, 2003). Complementing this, Resource Dependency Theory highlights the importance of exchanges and connections between actors and organizations to facilitate resource acquisition (Pfeffer & Salancik, 2003). Actors in firms interact with each other internally within their policy framework and externally via market transactions, which, in turn, affects firm behavior and outcomes. Furthermore, institutional theory highlights the unique institutional settings in China that impose pressure and expectations on firms and individual actors to conform to and seek legitimacy for resource optimization at the firm level and to maximize personal goals and interests at the individual level (Chen et al., 2016). In the post-reform period, the managerial labor market in China took a development path towards the Western market, especially for publicly listed firms where information disclosure is increasingly transparent and moving towards international standards (He et al., 2017). As job mobility increases and labor market competition intensifies, CEOs face the imperative of securing their positions and

resources while excelling within a dynamically evolving institutional landscape. Unlike their counterparts in the West, CEOs in Chinese firms negotiate and manage intricate relations and resources where blockholders and socially and politically connected directors are actively present and engaged.

Finkelstein (1992) defines power as "the capacity of individual actors to exert their will" (p. 506) and provides various dimensions of how I can inspect power. I focus on structural, ownership, and prestige power and potential hindrances in the context of CEO turnover. Expert power, derived from CEOs' relevant expertise and experience, grants them the power to mitigate uncertainty and manage contingencies arising in the context of their organization and market (Finkelstein, 1992). While this is an important dimension, inferior data on CEOs' education and professional profiles in China prohibits meaningful and robust analysis.

Structural power

As the top executive in an organization, CEOs gain legislative rights to influence other members through structural and hierarchical authority (Finkelstein, 1992; van Essen et al., 2015). Previous hierarchical structures determined future patterns and the formation of power in organizations (Hambrick, 1981). Therefore, by exercising their structural power as insiders, CEOs can exert an increasing influence on strategic decisions in top management teams and on the operation of the board of directors. CEOs possess insider information as the core agent of a firm, whereas the board of directors incurs the cost of extracting and gathering information (Alam et al., 2014). Information asymmetry affects a board's effectiveness in evaluating managerial performance and strategic decisions, such as CEO turnover, which often relies on external market information as a relative performance evaluation (Jenter & Kanaan, 2015). CEO-chair duality can affect various aspects of firm behavior and outcomes (Bliss et al., 2011;

Finkelstein & D'Aveni, 1994). When CEOs concentrate on the power between the top management team and the board of directors, they influence the structures of the management and board, and subsequently, any changes in the future and firm performance (Harrison et al., 1988). Furthermore, powerful CEOs can influence board membership and agendas to strengthen their structural powers (Joseph et al., 2014).

The board of directors is the first line of defence against managerial shirking and is tasked with CEO appointment and dismissal, contracts and compensation, review and approval of executive functions, and performance. However, they are influenced by bounded rationality and behavioral biases (He & Fang, 2016), references based on external information (Jenter & Kanaan, 2015), and shareholder pressure (Fisman et al., 2014). Many studies have found that the structure and composition of the board of directors are associated with CEO turnover and succession (Brunello et al., 2003; Dah et al., 2014; Graham et al., 2020). In terms of structure, board size affects the dynamics of diversity, depth of views, and deliberations in strategic decision making (Goodstein et al., 1994; Mak & Kusnadi, 2005). The composition of directors' knowledge and expertise influences board policies, procedures, and governance effectiveness (Anderson & Reeb, 2004). Shareholders influence board composition and use it as a governance mechanism to balance CEO power (Baldenius et al., 2014). Among these characteristics, board independence has been rigorously examined and has become a common feature of corporate governance codes worldwide. Laux (2008) proposes that higher board independence indicates weaker social links between CEOs and directors, and is more assertive in punishing poorly performing CEOs, resulting in higher CEO turnover. However, co-opted directors can deter CEO turnover (Coles et al., 2014) when the interests and resources linked to the CEO are at stake. Institutional theory suggests that organizational behavior becomes similar as actors conform to

norms and shape collective rationality to access resources and be legitimized (DiMaggio & Powell, 2000). As CEO appointment, dismissal, and monitoring are vital strategic decisions of the board of directors, we hypothesize that a higher CEO's structural power is linked to lower turnover; however, this power is mitigated by strong governance mechanisms through the board of directors.

Hypothesis 1: CEO structural power is negatively related to CEO turnover.

Hypothesis 1a: Board structure affects CEO turnover, regardless of CEO powers.

Ownership power

CEOs with significant shareholdings align their interests closely with those of shareholders, and therefore, increase their interactions and influence the board of directors. Agency Costs are mitigated through optimal contracting and bonding between the principal and agents, with residual costs remaining due to imperfect information. As part of the contract, executive remuneration incentivizes CEOs' alignment with shareholder interests. Besides receiving a salary, CEOs are paid in shares that motivate them to maximize shareholder wealth through share price performance while bearing part of the costs of value loss (Jensen & Meckling, 1976). The extent to which managerial ownership mitigates CEOs' shirking is debatable. According to the market control literature, higher managerial ownership makes a firm less attractive as an acquisition target, but ownership is significantly lower in contested and unsuccessful acquisitions (Song & Walkling, 1993). Managerial actions towards an acquisition can affect the target firm's value in different ways. For example, managerial ownership is related to positive returns in the target shareholder value if CEOs resist acquisition (Song & Walkling, 1993) but results in more managerial shirking associated with choosing value-diminishing acquisitions in the case of golden parachutes (Bebchuk et al., 2014). Furthermore, equity

liquidity influences how managerial ownership affects firm performance, resulting in a negative relationship between managerial ownership and Tobin's q, but a concave relationship in larger firms (Fabisik et al., 2021). Additionally, higher managerial shareholding motivates CEOs to make better investment decisions in a timely manner (Fabisik et al., 2021). CEOs' ownership also allows them to control information sharing and influences board decisions about their remuneration, appointment, and dismissal (Banerjee & Homroy, 2018; Boyer & Ortiz-Molina, 2008; Faleye, 2007). Although the effects are mixed, the literature supports the notion that managerial ownership influences CEOs' vested interests and actions in firms.

The extent to which managerial ownership motivates CEOs to control or influence their survival in firms with blockholders remains unclear. In addition to the board as a governance mechanism, the extent to which managerial ownership can sustain a CEO's influence depends on the overall ownership structure and characteristics in place. Corporate ownership characteristics, namely ownership concentration, shareholder type, and activism, affect key business decisions. The effects of ownership concentration transcend governance and firm performance differently, according to shareholder type. For example, institutional shareholders have economies of scale in terms of information and monitoring costs, which differentiate their activism in the capital market (Hadani et al., 2011; Hu et al., 2021). On the other hand, individual and family shareholders have strong ties between private and invested capital (Anderson & Reeb, 2004). China has experienced stages of ownership reform, including the privatization of state-owned enterprises (SOEs) (Liao et al., 2014). A notably important event was the Split Share Structure Reform of 2005, which demolished the dual share structure by allowing non-tradable shares to become tradable. All firms, especially SOEs, experienced an increase in performance and productivity, except for corporate governance and operating efficiency (Liao et al., 2014). While

the reform has increased shareholder activism to actively monitor firms, it is also common to observe the presence of blockholders, who may affect governance effectiveness (Chen et al., 2016). Consequently, the blockholder effects on CEO turnover and succession vary.

The relationship between ownership structure and CEO turnover also depends on the incentives of the different types of shareholders and the extent of their control over strategic decisions. CEOs in SOEs have two objectives: maximizing investor returns and fulfilling the government's socioeconomic objectives (Chang & Wong, 2009). Like other firms, SOEs implement modern governance practices to contract and remunerate their CEOs, prevent fraudulent activities (Chen et al., 2016; Shen & Lin, 2009), and optimize state asset allocation and performance (Chang & Wong, 2009). In individual/family run firms, CEOs are often members of the controlling shareholders or close acquaintances. The changeover of CEOs can be a family affair given that top leaders manage firm assets that influence private wealth. Zhu and Shen (2016) find that CEOs' accountability is scrutinized more in firms dominated by individual blockholders than in firms where Chinese state ownership is a blockholder. Institutional blockholders also actively monitor the top management teams, including selection and appointment. Because they have information and cost advantages (He & Fang, 2016), CEO turnover is a key strategic decision to monitor closely. Therefore, I postulate that CEOs' ownership power is negatively related to CEO turnover, but undermined by blockholders.

H2: CEOs' ownership power is negatively related to CEO turnover.

H2a: Ownership structure affects CEO turnover, regardless of CEO power.

Prestige power

CEOs' reputations, as perceived by shareholders and stakeholders in their institutional settings, validate the power they can exert over them (Finkelstein, 1992). CEOs are the central

decision-makers in major transactions and gather resources via their networks, which affect firm operations and performance. The Chinese business network structure is complex, with actors playing different roles as core and peripheral members, which determine whether they are leaders, bridging agents, or outsiders (Luo & Cheng, 2015). Strong network connections can cultivate high network embeddedness, where top managers exchange information and develop new market knowledge laterally between organizations (Luo & Hassan, 2009). While studies have found that political ties help mitigate uncertainty and arbitrage regulatory burden, thus improving firm performance (Haveman et al., 2017), they can also create opportunities for insider expropriation by blurring organizational boundaries (Dieleman & Widjaja, 2019). At the center of corporate decision making, CEOs are considered core actors in networks where outsider actors seek to connect information, resource access, and business development. However, the effects of CEOs' prestigious power through networking depend on their goals and the relative prestigious power of their surrounding network members.

A stream of research examines CEO prestige and forced turnover. CEO power can affect the effectiveness of governance mechanisms, including those of the board of directors, through their closeness to directors (Baldenius et al., 2014; Coles et al., 2014; Tan & Liu, 2016). This includes the appointment and dismissal of a person assuming a CEO position (Blank et al., 2022; Gao et al., 2012; Graham et al., 2020; Pi & Lowe, 2011). Research shows that CEOs' social capital, including political connections, can reduce the likelihood of turnover even in non-SOE-controlled firms (Cao et al., 2017). Furthermore, CEOs utilize their political connections to protect themselves from adverse actions when their firms do not perform well (Pi & Lowe, 2011; You & Du, 2012). However, the extent of CEO prestige can be mitigated by the board's external connectedness. Well-connected boards gain access to better information in complex

environments (Amin et al., 2020), have political ties to better manage contingencies during crisis periods (Carney et al., 2020), and enhance corporate innovation through better information sharing (Helmers et al., 2017). However, directors who hold three or more external directorships concurrently are ineffective monitors and are associated with poor turnover performance sensitivities, similar to boards of directors dominated by insiders (Fich & Shivdasani, 2006). I hypothesize that greater CEOs' prestige power through networking prevents CEO turnover, given their central and insider role in generating and safeguarding information; however, this power is weakened by the network connections of the board of directors.

H3: CEOs' prestige power is negatively related to CEO turnover.

H3a: The board network affects CEO turnover, regardless of CEO powers.

Methodology

We gathered data from the CSMAR database on CEOs, turnover, ownership, board of directors, and financial information for the period 2002 – 2022. We constructed unbalanced panel data to examine changes in CEO positions and potential time-variant effects over an extensive period. Table 1 illustrates the number of CEO turnovers and percentage of events in each year over the period. The percentage of incidents remained stable, accounting for 12–19% of the total number of firms annually.

[Insert Table 1]

As not all CEO departures carry similar weights on firm outcomes (Pi & Lowe, 2011), I delve into the reasons for the turnover (Table 2). Over the period to 2002-2022, the average percentage of CEO dismissal is 0.6%, with a decreasing trend from the highest percentage of 2.2% in 2002. The most cited reasons were reappointment (35.3%), position change (22.7%), contract expiration (15.2%) and resignation (7.6%). Reappointments are becoming increasingly common. Our tabulation shows a trend similar to that of Chang and Wong (2009), who examined similar reasons from 1995 to 2001. In a previous study, the main reasons were job change (31.45%), contract expiration (19.13%), and resignation (11.92%), while corporate governance reform accounted for 15.34%. Reappointment was not cited and dismissal remained low at 4.11%. Using this sample, I could not ascertain whether a CEO voluntarily agreed to be reappointed, change positions, and not renew their contract or resign. The recent departure of the founder-CEO of the China Renaissance, Bao Fan, cited his reason as "for health reasons and to spend more time on his family affairs' **Error! Bookmark not defined.** while he was being investigated by Chinese authorities. There was no clear reason for the departure of Daniel Zhang from Alibaba Group**Error! Bookmark not defined.**, which was assumed to be due to corporate restructuring. Together with a very low rate of dismissal, it would be inaccurate to define forced turnover within this sample because there is a lack of transparency for the cited reasons and events leading to departure, as argued by Shen and Lin (2009). Hence, I include all turnover incidents without classifying the reasons.

[Insert Table 2]

Power measures and relations

Following the literature, I used several power measures as explanatory variables. First, I measure CEOs' structural power in terms of CEO-Chair duality. Unlike previous studies that

used CEO-chair duality as a control variable (Chang & Wong, 2009; Shen & Lin, 2009), this study uses it as a proxy for CEOs' structural power over the board to explain CEO turnover. As hinderances to CEOs' structural power, I use several measures of governance mechanisms, following previous studies (Aghamolla & Hashimoto, 2021; Bhagat & Bolton, 2013; Brick & Chidambaran, 2010; Graham et al., 2020; Zona, 2014). Board size and the total number of board committees were measured. Board independence and CEO-Chair duality have a substitution effect (Graham et al., 2020) and are omitted. As institutional changes, the labor market, and economic development differ by region in China (He et al., 2017), I include a new variable that indicates whether independent directors with an accounting background are located in the same city as the firm's head office. This is a proxy for the quality of board composition. Furthermore, previous research shows that directors have less costly access to information if they are located closer to the firm's head office (Alam et al., 2014).

Second, I measure CEOs' ownership power in terms of managerial shareholding. I also included the log of the top executive salary to benchmark CEOs' quality and abilities against their peers, as under/overpayment affects the nature of CEO turnover (He et al., 2017). I measured other ownership characteristics as hinderances to CEO ownership. These variables include blockholders (Isakov & Weisskopf, 2014; Zhang et al., 2014) in terms of ultimate ownership concentration (ultpct), the largest shareholder's ownership percentage, the Herfindahl-Hirschman Index of overall ownership concentration, top 3/5/10 shareholders' ownership concentration, and ownership type, such as state-owned enterprises (SOE) and individual/family ownership (IND) (Chang & Wong, 2009; Shen & Lin, 2009). I also use two other measures of shareholder–director identity: the percentage of directors who hold shares in a firm (pctdirectorholdshare) and the percentage of directors who do not receive salary in a firm (non-

salarydirectorpct). These measures reflect economic incentives directly tied to firms in which directors have fiduciary duties for shareholders. Holding shares incentivizes directors to act like shareholders, while not receiving salary removes directors from having executive roles and being an outsider in the firm. There were significant differences in mean values between the groups.

Third, I measure CEOs' prestige power in terms of their political ties and the number of external directorships in other publicly listed firms. CEOs' political connections and leadership roles are specific to Chinese institutional settings (Cao et al., 2017; Sun & Ai, 2020; You & Du, 2012). CEOs' relationships with the board of directors affect the performance sensitivity of CEO turnover (Ma, 2022). Hence, I measured the percentage of co-opted directors on co-opted boards to reduce governance effectiveness (Sandvik, 2020).

Several control variables are included. CEO tenure insulates CEOs from forced turnover (Pi & Lowe, 2011), and long-serving CEOs are more likely to become chairpersons, thereby controlling the board of directors (Graham et al., 2020). Moreover, the sensitivity of CEO turnover increases as CEOs are nearing the end of their contract; however, long-tenured CEOs are not subject to the same scrutiny (Cziraki & Groen-Xu, 2020), as entrenched CEOs receive less board monitoring (Zhu & Shen, 2016). I also measure firm age and size (Total Assets) (Chang & Wong, 2009). Next, I include lagged ROA, as past firm performance can affect CEO Turnover (Shen & Lin, 2009). Public firms are more informationally transparent and accounting performance measures can reflect CEO quality and managerial performance (Gao et al., 2017). I also control for capital structure (leverage) (He & Fang, 2016). Finally, industry characteristics and the external environment can induce competitive factors that affect CEO performance (Scharfstein, 1988; Tan & Liu, 2016); hence, their appointments and dismissal. To control for

this, I constructed the Herfindahl-Hirschman index using company sales by industry code as a proxy for product market competition.

Prior to the empirical analysis, I examined the relationships between the explanatory variables and CEO turnover, t-test, Chi-Square Test of Independence (untabulated), and Pearson correlation coefficient (Table 3). The variable descriptions are also included in this table. In terms of structural power, CEO-chair duality has a weaker association with CEO turnover (0.10) than with non-CEO turnover (0.16, $p < 0.01$). The t-test results show that board size (board size) is larger, on average, in firms with CEO Turnover (8.83) than in firms without (8.24). There were no significant differences in board independence between the groups. The total number of board committees is slightly higher in firms without CEO turnover.

From the perspective of ownership power, departing CEOs have a significantly lower shareholding (2.6%) and receive lower salaries (RMB 879,374) than those who stay (5.1%; RMB 923,504). This is consistent with He et al. (2017), who find that underpaid CEOs are more likely to leave the firm given that they are motivated by seeking fairness and equity, as improved information transparency of executive compensation helps facilitate benchmarking against their peers. Only ultimate shareholding (ultpct) shows a statistically significant difference between the groups. Firms that experienced CEO Turnover had a lower concentration of ownership by less than one percentage point compared to firms that did not. The Chi-Square Test of Independence indicated a significant relationship between CEO Turnover and SOE and IND. Compared with non-SOEs (14.3%, $p < 0.01$), 16.4% of SOE firms experienced CEO Turnover. In firms with CEO turnover, the average percentage of directors holding shares on the board is 20% lower than that of firms without CEO turnover, at 24%. However, the percentage of directors who do not receive a salary is higher in firms with CEO turnover (22%) than in those without (20%). In

terms of prestig power, CEOs who leave have fewer external directorships (1.2) than their counterparts (1.6). However, there were no significant differences between the two groups in terms of their political connections and leadership. The percentage of non-CEO co-opted directors is higher in firms with CEOs (0.43) than in those with departing CEOs (0.35).

On average, CEOs who leave their firms have 1.4 years shorter tenure (mean: 4.0) than CEOs who remain there (mean: 5.4). The tenure in our sample (2002-2022) is longer than that in Chang and Wong's (2009) previous study (2.43) for 1995 – 2001. Given a longer tenure, we use the full year of current financial performance instead of the half-year performance in Chang and Wong (2009). CEO tenure has a significantly positive correlation with the percentage of directors who are not co-opted by the CEO (0.7694). This contradicts the intuition of how CEOs accumulate power over the board of directors by influencing their appointments. However, this can be unique to the institutional environment and labor market of directors in China, where directors can also be incumbent or tied to blockholders; hence, CEOs have less co-option. Table 3 shows several strong correlations between board and CEO characteristics, while ultimate shareholding is not strongly correlated with any of the measures. The percentage of directors who hold shares is significantly negatively correlated with the percentage of directors who do not receive a salary (-0.3937), but significantly positively correlated with the CEO's shareholding percentage (0.3662). The higher the shareholding held by a CEO, the higher is the number of directors' shareholders of the same company. However, the more shares directors hold, the fewer they work at the same company. This implies a segregation of agents and principals among the directors on a board, which raises an interesting issue regarding how directors are incentivized to perform their roles. A board that has four key committees, namely Audit, Risk, Nomination and

Compensation, is associated with a higher number of other committees. This may also be influenced by industry and firm characteristics.

[Insert Table 3]

Empirical Analysis

Following Pi and Lowe (2011), I employ the GEE method to examine the effects of CEO Power on CEO turnover using panel data with binomial outcomes and a logit link function with a first-order auto-regression working correlation matrix. The GEE analyzes longitudinal panel data that are likely to be correlated within clusters, in this case, between firms and industries. The model:

$$Logit\{E(CEOTurnover_{it})\} = X_{it}\beta CEOTurnover \sim Bernoulli$$

where $CEOTurnover = \begin{cases} 1 & if\ a\ CEO\ leaves\ the\ position \\ 0 & otherwise \end{cases}$

where x_{it} represents ownership, board of directors, and CEO power are explanatory variables, *i* denotes a firm, and *t* denotes the year.

Endogeneity can arise when one or more explanatory variables are correlated with the error term, resulting in biased and inconsistent estimates that are commonly detected in corporate governance studies (He & Fang, 2016; Lin et al., 2023; Schultz et al., 2010). First, potential endogeneity exists between CEO Turnover and board and firm characteristics. There is a two-way effect between incumbent CEOs, the composition and function of the board of directors, and the resultant firm's strategies and performance. To address this, we use lagged explanatory variables in the model (He & Fang, 2016), to examine how factors in the previous period (*t-1*) affect CEO Turnover in the following period (*t*).

Results

Table 4 presents the results of the GEE model. The Structural model shows that CEO-Chair duality deters CEO turnover at a predicted probability of 0.52 ($\frac{1}{1+e^{-0.0794}}$) less likely to depart from a firm, supporting H1. Governance mechanisms such as board size, the number of key board committees, and the location of independent directors with accounting backgrounds do not affect CEO Turnover, with a small magnitude and insignificant effect. This rejects H1a and shows that a CEO's structural power overcomes the influence of governance mechanisms. It is vital to separate the roles and authority of the board of directors and top executives to ensure that performance monitoring and management are efficient. Unlike Zhang et al. (2014), board structure plays a less important role in CEO turnovers. Board independence has no significant effects. This does not support previous empirical evidence that higher board independence deters forced CEO turnover (Kato & Long, 2006; Pi & Lowe, 2011), questioning the effectiveness of governance mechanisms with high CEOs' structural power.

The Ownership model shows the channels through which CEOs influence turnover. First, lower CEO shareholding is related to a higher predicted probability of CEO turnover, at approximately 0.50 ($\frac{1}{1+e^{-0.0123}}$), supporting H2, and the literature that finds managerial ownership shields forced CEO turnover (Pi & Lowe, 2011). We use a chairperson's shareholding as a hindrance to the CEOs' ownership power. Chairperson shareholding has a positive and significant effect on CEO turnover, implying the effectiveness of incentivizing the chairperson to use equity plans to align their interests with those of shareholders. Similarly, the lower the executive salary, the higher is the predicted probability of CEO turnover at approximately 0.51 (

$\frac{1}{1+e^{-0.0536}}$). Following He et al. (2017), I calculate the underpayment or overpayment. Although we find a positive relationship between underpayments and CEO turnover, as in He et al. (2017), the effect is insignificant. By contrast, the presence of blockholders affects CEO turnover. The ultimate shareholding (ultpct) shows a predicted probability of 0.50, where a higher shareholding reduces the likelihood of CEO turnover. A similar relationship was found with SOE blockholders; however, the opposite was observed for individual blockholders, although the effects were not significant. This finding is consistent with previous studies on forced turnover (Pi & Lowe, 2011; Shen & Lin, 2009). The results may also be affected by other motives by shareholders, such as controlling shareholder-manager collusion and tunneling issues in China found by Zhang et al. (2014) using a five-year period of 2005-2009. Untabulated results using alternative measures, including the Herfindahl-Hirschman Index of nominal ownership concentration by the top one, three, five, and ten shareholders, show no significant effects of nominal ownership concentration on CEO turnover. This suggests that the complexity of shareholder activism and ultimate goals and objectives may differ among different types of shareholders. Furthermore, a higher percentage of directors who hold shares on a board is negatively related to CEO turnover, with a predicted probability of 0.61. This implies that using company shares in executive incentive plans should consider the overall shareholding structure of controlling and minority shareholders as well as shareholding by directors. This is because shareholding drives and changes the interests and incentives of principals and agents in firms, and the dynamic play in key decisions between them. Overall, the results show weaker managerial shareholding and strong influence by shareholder directors, supporting H2a.

The Expert model supports the Resource Dependency theory. External networks play an important role in CEO turnovers. The more outside directorship CEOs have, the less likely they

are to leave, as shown by the predicted probability of 0.51. A firm's resources may be tied to its CEO's ability to source and manage them. Hence, outside directorships give CEOs a competitive advantage in securing their top executive roles and stronger bargaining power with the board of directors and shareholders. However, the percentage of co-opted directors has no effect on CEO turnovers. Mobbs (2013) argues that directors' external appointments can threaten CEOs, as their expertise and experience can make them potential candidates for replacing incumbent CEOs. Hence, we investigate the average number of outside directorships held by directors on a board but find no significant effect on CEO turnover. Furthermore, the untabulated alternative models examining CEO's numbers of political appointments and political leadership roles provide insignificant results. The results support both H3 and H3a, where CEO prestige has a negative influence on CEO turnover, but the effects vary by connection type.

The overall model shows that ownership and external networks play an important role in CEO turnover, while the corporate governance structure shows no effect. CEOs influence their turnover through their shareholding and external networks, while ultimate shareholders affect the outcome through their ownership concentration and directors being incentivized through their shareholding. The results suggest that the more shares CEOs hold, the less likely they are to leave. Furthermore, CEOs' external directorships have a stronger influence than CEO-Chair duality, meaning that CEOs' professional expertise and experience are valued more as competitive advantages than the concentration of power and leadership in the executive team and board of directors' structure.

In terms of control variables, CEO tenure is negative, while firm age and size have positive effects on CEO turnover; all the results are significant. This supports the notion that the longer CEOs are incumbent, the less likely they are to leave a firm, which is similar to Zhang et

al. (2014). However, the results contrast with those of Zhang et al. (2014), who find that firm size is negatively related to CEO turnover, and He et al. (2017) find similar effects on both voluntary and involuntary turnover. The difference between this study and previous ones is the use of lagged variables. Although insignificant, I find that past financial performance is negatively related to CEO turnover, consistent with the literature (He et al., 2017; Pi & Lowe, 2011; Shen & Lin, 2009). This is because older and larger firms have adequate resources and business acumen to execute more effective governance, access a wider pool of executive talent, and better performance-driven managerial monitoring and compensation frameworks. CEO compensation, past firm performance, leverage, and market power do not influence CEO turnover, which is inconsistent with the findings of previous studies (Zhang et al., 2014). Overall, the results show that ownership structure is a key factor affecting CEO turnover, and CEOs also exert influence through their external networks.

[Insert Table 4]

Robustness test

I further examine CEO ownership power in different ownership settings based on the level of ultimate concentration and types of blockholders. Table 5 shows that a low ultimate concentration (below the median = 36.8%; Ultpctq1 and Ultipctq2) is positively related to CEO turnover. However, the ultimate concentration loses its effect on SOE and Individual blockholders. In the presence of individual blockholders, higher managerial shareholdings deter CEO turnovers. Furthermore, CEO-Chair duality has a positive effect on the overall model and SOE blockholders only. A similar effect is observed for the percentage of shareholder directors on the board. The executive salary is significantly and negatively related to CEO turnover when SOE blockholders are present. CEO Prestige power is the only channel that is robust across all

models. These results show that CEO power channels differ according to firm ownership settings.

[Insert Table 5 here]

Firm performance

CEO turnover has been found to impact firms, including performance (Kato & Long, 2006; Kim et al., 2021; Murphy & Zimmerman, 1993; Puffer & Weintrop, 1991; Salvi et al., 2024; Shen & Jr, 2002), capital structure (Staneva, 2024), shareholder wealth (Ting, 2013), risks (Srivastav et al., 2017), market reactions (Bae et al., 2023), and the board of directors (Farrell & Whidbee, 2000; Laux, 2008). Research has found that firm performance improves after CEO turnover due to institutional shareholding concentration, outsider-dominated boards, and externally appointed CEO (Huson et al., 2004). Additionally, CEO succession affects audit fees, which increase after the appointment of a new CEO (Bills et al., 2017; Brockman et al., 2022).

Following Chang and Wong (2009), I used an accounting performance measure to avoid noise trading in the Chinese stock market. I use CEO shareholding instead of chairperson shareholding in the following tests, because these variables have a strong and significant correlation (0.75). A set of control variables is employed, including firm age (years of incorporation), size (Total Assets), previous year performance, leverage (Total Assets/Total Debt), and product market competition (Herfindahl-Hirschman Index estimated using company sales by industry code), following previous studies (Cao & Chen, 2023; Chang & Wong, 2009; Cziraki & Groen-Xu, 2020; He & Fang, 2016). CEO age was omitted because it is strongly correlated with CEO tenure. I construct a variable by estimating the predicted CEO turnover (p_ceoturnover) using the generalized estimating equation (GEE) model to address potential endogeneity issues in ROA. This variable encompasses a set of explanatory variables in addition to the widely used performance-sensitivity measure of CEO tenure (Chang & Wong, 2009; Gao

et al., 2017). It consists of a new variation in the fitted residuals from the first-stage regression, which is constructed in a two-step regression model to examine the impact of CEO turnover (Qin & Yang, 2022).

First, using panel data, I run a fixed-effects model controlled for firm-level effects arising from the omitted variables. The firm-specific fixed effects are assumed to be uncorrelated between the firms. Table 6 presents the results. Predicted CEO turnover does not significantly affect ROA. Furthermore, none of the explanatory variables were significant. I further ran a random-effects model, followed by the Durbin-Wu-Hausman test. Similar results were also observed. The Hausman test shows a probability of <0.01, rejecting the null hypothesis that the coefficients between the two models are consistent and that the fixed-effects model is preferably more efficient. Significant differences are observed in the coefficients of the variables. In addition, note that the overall R^2 was negligible for both models, although it was significant at the 1% confidence level. The models could be affected by a long-period unbalanced dataset in which time-varying effects could change firm-specific characteristics. This can result in endogeneity between the explanatory variables and error terms, owing to omitted variables that may change over time.

Furthermore, I apply the system generalized method of moments (GMM) and difference-in-difference (DID) models. Following Ma (2022), I created an industry-averaged instrument. The average percentage of independent directors by industry was constructed as an instrumental variable in the GMM model. Independent directors can affect board functions and structures such as the total number of board committees and the design and setting of executive remuneration. However, individual firms are unlikely to affect the number of independent directors available in the selection pool of the director labor market in each industry. We find no correlation between

the instrumental variables and ROA. Table 6 shows consistency with previous models, except that the total number of board committees has a positive impact on ROA.

However, the DID model yields different results. Firm performance decreases after a CEO leaves the company. Board size is negatively related to ROA, while ultimate shareholding and SOE controlling shareholders have positive impacts on ROA. State blockholders are incentivized to discipline poorly performing CEOs to protect state assets and manage external pressure (Chang & Wong, 2009). CEO turnover and other executive and board variables do not affect ROA. This aligns with the findings of Cao et al. (2017), who found that firm performance does not improve after CEO turnover, which contradicts the mixed effects of CEOs' political connections, board connections, and the presence of blockholders. Post-CEO departure performance can also be related to inefficient capital expenditures in larger firms (Ullah, 2019). Furthermore, CEO duality and tenure have no effect on performance when the firm is making losses (Chang & Wong, 2009), which conflicts with Shen and Lin (2009), who find that duality is negatively related to turnover. These results strongly suggest that corporate governance has broad and complex functions and structures. Therefore, the interactions between different governance mechanisms have varying effects on firm outcomes in different institutional and corporate settings.

I run a robustness test with adjusted ROA following He and Fang (2016) but find insignificant results. Furthermore, I use the predicted probability of CEO turnover as well as lagged explanatory variables and find no significant results.

[Insert Table 6]

I run further robustness tests considering the regulatory reforms that have aimed to strengthen corporate governance, shareholder protection, and firm performance since 2001 using the DID model. Similar to many other countries, China has implemented important corporate governance guidelines and standards to promote and enhance management accountability and transparency. The following table shows key regulatory developments.

[Insert Table 7]

Accordingly, China has undergone major development since prescribing the Code of Corporate Governance of Listed Companies in 2001. This was followed by a series of amendments and guidelines to improve the roles of companies, especially State-Owned Enterprises, with a significant move to standardize company types and structures through the amendments of the Company Law in 2005. Therefore, I create a dummy variable, Post2005, to capture the effects of strengthened guidelines and regulations on firm performance. Furthermore, a key development in 2016 aimed to strengthen the use of equity, as incentive plans for executives are captured in another variable, Post2016.

Table 8 presents the results of this study. Consistent with previous results, firm performance declined in the period after CEO turnover in both models (Post). The predicted CEO turnover (p_ceoturnover) has a positive impact on firm performance but is not robust. The interaction between Post-and CEO turnover has a negative impact on firm performance, although the effects are insignificant. These results are inconsistent with Salvi et al. (2024), who found that new CEOs bring strategic changes and improvements to firm performance. The results show that CEO turnover may be due to correcting poor executive performance, but a change in top executive leadership may have a negative impact on performance in the short run before new CEOs grasp their role in improving performance. Importantly, regulatory reforms in corporate

governance and shareholder protection in 2001-2005 had a positive impact on firm performance. However, firm performance has decreased since 2016. The COVID-19 pandemic has a negative effect on firm performance but is inconsistent and significant across both models. Unlike the factors that influence CEO turnover, firm performance is negatively affected by board size; ultimate ownership has a positive effect, and individual controlling shareholders have a negative effect. Furthermore, the percentage of directors holding shares and executive salaries have positive effects on firm performance. This suggests that individual governance mechanisms and channels of influence by executives, directors, and shareholders, and their interplay dynamics, are used discretely to influence and achieve different objectives and goals. Among the control variables, only lagged performance has a significant negative effect on firm performance.

[Insert Table 8]

Discussion

Overall, the results highlight the important developments in corporate governance practices in China. Since various guidelines and regulations were enacted in the period 2001-2005, corporate governance mechanisms have been standardized across publicly listed firms. China has shown a governance structure and composition similar to international guidelines. The results show that firm performance has improved post-2005. Therefore, differences in the effects of these standard mechanisms in terms of structure are not expected to differ significantly between firms. What may cause differences in governance effects is most likely due to the composition, namely the interplay of individual principals and agents, which in turn make decisions about firm-specific organizational hierarchies and policy frameworks that affect corporate powerplay. This is further supported by robustness tests that show that amendments made to executive equity incentive plan measures in 2016 have no effect on firm performance, but managerial shareholding affects CEO turnover. Therefore, the effects of corporate governance are transmitted not directly through the structures put in place but via dynamic interplay in the composition of actors. CEO ownership and prestige dominate the structural power to influence CEO turnover, whereas other governance structural mechanisms play a role in monitoring performance. Therefore, endogeneity exists between governance structure and composition as well as their links with corporate ownership, which influences CEO turnover and performance.

The use of equity incentive plans in executive management is complex given the domination of blockholders and shareholder directors in China. The results show that CEO ownership power through managerial shareholding is robust in affecting CEO turnover, whereas executive salaries play a role. The literature has also shown that complex executive

compensation affects CEOs' willingness to leave based on market information and peer comparison and their likelihood of being dismissed based on their performance. This complexity is exacerbated by the presence of both blockholders and shareholders. When blockholders hold majority shares in a firm, CEOs who receive equity incentives wrestle with their contractual executive role and minority shareholder position to hinder potential expropriation by dominant shareholders. This creates conflicting objectives between principals and agents in the CEOs. The question that remains to be answered is whether CEOs act to fulfil their contractual role as top executives or exercise shareholder activism as minority shareholders against blockholders. Another perspective yet to be systematically investigated is whether these two conflicting objectives are aligned against potential majority shareholder expropriation.

According to guidelines and regulations, governance mechanisms are put in place to safeguard shareholder interests and improve firm performance. However, strategic corporate decisions are both broad and complex. For example, CEO turnover is a strategic decision that is important as part of board function, and the Remuneration Committee specifically sets up recruiting, selecting, compensating, monitoring, and managing top executive performance. On the other hand, CEO turnover is affected by other strategic decisions, such as corporate growth, capital structure, and executive management, which, in turn, are strongly monitored by the board of directors. In the presence of information asymmetry, different governance mechanisms are put in place to collect data to aid rational analysis and decision-making by the board. In terms of the structural power of CEOs and directors, CEO turnover is an outcome of the interaction between multiple governance mechanisms, and this combination is unique based on the reasons for CEO departure. For example, if a CEO is dismissed because of poor firm performance, the governance mechanisms used to reach this decision may include board size and the composition of expertise

and experience of directors to decipher multifarious strategic and financial information. This could, in turn, be affected by the balance between executive, non-executive, and independent directors' composition, their linkage with the CEO, and shareholding in the firm to endorse or deter the decision to penalize the CEO. If a CEO voluntarily leaves a firm, the governance mechanism that could affect this decision is likely to be associated with the effectiveness of the compensation design and mechanism, which could be driven by both directors and blockholders. Nevertheless, this discussion raised the importance of individual directors' expertise and experience, and how they complement each other on a board of directors across different strategic decisions. It takes more than one competent director on a board to execute the functions of governance mechanisms and their interplay to optimize strategic outcomes, highlighting the significance of dynamic play between executives and directors (Graham et al., 2020). Overall, this emphasizes the significant effect of power play between principals and actors through ownership, expertise, and prestige power, in addition to structural power that endogenously grants them composite power.

Conclusion

I use the longest panel data from to 2002-2022 to examine how CEO power affects CEO turnover in the presence of blockholders and modern governance mechanisms. The frameworks of Agency Cost Theory and Resource Dependency Theory are used to explain the interplay between powerful CEOs, directors, and shareholders through three main CEO power channels: structural, ownership, and prestige. I also consider institutional theory to incorporate the setting of Chinese corporate governance developments in guidelines and regulations. I address this gap in the literature, in which the interplay of the specific power between principals and actors in CEO turnover in the presence of dominating blockholders is understudied. I provide important

insights into the effectiveness of governance mechanisms, including board structure, CEOs' and directors' equity incentives, and their external networks, on CEO turnover and performance when dominant blockholders are present.

The results show that CEOs deter their turnover mainly through their ownership power and that CEO departure leads to poor firm performance in the post-turnover period. These results are robust and significant. Furthermore, the number of directors holding shares is negatively linked to the likelihood of CEO turnovers. CEO turnover is lower when ultimate shareholding is higher in SOE-shareholder-dominated firms. In terms of structural power, CEO turnover is negatively related to CEO-Chair duality, while board size, independence, and other characteristics have insignificant effects. However, the CEO-chair duality effect was not significantly robust. In terms of prestige power, CEOs' number of external directors is negatively and significantly related to turnover and the results are robust in the presence of other governance structures and ownership variables. However, the presence of SOE and individual blockholders and their ultimate shareholding percentage change the effects of some power measures and governance effectiveness on CEO turnover. Firm performance is affected by CEO shareholding and external directorships, implying that CEO ownership and prestige power dominate other channels.

Several key topics for future research are also discussed. First, the endogeneity between governance structure and composition and their link to corporate ownership structure affects key strategic decisions such as CEO turnover and firm performance. Furthermore, endogeneity exists among the power channels of CEOs, directors, and shareholders. Second, the setting of Chinese listed firms provides insight into the complexity of equity-based incentives in executive management in the presence of blockholders and shareholder directors. This highlights the

conflicting objectives of CEOs, as contractual and minority shareholders. Third, the diversity of governance mechanisms and their combined effectiveness should be considered when a board of directors makes different strategic decisions. In some cases, blockholders can play a role in the dynamics of governance mechanisms and alter their effects on strategic outcomes. Ultimately, it is important to consider the power play between principals and actors through endogenous channels.

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