Stock Prices Reaction on the Announcement of CEOs Change

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ABSTRACT

The prime objective of any firm is to maximize shareholders' wealth that is determined on the basis of stock price in stock market. Stock price reacts to macro and micro factors, especially publically available about a company's information. Investors perceive every information either positive or harmful to the firm's performance. Is stock price reacts to the announcement of CEOs change? Is yes, is the change is positive or negative or mixed trend. The study aimed to know the stock price reaction on the announcement of change of CEOs of the select five companies' stock during the study period 2019 to 2022. All the sample companies were listed on the BSE. Using simple random technique, the researcher selected five companies for the study. *Closing stock prices for 30 days before and after event date were obtained. It is found that there is a mixed reaction of stock price to the information about the change of CEO. The study helps equity investors for taking investment decisions.*

Key words: CEO, Announcement, Change, Stock Price, Return

INTRODUCTION

Equity share capital is the primary source for public limited companies, and it can be raised through the issue of shares in the new issue market through the Initial Public Offer (IPO). Equity stock is recorded in the company's books at par value, and share certificates are issued at par value. The main objective of any public limited company is the maximization of shareholder wealth. Shareholders' wealth is maximized only when the stock price at which it trades in the stock market is higher than the par value. However, from an investor's point of view, shareholder wealth is maximized only, when the stock is trading above the allotted price in the primary market or bought in the secondary market.

The issuer lists the shares on the stated stock exchange after allotment in the primary market. The stock price in the stock market is affected by various factors - micro-economic or macro-economic. The price of a stock primarily depends on demand and supply. The demand and supply of stock are affected by information about the company. In other words, investors' decisions to buy or sell a stock depend on publicly available information. For example, Government is withdrawing subsidy given to the electric two-wheelers buyers under 'Faster Adoption and Manufacturing' (FAME) III scheme. This news can affect stock prices of electric two wheelers companies. Whatever may be the information or news, stock price reacts, but its impact on return may be positive or negative.

A Chief Executive Officer (CEO) takes corporate level decisions. He acts as a central point between the Board of Directors (BODs) and the stakeholders. Success of a firm depends corporate level strategy.

Therefore, information of change of CEO affects stock performance. Equity investors want to know why a CEO stepped down. They are worried about a new CEO joining, whether the change is going to be good or bad for the bottom line. Good or bad, it is news, and news generally makes a stock price more volatile in the short-term and affects a company's market capitalisation. The higher the stock price, the more a company is worth in market value terms. To know the existing research on the topic, researchers reviewed published literature and the reviews are in order.

Review of literature

Existing research papers have been reviewed to find a research gap. The collected literature reviews helped the researchers in framing scope for the study. Mkrtchyan et al. (2023) examined the gradual, increase in participation of CEOs on social and political issues, which is known as CEO activism. Researcher aimed to know the impact of CEO's activism on a firm's value calculating a three-day abnormal return. CEO characteristics like age, tenure, and directorships were taken from BoardEx, which provides information on the CEO. Accounting information required for the study obtained from Compustat and stock return data from the Center for Research in Security Prices (CRSP). Three thousand six hundred thirty-five firm-year observations for 445 firms were the sample taken for the study. The sample was selected from the S&P 500 at any point between 2010 and 2019, excluding utilities and financials. The study suggests that investors' socio-political preferences were the main channel through which CEO activism affects equity demand and stock prices. Notably, CEOs are less likely to be fired when their activities generate positive market responses.

Jabbar (2021) aimed to examine the reaction of the market to the CEO changes using abnormal stock returns. One hundred two companies' stock trading on the Tehran Stock Exchange from 2011 to 2015 were considered for the study. The research was based on publicly available information. The results showed that stocks were underrated at the time of the change of CEO, and stock returns were less than expected. There was significant negative relationship between CEO change and abnormal stock returns.

Halff & Gregory (2020) studied the positive impact and financial gain enjoyed by stockholders due to the information leak about change of CEO. The study found that, increase in online search for the name of new CEO prior to announcement of information to the public through firm or media or blogger developer. Half of the sample companies' stock price reacted to the unexplained financial event. The study found that a lucky few investor might earn stock returns from non-publicly announced information, which is an illegal activity and not taken any action.

Akhgar & Zaheddoust (2019) analyzed the outcome of CEO tenure on the relationship between company performance and forced turnover. The study found that the performance-forced turnover relationship was conditional on CEO tenure. The findings indicate a continuous negative relationship between company performance and forced turnover during an inside CEO's tenure.

Andreou et al. (2017) studied how CEO age is associated with stock price crash. The sample comprises of 18,649 firm-year observations from different industries during 1995to 2013. It is noted that company with younger CEO is more likely can experience stock price crashes, including crashes caused by the disclosure of negative news in the form of breaks in consecutive earnings increases. It is because of the strong presence of young CEOs at the managerial level. Overall, the findings highlight the importance of CEO age for firm policies and outcomes.

Wells (2002) studied the extent of earnings before and after CEO change at select Australian firms. The sample consisted of 77 CEO changes reported by 53 companies from 1984 to 1994 at different times. It was found that there was no empirical evidence of an increase in income before and after the change of CEOs.

Lubatkin et al. (1989) analyzed the stockholder reactions to the CEO change in 477 large corporations that were earning with excess stock returns. Daily excess returns data for 300 trading days before and after the succession announcement was analyzed. The study found that investors were favourably inclined to successions in which outsiders are appointed to financially healthy firms.

Bonnier & Bruner (1989) analyzed the reaction of stock price to management change in distressed firms based on excess returns. Samples of 70 firms were chosen out of 87 management changes over the period. The sample companies were listed on the New York Stock Exchange from 1969 to 1983. The study found that excess returns were significantly positive.

Warner et al. (1988) studied the relationship between a company's stock performance and due to the change in management. It was found that there was an opposite relationship between the stock return and management changes.

Beatty & Zajac (1987) conducted a comprehensive study on CEO change and firm performance in large corporations: Succession and manager effect. The authors argue that the succession and performance relationship result from two factors: manager effects and succession effects. The study is based on 209 large companies. The study revealed that the announcement of a change of CEOs negatively affected the value of the companies since successor CEO decisions influence investment and production.

Research gap

From the review of existing studies, it is observed that many researchers conducted research on CEO changes, but they are not between 2019 to 2022 period, especially in India. The present study is an improvement over the earlier studies.

Statement of the problem

This research paper aims to analyze the impact of a change in CEO announcements on selected stock prices. Stock prices are going to be affected due to various reasons, like elections, changes of top-level employees, launching of new products, CEO changes, interest rates, inflation-deflation, demand-supply, merger and acquisition announcements, stock price appreciation, the image of the company, and different product types. We are considering studying the impact of changes in CEO announcements on selected stock prices. Will a change of CEO affect the stock price? If yes, what are the changes in stock price before and after one month? The purpose of the study is to find out the answers to these issues.

Objective

The study's objective is to know the impact of the announcement of a change in CEO on stock performance.

METHODOLOGY

The study is an event study. The present study is based on the daily closing stock price for 30 days before and 30 days after announcement of CEO changes of select companies obtained from the BSE (Bombay Stock Exchange). During the study period from 2019 to 2022, 43 companies had announced CEO change. All the sample companies were listed on the BSE. Using simple random technique, the researcher selected five companies for the study. The sample technique is used because all the 43 companies are similar in terms of announcement of CEO change and to avoid bias. The sample companies are Jubilant FoodWorks Ltd. (JFL); Godrej Properties Ltd. (GPL); YES Bank (YB); Wipro Ltd. (WL); and HDFC Bank (HDFC). The historical closing stock price is analyzed using daily returns.

The event window is the period within which reaction of stock prices to the announcement of CEO change is measured to estimate the short-term reaction to the stock market. The event window for the study is 61 days i.e., 30 days before and 30 days after announcement of CEO change. The event day is *To,* 30 days before event day are designated as T_{-30} *to* T_{-1} and 30 days after event day are designated as T_{+30} *to* T_{+1}. Event window for the select five companies is:

Name of the Company	Event Date	Event Window
Jubilant FoodWorks Ltd. (JFL)	11th March, 2022	27th January to 27th April, 2022
Godrej Properties Ltd. (GPL)	31st December, 2022	21st November, 2022 to 13th Feb., 2023
YES Bank (YB)	31st January, 2019	16th November, 2019 to 12th Feb., 2019
Wipro Ltd. (WL)	31st January, 2022	19th December to 19th March, 2020
HDFC Bank (HDFC)	26th October, 2020	11th September to 8th December 2020

RESULTS AND DISCUSSION

Impact of announcement of CEO change on stock price was studied using normal stock return. The daily stock return is calculated as follows:

$$\text{Daily Stock Return} = \frac{\text{Daily Closing Stock Price} - \text{Daily Opening Stock Price}}{\text{Daily Opening Stock Price}}$$

Table 1 Stock return for 1st day, 7th day, 15th day, and 30th day before and after CEO changes of select companies

Company	Announcement of Change of CEO	Stock Return (%)			
		Day 1	7 Days	15 Days	30 Days
Jubilant FoodWorks Ltd. (JFL)	Before	2.2451	-1.8296	-0.9575	-6.0326
	After	-12.2391	1.1425	2.6069	-2.5812
Godrej Properties Ltd. (GPL)	Before	0.6865	-2.1484	1.6710	-1.2716
	After	0.9512	-0.3780	-1.9199	-1.9028

YES Bank	Before	0.1929	4.0100	-0.3309	-7.2139
	After	0.2171	0.2414	0.1302	-0.3463
Wipro Ltd	Before	-2.4519	-0.5059	-0.7491	0.3625
	After	0.2534	0.1453	-0.6105	-3.6996
HDFC Bank	Before	0.2027	-3.4874	0.6685	-1.0912
	After	1.8333	0.7572	0.8022	0.2951

Source: Calculated with the use of the closing stock price of the sample companies

Jubilant FoodWorks Ltd.

Jubilant FoodWorks Ltd. (JFL) operates Domino's Pizza and Dunkin' restaurants in India. The CEO of JFL resigned as CEO and whole-time director on 11th March, 2022. He continued in his current role until 15th June, 2022. He joined as CEO in April 2017.

The Pratik R Pota, CEO of JFL stepped down on 11th March, 2022 (see Table 1). One day before CEO change, the stock return was positive (2.24 percent), but the stock incurred loss on 7, 15, and 30 days before the announcement of CEO change. After announcement of CEO change, on day one stock return recorded the highest loss at 12.24 percent indicating that the CEO change will harm the company. However, a positive return was recorded after announcement of CEO change on seven day and 15 days at 1.14 percent and 2.61 percent respectively. This indicates that the announcement of CEO change had a positive impact on the stock price of the company. The stock return was at its average level after 30 days of the announcement of the CEO, at -2.58 2.58 percent.

Godrej Properties Ltd.

Godrej Properties Ltd. (GPL), a subsidiary of Godrej Industries Ltd., is a real estate company. It constructs and develops residential, commercial, industrial, and township properties. The company's residential properties include The Trees, Godrej 101, Godrej 24, Godrej Central, Godrej Azure, and Godrej Aqua. Mohit Malhotra has resigned as the Managing Director (MD) and CEO of Godrej Properties, with effective 31st December, 2022. He worked for 12 years. Gaurav Pandey, CEO-North Zone, replaced Malhotra w.e.f. 1st January, 2023. The CEO of GPL stepped down on 31st December, 2022.

The stock returns of Godrej were recorded positively on the 1st day with 0.68 percent and on the 15th day with 1.67 percent (see Table 1). Seven and 30 days before the announcement of the CEO change; it was negative 2.1484 percent and 1.2716 percent respectively. Stock return was improved immediately (day one) after the announcement of CEO change by 0.2647 percent. However, after seven days, 15 days, and 30 days, the stock return recorded negative values of - 0.3780, -1.9199, and -1.9028, respectively. It indicates that the announcement of CEO change harmed the share price of the company.

YES Bank

Rana Kapoor stepped down as CEO on 31st January, 2019, after the bank's founder completed his truncated term, the lender said in a statement. The RBI denied Kapoor an extension to his term twice last year without a reason and asked Yes Bank to find a new CEO by 1st February.

YES Bank's stock return one day before the announcement of a new CEO was 0.1929 percent (see Table 1). After announcing the CEO change, the stock return increased from 0.1929 percent (a day before the announcement) to 0.2414 percent on seventh day after the announcement. Later, the stock return showed a declining trend and recorded loss (-0.3463 percent) by the end of 30 days after the announcement of the new CEO. This indicates that the announcement CEO change had a positive impact on the share price of YES bank and moved towards normal.

Wipro Ltd.

Wipro is a leading technology services and consulting firm dedicated developing innovative solutions for various issues of clients. Wipro Ltd. CEO and MD Abidali Z. Neemuchwala stepped down on 31st January, 2020, due to family commitments. He was working since April 2015 and was appointed as CEO on 1st February, 2016. He built a strong execution mindset, drove vital acquisitions, and scaled digital businesses globally.

From Table 1, we can observe that Wipro's stock was incurring losses 15 days before the announcement of CEO change. Thirty days before announcement of CEO change, stock performance was positive (0.3625 percent). In other words, stock returns slowly moved from positive to negative, recording -2.4519 percent just one day before the announcement of the change of CEO. However, immediately after the announcement of the change of CEO, the stock performance turned positive (0.2534 percent) from negative, but 15 days after the announcement of the change of CEO, it again went towards loss and recorded -0.6105 percent and -3.6996 percent at the end of 15 days and 30 days after the announcement of the change of CEO. This indicates that the announcement of CEO change had a positive impact immediately but again back to normal 30 days later.

HDFC Bank

Aditya Puri retired as Managing Director and founder CEO on 26th October, 2020. Twenty-six years ago, Puri stepped down as the head of Citibank Malaysia to take charge of a banking start-up in Mumbai, HDFC Bank. Under his leadership, HDFC Bank became the highest-valued financial institution in India and the 10th most valuable bank in the world. He retired after the Reserve Bank of India (RBI) approved Aashidhar Jagadishan as MD and CEO.

Thirty days before the announcement of the retirement of Aditya Puri as MD and CEO, stock performance fluctuated between the lowest -3.4874 percent 7 days and 0.6685 percent on 15 days (see Table 1). After announcement of CEO change, stock return was high on Day one (1.833 percent) and later showed a declining trend and reached 0.2951 percent by the end of 30 days, indicating that it affected stock performance.

Average Stock Return

The 30-day average stock returns before and after the announcement of the change of CEO is given in Table 2.

Table 2 Average return before and after announcement of ceo change

Companies	Announcement of change of CEO	
	Before	After
Jubilant FoodWorks Ltd.	-0.7040	-0.1895
Godrej Properties Ltd.	-0.1163	-0.0995
Yes Bank	-0.3236	-0.1692
Wipro Ltd.	-0.0973	-1.0076
HDFC Bank	0.4329	0.4448

Source: Compiled Data based on the closing stock price.

The average stock return 30 days before the announcement of the change of CEO was recorded as unfavorable at all sample companies except HDFC Bank (0.4329 percent). Before announcement of CEO change, the highest loss was at Jubilant FoodWorks Ltd. (-0.7040 percent) and the lowest loss was at Wipro Ltd. with -0.0973 percent. The performance of the stock was similar to the performance before the announcement of CEO change. HDFC Bank recorded a positive average stock return of 0.4448 percent, and all four other companies incurred losses. After announcement of CEO change, the highest loss was at Wipro Ltd., with -1.0076 percent and the lowest loss can be seen at Godrej Properties Ltd., with -0.0995 percent.

Implications of the research

The study provided the reaction of stock prices of select five companies to the announcement of CEOs change. The study calculated stock return based on the closing stock price during the event window. Companies shall handle CEO change with care, and it should not harm stock prices. This can affect market capitalisation of company. The study helps investors to predict the stock price based on the information about CEO change and take appropriate investment decisions and minimize loss. It helps policy makers to take measures in announcement of CEOs change at appropriate time without affecting stock price.

Conclusion

The impact of the change in CEOs of select companies showed mixed results. The change of CEO at Jubilant FoodWorks harmed day one, but turned positive in the next 15 days and reached an average level after 30 days of the announcement. The stock return of Godrej Properties reached a positive level on day one, and the next 29 days, the stock return was recorded as loss. YES Bank's stock return was recorded positively by the change of CEO. The first 15 days and 30 days incurred losses. Wipro's stock recorded highest return after the announcement of change of CEO and later showed a declining trend, reaching its highest loss by 30 days after the announcement of the change of CEO. HDFC's stock performance was affected by the CEO change immediately on day one and later showed a declining trend and reached 0.2951 percent which is the lowest.

Stock performance 30 days before the announcement of the CEOs change were similar in all the sample companies, with a positive return just before one day (except Wipro), and a 7, 15, and 30 day return was negative for all companies except YES Bank. The announcement of a change of CEO affected all the companies' stock performance negatively. All companies recorded losses except HDFC Bank. HDFC Bank also incurred losses when compared to the 15-day stock return. Therefore, we conclude that the announcement of a change of CEOs at select companies affected negatively and incurred losses, keeping all other factors affecting stock performance the same.

Why is there a mixed reaction of stock prices to the announcement of CEOs change? There is scope for further research with the collection of equity investors' opinion on the reaction of stock prices to the announcement of CEO change.

Conflict of interests

At this movement, now, we hereby declare that there are no competing interests that exist.

Author's contributions

We both contributed equally to the theoretical development, analysis, interpretation and writing of the manuscript.

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