Discussion of “Top management team power in China: Measurement and an application”
By Bin Ke, Xinshu Mao, Bin Wang, Luo Zuo

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Xia Chen (Singapore Management University)
Summary and key findings

• Develop a measure of top management team (TMT) power
  • Order of TMT members in the annual report

• Validation of this measure
  • Correlated with proxies for structural power, ownership power, expert power, and prestige power (Finkelstein 1992)
  • Correlated with proxies for political power, seniority power, and gender power
  • Hold for SOE and non-SOE sample
  • Hold for both TMT board members and TMT non-board members
  • Hold for TMT members other than CEO and chairman
Proxies for the dimensions of power

• Structural power: executive director or not (EXEC_DIR), relative total cash compensation (COMP), number of titles (NUM_TITLES)
• Ownership power: share ownership (SHARE_OWN), founder or not (FOUNDER), controlling shareholder or not (CONTROLLER)
• Expert power: match between professional qualification and functional area (SKILL_MATCH), number of function area (NUM_FUNCTIONS), number of previous senior executive positions (NUM_POSITIONS)
• Prestige power: number of director positions (NUM_DIR), number of board seats in not-for-profit organizations (NUM_NONPROFIT), education (EDU)
• Political power: political connection (PC), position in parent company (PARENT_POS)
• Seniority power: age (AGE), tenure with the current firm (TENURE)
• Gender power: male or female (MALE)
Summary and key findings (cont’d)

• Application of this measure
  • CFO power and write-off of long-lived assets
  • Argument:
    • CFOs with greater power help their firms make more efficient investment decisions
    • CFOs with greater power are less likely to write off *bad* investments
  • Prediction and finding:
    • Firms whose CFOs have greater (relative) power are less likely to write off long-lived assets

• Comparison of this measure with compensation rank
  • Compensation rank is less correlated with the proxies for different dimensions of power
Contribution

• The TMT power measure is a very clever and concise measure
• It can potentially be used to test many different theories related to executive power

• This measure is specific to China context, due to culture and disclosure requirement
  • Still very useful
  • Can be used to test stories applicable in different settings, as well as stories unique to China context
Limitation of the measure

- This measure is not a measure of power distribution within TMT:
  - It is a ranking (from CEO/Chairman down to less powerful executives)
  - It cannot be used to capture CEO’s power relative to other executives
  - Its main use is the relative ranking of executives (other than CEO/chairman) within TMT (for example, is CFO ranked before or after CIO, is one division head ranked before or after another division head, etc.)
    - However, for example, even if a CFO is ranked before most of other executives, is the CFO powerful?
    - We don’t know CFO’s power relative to CEO; we don’t know the distribution of power among executives – is CFO a lot more powerful or somewhat more powerful than other executives?
Limitation of the measure (cont’d)

• The association between this measure and political power (PC, PARENT_POS), seniority power (Age, Tenure) and gender power (Male) may be mechanical
  • For example, executives with political connections, who are from parent company, who are older, and who have longer tenure, will be listed ahead of others
  • But it can be social norm; it does not necessarily mean a bigger role in firm decisions.
Limitation of the measure (cont’d)

• This measure may be driven by a few key determinants
  • For example, Table 6, Panel A (TMT members other than the CEO and chairman) (this may be the appropriate main table because CEO and chairman are likely always ranked first)
  • The factors with the highest t-statistics in column (1) (Full sample):
    • Exec_DIR (t=66.3), Comp (t=30.3), Age (t=19.2), Tenure (t=13.4), Number of previous executive positions (t=12.2)
    • These variables are also highly significant in other tables
  • So, does this measure mainly capture director position, compensation, and experience?
Comparison of the TMT power measure with compensation rank

• First, this may not be a fair comparison, because compensation in China may be subject to certain constraints (culture, political positions, etc.)

• Nonetheless, to me, the comparison test seems to suggest that the two measures (POWER, COMP_POWER) are quite similar
Comparison of the TMT power measure with compensation rank (cont’d)

- Table 8, Panel A, Column (1) POWER, Column (3) COMP_POWER, t-statistics

<table>
<thead>
<tr>
<th></th>
<th>POWER</th>
<th>COMP_POWER</th>
<th>Correlation Note</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Structural power</strong></td>
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<tr>
<td>EXEC_DIR</td>
<td>120.5</td>
<td>21.3</td>
<td>More correlated with TMT power</td>
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<tr>
<td>NUM_TITLES</td>
<td>-16.3</td>
<td>9.7</td>
<td>More pos. correlated with Comp power</td>
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<tr>
<td><strong>Ownership power</strong></td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>SHARE_OWN</td>
<td>7.2</td>
<td>11.0</td>
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<tr>
<td>FOUNDER</td>
<td>2.4</td>
<td>-0.4</td>
<td>Not correlated with Comp power</td>
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<tr>
<td>CONTROLLER</td>
<td>20.2</td>
<td>10.3</td>
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<td><strong>Expert power</strong></td>
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<tr>
<td>SKILL_MATCH</td>
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<td>4.6</td>
<td>Not correlated with TMT power</td>
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<tr>
<td>NUM_FUNCTIONS</td>
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<td>-6.4</td>
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<tr>
<td>NUMPOSITIONS</td>
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<td>11.7</td>
<td></td>
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</table>
Comparison of the TMT power measure with compensation rank (cont’d)

- Table 8, Panel A, Column (1) POWER, Column (3) COMP_POWER, t-statistics

<table>
<thead>
<tr>
<th></th>
<th>POWER</th>
<th>COMP_POWER</th>
<th>Notes</th>
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<tbody>
<tr>
<td>Prestige power</td>
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<tr>
<td>NUM_DIR</td>
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<tr>
<td>NUM_NONPROFIT</td>
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<td>-0.6</td>
<td>Not correlated with Comp Power</td>
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<td>EDU</td>
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<td>5.8</td>
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<tr>
<td>Political power</td>
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<tr>
<td>PC</td>
<td>19.0</td>
<td>-20.2</td>
<td>Not pos. correlated with Comp Power</td>
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<tr>
<td>PARENT_POS</td>
<td>6.5</td>
<td>0.4</td>
<td>Not correlated with Comp Power</td>
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<td>Seniority power</td>
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<td>AGE</td>
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<td>TENURE</td>
<td>16.2</td>
<td>19.6</td>
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<td>Gender power</td>
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<tr>
<td>MALE</td>
<td>12.3</td>
<td>11.8</td>
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Comparison of the TMT power measure with compensation rank (cont’d)

• The comparison seems to suggest that the key differences are:
  • Compensation is not correlated with being founder or not
  • Compensation is not correlated with political connection
  • TMT Rank is more correlated with being director or not (directors are always ranked before non-directors)
  • All these findings are intuitive

• I am not sure about the comparison of Adj. R-squared when firm, year fixed effects are included

• Compensation, after all, still seems to be a pretty good measure of power
  • Or compensation, in combination with founder, director status, political connection
  • Especially in contexts where TMT rank is not available
  • Relative advantage: compensation can be used to measure CEO’s power relative to other executives, can be used to measure power distribution among executives
Application: CFO power and long-lived asset Impairment

• Arguments:
  • CFOs with greater power help their firms make more efficient investment decisions?
    • Not necessarily the case; can be tested
  • CFOs with greater power are less likely to write off *bad* investments?
    • Not necessarily the case
    • CFOs with less power may be less likely to write off bad investments, if there is pressure from CEO and other executives to not write off *bad* investments

• It may not be a power story
  • For example, firms whose CFO are ranked higher among the executives: CFOs may play a greater role in strategy, investments, hence less likely to admit past mistakes
To conclude

• The TMT power measure is innovative and useful

• Apart from power, this measure may capture firm strategy, internal organization, etc.

• The authors can explore more applications of this measure
  • For example, firm performance, investment efficiency, different divisions’ performance and investment efficiency