

Discussion of “Top management team  
power in China: Measurement and an  
application”

By Bin Ke, Xinshu Mao, Bin Wang, Luo Zuo

ABFER 2019

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 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

	POWER	COMP_POWER	
Structural power			
EXEC_DIR	120.5	21.3	More correlated with TMT power
NUM_TITLES	-16.3	9.7	More pos. correlated with Comp power
Ownership power			
SHARE_OWN	7.2	11.0	
FOUNDER	2.4	-0.4	Not correlated with Comp power
CONTROLLER	20.2	10.3	
Expert power			
SKILL_MATCH	0	4.6	Not correlated with TMT power
NUM_FUNCTIONS	-6.0	-6.4	
NUM_POSITIONS	30.7	11.7	

# Comparison of the TMT power measure with compensation rank (cont'd)

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

	POWER	COMP_POWER	
Prestige power			
NUM_DIR	11.8	7.4	
NUM_NONPROFIT	6.3	-0.6	Not correlated with Comp Power
EDU	6.8	5.8	
Political power			
PC	19.0	-20.2	Not pos. correlated with Comp Power
PARENT_POS	6.5	0.4	Not correlated with Comp Power
Seniority power			
AGE	24.3	13.5	
TENURE	16.2	19.6	
Gender power			
MALE	12.3	11.8	

# 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