Does CEO power matter for the performance of retrenchment strategy?

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Abstract

Purpose – This research aims to examine the moderating role of CEO power on the relationship between retrenchment strategy and firm performance by framing the relationship under an agency theory, and power circulation theory.

Design/methodology/approach – This study focuses on a sample of 319 non-financial public listed companies in Malaysia from the year 2011–2016 and estimates the model under two-step GMM panel regression to eliminate the endogeneity issue.

Findings – The results show that the retrenchment strategy increased firm performance. Meanwhile, greater CEO power changes that retrenchment effect into increased performance. This study also indicates the CEO power strengthens the relationship between firm performance and retrenchment. However, CEO power does not have any effect on the performance of low retrenchment, and the performance of big firm size.

Research limitations/implications – The findings show that the higher CEO power cause higher firm performance and higher retrenchment. This research suggests that CEO power can make retrenchment strategy works and the decision made can affect the firm performance significantly.

Originality/value – This study examines the effect of CEO power on the performance of retrenchment strategy implementation by contesting agency theory, power circulation theory, and resource-based view theory within the emerging country context.

Keywords Firm performance, CEO power, Power circulation theory, Retrenchment strategy

Paper type Research paper

1. Introduction

There is no consensus in the strategic management literature regarding whether the implementation of retrenchment strategies enhance or diminish performance. From the perspective of the resource-based view, a retrenchment strategy is a strategic move of the organization for performance enhancement (i.e., Abebe, 2009; Goesaert *et al.*, 2015; Barbero *et al.*, 2017). Conversely, the proponents of agency theory argue that retrenchment strategy will reduce firm performance due to agency cost (Barbero *et al.*, 2020; Casillas *et al.*, 2019).

Haynes and Hillman (2010) have argued that CEO power may moderate the performance of strategy implementation, especially if the CEO is powerful vis-à-vis the board. A powerful CEO threatens the independent judgment of the board (Dalton and Kesner, 1987), and her/his preferences ignore the role of other board members (Boyd, 1994). By doing so, strategy

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