Ceo tenure a definite determinant of company performance

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In an article published by Harvard Business Review, they studied 356 U.S. companies from 2000 to 2010. They measured CEO tenure and calculated the strength of the firm-employee relationship each year by assessing things like retirement benefits and layoffs. The strength of the firm-customer relationship was also assessed by evaluating things like product quality and safety. The study also measured the magnitude and volatility of stock returns. This research led them to conclude that for a CEO to be very effective their optimal tenure length should be 4.8 years.

In a typical corporate setting, a CEO is analogous to the captain of a ship with the ultimate authority vested in him by the board of directors of the firm. By virtue of being in the role of a trustee, a CEO would be expected to make wise decisions that benefit the firm in the long or short term. Executive tenure is calculated by the number of years a CEO spends in office in that capacity of a CEO. However, the length of the tenure varies to a great degree from firm to firm.

The norm is usually that a CEO takes office, begins gaining knowledge and experience, and is soon launching initiatives that boost the bottom line. Fast-forward a decade, and the same executive is risk-averse and slow to adapt to change—and the company's performance is on the decline. New research examines the causes of this cycle. It has been discovered that CEO tenure affects performance through its impact on two groups of stakeholders—employees and customers—and has different effects on each. The longer a CEO serves, the more the firm-employee dynamic improves. However, an extended-term strengthens customer ties only for a time, after which the relationship weakens and the company's performance diminishes, no matter how united and committed the workforce is.

The underlying reasons for the pattern are believed to do with how CEOs learn. Prior research has shown that different learning styles prevail at different stages of the CEO life cycle. Early on, when new executives are getting up to speed, they seek information in diverse ways, turning to both external and internal company sources. This deepens their relationships with customers and employees alike. Nonetheless, as CEOs accumulate knowledge and become entrenched, they rely more on their internal networks for information, growing less accustomed to market conditions. Due to CEOs having more invested in the firm, they favor avoiding losses over pursuing gains. Their attachment to the status quo makes them less responsive to vacillating consumer preferences.

These findings have several implications for organizations. Boards should be watchful for changes in the firm-customer relationship. They should be aware that long-tenured CEOs may be skilled at employee relations but less adept at responding to the marketplace; these leaders may be great motivators but weak strategists, unifying workers around a failing course of action, for example. Finally, boards should structure incentive plans to draw heavily on consumer and market metrics in the late stages of their top executives' terms. This will motivate CEOs to maintain strong customer relationships and to continue gathering vital market information firsthand.

The CEO's term can also serve as a market signal for investors, with high tenure indicating the high credibility of the CEO certification. Based on agency theory, CEO tenure provides managerial incentives to maximize corporate value. It is possible that long tenure can help the CEO develop a high reputation, leading to greater commitment to the company. However, the CEO who stays on his job for a very long time may be too secure in their work. Van Ness et al. (2010) in the study in America found that the average term of office of the board members has a positive and significant impact on the company performance. Therefore, in conclusion, it is important that CEOs stay long enough that their impact on the company's performance can be noted and they should not be evaluated on the company's performance after having left the company.

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