CEO DUALITY AND FINANCIAL PERFORMANCE DURING COVID-19

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Abstract

This study aims to investigate the impact of CEO Duality on financial performance by examining manufacturing companies listed on the Indonesia Stock Exchange from 2018 to 2021. With a sample size of 844 companies selected based on specific criteria, data were collected from annual reports and audited financial statements. Utilizing multiple linear regression for analysis, the research findings suggest that CEO Duality does not significantly affect financial performance, both pre- and during the Covid-19 pandemic. However, its presence raises concerns about the independence of a company's board of directors, potentially influencing financial outcomes. The study concludes that CEOs and boards of commissioners demonstrate an understanding of their roles in achieving the company's objectives.

Keywords: CEO Duality, Covid-19, Financial performance

INTRODUCTION

The aim of a company's operations is to optimize the welfare of shareholders or investors through dividend decisions and policies, also known as efforts to maximize company value (Handriani & Robiyanto, 2018). The corporate board plays a crucial role in producing reliable financial information (Setyawan & Devie, 2017). Financial reports provide an overview reflecting the true state of a company and offer vital information about its financial performance to internal and external stakeholders.

Financial performance is a significant concern for investors, shareholders, and stakeholders, as it indicates the effectiveness and efficiency of utilizing assets and capital to generate income and profits over specific periods (Wahlen et al., 2014). Almajali et al. (2012) argue that various financial performance measures exist, such as profit margin, return on assets (ROA), and return on equity (ROE). Financial performance measures, including accounting/financial data (e.g., one-year profit impact, ROI, ROE, etc.), reflect a company's past performance (Aktan & Bulut, 2008).

Financial performance also assesses a company's overall financial condition over a specific period, enabling optimal resource utilization, maximizing service potential to customers, timely payments to employees, creditors, and vendors, and maintaining good credit risk (Adongo & Jagongo, 2013).

Financial ratios serve as crucial tools for measuring financial performance and company financial assets. Return on Assets (ROA) is an accounting-based financial performance ratio widely used by market analysts to assess a company's financial performance as it measures asset efficiency in generating income (Cohen et al., 1997).

In achieving good financial performance, management plays a crucial role in a company. Management's ability to efficiently manage resources, select appropriate strategies, reflects in the company's performance. In this regard, the board of directors plays a vital role in ensuring good governance systems, as they are involved in strategic and operational decision-making with long-term consequences and have responsibilities for all organizational events (Silingiene et al., 2015).

The board of directors is required to oversee the company's financial performance and ensure efficient and effective operations. Generally, they play a critical role in a company's success or failure. Boards need to swiftly transition from traditional company goals (market share, revenue growth) to company sustainability goals. The managerial abilities of board members are crucial during crises, as leaders need to make rapid decisions amid economic uncertainty and adapt to new work environments, online revenue streams, and alternative production processes.

The corporate board consists of the board of directors (Chief Executive Officer) and the board of commissioners (Chairman of the Board). CEO Duality refers to the practice where a single individual serves as both the board of directors (Chief Executive Officer) and the board of commissioners (Chairman of the Board) (Krause et al., 2014). According to Firdiansjah et al. (2020), based on Agency theory and Stewardship theory, one reason why CEO Duality is an intriguing topic for research is because there are two different arguments that underlie the cost-benefit relationship between the CEO and the board of commissioners. The first argument suggests that investors typically focus only on the profit information from financial performance without considering the procedural profits to be gained. Whereas the other argument states that CEO Duality creates a balance of interests where the board of commissioners collectively holds responsibility for the company's performance to maintain the company's image (Hashim & Devi, 2008).

Stewardship theory suggests that companies may be better off if the CEO also serves as a board of commissioners, as this approach contributes to maximizing joint performance, while Agency theory focuses on minimizing agency owner costs (Erikson et al., 2022). Duality reflects weaker oversight by the board of commissioners and stronger governance by the board of directors, while non-duality reflects a higher board of commissioners and weaker board of directors' power (Finkelstein, 1992).

Based on Law No. 40 of 2007, companies in Indonesia are required to follow the applicable regulations, namely the two-tier board or the separation of duties and roles between the board of directors and the board of commissioners. This regulation makes it impossible for companies to hold dual positions on the board of directors and the board of commissioners. In practice, in Indonesia, many companies still use a kinship system to fill these positions, where the positions are filled by two individuals who have a kinship relationship (spouses, parents, siblings, children, in-laws, grandchildren, nephews, etc.). Thus, in Indonesia, CEO Duality can be defined as the use of a kinship relationship system in the appointment of positions for the board of directors and the board of commissioners. In this situation, both positions are held by two individuals with a kinship relationship (Firdiansjah et al., 2020).

Several studies have indicated that CEO duality may reduce effectiveness in monitoring managerial decisions and actions, allowing CEOs to make decisions that increase their wealth rather than the company's performance. The separation of positions between the board of directors and the board of commissioners fails to provide oversight and control if kinship relationships are found in both positions (Lam & Shu Kam Lee, 2008).

Having a CEO associated with the chairman of the board may raise concerns about nepotism and favoritism within the company. This can lead to moral problems and low employee engagement levels, which can ultimately affect company performance. There are several potential reasons why a CEO associated with the chairman of the board may influence a company's financial performance. One reason is that this arrangement may create conflicts of interest. For example, the CEO may be more inclined to make decisions that benefit the chairman, rather than the company as a whole. This can result in the company making poor strategic decisions or taking unnecessary risks.

Previous research has found that CEOs with higher managerial capabilities have significantly higher cash surpluses, indicating better performance during the Covid-19 crisis (Kumar & Zbib, 2022). CEOs who also serve as chairman of the board may make faster decisions than other CEOs during the early months of the pandemic, giving them a competitive advantage (Hassan et al., 2022). In another study, companies with CEO duality experienced an increase in ROA of 0.011%, while comparable companies experienced a decrease in ROA of -0.086% (Hassan et al., 2022).

It has been widely discussed that the Covid-19 pandemic has caused a significant surge in uncertainty and widespread impacts on transportation, population mobility, healthcare, and the economy (Zhang et al., 2022). Since the "Great Depression" in the last century, the world has never faced a disaster like the Covid-19 case. Along with detrimental physiological and psychological effects, Covid-19 has shut down socio-economic trade. The first Covid-19 case was confirmed in the city of Wuhan, China, on December 31, 2019 (WHO, 2020). The global spread of the disease was confirmed and declared a pandemic on March 11, 2020 (WHO, 2020). In Indonesia, the first case was confirmed on March 2, 2020, and the first death was confirmed on March 11, 2020 (Ministry of Health, 2020).

In Sun & Li's (2021) study, evidence of poor financial performance due to the Covid-19 pandemic was found. In their research, the pandemic played a significant negative role in financial constraints, as evidenced by a drastic decline in sales growth in the first quarter of 2020 followed by a small impact on ROA, ROE, and ATO, each at 0.3, 0.08, and 5.2%.

According to Bose et al. (2022), companies operating in countries with more severe Covid-19 cases have experienced a decrease in company value, with a negative relationship between the impact of Covid-19 and company value. Looking at the increased market volatility in the US, with the standard deviation rate in March almost four times higher than in February, consistent with the increase in confirmed Covid-19 cases. This clearly demonstrates that the pandemic has created significant risks and uncertainties in the global financial markets. Return on assets (ROA) of companies is negatively related to the severity of the Covid-19 pandemic in early regression, measured by cumulative cases or new cases

(Hu & Zhang, 2021). Company revenue affected by the Covid-19 pandemic generally experienced a decline. Activity restrictions reduce consumer demand for goods and services, leading to a decrease in company revenue.

Different findings regarding the effects of governance mechanisms before and during the Covid-19 pandemic highlight the need for a more effective corporate governance framework. For example, results indicate that during the pandemic, effective decision-making processes require a smaller board or separation of the relationship between the board of directors and the board of commissioners. This study will cover two phases: before the first Covid-19 case was identified in 2018 and 2019 and during the Covid-19 outbreak in 2020 and 2021.

This research uses a quantitative approach by observing manufacturing companies listed on the Indonesia Stock Exchange from 2018 to 2021 according to criteria that support the research. The selection of the years 2018-2021 is because the researcher wants to determine the influence that occurs between before the Covid-19 pandemic arrives in Indonesia and during the pandemic on CEO Duality in company performance. For the selection of manufacturing companies, it is because, according to the Family Survey Business results (PwC, 2014), about 95% of companies in Indonesia are family-owned. Then, for the sector distribution in Indonesian companies, 50% come from companies in the manufacturing sector.

The writing of this research is expected to be beneficial and contribute to the development of theories and knowledge in the accounting world and serve as a source of information and reference for further research on the influence of CEO Duality on financial performance.

LITERATURE REVIEW AND HYPOTHESIS

Agency Theory

Agency theory supports the separation of functions between the board of directors and the board of commissioners because it believes that CEO duality can reduce the control function of the board of directors as executive managers, thus having a negative impact on company performance. Agency theory requires that in the event of ownership and regulation, the board of commissioners does not have significant interests in the company, and ultimately, they will prioritize their own interests and do something that could harm the company's welfare (Deegan & Blomquist, 2006). An independent board of commissioners from the board of directors can manage conflicts of interest to protect the interests of shareholders.

Agency theory opposes CEO duality, considering that the concentration of power is likely to be abused. Agency theory argues that managers cannot be trusted and therefore must be monitored and controlled by an independent board. (Erikson et al., 2022).

Stewardship Theory

Stewardship theory supports the existence of CEO duality by stating the positive effects of combining the CEO's roles on the company's sustainability to improve. (Mubeen et al., 2021). This theory suggests that managers act in the best interests of the organization; therefore, they are reliable and trustworthy. In this perspective, trust itself is the basis for effective functioning, not only for managers but also between the board of commissioners and the board of directors (Erikson et al., 2022). Some studies also state that combining the roles of the board of directors and the board of commissioners in one company allows for improved coordination processes, decision-making support, adaptability, and effective communication with external parties. (Goergen & Limbach, n.d.).

Stewardship theory can enhance a company's business productivity by maximizing shareholder interests. The role of CEO duality can enhance communication, management arrangement flexibility, and protect company interests through better business organization. (Mubeen et al., 2021). An important assumption in this theory is that managerial behavior, or in this case, board of directors, aligns with the interests of shareholders or the board of commissioners.

CEO Duality

CEO Duality can be defined as a practice where an individual holds two roles simultaneously as CEO (Board of Directors) and chairman of the board (board of commissioners) in a company (Cabral Lima da Costa & Silva Martins, 2019). The board of commissioners is tasked with monitoring managers, in this case, the CEO on behalf of shareholders. They design compensation contracts to hire and fire the CEO (board of directors). Meanwhile, the board of directors plays a role in formulating strategic recommendations to the board of commissioners and ensuring that these strategies are accepted and reflected in the business. With CEO duality, this benefits the company if they cooperate with the board of commissioners to create value (Mca, 2016).

CEO Duality can lead to a focus of power where the board of directors can control the board of commissioners and also weaken the efficiency of the board of commissioners in monitoring and controlling management (Fama & Jensen, 1983). Besides the formal power gained from CEO duality, combining positions in the company as a board of commissioners will allow that individual to significantly influence the board in managing information flow during board meetings and anticipate the process of appointing new directors (Dayton, 1984).

Financial Performance

Companies naturally have a goal to optimize the welfare of their shareholders. By improving company performance, the welfare of shareholders will be achieved. To enhance company performance, the field of strategic management must gather knowledge about theories that can help explain organizational performance and determine how managers can adjust strategies to improve company performance (Combs et al., 2004). The results of performance achievement measurements can serve as the foundation for company management or managers to improve their performance in the next period and can be used as a basis for reward and punishment.

CEO Duality on Financial Performance Before the Covid-19 Pandemic

Researchers debate the relationship between CEO duality and company performance enhancement. Two theoretical perspectives, namely agency theory and stewardship theory, are present. Agency theory argues that when the board of directors has a relationship with the board of commissioners, the oversight and control of the board of commissioners will weaken, and the interests of shareholders will be sacrificed for executive management, potentially leading to managerial opportunism such as higher executive compensation.

In theory, the board of directors exists to protect the interests of the company's shareholders and oversee managerial actions on behalf of shareholders by setting strategic policies and objectives. This protection occurs if the board of commissioners is independent of the board of directors.

According to Setyawan & Devie's research (2017), there is a negative relationship between CEO duality and financial performance. This can be interpreted as the discovery of a kinship relationship between the board of commissioners and the board of directors, which can further deteriorate financial performance. According to Mubeen et al. (2021), CEO duality has a negative influence on company performance, measured by ROI and ROE. Some results indicate that this can lead to a lack of independent oversight of CEO actions and decision-making, which can negatively impact company performance.

Most studies in the literature provide evidence that CEO duality has a negative impact on company performance, ultimately supporting agency theory.

H1 : CEO Duality has a negative effect on Financial Performance before the COVID-19 pandemic.

CEO Duality on Financial Performance During the COVID-19 Pandemic

From Hassan et al.'s research (2022), the shock of Covid-19 will demonstrate how CEO duality enables companies to respond more effectively during a crisis period. They will find it easier to coordinate or change corporate policy strategies with less pushback from the board of commissioners because in this case, the board of commissioners will be more inclined to support what the CEO sets. The research findings also indicate that CEO duality benefits companies with high information costs during the coronavirus outbreak. Companies with CEOs who have strong relationships with the board of commissioners appear to be more effective in managing the coronavirus outbreak because CEOs will be quicker in decision-making, even after controlling other corporate governance measures. This study supports the stewardship theory, which suggests that CEO duality has a positive effect on company performance because managers can essentially be trusted and are good for company resources (Mca, 2016). Based on previous research, there is a positive influence of CEO duality on Financial Performance during the Covid-19 pandemic; therefore, the hypothesis to be proposed in this study is:

H2 : CEO Duality has a positive effect on Financial Performance during the COVID-19 pandemic

RESEARCH METHOD

The data used in this study is quantitative, and it utilizes secondary data sourced from the financial reports and annual reports of manufacturing companies listed on the Indonesia Stock Exchange (IDX) during the period 2018-2021. The total sample size for this research is 844 samples, with 422 samples in each period, before and during Covid-19. The samples selected meet specific criteria in accordance with the research objectives, using a purposive sampling method.

Ceo Duality

In this study, CEO Duality will be measured using dummy data, where CEO Duality is coded as 1 if there is a familial relationship between the board of directors and the board of commissioners. However, if no familial relationship is found between the board of directors and the board of commissioners, it will be coded as 0 (Abels & Martelli, 2013). Data regarding the board of directors and the board of commissioners are obtained from the relationships outlined in the company's annual reports, which can provide information about the personal details of the board of directors and the board of commissioners.

Financial Performance

The dependent variable used in this observation is the financial performance of the company measured by profitability (ROA). Cohen, Chang, and Ledford (1997) state that ROA is widely used by market analysts as a measure of financial performance because it can gauge the efficiency of assets in generating company revenue. The formula for ROA is:

$$\text{ROA} = \frac{Net\ Profit}{Total\ Assets}$$

Firm Size

Firm size can be described as a measure that classifies the magnitude of a company, distinguishing between large and small enterprises. Company size can be calculated based on total assets. Firm size is measured using the formula:

$$\text{Size} = \text{Ln Total Assets}$$

Leverage

Leverage is used to indicate a company's ability to meet its debt obligations. Companies with high leverage levels imply that they use a larger amount of debt to finance their investment activities, which can lead to increased risk levels and impact the financial performance of the company (Mishra et al., 2019). This ratio is measured using the formula:

$$\text{LEV} = \frac{\boldsymbol{Total\ Liabilities}}{\boldsymbol{Total\ Assets}}$$

Current Ratio

The current ratio is used to demonstrate a company's ability to meet its short-term liabilities that have come due with its current assets. The current ratio is considered a liquidity ratio indicator. This ratio is calculated using the formula:

$$\text{Current ratio} = \frac{\boldsymbol{Current\ Assets}}{\boldsymbol{Current\ Liabillities}}$$

Data Analysis Technique

The researcher conducted descriptive statistical analysis to obtain general characteristics of the collected data. The classical assumption tests used include normality test, multicollinearity test, autocorrelation test, and heteroskedasticity test. The researcher performed hypothesis testing using the multiple linear regression statistical test. Testing was done using the t-test and coefficient of determination. The study was conducted using STATA 14.

The objective of this research is to determine the relationship between independent and dependent variables. This analysis is used as a tool for predicting the dependent variable, which is the financial performance of the company, with the independent variable being CEO Duality. The multiple linear regression equation is presented below:

$$\boldsymbol{ROA_{i,t} = \alpha + \beta_1 DUAL_{i,t} + \beta_2 LEV_{i,t} + \beta_3 SIZE_{i,t} + \beta_4 CR_{i,t} + \mathrm{e}} \qquad \textbf{(1)}$$

Explanation:

ROA	: Return on Assets
α	: Costant Value
$DUAL_{i,t}$	: CEO Duality for company *i* in period *t*
$LEV_{i,t}$	: Leverage for company *i* in period *t*
$SIZE_{i,t}$	: Firm Size for company *i* in period *t*
$CR_{i,t}$	: Current Ratio for company *i* in period *t*
$\beta_1 - \beta_3$	: Coefficient Values *i* in period *t*
e	: Error

RESULTS AND DISCUSSION

Statistical description

In this study, descriptive statistical analysis aims to provide an overview of the variables that will be used, namely CEO Duality as the independent variable, and Financial Performance as the dependent variable. The research period is divided into two time periods: before the pandemic (2018-2019) and during the pandemic (2020-2021). This variable description presents minimum, maximum, mean, and standard deviation data in Table 4.1

Table 4.1 Statistical description

Variable	*Obs*	*Mean*	*Std. Dev*	*Min*	*Max*
DUAL before	422	.4218009	.4944332	0	1
DUAL during	422	.4952607	.500571	0	1
FS before	422	21.2654	1.658688	18	24
FS during	422	21.33886	1.547769	19	24
LEV before	422	.4969905	.2246405	.14	.92
LEV during	422	.4700948	.2139794	.16	.82
CR before	422	.0203327	.0147827	.0046	.0579
CR during	422	.0203832	.0131417	.0061	.0483
ROA before	422	.0498578	.0771707	-.09	.21
ROA during	422	.0380806	.0743067	-.08	.17

Hypothesis test

This research underwent examination through Multiple Regression analysis and hypothesis testing using a t-test with a significance level of 5%, and the outcomes are presented in Table 4.2

Table 4.2. Hypothesis Test

Variable	Coefficient	St. Error	t	Sig
Constant	-.0996012	.0473581	-2.10	0.036
CEO Duality	-.0080832	.007296	-1.11	0.269
Leverage	-.0436583	.016021	-2.73	0.007
Firms Size	.0066102	.0021522	3.07	0.002
Current Ratio	1.67212	.240921	6.94	0.000

Note: *: significant at the 1% level; **: significant at the 5% level;

Based on the results obtained from the multiple linear regression analysis in Tables 4.2 and 4.3, the equation for multiple linear regression is as follows:

ROA = -.2082431 + .0069155 DUAL + -.0897693 LEV+ .012546 SIZE+ .8527264 CR

The t-test is conducted to determine the influence relationship between the independent variable and the dependent variable in the research. Based on Tables 4.1 and 4.2, for the periods before and during Covid-19, it can be concluded that:

1. The P value for the CEO Duality variable (DUAL) is P>|t| = 0.269. Since the value of 0.269 is above the critical threshold of 0.05, it can be inferred that in this study, CEO Duality does not have a significant impact on Financial Performance in the period before the Covid-19 pandemic (H1 Rejected).
2. The P value for the CEO Duality variable (DUAL) is P>|t| = 0.301. Since the value of 0.301 is above the critical threshold of 0.05, it can be inferred that in this study, CEO Duality does not have a significant impact on Financial Performance during the Covid-19 pandemic (H2 Rejected).

CEO Duality on Financial Performance Before the Covid-19 Pandemic

Based on the conducted research, it is found that CEO Duality does not have a significant impact on financial performance during the period of 2018-2019 with 422 samples. It can be concluded that CEO Duality, interpreted as the relationship between the board of commissioners and the board of directors involving family ties (spouse, parent, sibling, child, in-law, grandchild, nephew/niece), does not enable the CEO to make decisions that enhance personal wealth. This study aligns with Daily & Dalton (1992), asserting that there is no relationship between CEO Duality and financial performance. Independent CEOs and boards, even with family ties, are believed to monitor and control management activities as usual without bias (Mca, 2016). In Kusumawardani's study (2021), the reason CEO Duality does not significantly impact a company is attributed to the integrity of the CEO and the board of commissioners, placing themselves in line with their respective roles. In conclusion, this research indicates that CEOs and boards of commissioners can understand their individual conditions even with family relationships between them. CEO Duality also demonstrates a separation of control in management decision-making (Setyawan & Devie, 2017).

CEO Duality on Financial Performance

During the COVID-19 Pandemic Based on the research findings during the Covid-19 pandemic, it is revealed that CEO Duality does not have a significant impact on financial performance. This result differs from Hassan et al.'s (2023) study, which indicates that CEO Duality benefits companies with high information costs during the coronavirus outbreak, and companies with a CEO having a strong relationship with the board are more effective in coping with the Covid-19 pandemic. This does not support the idea that CEOs with connections to the board of commissioners can make faster decisions than companies without CEO Duality during the pandemic, providing them a competitive advantage. Additionally, the research suggests that CEO Duality adds value, especially during the Covid-19 pandemic crisis when uncertainty is high. In the CEO position within a company, there is a greater sense of responsibility, leading CEOs to uphold their credibility and avoid fraudulent financial reporting, even during periods of crisis (Preicilia et al., 2022).

Additional Analysis

This analysis is conducted by performing an independent samples t-test, comparing the mean differences between two samples (Ghozali, 2020). The purpose of this analysis is to determine the differences between values before the Covid-19 pandemic and during the Covid-19 pandemic.

Table 4.3 t-test

Variable	*Obs*	*Mean*	*Std. Dev*	*Min*	*Max*
WROAbe~e	422	.0498578	.0771707	-.09	.21
WROA10~g	422	.0380806	.0743067	-.08	.17

Note: *: significant at the 1% level; **: significant at the 5% level;

Figure 3 indicates that there is a significant difference in ROA values before and during the Covid-19 pandemic. It can be concluded that CEO Duality in 844 companies does not significantly impact financial performance. This aligns with Hypothesis 2, which states that CEO Duality has a positive impact on Financial Performance during the COVID-19 pandemic, not supported by the ROA numbers during the pandemic, which remained on a decline. This is consistent with the study by Preicilia et al. (2022), stating that in crisis conditions, the corporate board will understand their respective roles in controlling the company.

CONCLUSIONS AND SUGGESTIONS

With the existence of CEO Duality in a company, it is suspected that it can raise questions about the independence of a company's board, which can affect the company's financial performance. Through the testing conducted in this study, it can be concluded that the influence of CEO Duality and the choice of comparison periods between before and after the pandemic does not significantly affect the financial performance variable. Independent directors are considered important monitors and advisors in a company. CEO Duality is an important factor in the leadership structure of the board and management team. Companies with CEO Duality do not significantly affect financial performance because both the CEO and the board of directors understand their respective positions in pursuing the company's goals

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