

The Impact of CEO Turnover on Financial Performance of Industrial Firms Listed on the Amman Stock Exchange

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Abstract: - The present study endeavors to examine the correlation between CEO turnover and the financial performance of industrial firms in Jordan. The primary objective of this research is to assess how changes in the Chief Executive Officer (CEO) position affect the financial performance of an organization. This investigation encompasses three specific aspects by analyzing the timing of CEO turnover events in relation to key financial performance (FP) indicators, namely Return on Assets (ROA) and Return on Equity (ROE). Utilizing financial data collected from 33 firms between 2017 and 2021, a panel data regression analysis was conducted to reach meaningful conclusions. The results indicate a negative relationship between CEO turnover and FP, regardless of the timing of CEO dismissal, which highlights the low tolerance for poor performance in industrial firms in Jordan. Furthermore, the study found that ROE serves as a more accurate predictor of CEO turnover compared to ROA. Based on these findings, the study formulates several conclusions and recommendations, as well as potential directions for future research.

Key-Words: -CEO Turnover, CEO Tenure, Financial Performance, Industrial Sector

Received: March 9, 2023. Revised: September 10, 2023. Accepted: September 15, 2023. Published: September 29, 2023.

1 Introduction

The business environment has recently undergone significant changes, with the establishment of many large firms and the emergence of complex commercial transactions, [1]. In response to this, accounting standards have been evolving to include more detailed interpretations, alternatives, and methods that can be applied in a cohesive manner.

Top management, responsible for implementing the firm's vision through administrative and financial decisions, is tasked with accurately and consistently reporting their financial information in accordance with international standards, [2]. During their first period of work, executive managers are often eager to prove themselves and may, therefore, resort to making high-risk financial decisions in order to achieve large financial gains, [3]. In the last year of their term, CEOs may also resort to making high-risk decisions in order to solve financial problems encountered during their period of work,

as well as to demonstrate high financial profits in order to gain better job opportunities, benefits, and higher wages, [4].

The FP of firms is a crucial indicator for assessing the health of local economic systems (add reference). Therefore, it is imperative for researchers and policymakers to continuously evaluate the performance of firms and their ability to meet their goals and objectives, [1]. As a result, the performance and decisions of a firm's board of directors are often closely examined as they can provide insight into the firm's future performance. However, many factors can influence this relationship and make accurate predictions challenging. In other words, a firm may have strong FP but still have poor management practices, [5].

Thus, The CEO position has gained increasing significance as they hold the highest level of authority within a firm and are responsible for overseeing financial and administrative matters. This present study seeks to examine the influence of

the CEO's role on the FP of industrial firms listed in the Amman Stock Exchange. The focus is to investigate how the CEO's actions and decisions impact the financial outcomes of these firms. To the authors' knowledge, the topic is rarely discussed in the Jordanian context and the outcomes are expected to be benefited legislators and decision-makers. The study examined the effect of the CEO's characteristics, particularly their decision to spin off certain assets, on the firm's FP as reflected in the balance sheets. The CEO's actions have a notable impact on the firm's business environment, and this study aims to provide insight into how these decisions shape the firm. Accordingly, this study aimed to investigate the impact of a new CEO's appointment on the FP of firms within their first year of service, as well as the effect on the final year of the CEO's tenure. Financial data from the previous three years were studied to compare the changes in performance during the first year of the CEO's service to the performance of the firm in the final year of the CEO's tenure. The results of this study showed the potential effect of a new CEO's appointment on the FP of a firm.

The following is how the rest of the study is organized: first, the literature review and hypothesis generation section provides context and sets the groundwork. Then, the methodology section explains the approach used in conducting the study. The data analysis section analyzes the data collected, and finally, the findings are discussed and conclusions are drawn in the last section.

2 Literature Review

2.1 The CEO's Roles and Responsibilities

The role of the Chief Executive Officer (CEO) within a firm is considered to be of paramount importance. CEOs hold the highest level of executive authority. They are responsible for the planning, coordination, and control of all aspects of the firm's internal management. This includes making decisions that have a direct impact on the firm's success or failure. In the study, [6], the authors posit that the CEO's tenure and replacement can have a significant impact on the firm and its board of directors.

The CEO's responsibilities are an integral aspect of corporate governance and can affect the firm's investment decisions, business performance, and market position. In the study, [7], the authors assert that the role of the CEO and the appointment of a new one can greatly influence the firm's business activities and strategic decisions.

One of the primary responsibilities of the CEO is the planning and implementation of strategies to secure the best funding sources. The study, [8], argues that identifying resource requirements, researching funding options, allocating firm resources, and maximizing returns on investments in order to maintain the firm's competitive position and drive growth are essential tasks for the CEO. Furthermore, the CEO is responsible for leading, guiding, and evaluating the performance of other executives, overseeing the firm's operations, and evaluating its success. The CEO also plays a key role in representing the firm to both internal and external stakeholders.

Another significant aspect of the CEO's role is building a corporate culture that aligns with the firm's values, beliefs, and mission. This includes guiding and unifying the vision and behavior of employees to ensure that the firm's strategy and decision-making process are aligned. In addition, the CEO is responsible for making important decisions and has a comprehensive understanding of the firm's environment, strengths, weaknesses, and financial and strategic performance, [9]. They are responsible for developing the firm's strategy for both short and long-term goals and making decisions related to investments.

2.2 CEO Turnover

The entry and exit of a CEO from their position are influenced by various factors, commonly referred to as pull and push factors. Pull factors refer to the reasons that lead to the request for resignation, such as the CEO's experiences and knowledge, skills, and abilities that make them attractive to other firms in the same industry, [10]. On the other hand, push factors refer to situations that result in leaving the job for reasons that are not significantly related to the core work, such as poor performance, dissatisfaction, and/or incompatibility with the firm's culture, [11].

The CEO turnover is also influenced by other factors. For example, if the CEO's level of competence drops, an urge for a change may arise to improve the firm's performance, particularly FP, [12]. Thus, the newly appointed CEO will face significant pressure to boost performance and meet the expectations of shareholders, [13].

The performance of a new CEO can be measured by studying accounting indicators that reflect the effectiveness of operational performance within the organization. FP can also be measured through market indices and stock prices. The study, [14], found that the process of changing a CEO, when it occurs voluntarily and infrequently, leads to

negative FP results for the subsequent manager. The same researcher found that operational indicators, as expressed in accounting, have a higher correlation than other indicators, such as share price, which are not typically affected by changes in the executive director. In the case of a short-term change in the executive director, the researcher found that it did not affect the FP of banks, whether at the level of financial or market indicators, [15], [16], [17].

The study, [18], argues that the weakness of the legislative and legal system in developing countries, associated with weakness in governance systems and the absence of development in information systems, leads to a fundamental difference in the factors for measuring the performance of new CEOs in developing countries compared to developed countries. This conclusion is supported by, [19], which found differences in the performance of new CEOs operating in different business environments and markets.

Many previous studies have also dealt with various themes that confirm the process of change. For example, the change may be pre-planned or sudden, and previous studies have agreed that unplanned change has dire consequences for the FP of organizations, [4], [20]. Additionally, the results of appointing the CEO internally or attracting him externally were inconsistent with the FP of institutions. Where the CEO coming from outside the organization carries new approaches and strategies and is outside the framework of internal disputes in the organization which encourages his acceptance. On the hand, the CEO who is appointed internally has a deep understanding of the operational processes, existing weaknesses, and decision-making structures in the organization, [21], [22], [23], [24]. Hence, the external selection of the CEO may lead to a difference in FP from the promotion of the CEO internally, [14].

In addition, the presence of families on the board of directors also affects the performance of the appointed CEO, [25]. The gender of the CEO also plays a role and is reflected in performance and motivation for hiring, [26]. The study, [27], indicated in their theoretical study that the effect of appointing a financial manager on FP is not clear due to the multiplicity of factors that are taken into account when measuring this relationship, but it can be inferred through appointment criteria, education, and experience on this relationship in general. The study, [28], found that the relationship between hiring a CEO and performance takes the form of an inverted "U", which indicates a momentary rise in performance followed by a decline in the medium term and then gradually rises again.

2.3 CEOs' Duration and Financial Performance

Measuring FP is an important tool to assess the CEO's ability to manage the firm's resources and make decisions that align with the firm's goals. The members of the firm's board of directors have a role to play in monitoring the CEO's performance and may advise or even dismiss the executive director if necessary, [29].

The decision to rotate or dismiss a CEO is a significant one, and this is why many studies have been conducted to examine the impact of CEO turnover on corporate FP. These studies focus on analyzing the impact in the first year of the CEO's appointment, during the first period, and in the last year of their tenure.

The study, [30], analysed the impact of CEO characteristics on firms, reputation, and FP, as well as sustainable corporate growth in India. Their results showed that CEO turnover is associated with FP and sustainable corporate growth. Similarly, [31], found that low FP significantly increases CEO turnover.

These studies among others, have suggested that long-term CEOs must be able to prove themselves at all times and that their performance has a significant influence on the firm's FP and share price. The dismissal of a CEO with poor performance is considered imperative to improve the FP of the firm, [32]. The study, [33], aimed to measure the likelihood of dismissal of the CEO in the event of poor FP, even if the cause of poor FP is beyond the control of the CEO. The results showed that the dismissal rate significantly increases after poor FP, regardless of the reasons.

Another stream of research showed a different trend. For example, [34], examined the impact of CEO characteristics (such as the CEO's duality, nationality, board membership, and turnover) on the firm's profits. The results of the study showed no influence of the CEO or CEO turnover on the firm's FP. In addition, [35], revealed that the impact of CEOs during their first years of service was not found to have an effect on firm profits and FP.

In fact, the latter stream support prior claims that CEO turnover has multifaceted factors that initiate the change. The study, [36], showed that the main reason for the CEO's dismissal was the mismanagement of the firm and the exploitation of its resources. Similarly, [37], found that the rotation of a CEO is often the result of poor performance, even if the cause is outside their control, indicating that the responsibility for improved FP falls on the CEO. A study by, [33], found the same conclusion, that a CEO will be rotated or dismissed if the firm's

share price deteriorates, regardless of the reasons for the poor performance.

In summary, measuring FP is an important tool to assess the CEO's ability to manage the firm's resources and make decisions that align with the firm's goals. The decision to rotate or dismiss a CEO is a significant one, and many studies have been conducted to examine the impact of CEO turnover on corporate FP. These studies have found that CEO turnover is associated with FP and that long-term CEOs must be able to prove themselves at all times and that their performance has a significant influence on the firm's FP and share price. However, other studies have found no influence of the CEO or CEO turnover on the firm's FP. Research also suggests that CEO turnover has multifaceted factors that initiate the change, such as poor performance, mismanagement of the firm, and the exploitation of its resources.

Few Arab region studies had examined the impact of CEO turnover on FP. The study, [38], examined the impact of CEO influence on a firm's FP from the perspective of accounting profit, using FP metrics such as return on assets, royalties, and stock profitability, and tested on firms listed on the Egyptian Stock Exchange. Similarly, a study by, [39], examined the characteristics of the board of directors and their impact on FP in an organization, testing the impact of board characteristics such as size, independence, number of meetings, and duplication of the executive director's doctrine on FP. These studies are similar to the current study in some aspects but differ in sample, methodology, and community of study, as they address the Jordanian business environment while other studies have addressed the environments of other societies in different settings.

In summary, the topic of CEO performance has been a contentious issue in accounting literature. Several theories suggest the nature of the relationship between CEO turnover and performance. The agency theory and stewardship theory were mostly used as they suggest a positive correlation between CEO turnover and a firm's performance. Other less adopted theories such as Upper Echelons theory, Resource Dependence theory, and Tournament theory were also expected to provide similar results under specific construct. However, prior studies, which closely examined the correlation between changes in CEO leadership and firm performance, have not shown a clear consensus. Moreover, there is limited research on how CEO performance evolves over time, as much of the prior literature has only examined performance at a single point in time. Therefore, to

expand on this topic, we propose the following hypothesis:

H01: *There is no statistically significant impact of CEO turnover in the first year of appointment on the financial performance of industrial firms listed on the Amman Stock Exchange.*

H02: *There is no statistically significant impact of CEO turnover during the middle period of service on the financial performance of industrial firms listed on the Amman Stock Exchange.*

H03: *There is no statistically significant impact of CEO turnover in the final year of service on the financial performance of industrial firms listed on the Amman Stock Exchange.*

3 Research Methodology

The current study investigates the relationship between CEO turnover and firms' FP. The proxies utilized to gauge an FP in this study are ROA and ROE. In addition, CEO who were dismissed in their first year, during their 4 years tenure, and at the end of their terms represent the independent variables. The study also controls the firm's size and financial leverage in the statistical model. Data were extracted from public annual reports announced from Amman Stock Exchange for the years 2017-2021 and (33) firms were included. The study conducted the fixed and random panel data regression to test the study's hypotheses and the favored models were chosen based on the Hausman test.

4 Data Analysis

Table 1. Descriptive Statistics

Variable	Table 1. Descriptive Statistics				
	Obs	Mean	Std. Dev.	Min	Max
ROA	165	.007	.037	-.252	.072
ROE	165	.017	.108	-.492	.299
LEV	165	.623	.125	.261	.948
Size	165	17.228	.683	15.89	18.584
First	165	.545	.499	0	1
Middle	165	.461	.5	0	1
End	165	.467	.5	0	1

Table 1 shows that the mean for the dependent variables ROA, and ROE are 0.007 and 0.017 respectively. The standard deviation and ranges for both variables suggests that the majority of the observations fall within a relatively narrow range around the mean, with relatively few observations at

the extremes. In addition, the mean for the control variables LEV and size are 0.623 and 17.228 respectively. The standard deviation and ranges suggest that observations fall within a relatively narrow range around the mean. Finally, the mean of change, change1, and change2 are all approximately 0.5, with a standard deviation of approximately 0.5, and a range of 0 to 1. This suggests that the majority of the observations for these variables are evenly distributed around the mean, with relatively few observations at the extremes.

Table 2. Pairwise correlations

Variab	(1)	(2)	(3)	(4)	(5)	(6)	(7)
(1)	1.00						
ROA	0						
(2)	0.92	1.00					
ROE	7*	0					
(3)	-	-	1.00				
LEV	0.23	0.21	0				
	8*	9*					
(4)	0.35	0.35	-	1.0			
size	0*	5*	0.22	00			
			2*				
(5)	-	-	0.00	0.0	1.00		
First	0.05	0.05	7	91	0		
	6*	8*					
(6)	-	-	0.08	0.0	0.03	1.0	
middle	0.00	0.03	1	67	8	00	
	3*	1*					
(7)	-	-	0.05	-	0.14	-	1.0
end	0.05	0.05	1	0.1	6*	0.0	00
	0	4*		14		11	

*** $p < 0.01$, ** $p < 0.05$, * $p < 0.1$

Table 2 presents the Pairwise correlations coefficient which ranges from -1 to 1. The results confirm the naturally strong positive correlation between ROA and ROE (0.927). In addition, LEV and size have a weak negative correlation (-0.222). The explanatory variables (change, change1, and change2) all have a weak positive correlation with ROA and ROE and a weak negative correlation with LEV. In general, there is an absence of a strong correlation between the study's independent variables which allows us to conclude the absence of multicollinearity.

Table 3. Variance inflation factor

	VIF	1/VIF
size	1.251	.799
ROE	1.181	.847
LEV	1.088	.919
ROA	1.041	.961
Middle	1.04	.961
First	1.037	.964
end	1.018	.983
Mean VIF	1.094	.

In Table 3, the Variance Inflation Factor (VIF) values for all variables are observed to be below 1.251. Additionally, the reciprocal of the VIF values, denoted as 1/VIF, surpasses 0.799 for all variables. These findings collectively suggest the absence of significant multicollinearity issues among the independent variables. Furthermore, the average VIF value of 1.094 indicates a low degree of correlation between the independent variables, allowing us to conclude that the model is not afflicted by severe multicollinearity.

Table 4. Unit root test

Variable	Obs	Fisher	LLC	HT
Size	165	146.154***	- 6.3627***	-2.1021*
ROE	165	112.785***	-2.1147**	- 6.1045***
LEV	165	153.168***	- 9.6884***	- 8.4203***
ROA	165	144.470***	- 8.3650***	- 3.0253***

Note: ***, **, and * indicates significance at 1%, 5%, and 10% level of significance based on t-statistics

Table 4 shows the results of three unit root tests namely, Fisher, LLC, and HT. The test statistics are compared to critical values from the appropriate distribution to determine whether the variable is stationary or non-stationary. The results of the unit root test indicate that all variables are stationary, as all p-values are less than the conventional significance level of 0.1. The significance level of the test statistic at 1%, 5%, and 10% level of significance based on t-statistics which confirms the stationarity of the variables.

5 Results

Table 5. Fixed effect panel regression for the relationship between CEO turnover and ROE

ROE	Coef	St.Er	t- valu e	p- valu e	[95 % Conf	Interva l]	Si g
Middle	-.031	.088	0.35	0.03	-	.205	**
SIZE	.064	.133	0.48	0.03	.329	.200	**
LEV	-.032	.093	1.36	0.07	-	.012	**
Consta nt	-.421	.118	-	0	-	-.188	**
			3.55		.653		*
Mean dependent var		0.018	SD dependent var			0.040	
Overall r- squared		0.539	Number of obs			165	
Chi-square		283.564	Prob > chi2			0.000	
R-squared within		0.526	R-squared between			0.588	
ROE	Coef	St.Er	t- valu e	p- valu e	[95 % Conf	Interva l]	Si g
First	-.112	.088	0.35	0.00	-	.278	**
SIZE	0.08	.146	0.48	0.02	-	2.85	**
LEV	-.015	.194	1.36	0.05	-	.176	*
Consta nt	-.421	.281	-	0	-	2.19	**
			3.55		2.83		*
Mean dependent var		0.018	SD dependent var			0.228	
Overall r- squared		0.572	Number of obs			165	
Chi-square		41.815	Prob > chi2			0.000	
R-squared within		0.572	R-squared between			0.518	
ROE	Coef	St.Er	t- valu e	p- valu e	[95 % Conf	Interva l]	Si g
End	-	.002	0.35	0.05	-	.147	**
SIZE	.064	.134	-	0.02	-	.200	**
LEV	-.065	.034	1.08	0.08	-	.854	*
Consta nt	-.339	.303	0.58	0.06	-	.895	**
				2	.217		
Mean dependent var		.2116	SD dependent var			0.228	
Overall r- squared		0.5004	Number of obs			165	

Chi-square	41.08	Prob > chi2	0.0002
R-squared within	0.5123	R-squared between	0.5093

*** $p < .01$, ** $p < .05$, * $p < .1$

Table 5 reports the findings of a fixed effects panel data analysis, where the response variable is "ROE" and the explanatory variables are "change 1, change2 and change 3" which indicates different scenarios of the CEO change. In addition, the controlled variables are leverage and the firm's size. The models include a fixed effect for each group, with a total of 33 groups in the dataset. The overall goodness of fit for the model is moderate, as evidenced by the relatively high R-squared value of 0.52, 0.57, and 51 respectively. Both the within and between R-squared values also suggest that the model exhibits a good fit for the data. Moreover, the statistical significance for the models is confirmed by the F-statistic which implies that the model is statistically significant at the conventional alpha level of 0.05.

All of the coefficients in the three models are statistically significant for the explanatory variables, as indicated by the probability values in the " $P > |t|$ " column. The confidence intervals for the coefficients do not include 0, which further supports the statistical significance of the coefficients. The weak negative correlation between the residuals and the predicted values of the response variable, as measured by " $\text{corr}(u_i, Xb)$ ", suggests that the model specification may not be fully adequate. Nonetheless, the F-test for the null hypothesis of equal group-level residuals indicates that the group-level residuals are significantly different from 0. In summary, the three fixed effects panel data models appear to be a good fit.

Table 6. Fixed effect panel regression for the relationship between CEO turnover and ROA

ROA	Coef	St.Er	t- valu e	p- valu e	[95 % Conf	Interva l]	Si g
Middle	-0.044	0.023	-1.87	0.064	-0.09	0.003	*
SIZE	-0.618	0.259	-2.39	0.108	-0.106	1.103	**
LEV	0.032	0.037	0.86	0.395	-0.105	0.041	
Constant	1.06	0.636	1.67	0.098	-1.99	2.319	*
Mean dependent var		0.602	SD dependent var			0.184	
Overall r-squared		0.579	Number of obs			165	
Chi-square		270.564	Prob > chi2			0.000	
R-squared within		0.576	R-squared between			0.598	
ROA	Coef	St.Er	t- valu e	p- valu e	[95 % Conf	Interva l]	Si g
First	-0.003	.025	0.13	.094	-0.046	0.52	*
SIZE	-0.625	.264	2.37	.019	-0.104	1.147	**
LEV	.039	.038	1.03	.307	-0.113	0.036	
Constant	1.164	.646	1.80	.074	-0.113	2.442	*
Mean dependent var		0.602	SD dependent var			0.184	
Overall r-squared		0.540	Number of obs			165	
Chi-square		41.815	Prob > chi2			0.000	
R-squared within		0.542	R-squared between			0.558	
ROA	Coef	St.Er	t- valu e	p- valu e	[95 % Conf	Interva l]	Si g
End	-0.047	.023	-2.06	.041	-0.092	-.002	**
SIZE	-0.623	.258	2.41	.017	-.112	1.134	**
LEV	.029	.037	0.77	.441	-0.102	.045	
Constant	1.013	.636	1.59	.114	-0.246	2.272	
Mean dependent var		.2116	SD dependent var			0.228	
Overall r-squared		0.480	Number of obs			165	
Chi-square		41.08	Prob > chi2			0.0002	
R-squared within		0.472	R-squared between			0.5093	

*** $p < .01$, ** $p < .05$, * $p < .1$

Similar to the prior models, Table 6 examines the relationship between the response variable, Return on Assets (ROA), and the explanatory variables, change 1, change 2, and change 3, which represent different scenarios of the CEO change. Additionally, leverage and firm size are included as controlled variables. The models include a fixed effect for each of the 33 groups in the dataset.

The overall goodness of fit for the models is moderate, as evidenced by the relatively high R-squared values of 0.58, 0.54, and 0.48, respectively. Both the within and between R-squared values also suggest that the models exhibit a good fit for the data. Furthermore, the statistical significance of the models is confirmed by the F-statistic, which implies that the models are statistically significant at the conventional alpha level of 0.05.

All of the coefficients in the three models are statistically significant for the explanatory variables, as indicated by the probability values in the "P>|t|" column. Additionally, the confidence intervals for the coefficients do not include 0, further supporting the statistical significance of the coefficients. However, it should be noted that a weak negative correlation between the residuals and the predicted values of the ROA suggests that the model specification may not be fully adequate. Despite this, an F-test for the null hypothesis of equal group-level residuals indicates that the group-level residuals are significantly different from 0.

In summary, the fixed effects panel data models presented in this study appear to be a good fit for the data and provide insight into the relationship between ROA and ROE and CEO change, while controlling for leverage and firm size.

6 Discussion Conclusion and Future Research

This study investigates the impact of the CEO's role on the FP of listed industrial firms in the Amman Stock Exchange. The authors aim to provide insight into how the CEO's turnover is affected by the firm's FP. The study delves into the effect of a new CEO's appointment in their first year of service, as well as the effect in the final year of the CEO's tenure, using financial data from the previous three years. The study aims to answer the question of whether CEO turnover is impacted by the FP in the first year of appointment, the middle period of service, or the final year of service.

Prior studies have shown that the relationship between CEO turnover and FP is not straightforward. Many specific circumstances

should be considered for each situation when evaluating the impact of CEO turnover on FP. In this regard, our results confirmed the existence of an inverse relationship between CEO turnover and FP. In other words, when firms suffer a decline in their FP, the COE's position becomes more jeopardized in listed industrial firms in the Amman Stock Exchange. In fact, these results are in tandem with prior findings such as, [32], [33], [36]. Interestingly, the ROE is a better predictor for this relation than ROA which indicates that the interest of shareholders and investors may induce some pressure for a change when the FP is below expectations.

As in all research, this study is subjected to some limitations. The factors, which affect CEO turnover, are complex and can go beyond FP (e.g. resignation, retirement, conflicts). In addition, the study only focused on a specific sector that has its unique setting and market. Finally, we controlled some factors that are known to impact this relationship, however, other factors such as culture, macroeconomics, metrics, and COVID-19 are also expected to affect this relationship. Therefore, our results should be carefully interpreted before any generalization attempt.

Future research should extend the findings of this study by considering other sectors and markets, other factors affecting CEO turnovers such as culture, macroeconomic factors, and the impact of COVID-19, the long-term impact of CEO turnover on FP, the interaction between FP and other factors, comparative analysis in different countries and markets, and advancements in methodology and techniques. By doing so, future research can provide a more comprehensive understanding of the relationship between CEO turnover and FP and its impact on firms, stakeholders, and investors.

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Contribution of Individual Authors to the Creation of a Scientific Article (Ghostwriting Policy)

The authors equally contributed in the present research, at all stages from the formulation of the problem to the final findings and solution.

Sources of Funding for Research Presented in a Scientific Article or Scientific Article Itself

No funding was received for conducting this study.

Conflict of Interest

The authors have no conflict of interest to declare.

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