

CEOS CHARACTERISTICS AND THE SUCCESSFUL OF TURNAROUND STRATEGY: EVIDENCES FROM INDONESIA

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ABSTRACT

Extensive investigation had been conducted in previous studies regarding the effect of top leader characteristics and organizational performance. Even though conclusive effect of each dimension were not consistence, most studies agree the significant impact of top executives. Nevertheless, studies in particular context such as turnaround are limited especially in the interaction with strategy field. This study aims to investigate the effect of top leader (i.e. CEO) on performance under the condition of turnaround strategy. Using 81 companies listed in Indonesia Stock Exchange (IDX), this study reveals several results. Most investigated variables found significant effect on turnaround performance such as educational and functional background, tenure in position and in organization. However, study found no relationship between CEO characteristics and strategic orientation. In contrast, in line with expected assumption, prospector strategy has positive impact on turnaround performance.

Key word: Turnaround Strategy, CEO Characteristics, Strategy Orientation, Indonesia Evidence, Turnaround Process.

BACKGROUND

Prominent theory of upper echelons received significant attention from scholars. This view has been used to explain organizational performance from strategic leadership literature. Hambrick and Mason (1984) argued that organization is a reflection of its strategic leader because they are the actors who making and implementing strategic decisions. Afterwards, scholars have started to work on the connection between leader characteristics and organizational performance. Despite of common believed that strategic leaders have significant determination on performance, the conclusive finding of specific characteristics has not achieved yet (Finkeilstein, Hambrick, & Cannella, 2009). Previous studies found that performance will increase as their companies lead by short tenure executives (Puranam, 2001). On the other hand, the growth appeared to be sustain when companies are directed by senior executives (Sorenson, 1999). Other studies did not find any relationship (Boone, Brabander, & Witteloostujin, 1996; Iaquinto & Frederickson, 1997; Balkin, Markman, & Gomez-Meija, 2000). Similar findings also generated for industrial setting. Each industry has not indicated a consistence result for each variable.

Situational theory stated that neither single characteristics nor single styles should satisfy every work condition (Daft & Lane, 2008). Successful leader in competitive market cannot be a guarantee for their success in the soundless competition. Daft and Lane (2008) argued that the style of leaders should align with organizational problems and environmental conditions. Therefore, traits of leader which usually determined their style will also considerably different (Bass, Avolio, Jung, & Berson, 2003; Fulmer, 2000).

Environmental situation required company to take rational measures for continuously adapt with change. Often companies failed in the process which consequently brings them into critical conditions. At this point, leaders need to consider strategic moves in order to save their companies (Pretorius, 2008). Strategic moves are necessary to avoid the condition of stuck in the middle (Porter, 1979). Generic strategy to solve this problem is by initiating turnaround strategy of setting new direction and cutting operational inefficiency.

Significant impact of turnaround strategy is not as sound as the investigation of the topic especially the investigation in the strategic leadership perspective. Very rare found the empirical paper regarding the successful of turnaround strategy based on the characteristics of leaders. There are empirical papers on turnaround strategy, but it discussed from the corporate strategy (Smith & Graves, 2005), financial moves (Evans, Chitnomrath, & Christopher, 2013), marketing tactics (Day & Moorman, 2013) and porter's generic strategy (Pretorius, 2008). Few papers are discussed the strategy from leadership view such as Harker and Sharma (2000) discussed organizational development conducted by leaders, Boyd (2011) explains generic steps of how leaders implement turnaround strategy.

This paper discusses turnaround strategy from the perspective of strategic leadership using upper echelon theory as foundation. As Hambrick and Mason (1984) stated that the characteristic of top leader could be use as dimensions to understand organization, this paper attempted to seek particular characteristics of leaders on the successful of turnaround strategy. The characteristics are limited to demographical traits which are educational level, functional background, and tenure.

Most studies in strategic leadership argued that the characteristics of leader determined the choice of particular strategy. Finkeilsten et al (2009) stated that leaders who have extensive experience in output functional are more risk takers rather than that of from throughput functional. However, there are limited evidences from particular turnaround process. Similarly, educational level which posited as proxy of cognitive complexity often associated with innovation (Wally & Baum, 1994), however previous studies were conducted in normal condition.

Executive tenure often reflected as degree of experiences of executives serving in any particular organization. However, this dimension has been conceived in three ways of tenure in position (Hambrick & Fukutomi, 1991; Miller, 1991), tenure in organization (Thomas, Litschert, & Ramaswamy, 1991), and tenure in industry (Hambrick, Geletkanycz, & Frederickson, 1993). Extensive studies on this dimensions neglect the critical contingency condition such as turnaround besides the important role of leader in the critical situations. Furthermore, results from previous studies were not consistence regarding the effect of each dimension on strategy and performance (Finkeilstein, Hambrick, & Cannella, 2009).

This paper posits strategic orientation of Miles and Snow (1978) as intervening variable focusing on prospector and defender. Both strategies consider as continuum which reflected the position of strategy on its tendency of action. This typologi considered appropriate to implement turnaround approach because it provide fundamental basis of orientation. Since turnaround condition was derived from inability of company to cope with external environment, prospector strategy should satisfy company in providing new direction and initiatives. Another problem required turnaround initiative is operational inefficiency. Company could consider imitation of competitor's moves in order to solve internal inefficiency. This approach mandate executive to consider defender orientation.

LITERATURE REVIEW

Turnaround strategy is an attempt of organization to restore organizational performance. Restoration refers to improvement of significantly poor into healthy performance (Boyd, 2011). Turnaround process implements by identified the cause of problem and adopted particular strategy to reverse poor condition into sustain profitability (Barker & Duhaime, 1997). CEOs as the apex within organization is the leader of the restoration process which authorize to initiate particular stages and approaches.

There are three stages involve in turnaround process (Lohrke, Bedeian, & Palmer, 2004). First, leaders need to seek the problems causing sustain poor performance. Problems were coming from diverse sources from either environmental turbulences or internal inefficiency as well as from the summation of both dimension. In the next stages, leaders need to establish appropriate strategies to cover the problem and implement those carefully and consistently. Final stage is by conducting overall evaluation on the process whether it needs to continue or take corrective action (Pearce & Robinson, 2013).

Upper echelons theory introduced by Hambrick and Mason (1984) assume that strategic actions of company are the consequences of decision made by its top leaders. Hence, the organization is the reflection of its top leaders. In conjunction to this assumption, Hambrick and Mason explained bounded rationality as the foundation. The concept says that leaders tend to filter information and options in the decision making based on their values, knowledge and experiences (Finkeilstein, Hambrick, & Cannella, 2009). Relying to the theory, every strategic decision was a product of humanistic traits of leaders.

Similar argument also employed for turnaround situation. Leaders need to design their organizational transformation such as system, culture or operational activity (Evans, Chitnomrath, & Christopher, 2013). Turnaround strategy required leaders to establish positive communication culture in order to build organizational trust (Boyd, 2011; Lawson & Price, 2003). Moreover, Lawson and Price (2003) argued that the transformation should clearly define and communicate to entire unit within organization. Rely on the upper echelons theory, the successful of turnaround process should be imposed to leaders.

Successful turnaround is not only required internal transformation but also external communication measures especially to direct customers (Day & Moorman, 2013). This action will help company to gain public trust which have declined during crisis (Evans, Chitnomrath, & Christopher, 2013). Although it is difficult to regain the trust, publicity of turnaround initiative shown the commitment of company to transform (Smith & Graves, 2005; lawton,

Rajwani, & O'Kane, 2011). Leaders also must responsible to ensure the publicity is conducted in favor of company.

Hambrick and Mason (1984) argued that organizational performance is the function of strategy and decision taking by its leader. Strategy and decision are determined from value and experience such as belief, educational background, tenure and among others. Therefore, value and experience which reflected from characteristics of leader will impose organizational performance. The logic of upper echelon was explained in three-stage filtering process that involves limited field of vision, selective perception and interpretation (Hambrick & Mason, 1984; Finkeilstein, Hambrick, & Cannella, 2009). The theory instructed that an attempt to understand performance and strategy should look into leaders orientation which shaped the filtering process (Hambrick & Mason, 1984).

Leaders orientation could be identified from two major classes of psychological properties and observable variable of experiences (Finkeilstein, Hambrick, & Cannella, 2009). The first classes provide foundation for executive to filter and interpret stimuli, hence it leads executive to certain choices. Several psychological variables like cognitive, value and belief are often examined in previous studies. Similar purpose with the first classes, observable dimension often seen as the reflection of leader experiences such as functional and educational background, tenure and age. Both classes are believed acting as strategy and performance determinant whether it use simultaneously or respectively.

Observable dimension often used as proxy of behavior as substitute for psychological properties (Finkeilstein, Hambrick, & Cannella, 2009). Given many obstacles occurred in identified psychological properties of leader, researches tend to make assertion of observable variable in explaining psychological traits. There are opposite arguments to dilute the process. Some scholars argued that observable dimensions are lack conceptual clarity since it only posits as a proxy. However, as the limitation to collect psychological data from leaders in large companies, using particular observable dimensions are more reasonable.

Educational characteristics were often used in previous investigation. Even though executives are far beyond their formal education, hence it would be difficult to use as proxy of experience, the dimension is still appropriate to reflect cognitive style of CEO (Hitt & Tyler, 1991). However, the manners of measurement should be modified from educational background in specific major to educational level. Many scholars have made relationship between higher level of education and innovation. They argued that higher level associated with open-mindedness. As prospector required more innovativeness than defender, CEO with higher degree will more competent with prospector strategy. Since higher level or education reflects cognitive complexity and ability to discern pattern, highly educated CEO should be able to identified problems and established sufficient choices in turnaround process.

Hypothesis 1: CEO educational level has positive relationship on prospector strategy, as well as toward turnaround performance.

Functional background is most frequent variable used as proxy of executive's experience. Functional experience has been related to choices of information and response on stimuli (Finkeilstein, Hambrick, & Cannella, 2009), hence it will determine particular strategic moves and organizational performance. Functional background could have classified into two

classes of output (i.e. marketing, sales, finance and R&D) and throughput (law, operation, production, accounting) oriented. The first contains of functional which often involves with final performance such as number of sales, budget absorption and efficiency, revenue. In contrast, throughput functional are more related to operational process within company that does not directly determined final performance.

Previous studies found CEO with output oriented tend to choose prospector strategy rather than defender. Study conducted by Litschert and Ramaswamy (1991) on computer industries found 77 per cent of CEOs using prospector strategy have output oriented functional background. On the meanwhile, 90 per cent of CEOs using defender strategy were throughput functional background. As turnaround process required attention to final performance and alignment to particular external environment, CEO with output function is more relevant to understand both condition. Moreover, output functional were associated with innovativeness which are needed for implementing turnaround strategy

***Hypothesis 2:** CEOs with output functional background will pursue prospector strategy while CEOs with throughput functional background will pursue defender strategy. CEOs with output functional background will turnaround performance more significantly rather than CEOs with throughput functional background.*

Organizational tenure is known as indicator of experiences within particular job. Most influential study on the effect of tenure toward organizational change discovered Inverted-U shape relationship (Finkeilstein, Hambrick, & Cannella, 2009). It means that CEOs initiated more change program in their early career and it will decrease after particular time (Hambrick & Fukutomi, The Seasons of a CEO's Tenure, 1991). Long tenure CEOs will more comfort with internal stability and industrial average. It is difficult to expect substantial change from long tenure CEO's which means they were associated with defender strategy rather than prospector. Given the need for change that required for implementing turnaround strategy, it will more rational to expect that CEOs with less tenure contribute more favorable than that of long tenure.

***Hypothesis 3:** CEOs with long tenure (i.e. position, organization and industry) will pursue prospector strategy while CEOs with short tenure will pursue defender strategy. There is negative relationship between CEOs tenure and turnaround performance.*

Turnaround strategy required company to initiate internal transformation process both on how they interpret the environment and on how they implement daily operational activity (Furrer, Pandian, & Thomas, 2007; Panicker & Manimala, 2015). Furthermore, the strategy needs authentic solution based on particular problem faced (Boyd, 2011; Day & Moorman, 2013). Prospector strategy was associated with initiative action of companies regardless of competitors move (Miles & Snow, 1978). It means that company will act based on what they need to. In compare to defender strategy that usually tend to follow what competitors did, prospector strategy was more reasonable to ensure successful of turnaround process.

***Hypothesis 4:** Prospector strategy will more favorable for turnaround performance rather than defender strategy.*

METHOD

Data and Sample

The study was conducted in Indonesia's business landscape which considering all companies listed in the Indonesia Stock Exchange (IDX). There are 513 companies listed in that secondary market. The data were generated from companies that have experienced turnaround process. We filtered companies implementing turnaround as its financial condition reported in the annual report. The sample was companies having ROA less than the standard free interest risk for two consecutive years, then having an increasing ROA higher than the standard also for two consecutive years (Francis & Desai, 2005). Of companies listed in IDX, there are 85 that had implemented the strategy. However, only 81 firms could be using in analysis because of missing data problems.

Measurements

CEO characteristics defined as demographical traits having by each CEO which was reflected from particular characteristics (i.e. educational, functional and tenure). Educational background defined as the level of degree hold by each executive that reflected level of cognitive complexity of each CEO (Smith, et al., 1994; Wally & Baum, 1994). Educational background was measured by identification of last degree of executive formal education. The results were arranged from one to four which reflected higher value for higher level. Functional background identified from the last functional experienced of each executive before they started as CEOs (Thomas, Litschert, & Ramaswamy, 1991). Operational measurement of functional background was through classifying into two categories of output and throughput functional. Output oriented functional includes marketing, finance and general manager while throughput oriented contains of law, operational and accounting.

Tenure CEOs defined as years' period of CEO within particular work (Hambrick, Geletkanycz, & Frederickson, Top Executive Commitment to The Status Quo: Some Test of Its Determinants, 1993). Tenure contains of three categories of tenure in position, organization and industry. Tenure in position means years experienced by CEOs as top executive in the observed companies (Hambrick & Fukutomi, The Seasons of a CEO's Tenure, 1991) while in organization was years' period of CEOs worked within observed company (Miller, 1991). Realizing that CEOs often moving around across companies given same industry, this study considered this dimension has contributed on successful turnaround (Hambrick, Geletkanycz, & Frederickson, Top Executive Commitment to The Status Quo: Some Test of Its Determinants, 1993). Tenure in industry was defined as years' period CEO have work within industry of observed company. Turnover performance was measured from return on assets of observed company which reflected their ability to generated profit as well as to made assets efficiency.

Data Analysis

The data was analyzed using statistical approach which considering appropriate method for panel data. The STATA 12 was used as software analysis that allowed to test developed hypothesis with panel data. Furthermore, the hierarchical regression method considered for identifying intervening effect of strategic orientation for each relationship of CEOs characteristics and turnaround performance (Baron & Kenny, 1986). The rules for hierarchical method refer to the guideline proposed by Baron and Keanny (1986).

RESULT

No	Variables	Observation	Mean	Std.Dev	Min	Max
	Number of Employee	324	1438.95	2717.44	5	15423
1	ROA	324	-1.935	75.88	-539.98	363.86
2	Strategy	324	.456	2.79	-26.30	27.58
3	Edu Level	324	2.382	.562	1	4
4	Output functional	324	.886	.317	0	1
5	Throughput functional	324	.113	.317	0	1
6	Tenure in organization	324	12.45	10.63	1	45
7	Tenure in position	324	8.678	9.529	1	40
8	Tenure in industry	324	20.31	10.10	1	45

Data was obtained from official financial report of companies listed in Indonesia Stock Exchange. Total companies indicated in turnaround condition were 85 companies. The data from each companies were collected for four respective years' period that involved two stages of decreasing and increasing performance. However, four companies had not published required item needed for this study in their annual report. Hence, total data used to test the hypothesis was 324 observation generated from 81 companies listed in Indonesia Stock Exchange. Descriptive of data are explained in the table 1.

Since involved observation period contains of decreasing and increasing return on asset, standard deviation of data was salient. Similar with description of employees that appeared in high dispersion of standard deviation. As the strategy reflected in orientation continuum of prospective and defender, higher score indicates more pursue toward prospector position. Tenure was identified in years, so the scores in the table indicating years of services each CEO within dimensions. Regression analysis was implemented to detect both direct and intervening relationship of framework. It resulted the direct relation of CEO characteristics on performance, but it did not support mediating effect of strategy orientation. F-test on the direct effect was agreed with model ($t = 5.82$, $p < .01$) while the score on the relationship of independents toward strategy orientation was not supported prediction ($t = .50$, $p > .10$). The results of hypothesis testing are explained in the table 2.

Variables	ROA	Strategy	ROA*
Edu Level	** -4.97 (.000)	.18 (.856)	-
Output functional	^a 1.81 (.075)	-.97 (.335)	-
Throughput functional	^a -1.81 (.075)	.97 (.335)	-
Tenure in organization	* -2.53 (.014)	-.12 (.907)	-
Tenure in position	** 2.68 (.009)	-.64 (.525)	-
Tenure in industry	.76 (.450)	.15 (.885)	-
Strategy			.043 (2.04)
F	5.82 (.000)	.50 (.775)	4.17 (.0426)

Analysis shown the direct influence from executive's education level ($t = -4.97, p < .01$) and organizational tenure ($t = -2.53, p < .05$). These dimension were found having negative impact on performance. Tenure in position appeared having positive impact on performance ($t = 2.68, p < .01$) while tenure in industry did not shown significant relation with organizational performance. Result exhibited positive effect of output functional on performance ($t = -1.81, p < .10$) while negative impact on the relationship between throughput functional and performance ($t = -1.81, p < .10$).

Surprising outcome appeared on the relationship of CEO characteristics on strategy orientation. different with developed hypothesis, none of the independent variable generated significant effect on strategy orientation. This relationship does not agree with part of logic of upper echelon theory which posits high correlation of executive traits and strategic choices. Since the typology used in the study was limited to prospector and defender, further interpretation will only reflect only for both types.

Expected result found on the relationship of strategic orientation and organizational performance. It shown positive relationship between both variables ($p = .043 < .1, \beta = 0.004$). Positive relation means the more companies pursue prospector strategy, the higher its performance are. Since the relationship of CEO characteristics and strategy does not exist, while many of those are correlated with organizational performance, it can be concluded that the mediated relationship did not occurred through strategy orientation on the relationship of CEO characteristics and organizational performance.

DISCUSSION

Results reveals important insight in understanding turnaround strategy at the framework level. First, there is significant contribution of top leader in implementing their company's turnaround. Most characteristics having by leaders are accounted for successful of turnaround process. Second, implemented strategy in turnaround process are not determined by leader characteristics. Few arguments could explain the uncommon result. Finally, the more prospector orientation strategy is, the more benefit companies will have enjoyed. In other word, companies should consider many innovative measures in implementing turnaround strategy.

Direct effect between CEOs characteristics and turnaround performance appears for most investigated variables. However, some finding are not appeared as it was expected. CEOs educational level has negative relationship with performance. It indicated that CEOs with high

educational level will more difficult in leading their companies while in the turnaround stages. The results were not in line with the hypothesis which expected otherwise. As education level associated with cognitive complexity and discern among pattern, while in turnaround process CEOs faced explicit problems, the complexity of cognitive will delay the process since high education CEOs intent to consider more options.

Output oriented functional background was favorable for companies in turnaround stages. As it has been expected, CEOs with output function was associated with innovativeness that are needed for ensuring successful turnaround. Additional explanation that could add on the results is the close relation of output functional with flexibility in action and ability to understand external stimuli. These abilities are considered important in implementing turnaround strategy. The result supports previous finding of Litschert and Ramaswamy (1991) who found 77 per cent CEO implementing prospector strategy were output functional background.

On the other hand, throughput function does not support turnaround strategy. Results shows negative impact of the function while leader was implementing the strategy. As functional fit between strategy and functional expertise was comfortable and it may generate optimum performance (Strandholm, Kumara, & Subramanian, 2004), CEOs will prefer to choose strategy-functional fit. However, internal focus of throughput strategy should be derived from external assessment of market because the objective of turnaround is gaining substantial incremental performance either from sales activity that required creative marketing programs or internal efficiency that required innovation in finance tactics.

Results indicated negative relationship of tenure in organization and turnaround performance which appears as expected in hypothesis. CEOs with long tenure in organization have internalize internal culture and mindset which were usually difficult to change (Miller, 1991; Finkelstein, Hambrick, & Cannella, 2009)(..). Meanwhile, turnaround strategy required substantial change of internal process including its culture and daily activity. It is difficult to expect CEOs who have internalize organizational process will initiate transformation program in turnaround strategy.

In the contrary, there is positive effect between tenure in position and turnaround performance. This finding was different with hypothesis that said otherwise. Result implicated that turnaround process should lead by a leader who have long enough period of serving as CEO. Since turnaround involves high frequent and substantial change, Long tenure CEO has had sufficient power to control and to get supported from entire employee. Sufficient power contributed significant impact on the successful of implementing strategy.

Orientation strategy has positive effect on turnaround performance. Orientation strategy was defined as continuum of prospector and defender of companies. Higher scores indicate more tendency on prospector. Therefore, results implied that the more companies pursued in prospector strategy, the higher turnaround performance are. Since companies in critical condition need for substantial measures which appropriate and sufficient with their internal problems to catch with external condition, the solution should be authentic. Companies should not imitate competitor's strategy or other companies, but it should design and initiate strategy for solving their problems.

Prospector strategies are more relevant because the nature of the strategy is through initiate innovation regardless of competitor's moves. Prospector oriented companies are market

pioneer that penetrated to market based on their capability. In other hand, defender strategy are more followed oriented moves. Companies implementing defender strategy tend to imitate what their competitor does in the market.

Most studies in strategic leadership found relationship of leader characteristics on strategic choices. However, this study revealed otherwise. There is no relationship from any investigated CEOs characteristics on strategic orientation. This finding implied the decision of using any particular strategy are not determined by leader characteristics. Since turnaround process is a reasonable move as reaction of particular problems, the choices seem clear and more objective than typical logic of filtering process. Another possibility for explaining the finding is nature of turnaround strategy that required company becoming prospector whether it oriented to stabilization or recovery (Lohrke, Bedeian, & Palmer, 2004).

CONCLUSION

This study found direct relationship of CEOs characteristics and turnaround performance. Educational level and tenure in organization have negative impact on performance as well as CEOs with throughput functional background. Conversely, output functional background and tenure in position favors turnaround performance. The study also supported old assumption of relationship between strategy and performance. It implied more prospector oriented a company implementing turnaround, the higher their performance will be.

Against upper echelons theory, this study reveals that CEOs characteristics did not determined strategy orientation. It suggests that filtering process are different under particular circumstance especially in turnaround process. As the company has critical condition, it seems that the limited field of vision explaining in the upper echelons theory focus on solving current problem than setting future direction.

This study was limited to the demographical traits of CEOs that some scholars do not confidence with the logic of proxy. Future study should accommodate psychological dimension in order to seek clear explanation of CEOs and performance relationship under turnaround process. In addition, since this study limited on four years' turnaround, future inquiry should take more range of years in order to identify more convincing pattern of turnaround strategy.

Based on the upper echelons theory suggested to take consideration on leader as team. The finding of this study does not supported CEO's characteristics and strategy orientation, it may cause by the nature of strategic decision process. The process is involved several stages which usually implemented systematically. However, the nature of this process are engaging other member within organization especially top management teams. Many scholars argued that top management team has more variance in explaining organizational performance rather than CEOs as a single leader. Furthermore, top management team helps company to broaden their perspective and rationality that resulted more information into the table.

Another perspective of resources dependent theory seems applicable in understanding turnaround phenomena. Companies in the declining situation usually need to acquire additional resources such as capital, expertise, and political support. Based on the theory, acquisition of person who has power and influence on the relevance resources will improve companies position toward needed resources (Finkeilstein, Hambrick, & Cannella, 2009). Therefore,

successful turnaround strategy may determine by the network of its board of director or board of commissioner.

Unsupported relationship of strategy and performance should be taken into more inquiry fashion. This finding against traditional assumption of strategy and performance relationship. Even though it could be argued that companies in turnaround position are using similar pattern of strategy, consideration of other kind of strategy as mediating variable should be take into account. Moreover, other kind of strategy may more appears as consequences of CEO's characteristic such as porter's generic strategy or other kind of grand strategy.

This study is conducted under specific operational definition of turnaround condition. ROA and free risk were used as basic measurement. Companies who have REO less than standard free risk for two consecutive years, then increasing on the next two consecutive years are included as sample. However, there are another operationalization of turnaround condition. Another study was operationalized turnaround using Altman score of financial distress (Smith & Graves, 2005). Furrer et al, (2007) was defined turnaround from business publication that they seek for companies who mentioned in turnaround or declined position.

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