Stock Market Reaction to the Changes of Corporate Directors

Sorasart Sukcharoensin*

This paper examines the stock market's reactions to the announcements of corporate director changes. In general, there is no significant stock price effects for the appointment or departure of inside directors. Further analyses reveal that additions of independent directors to the firms are beneficial when boards are dominated by a management team or when firms do not voluntarily improve their minimum mandated number of independent directors. Finally, the stock market negatively reacts to the departures of independent directors. The results suggest that independent directors are important in the firm's governance structure, especially for those boards that need outside monitoring.

1. Introduction

The board of directors plays a pivotal role in corporate governance. The primary responsibilities of the board are to provide strategic directions, ratify major corporate decisions, and monitor the management team. Most corporate boards have a mixture of the firm's top executives, and non-executive directors from outside. The inside directors provide valuable information about the firm's activities, while outside directors may contribute their expertise in monitoring the management team.

* National Institute of Development Administration; Tel: (662) 377-7400-19 Ext. 3236; Fax: (662) 249-7371; E-mail: sorasart@nida.nida.ac.th

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Prior works regarding the value of boards are inconclusive. Rosenstein and Wyatt (1990) focus on the stock market reaction to the appointment of outside directors and report a significant increase in stock prices on the day of the announcement when firms appoint additional outside directors for a sample of large US firms. Recently, Lin, Pope, and Young (2003) have examined outside director appointments in the UK and find that shareholders do not benefit from appointing outside directors. Rosenstein and Wyatt (1997) study stock price reaction to appointments of inside directors. In general, they find that stock prices are not significantly different from zero when inside director is added to the board.

The studies in this line of research usually focus on one particular type of director appointment. Doing so, Hermalin and Weisbach (2001) argue that the appointment of corporate board members can simply reflects a value-increasing event associated with director changes, rather than anything in particular about the value of the director's appointment. Also, if the researchers find the evidence of a positive wealth effect of outside director appointments to the firms, it does not imply that the appointment of an insider is harmful to shareholders. If firms adjust their board members to suit their internal needs for human capital or to respond to new challenges, then inside director appointments may also increase shareholder wealth.

Furthermore, most of the studies document the stock market reaction to director appointments using evidence from the US. Understanding how investors in the emerging market view these changes of a particular type of directors are valuable for several reasons. First, the stock price effect of the changes of corporate directors in the emerging market can be different from that of well-developed countries. Second, the board structures are also different. Specifically, boards of directors in the emerging market are numerically dominated by insiders, while the US boards are typically outsider-dominated. Moreover, some exchanges in an emerging market; for example, The Stock Exchange of Thailand, require a

minimum number of independent directors, while there is no such requirement in the well-developed markets.

This study provides evidence on the stock market reaction to the appointments of inside and outside directors in the same study so that unclear effects can be avoided. It also proposes an investigation of how investors respond to the departures of corporate directors, which has never been studied before. Using on a sample of listed firms in Thailand, the results in this study suggest that there is no significant stock price effect of adding inside or outside director to the board.

Additional analyses reveal that additions of independent directors to the firms are valuable for firms whose boards are dominated by the management team or when firms do not voluntarily improve their minimum mandated number of independent directors. Finally, the evidence suggests that the stock market negatively reacts to the event associated with the departures of outside directors. One interpretation of this finding is that the market views their departure as a bad signal for the firm's governance structure. This pattern is also more pronounced when the boards are dominated by the management team or when firms do not voluntarily improve their minimum mandated number of independent directors.

The paper is organized as follows. Section 2 provides theoretical background and develops hypotheses. Section 3 describes the sample selection procedure and research methods. Empirical results are presented in Section 4 and Section 5 address the limitations of the study and future research. Section 6 concludes.

2. Theory and Hypothesis

2.1 Inside Directors and the Announcement Effect

The effective decision-making hypothesis contends that inside directors provide useful information of the firm's operations in developing business strategies (Fama and Jensen, 1983). This

hypothesis predicts that the stock market considers the announcement of inside directors as a sign of improvement. Therefore, the market will positively react to the addition of inside directors onto the corporate board. Consistent with this view, Furtado and Rozeff (1987) study the wealth effect of the announcements of internal promotions and find a positive reaction to top executive appointments into the firms.

However, the presence of top management on the board may lead to collusion and wealth expropriation (Fama, 1980). The entrenchment hypothesis argues that inside directors can be added to corporate boards to ensconce the incumbent management team. Weisbach (1988) notes that inside directors are less likely than outside directors to challenge the incumbent CEOs to whom their careers are tied. They also have incentives to protect any above-market compensation or excess non-pecuniary benefits that they receive through their positions as managers. Therefore, under this view, the investors will negatively react to the addition of inside directors onto the corporate board.

The two alternative arguments can be formally tested against the following null hypothesis.

H1: There is no announcement effect of appointing inside director to the board.

In sum, the existing literature on inside director appointments assume that the market positively views the events that are associated with efficient decision making to shareholders and react negatively to the events that associate with managerial entrenchment. If this is in fact the case, and the investors are rational, then the departure of the inside director might create the opposite response under each hypothesis.

Some studies on management turnover also suggest otherwise that the market views management turnover as a sign of corporate improvement and agency cost reduction (Warner, Watts, and Wruck,

1988; Weisbach, 1988; Denis and Denis, 1995). If the purpose of having inside directors on the board is to endorse the managerial decision, then the stock market will react favorably to the announcements of insider departure. The market will treat these announcements as events that are associated with a reduction in the firm's agency problems.

In contrast, several studies support this argument that there is a significantly negative stock price effect of top executive departure announcements (Furtado and Karan, 1985; Gilson, 1989). These prior works suggest that the stock market views the inside director departure to be unfavorable. If the purpose of having inside directors on the board is to strengthen the firm's decision-making process, then the stock market will react negatively to the announcements of insider departures. The market will treat these announcements as events that are associated with a symptom of corporate problem or evidence of poor performance.

Therefore, these two arguments can be tested against the following null hypothesis.

H2: There is no announcement effect of inside director departure from the board.

2.2 Independent Outside Directors and the Announcement Effects

One responsibility of outside directors is to monitor the management's activities. The incentive-alignment hypothesis suggests that outside directors are valuable to the firms. Several studies support this view that outside directors are more vigilant in replacing poor management, monitoring managerial behavior, and protecting investor capital (Weisbach, 1988; Brickley, Coles, and Terry, 1994; Rosenstein and Wyatt, 1990).

Contrary to the argument that outside director incentives are aligned with those of shareholders, several critics have argued that

outside directors will not necessarily act in shareholder interests. Mace (1986) finds that management generally dominates the board by the selection of friendly outsiders. If the top management's incentives are not aligned with those of shareholders, they may nominate outside directors who are more inclined to support their decisions.

Consequently, if investors view the purpose of having outside directors on the board as to avoid scrutiny or endorse the firm's incumbent management, then the stock market will react negatively to the announcements of outside director appointments.

Therefore, these two arguments can be tested against the following null hypothesis.

H3: There is no announcement effect of appointing independent outside directors to the board.

Previous works on outside directors suggest that the stock market positively views the events that are associated with incentive alignment to shareholders or those that improve the governance process of the firm. The stock market also negatively reacts to those announcements of adding outside directors to lower board effectiveness or entrench the management of the firms. Therefore, the departure of outside directors should create the opposite response under each hypothesis.

If outside directors are perceived as improving the governance process of the firm, then outside director departures should signal an adverse effect on shareholder wealth. Therefore, the incentive-alignment hypothesis predicts a negative stock price effect of outside director departures.

On the other hand, if outside directors are appointed to endorse the management's decision, the stock market should view outside director departures as favorable events and should be associated with an increase in shareholder wealth.

Therefore, these two arguments can be tested against the

following null hypothesis.

H4: There is no announcement effect of independent outside director departures from the board.

3. Data and Research Methods

3.1 Sources of Data

This study investigates the stock price effect of the appointment and departure of corporate directors for listed companies in the Stock Exchange of Thailand (SET) between July 1997 and December 2000. The information on the announcements concerning director changes is obtained from the news section of the I-SIMS database. This source contains news and announcements of director nominations or departures of the listed firms in the SET.

Information concerning the background of directors is collected from the disclosure Form 56-1. This disclosure form contains information of directors such as their past experience, current professional affiliation, and relationship with the firms. The stock price information and the SET index are obtained from the I-SIMS database and DATASTREAM, respectively.

3.2 Sample Selection Procedure

The sample selection starts with a search for the announcement date of director changes in the I-SIMS database. The announcement date [0] is defined as the earliest public disclosure of the announcement of director change appearing in the company news section of the I-SIMS database. The announcement should include the director's name, announcement date, and other information of the firm.

Second, the sample is restricted to those non-financial listed firms. One reason is that most announcements concerning director changes in financial firms are board changes resulting from corpo-

rate restructuring or significant ownership structure changes after the financial crisis in July 1997. Many of them are either contaminated with other corporate restructuring announcements or accompanied with multiple types of director changes.

Another reason is that financial companies are subject to different sets of monitoring mechanisms, which may have effects on the analysis (Booth, Cornett, and Tehranian, 2002). One example is the externally imposed scrutiny from organizations such as the Bank of Thailand and the interference from the government.

Third, the sample is separated into two groups: appointment and departure. The announcement is eliminated if it contains two events at the same time since it is less clear-cut which type of board turnover dominates the stock price effects.

Then, to minimize contemporaneous effects of other events contamination, announcements are eliminated if the news item is surrounded by information about mergers, corporate restructuring, earnings, dividends, or other announcements that could affect shareholder wealth. Since these confounding events may obscure the effect of the interest in the event, these contemporaneous announcements are excluded over the five trading days before and after the announcement date.

Next, the names of all directors are recorded for each announcement from the I-SIMS database between 1997 and 2000. Directors are classified according to their professions and business relationships with the firm. Inside directors are current employees of the firm. Independent outside directors have no affiliation with the firm beyond being members of the firm's board and holding less than 0.5% of outstanding shares.[1] Affiliated or gray directors are former employees, relatives of the CEOs or directors that have significant transactions or business relationships with the firm. The examples are the firm's former employees, relatives of top

[1] See the SET (1998) regulation about the qualification of outside director (Items 3(1) and (2), respectively).

management, or those having business relationships with the firm, etc.

The sample includes those announcements where only one type of director is added or departs the company. This allows focusing on the market reaction to the appointments or departures of a specific kind of director and eliminates confounding events induced by multiple types of director announcements. Announcements relating to multiple types of directors usually coincide with regular board meetings, which are usually contaminated with other board resolution announcements.

Finally, announcements are also eliminated if they do not have sufficient stock return data over the period from 170 days before through 20 days before the announcement date. These selection criteria result in clean samples of 27 appointments of inside directors, 116 appointments of outside directors, 50 news items associated with inside director departures, and 88 observations of outside director departures as shown in Table 1.

Table 1 Frequency Distribution of Announcements by Year

	1997	1998	1999	2000	Total
Inside director appointments:					
Frequency	3	3	11	10	27
(%)	(11.11%)	(11.11%)	(40.74%)	(37.04%)	(100.00%)
Inside director departures:					
Frequency	10	9	15	16	50
(%)	(20.00%)	(18.00%)	(30.00%)	(32.00%)	(100.00%)
Outside director appointments:					
Frequency	6	19	71	20	116
(%)	(5.17%)	(16.38%)	(61.21%)	(17.24%)	(100.00%)

Table 1 Frequency Distribution of Announcements by Year (continued)

	1997	1998	1999	2000	Total
Outside director departures:					
Frequency	16	15	28	29	88
(%)	(18.18%)	(17.05%)	(31.82%)	(32.95%)	(100.00%)
Total	**35**	**46**	**125**	**75**	**281**

Source: The information employed in this study is obtained from the company news section in the I-SIMS (Integrated SET Information Management System) CD-Rom provided by the Stock Exchange of Thailand.

The reason that there are less announcements concerning inside directors is that management usually does not departs the board frequently. Any inside director changes are generally made during the annual board meeting when several issues have been announced such as dividend or earning announcements (Dedman and Lin, 2002).

3.3 Statistical Methods

The standard event study methodology is employed to measure abnormal returns (Brown and Warner, 1985). The magnitude of the abnormal performance around the time of the announcements is a measure of how investors anticipate changes in corporate governance structure of that particular firm.

For each announcement, the 150-trading-day period [-170, -21] prior to the event window is used as the estimation window for parameter estimations. The market model is estimated by running a regression for the days in this period. The more days used in estimating the regression, the better the asymptotic property of the regression results. However, this gain in efficiency should be traded off with a lower number of data due to missing stock returns. Therefore, this study uses 150 trading days prior to the window period as the

parameter estimation of the market model in the same fashion of Rosenstein and Wyatt (1990, 1997) and Lin et al. (2003).

$$R_{it} = \alpha_i + \beta_i R_{mt} + \varepsilon_{it} \quad (1)$$

R_{it} is the continuous compound return for stock i at time t, R_{mt} is the continuously compounded return on the SET index over the same day, serving as the market index, and ε_{it} is the zero mean disturbance term. The parameter estimates of $\hat{\alpha}_i$ and $\hat{\beta}_i$ from the market model are used to obtain predicted returns.

$$\hat{R}_{it} = \hat{\alpha}_i + \hat{\beta}_i R_{mt} \quad (2)$$

Next, the residual, r_{it}, for each day for each firm is calculated. The abnormal return, r_{it}, for firm i at time t is the difference between the actual continuously compounded return for firm i at time t, R_{it}, and the expected return for that period based on the estimated market model parameters, $\hat{R}_{it}$. It represents the abnormal return, that is, the part of the return that is not predicted and is, therefore, an estimate of the change in the firm's value on that particular day, which is caused by the event.

$$r_{it} = R_{it} - \hat{R}_{it} \quad (3)$$

The abnormal returns for each observation are averaged across firms to produce the average abnormal return for that day, AR_t, where n is number of firms in the sample.

$$AR_t = \frac{\sum_j r_{it}}{n} \quad (4)$$

The cumulative abnormal return (CAR) is calculated as the sum of the abnormal returns over the announcement period from a to b. The cumulative average residual represents the average total

effect of the event across all firms over a specified time interval. It is possible that the information regarding director changes may be available to the market on the day before the announcement date or the day following the announcement date. Therefore, I calculate the cumulative abnormal return over the two-day announcement period [-1, 0] and [0, +1]. In addition, I also compute *AR* and *CAR* for various intervals within the period [-5, +5] to assess the overall trend of the market reaction around the announcement.

$$CAR = \sum_{t=a}^{b} AR_t \tag{5}$$

The corresponding test statistic involving the cumulative abnormal return is based on the following *t*-statistic for each event window. For the degree of freedom above 30, the *t*-statistic in Equation (6) has, approximately, a standard normal distribution. This statistic tests the null hypothesis that the residual for a single firm is equal to zero. Intuitively, it is the comparison between the values of the residual to its estimated sample standard deviation (Brown and Warner, 1985).

Only if this ratio is greater than a specified critical value can the researcher reject the null hypothesis with some degree of confidence. For instance, if the ratio is greater than 2.58 or 1.96, then the null hypothesis is rejected at 1% and 5% confidential level, respectively. However, when the ratio is greater than 1.65 but less than 1.96, it is interpreted that there is mild evidence to reject the null hypothesis. However, the conclusion based on the 10% confidential level alone should be cautiously interpreted. It should be inferred in accordance with other window periods being investigated in the study for more insightful meanings.

$$t = \frac{CAR}{\sum_{t=a}^{b} \hat{S}(AR)} \tag{6}$$

The degrees of freedom are 149 and the estimated standard

deviation of the average residuals, $\hat{S}(AR)$, for firm j using data from the estimation period is defined as:

$$\hat{S}(AR) = \left[\frac{1}{149} \sum_{t=-170}^{-21} \left[AR_t - \overline{AR_t} \right]^2 \right]^{1/2} \quad (7)$$

The same 150 trading days prior to the window period, [-170, -21], is also used as the number of observations to calculate the degree of freedom for the estimated standard deviation of the average abnormal return, , for consistency.[2]

4. Event Study Results

To differentiate the stock price effects of the changes of corporate directors, the results are reported separately for each type of director appointment and departure in Table 2 to 5. Table 2 reports the stock market response to the announcement of inside director appointments onto the corporate boards. The stock market responses to the announcements of inside director departures from the corporate boards are reported in Table 3. Next, the cumulative abnormal returns and the test statistic at the announcements of outside director appointments are reported in Table 4. Lastly, the stock price effects of the announcements involving outside director departures are reported in Table 5.

For the entire sample, the results in Panel A of Table 2 reveal that the cumulative abnormal returns are not statistically significant from zero. Next, two board characteristics are used, the minimum mandate number of independent directors and whether the management team holds more than 50% of the board seats. The results are also unaffected by any subsample analysis when the samples are

[2] A test based on 200 trading days is also performed and the results do not change significantly.

categorized by the firm's board structure as reported in Panel B and C of Table 2 and the cumulative abnormal returns of these two board characteristics are also graphed in Panel A and B of Figure 1.

The evidence suggests that there is no benefit or signal associated with the appointment of inside directors onto corporate boards. This is consistent with the Rosenstein and Wyatt (1997) findings that any gain in board effectiveness or efficiency offset the potential costs of managerial entrenchment.

Table 2 Inside Director Appointments

	Announcement Period Windows						N
	[-1,0]	[0]	[0,1]	[-1,1]	[-2,2]	[-5,5]	
Panel A: Cumulative abnormal returns for the full sample							
Full sample	0.008 (0.589)	0.003 (0.308)	0.000 (-0.007)	0.005 (0.297)	-0.004 (-0.207)	0.019 (0.641)	27
Panel B: Cumulative abnormal returns for the subsamples partitioned by the minimum number of independent directors required by the SET							
Firm that voluntarily improve thier minimum mandated number of independent directors	0.003 (0.169)	-0.005 (-0.476)	-0.002 (-0.153)	0.006 (0.288)	0.002 (0.073)	0.029 (0.775)	16
Firm that do not voluntarily improve thier minimum mandated number of independent directors	0.014 (0.866)	0.015 (1.246)	0.003 (0.201)	0.003 (0.152)	-0.013 (-0.491)	0.004 (0.113)	11
Difference	-0.012 (-0.588)	-0.020 (-1.263)	-0.006 (-0.253)	0.003 (0.067)	0.015 (0.425)	0.025 (0.408)	

Table 2 Inside Director Appointments (continued)

	Announcement Period Windows						N
	[-1,0]	[0]	[0,1]	[-1,1]	[-2,2]	[-5,5]	
Panel C: Cumulative abnormal returns for the subsamples partitioned by the management-dominated board							
Management-dominated boards	0.021 (1.115)	0.016 (1.180)	0.013 (0.687)	0.019 (0.790)	0.025 (0.811)	0.034 (0.767)	10
Nonmanagement-dominated boards	-0.001 (-0.040)	-0.005 (-0.441)	-0.008 (-0.493)	-0.004 (-0.181)	-0.021 (0.833)	0.010 (0.272)	17
Difference	0.022 (0.909)	0.021 (1.204)	0.021 (0.845)	0.022 (0.737)	0.046 (1.150)	0.024 (0.443)	

The cumulative abnormal returns for appointments of the firm's inside directors are presented. The *t*-statistics are reported in the parentheses.

Table 3 reports the stock market response to the announcements of inside director departures from the corporate boards. In general, there is no significant announcement effect of inside director departures from the board. Again, any gain in inside director effectiveness offset the potential costs of managerial entrenchment, resulting in an insignificant gain or loss on shareholder wealth. The results persist when partitioning the sample by previous board characteristics as shown in Panel B and C of table 3 and Panel A and B of the Figure 2.

Table 3 Inside Director Departures

	Announcement Period Windows						N
	[-1,0]	[0]	[0,1]	[-1,1]	[-2,2]	[-5,5]	
Panel A: Cumulative abnormal returns for the full sample							
Full sample	-0.003	-0.004	0.000	0.002	-0.008	0.027	50
	(-0.313)	(-0.666)	(0.028)	(0.152)	(-0.560)	(1.212)	
Panel B: Cumulative abnormal returns for the subsamples partitioned by the minimum number of independent directors required by the SET							
Firm that voluntarily improve thier minimum mandated number of independent directors	-0.006	0.001	0.015	0.009	-0.002	0.023	16
	(-0.323)	(0.078)	(0.888)	(0.416)	(-0.087)	(0.554)	
Firm that do not voluntarily improve thier minimum mandated number of independent directors	-0.002	-0.007	-0.007	-0.002	-0.011	0.029	34
	(-0.149)	(-0.856)	(-0.591)	(-0.110)	(-0.611)	(1.067)	
Difference	-0.004	0.008	0.022	0.010	0.009	-0.007	
	(-0.182)	(0.548)	(1.066)	(0.405)	(0.274)	(-0.147)	
Panel C: Cumulative abnormal returns for the subsamples partitioned by the management-dominated board							
Management-dominated boards	-0.019	-0.008	-0.003	-0.014	-0.027	0.014	16
	(-1.247)	(-0.738)	(-0.173)	(-0.733)	(-1.115)	(0.398)	
Nonmanagement-dominated boards	0.004	-0.003	0.002	0.009	0.000	0.033	34
	(0.365)	(-0.336)	(0.132)	(0.599)	(0.005)	(1.157)	
Difference	-0.023	-0.005	-0.004	-0.023	-0.027	-0.019	
	(-1.234)	(-0.419)	(-0.218)	(-0.944)	(-0.923)	(-0.326)	

The cumulative abnormal returns for departures of the firm's inside directors are reported. The *t*-statistics are in the parentheses.

Table 4 reports the cumulative abnormal return and the test statistic at the announcements of outside director appointments. The cumulative abnormal return for all samples is not statistically different from zero as shown in Panel A of the table. However, when the sample is categorized according to its board structure, the results are statistically meaningful for firms with management-dominated boards and for those who maintain or have less outside directors than the minimum mandate.

As shown in Panel B of the table, the cumulative abnormal return for firms that do not voluntarily improve their minimum mandated number of independent directors is 1.7% at the announcement date. The return is statistically significant at the conventional level. The two-day cumulative abnormal returns of outside director appointments from the announcement date to one day after the announcement date. The return of 1.9% is statistically significant at the 10% level. Panel A of Figure 3 confirms the results. The cumulative abnormal returns of outside director appointments for non-voluntary group are below the voluntary firms from five days before the announcement date to one day after the announcement date.

Announcements associated with firms with management-dominated boards have a statistically significant cumulative abnormal return of 2.1% at the announcement date and a two-day cumulative abnormal return of 2.9%. Both are statistically different from zero at the 10% level as shown in Panel C of Table 4. The cumulative abnormal returns of both groups are presented in Panel B of Figure 3. The picture shows a sharp drop in the cumulative abnormal returns of the management-dominated firms cumulative abnormal return from five days before the announcement date to one day after the announcement date. A small recovery takes place a few days after the announcement date. However, such recovery is followed by a strong decline eventually.

Overall, the evidence in this table supports the balanced board concept that an effective board should be a mixture of inside and

outside directors. If a balanced board is valuable, then firms adding outside directors to firms with a low number of outside directors or to an insider-dominated board will benefit the firm (Mace, 1986; West, 1985).

Table 4 Outside Director Appointments

	Announcement Period Windows						N
	[-1,0]	[0]	[0,1]	[-1,1]	[-2,2]	[-5,5]	
Panel A: Cumulative abnormal returns for the full sample							
Full sample	0.003	0.008	0.002	-0.002	-0.008	0.023	27
	(0.348)	(1.273)	(0.280)	(-0.221)	(-0.599)	(-1.176)	
Panel B: Cumulative abnormal returns for the subsamples partitioned by the minimum number of independent directors required by the SET							
Firm that voluntarily improve thier minimum mandated number of independent directors	-0.005	-0.001	-0.013	-0.017	-0.012	-0.011	60
	(-0.451)	(-0.115)	(-1.237)	(-1.312)	(-0.712)	(-0.457)	
Firm that do not voluntarily improve thier minimum mandated number of independent directors	0.011	0.017**	0.019*	0.013	-0.004	-0.036	56
	(0.984)	(2.074)	(1.659)	(0.960)	(-0.217)	(-1.357)	
Difference	-0.016	-0.018	-0.032**	-0.030	-0.008	0.025	
	(-1.021)	(-1.571)	(-2.053)	(-1.602)	(-0.339)	(0.659)	
Panel C: Cumulative abnormal returns for the subsamples partitioned by the management-dominated board							
Management-dominated boards	0.009	0.021*	0.029*	0.016	0.017	-0.048	28
	(0.538)	(1.867)	(1.788)	(0.821)	(0.665)	(-1.277)	
Nonmanagement-dominated boards	0.001	0.003	-0.006	-0.016	-0.009	-0.015	88
	(0.131)	(0.537)	(-0.682)	(-1.150)	(-0.563)	(-0.756)	

Table 4 Outside Director Appointments (continued)

	Announcement Period Windows						N
	[-1,0]	[0]	[0,1]	[-1,1]	[-2,2]	[-5,5]	
Difference	0.007	0.018	0.034*	0.032	0.026	-0.032	
	(0.404)	(1.362)	(1.892)	(1.280)	(0.856)	(-0.741)	

The cumulative abnormal returns for appointments of the firm's independent directors are presented. The *t*-statistics are in parentheses. ** Significant at the 0.05 level. * Significant at the 0.10 level.

The stock price effects of the announcements involving outside director departures are reported in Table 5. For full sample in Panel A of, cumulative abnormal returns are negative for most event windows, suggesting that the stock market perceives the positive value of outside directors and reacts negatively when outside directors leave the board.

In other words, the announcements of outside director departures in general have a negative effect on shareholder wealth. In the subsample analysis, the significant cumulative abnormal return is about -3% for event window period from one day preceding the announcement date to one day after the announcement date for firms that do not voluntarily improve their minimum mandated number of independent directors required by the SET as shown in Panel B of Table 5. For event window period from two days preceding the announcement date to two days after the announcement date, the cumulative abnormal return is -3.2%. Finally, the cumulative abnormal return is -1.9% for event window period from one day preceding the announcement date to the announcement date. Panel A of Figure 4 captures a similar negative pattern here.

As reported in Panel C of Table 5, the cumulative abnormal returns for management-dominated subsample are negative and statistically significant in most event windows, while the cumulative abnormal returns for nonmanagement-dominated boards are negative, but not significant. The cumulative abnormal returns are

-1.1% for event widow period from the announcement date to the day after, -1.9% for one day before and after the announcement date, 2.5% for event period two days before or after the announcement date, and 3.4% for event period five days before or after the announcement date. The cumulative abnormal returns are plotted in Panel B of Figure 4. For this illustrative sample, both sample groups have a negative trend, but the cumulative abnormal returns of the management-dominated samples are much lower.

Table 5 Independent Director Departures

	Announcement Period Windows						N
	[-1,0]	[0]	[0,1]	[-1,1]	[-2,2]	[-5,5]	
Panel A: Cumulative abnormal returns for the full sample							
Full sample	-0.012*	-0.005	-0.011	-0.018**	-0.025**	-0.028*	88
	(-1.672)	(-0.943)	(-1.474)	(-2.024)	(-2.185)	(-1.669)	
Panel B: Cumulative abnormal returns for the subsamples partitioned by the minimum number of independent directors required by the SET							
Firm that voluntarily improve thier minimum mandated number of independent directors	-0.007	-0.003	-0.005	-0.009	-0.020	-0.019	50
	(-0.786)	(-0.430)	(-0.547)	(-0.841)	(-1.476)	(-0.927)	
Firm that do not voluntarily improve thier minimum mandated number of independent directors	-0.019*	-0.008	-0.018*	-0.030**	-0.032*	-0.041	38
	(-1.728)	(-0.988)	(-1.671)	(-2.204)	(-1.803)	(-1.580)	
Difference	0.012	0.005	0.014	0.021	0.012	0.022	
	(0.786)	(0.462)	(0.900)	(1.109)	(0.389)	(0.582)	

Table 5 Independent Director Departures (continued)

	Announcement Period Windows						N
	[-1,0]	[0]	[0,1]	[-1,1]	[-2,2]	[-5,5]	
Panel C: Cumulative abnormal returns for the subsamples partitioned by the management-dominated board							
Management-dominated boards	-0.010	-0.002	-0.011*	-0.019**	-0.025**	-0.034**	71
	(-1.506)	(-0.519)	(-1.684)	(-2.305)	(-2.364)	(-2.143)	
Nonmanagement-dominated boards	-0.020	-0.014	-0.007	-0.013	-0.023	-0.004	17
	(-0.979)	(-1.016)	(-0.363)	(-0.509)	(-0.724)	(-0.079)	
Difference	0.010	0.012	-0.004	-0.007	-0.002	-0.030	
	(0.218)	(0.685)	(-0.414)	(-0.556)	(-0.389)	(-0.871)	

The cumulative abnormal returns for departures of the firm's independent directors are presented. The *t*-statistics are in parentheses. ** Significant at the 0.05 level. * Significant at the 0.10 level.

5. Future Research

The stronger and more insightful contributions may be achieved if one can get more detailed information on director quality and substitutions. One limitation of this study is that it assumes each director have similar qualities. In fact, there may be a different director qualities effect among the board members. Directors must also possess the necessary time, expertise, and incentives to carry out their board duties effectively.

Furthermore, director replacement is also important; for example, the implications for the appointment of new directors who replace either inside or independent directors may be different as well. As a result, the stock market response for such announcements may be dissimilar.

However, the Stock Exchange of Thailand does not require the listed firms to disclose such information. Therefore, with this

limitation, the results in this study can be extended in future research when the disclosure quality for the listed firms improves. This will enable us to differentiate the impact of corporate director changes, accordingly.

6. Conclusions

This study examines the stock price reaction to inside and outside director changes on the day around the announcements. In general, there is no significant stock price effect for the appointment of executives onto the corporate board. In addition, the cumulative abnormal returns for inside director departures are also insignificantly different from zero

The stock market reaction to outside director appointments for the full samples is indistinguishable from zero. In the subsample, however, the market perceives additions of outside directors onto corporate boards as value enhancing for firms that do not voluntarily improve their minimum mandated number of outside directors and firms with management-dominated boards.

Finally, the evidence suggests that the stock market reacts negatively when firms release the news of outside director departures to the public. The results imply that costs associated with outside directors leaving the boards of directors outweigh the benefits. Moreover, these costs are more pronounced for firms that do not voluntarily improve their minimum mandated number of outside directors and firms with management-dominated boards. Overall, the results in this study indicate that monitoring the value of the outside directors is important in the firm's governance structure, especially for those boards that need outside monitoring.

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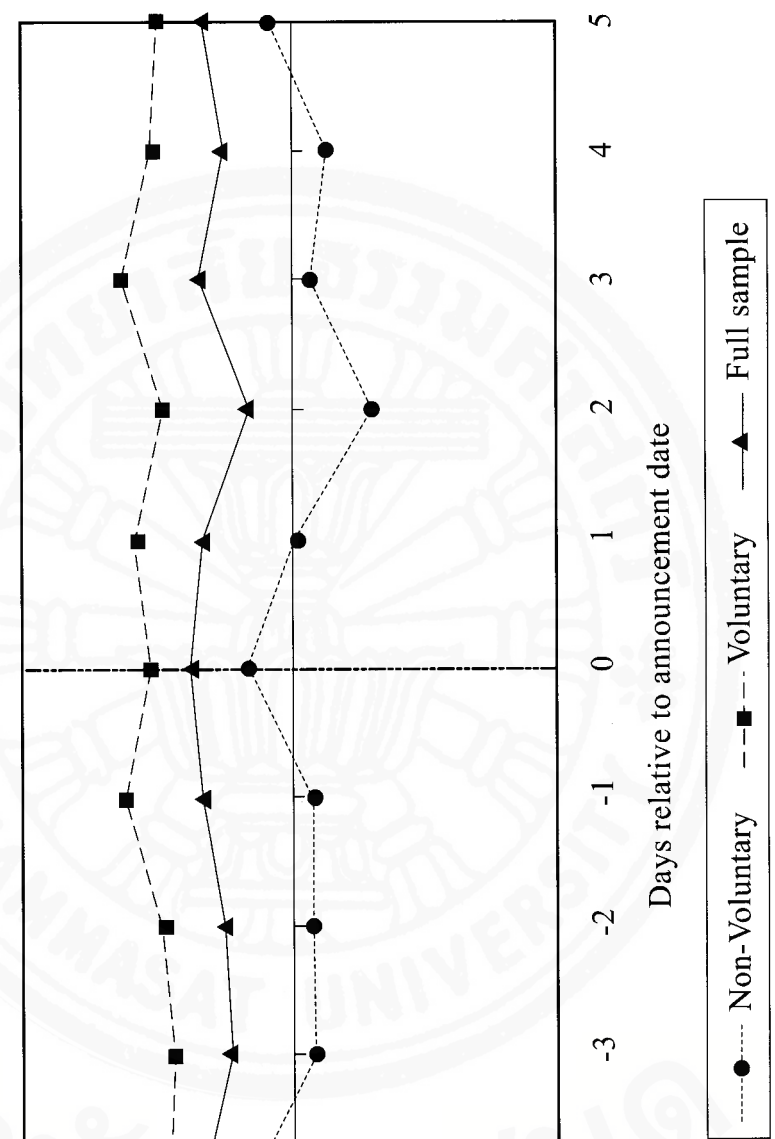
Figure 1 Inside Director Appointments

Panel A. Cumulative abnormal returns for the subsamples partitioned by the minimum number of independent directors



Panel B. Cumulative abnormal returns for the subsamples partitioned by the management-dominated board

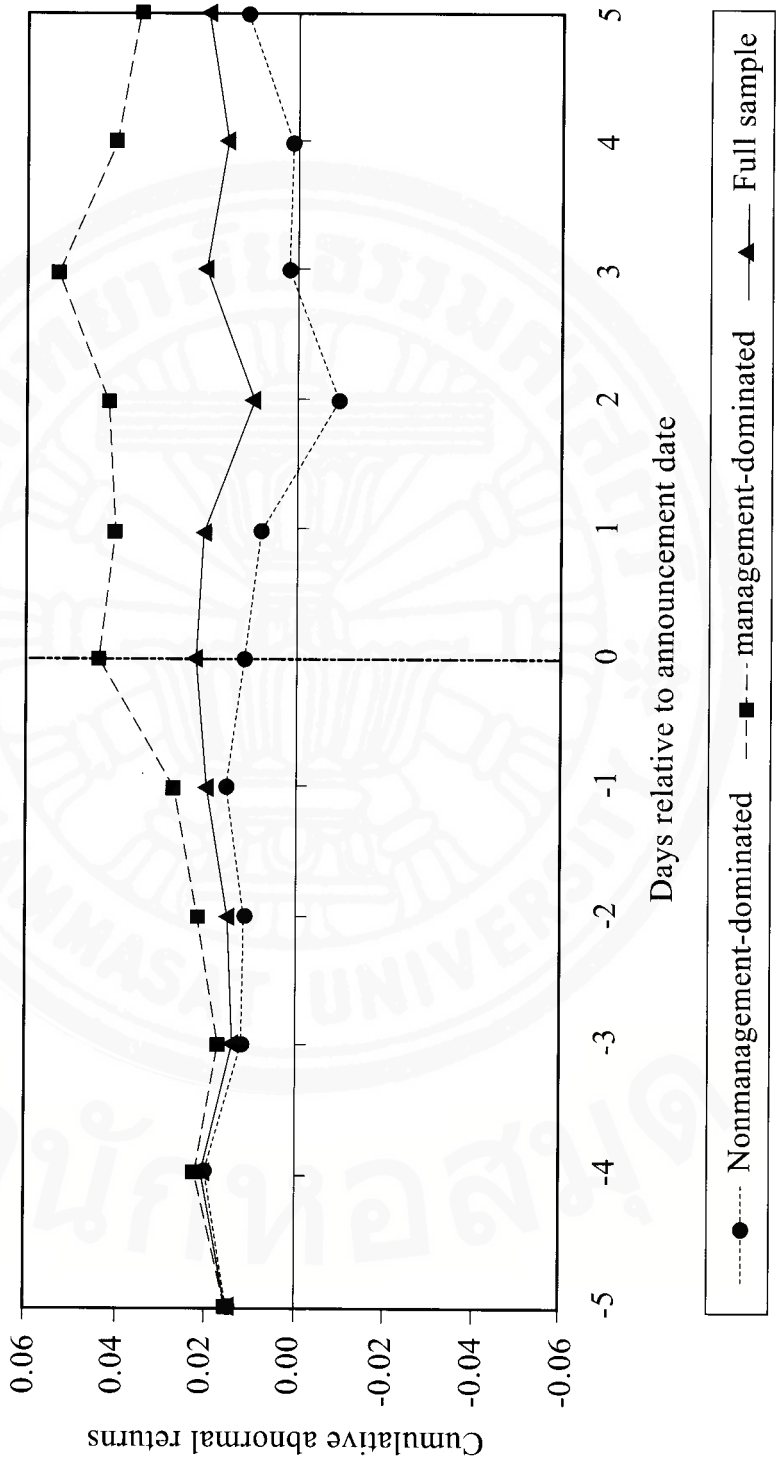
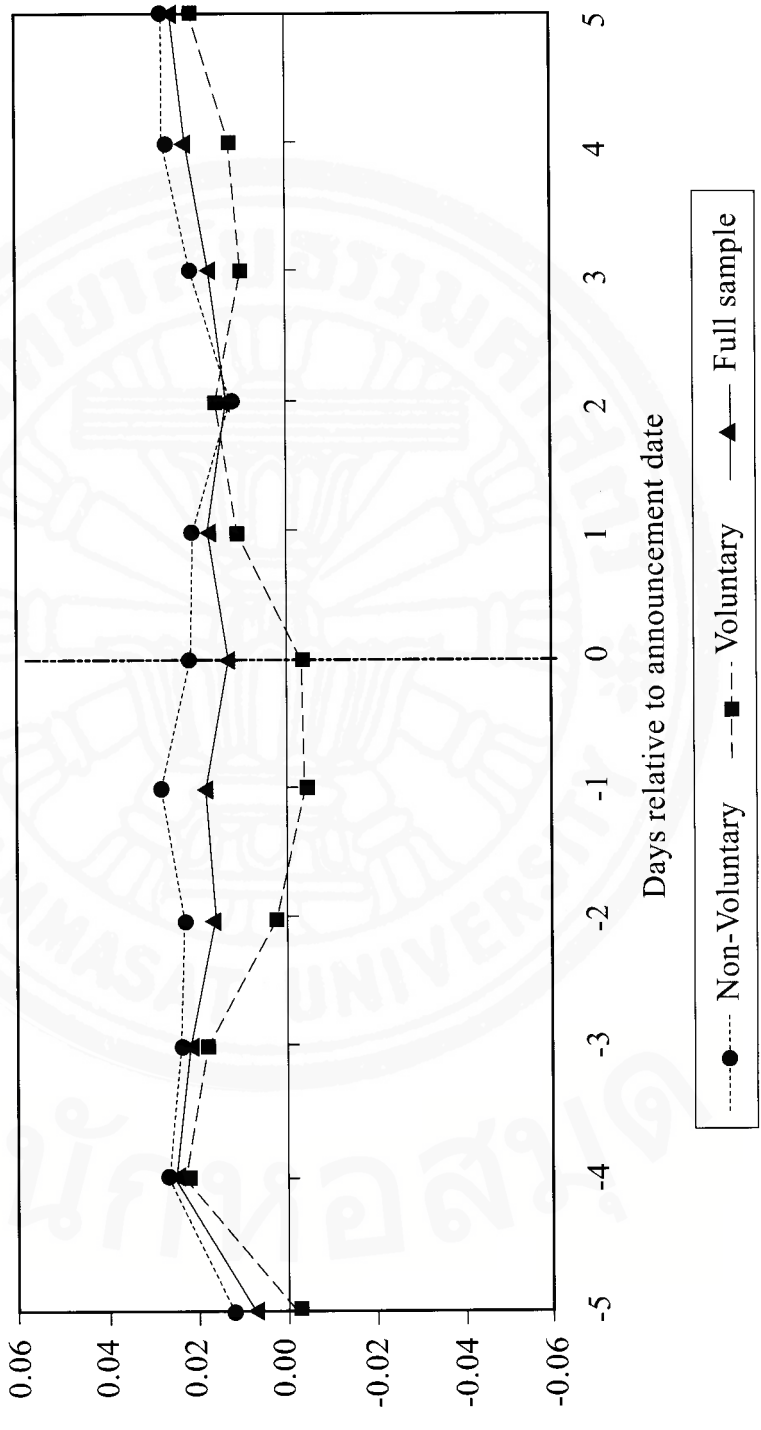


Figure 2 Inside Director Departures

Panel A. Cumulative abnormal returns for the subsamples partitioned by the minimum number of independent directors



Panel B. Cumulative abnormal returns for the subsamples partitioned by the management-dominated board

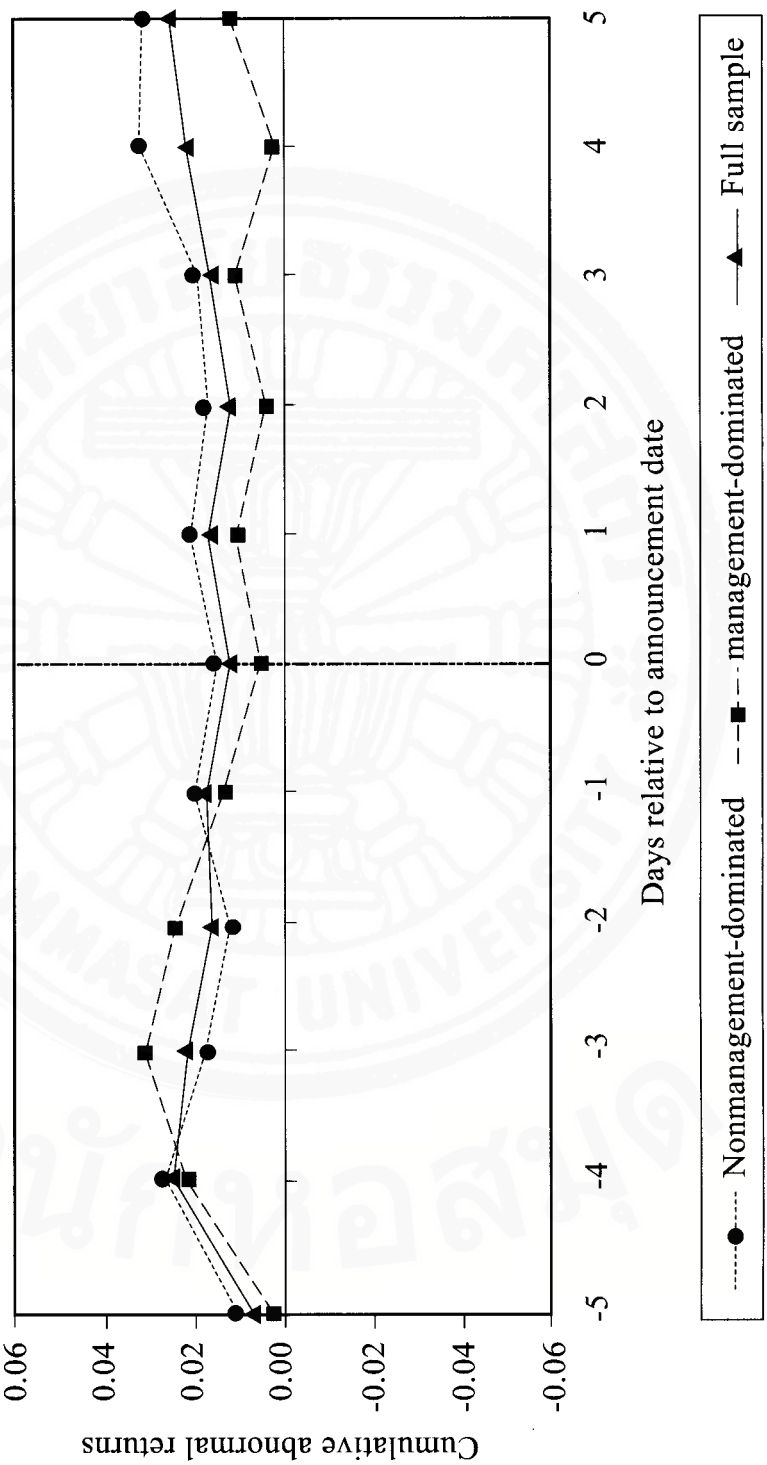
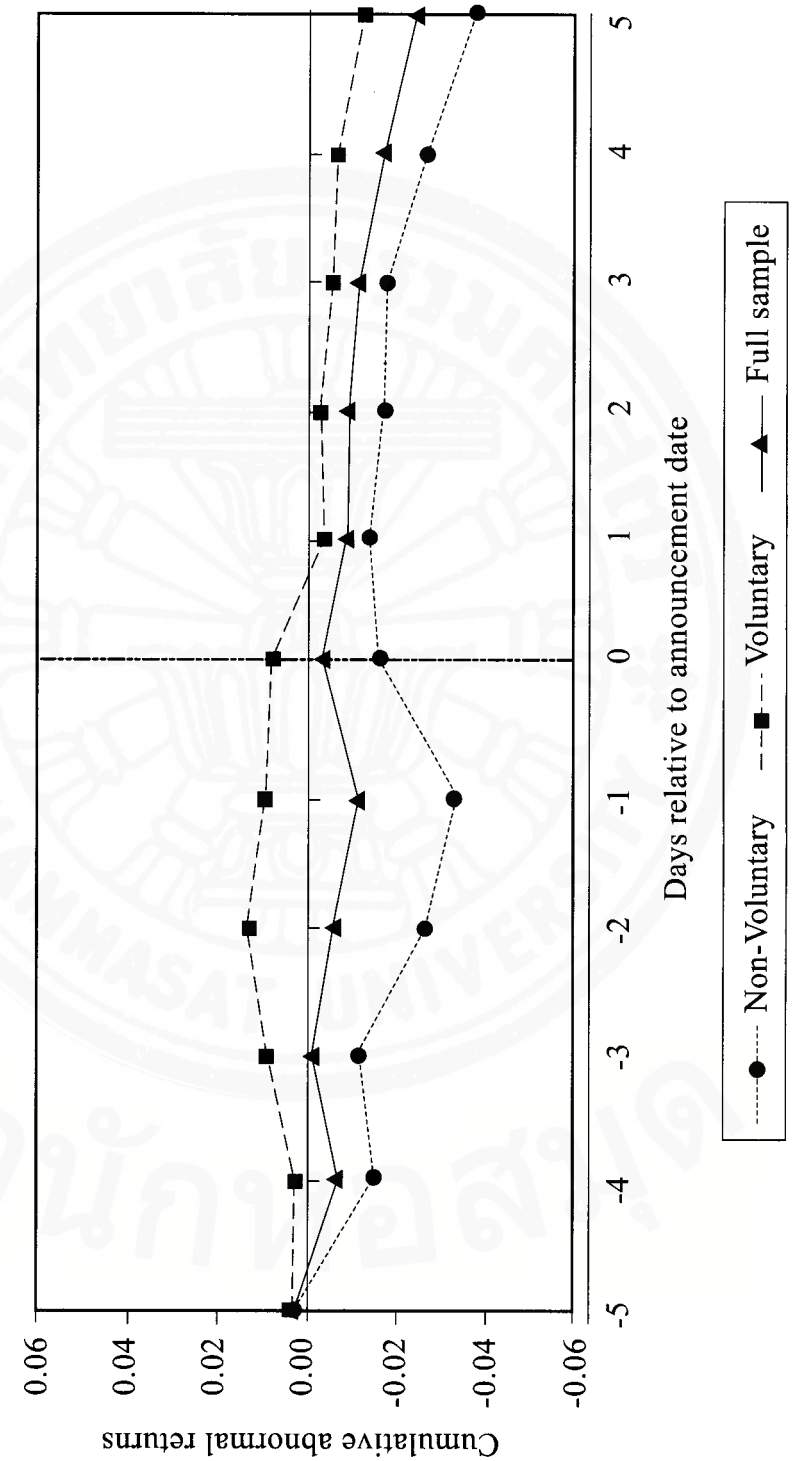


Figure 3 Outside Director Appointments

Panel A. Cumulative abnormal returns for the subsamples partitioned by the minimum number of independent directors



Panel B. Cumulative abnormal returns for the subsamples partitioned by the management-dominated board

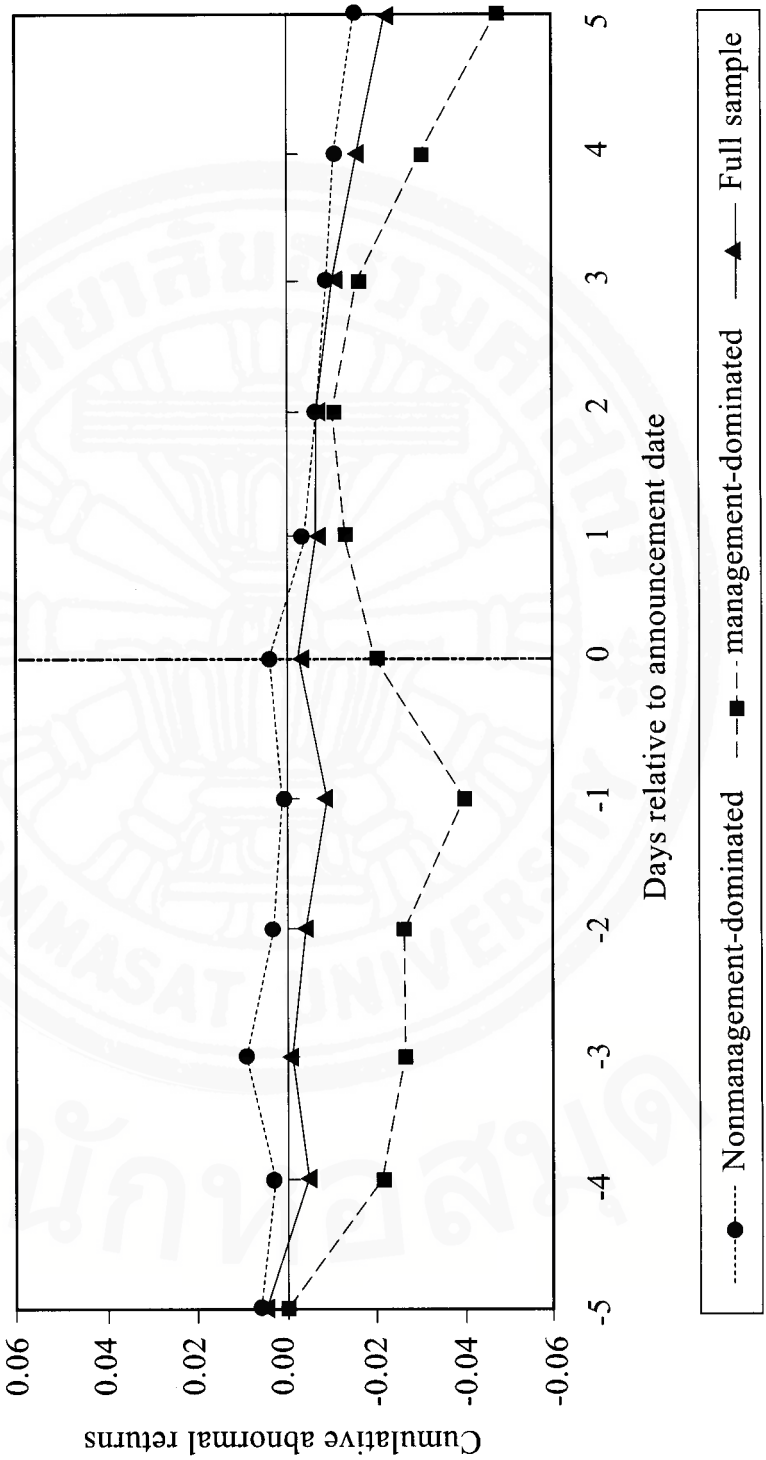
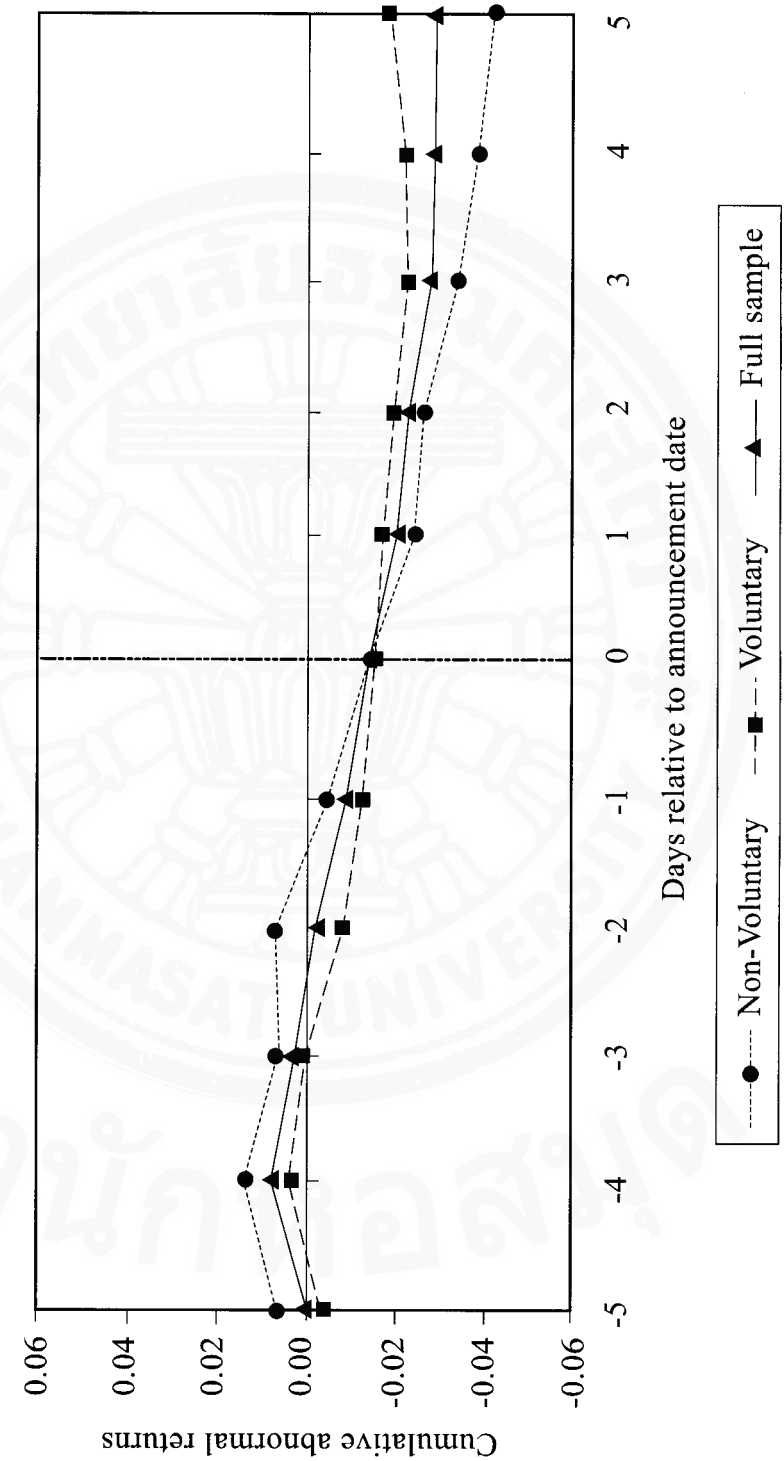


Figure 4 Independent Director Departures

Panel A. Cumulative abnormal returns for the subsamples partitioned by the minimum number of independent directors



Panel B. Cumulative abnormal returns for the subsamples partitioned by the management-dominated board