

**Asian Finance Association 2009 International Conference**

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### **Monitoring Managers: Does it Matter?**

#### **Abstract**

We test the main predictions of principal-agent theory by examining under what circumstances boards discipline managers and whether such interventions improve performance. We exploit exogenous variation due to the staggered adoption of corporate governance laws across countries coupled with detailed "soft" information about management actions, competence, and shareholder interventions in a large sample of companies between 1993 and 2008. We find that when given the legal power to do so, boards fire CEOs in response to poor performance, especially if they hold the CEO responsible for the poor performance or have come to view him as incompetent. Consistent with agency models, we find that CEOs are not fired when performance deteriorates due to factors beyond their control. Following forced management turnover, companies see performance improvements and their investors are considerably more likely to eventually sell them at a profit. Our results suggest that a shareholder-friendly legal framework coupled with the presence of large minority shareholders can improve performance.