Tourism Management Perspectives 18 (2016) 111–117

Contents lists available at ScienceDirect

Tourism Management Perspectives

journal homepage: www.elsevier.com/locate/tmp

Determinants of CEO strategic risk-taking in the airline industry

Won Seok Lee [a], Joonho Moon [b,*]

[a] BK21 Plus Research Associate, Department of Convention Management, Kyung Hee University, 26, Kyungheedae-ro, Dongdaemun-gu, Seoul 130-701, Republic of Korea
[b] Department of Tourism Administration, Kangwon National University, Hyoja2-Dong, Kangwon University Rd, Chooncheon 200-701, Republic of Korea

ARTICLE INFO

Article history:
Received 24 September 2015
Received in revised form 25 January 2016
Accepted 26 January 2016

Keywords:
Strategic risk-taking
Airlines
CEO age
CEO tenure
CEO education

ABSTRACT

The literature that has applied a conceptual framework of upper echelon theory has demonstrated that the observable background information of CEOs explains organizations' strategic outcomes. Although CEOs' roles in strategic execution in various fields have been widely researched, extant studies have hardly examined the relationship between observable CEO characteristics and strategic risk-taking in the context of the airline industry. This study thus investigates the strategic risk-taking behavior of CEOs in the U.S. airline industry by employing their observable background information (e.g., age, tenure, and education). We examined 15 airlines that are publicly traded on the U.S. stock market (e.g., NYSE, NASDAQ, and AMEX). Ordinary least squares (OLS) were selected for the data analysis. The results indicate that a CEO's tenure and education play a significant role in accounting for airlines' strategic risk-taking.

1. Introduction

Chief executive officers (CEOs) are typically authorized to make strategic choices given their value and cognitive base. In terms of CEOs' strategic choices, prior research has found a certain link between the cognitive base and value of top managers and their effects on strategic execution (Finkelstein & Hambrick, 1996). Initially, Weiner and Mahoney (1981) explained the association by introducing stewardship theory. The conceptual framework of stewardship theory addressed the connection between the cognitive base and value of top managers and organizational performance. The theory, however, is too complicated to employ the concept in empirical research due to the difficulty in measuring the cognitive base and values. To compensate for the theory's shortcomings, Hambrick and Mason (1984) introduced the upper echelon theory, which technically complements the stewardship theory but is more convenient for empirical research. According to the upper echelon theory, firms' decisions, especially risk-taking ones, can be characterized by CEOs' observable background information. In particular, older and longer tenured managers are more likely to become defenders who are highly specialized in a limited area of operations or in improving existing operations, whereas more educated CEOs are more likely to become prospectors who pursue new market opportunities and trends to achieve innovation (Hambrick, 2007; Miles & Snow, 1978). (See Fig. 1.)

Firms make different strategic choices depending on other players' strategic actions in the same industry, or industries' unique characteristics cause idiosyncratic strategic decisions (Baird & Thomas, 1985; Boyd & De Nicolo, 2005; Bromiley, 1991; Chatterjee & Hambrick, 2007). Because the airline industry possesses distinctive characteristics, such as sensitivity to economic conditions and a relatively high barrier to entry (compared to other industries such as the restaurant industry), the strategic choices of airlines are likely to develop in unique ways (Cho & Hambrick, 2006; Ito & Lee, 2005; Snider & Williams, 2011). Airlines, for instance, implement various strategies in their operations. Some airlines engage in strategic alliances, offer international business routes, and provide full-service carriers, whereas others operate only domestic routes and supply low-cost carriers without strategic alliances (Delta, 2013; Jetblue, 2013).

The prior literature has presented evidence of a relation between firms' strategic choices and CEOs' observable characteristics. Moreover, the strategic execution of airlines appears to be unique. That said, studies have scarcely examined the connection between the attributes of airlines' upper echelon employees and strategic execution. In this study, we presume that CEOs' observable socio-demographic information, such as age, tenure, and education level, would be associated with airlines' strategic risk-taking as a unique manner. Therefore, the purpose of the present study is to investigate whether the conceptual framework of the upper echelon theory is validated in the context of airlines. To accomplish this, ten airline firms publicly traded on the U.S. stock market were chosen as a study sample. CEOs' background information, including their age, tenure, and education levels, was gathered to account for how the strategic risk-taking of airlines differs depending on CEOs' observable background information. The information was derived from Compustat and Execucomp using the standard industry classification code (SIC) 4512. The study period is from 1999

* Corresponding author.
E-mail addresses: lws79877@gmail.com (W.S. Lee), joonhomoon0412@gmail.com (J. Moon).

http://dx.doi.org/10.1016/j.tmp.2016.01.009
2211-9736/

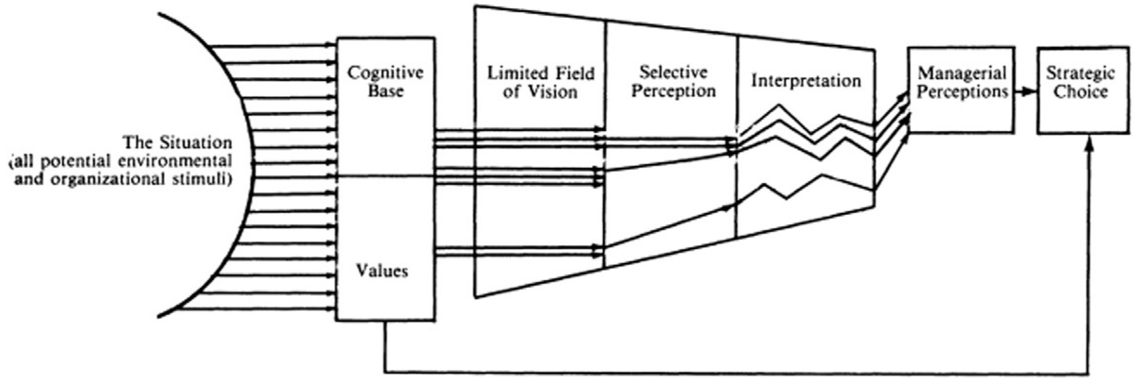

Fig. 1. Strategic choice under condition of bounded rationality Source: Hambrick, D., and Mason, P. (1984). Upper echelon: The organization as a reflection of its top managers, Academy of Management Review, 9(2) 193–206.

to 2013. Ordinary least squares (OLS) served as the main instrument of data analysis by containing several control variables.

2. Theoretical foundation

2.1. Upper echelon theory

Weiner and Mahoney (1981) explained the association between the cognitive base and value of top managers and strategic choice by introducing stewardship theory. Although they introduced stewardship theory to explain the relation between the value of top managers and organizational outcomes (e.g., financial performance and strategic decision making), the theory has been criticized for the difficulty in using it to measure psychometric properties. In particular, to measure the value of top managers stewardship theory considers the coordination between company and performance year, leadership strategy related to capital structure (e.g., debt ratio and retained earnings), and timing of leadership. To compensate for this theory's shortcomings, Hambrick and Mason (1984) introduced the upper echelon theory, which is conceptually similar to stewardship theory but recommends more convenient and observable measurements. That is, upper echelon theory similarly argues that organizations' outcomes are regarded as a reflection of top managers in their strategic decision making (Finkelstein, Hambrick, & Cannella, 2009). A central premise of upper echelon theory is strategic choice under conditions of bounded rationality. Strategic choice under conditions of bounded rationality refers to the fact that relevant information regarding business is too extensive for managers to scan every aspect. Therefore, Finkelstein and Hambrick (1996) argued that managers are more likely to rely on their cognitive base and value when making strategic decisions.

Again, Hambrick and Mason (1984) noted that measuring the value and cognitive base of managers is complicated, so they suggested more convenient instruments. In particular, they recommended using observable background information. Among various observable elements, age (Colombelli, 2015; Matta & Beamish, 2008; Yunlu & Murphy, 2012), tenure (Baixauli-Soler, Belda-Ruiz, & Sanchez-Marin, 2015; Chen, 2013; Simsek, 2007), and level of education (Damanpour & Schneider, 2006; Qian, Cao, & Takeuchi, 2013; Wiklund & Shepherd, 2003) were recognized as the most accessible and observable demographic factors; hence, numerous studies have validated the upper echelon theory by applying these three attributes. For example, by examining 122 top managers, Hitt and Tyler (1991) found that firms' strategic risk-taking was negatively influenced by CEOs' age. Similarly, Coles, Daniel, and Naveen (2006) showed the negative relationship between CEO tenure and strategic risk-taking by analyzing S&P 500 firm managers. Barker and Mueller (2002) similarly demonstrated a positive association between the formal education level of top managers and strategic risk-taking by looking at firms listed in the Business Week 1000.

3. Hypotheses development

3.1. CEO age and strategic risk-taking

Age is the first determinant of strategic risk-taking that needs to be verified. Hambrick and Mason (1984) argued that older top managers have less mental stamina than younger top managers and that lower stamina is associated with a decreased ability to integrate new knowledge and information in strategic decisions. The extant literature has shown a negative association between managers' physical age and strategic risk-taking. In other words, once older top managers achieve a certain financial level, they do not want to risk losing that status by taking risks in their careers (Eisenhardt & Schoonhoven, 1990; Finkelstein et al., 2009; Herrmann and Datta, 2006; Zhang, 2006; Zhang & Rajagopalan, 2010). For example, Combs, Michael, and Castrogivanni (2004) consistently maintained that older top managers are less likely to change their business formation because it requires operating risk and complexity to top managers. Seo and Sharma (2013, 2014) also found that the age of CEOs negatively affected strategic risk-taking by studying restaurant companies that are publicly traded in the U.S. stock market. The results were also confirmed in case of top management teams; Wiersema and Bantel (1992) verified that strategic risk-taking, such as changing the business format and unrelated diversification, are negatively associated with CEOs' age. Given the literature review, this study proposes the following research hypothesis:

H1. Older CEOs of airlines take less strategic risk.

3.2. CEO tenure and strategic risk-taking

The second domain to account for the strategic risk-taking is the tenure of top managers. Tenure refers to the length of time served as a top manager in an organization (Hambrick & Mason, 1984). According to Hambrick (2007), top managers who have served in one organization for a long period of time prioritize their job stability, which leads them to avoid risk in their strategic decisions. Given the characteristics, the extant literature demonstrates that longer-tenured top managers could be characterized as defenders who place greater value on organizations' stability, along the lines of Miles and Snow (1978). For example, Chatterjee and Hambrick (2007) uncovered a negative correlation between strategic risk-taking and the tenure of CEOs in the software and hardware industries. Previous research has also found that longer-tenured American top managers avoided strategic risk-taking (Chin, Hambrick, & Treviño, 2013; Simsek, 2007). Similarly, by studying top managers at computer, chemical, and natural gas distribution companies, Finkelstein and Hambrick (1990) noted that longer-tenured top management teams implemented their strategic execution in a more