

Diversity on Corporate Boards and Firm Performance: An Empirical Evidence from Malaysia

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ABSTRACT

This study examines the relationship between gender diversity among corporate board and firms' financial performance using 100 non-financial companies in Malaysia. This study uses data from 2009 to 2013. Return on equity measures the financial performance. Gender diversity measured by the number of females on board. This study incorporates descriptive statistics, correlation testing, and regression analysis. However, the results of gender diversity have a positive impact on performance (ROE).

Keywords: Gender diversity, Boards, Market performance, ROE.

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1. INTRODUCTION

Developing societal, political and cultural views of corporate board members & top management teams are part of demographic diversity at top management level. In addition, the major factors are better corporate governance and the global desire (Monks and Minow, 2004). According to Co-operation & Development Report (2004) the world faced high-profile scandals like Worldcom, Enron & Adelphia and policy makers began to concentrate on the issues of corporate governance. Mitton (2002) argued that the Malaysian economy severely affected by the financial crisis, and many major corporations had shut down in 1997. This corporate failure on the financial crisis was the result of poor corporate governance.

Corporate governance is a strong pillar of any business organization. Corporate governance means something broader than corporate management, given achieving strategic goals (Kochan *et al.*, 2003; Bairathi, 2009). Effective corporate governance matters handle shareholders issues (Hassan and Marimuthu, 2015). Diversified Corporate boards have a very significant impact on firm performance, firm value creation, wealth maximization and enhance stakeholder's confidence. Demographic diversity has a positive impact on firm performance (Hassan and Marimuthu, 2014). In contrast, Adams and Ferreira (2009) found that gender diversity among board members could result in poor firm performance. According to Zainal *et al.* (2013) ethnicity and firm performance have a positive and significant relationship in the Malaysian context—Some researchers have found that there is no relationship between ethnic diversity and firm financial performance in Malaysia (Monks, 2005). Hence, results are inconsistent regarding ethnic diversity. Gender diversity among boards has a positive relationship with organizational performance. Organizational performance includes the firm's financial performance. There are ambiguity and inconsistency among previous research studies (Ibarra *et al.*, 2010). The results seem to be inconsistent. Previously, studies used simple statistical tool and techniques to investigate the diversity issue. There is a need to investigate diversity issues in a more holistic way by using different sample size and sampling techniques (Hassan *et al.*, 2015). It is keen interest for many researchers to explore demographic diversity with regard to firm performance.

This empirical examination offers more insights on demographic diversity at the board level and its impact on firm performance. The empirical analysis is confined to 12 fully-fledged sectors and 100 non-financial Malaysian selected on the basis of judgmental sampling during the period of 2009-2013. This paper includes the extent to which the findings differ from the general expectations as argued by the previous studies. Empirical studies showed that there is a strong correlation between demographic diversity and firm performance (Pitts, 2005; Hassan *et al.*, 2015; Hassan *et al.*, 2016).

In recent years, diversity issues are examined with regard to the firm performance of the listed companies Malaysia. While extensive literature exists on diversity issues, this issue is still under debate and inconsistent results. Furthermore, there is a need to investigate this problem in a more holistic way and with rigorous statistical estimation. The paper attempts to fill the gap in the existing literature, discuss the empirically diverse corporate boards, top management teams simultaneously and its impact on the firm performance.

The main contribution is for the Malaysian government, and other regulatory bodies may use the results of a study. This research is unique in considering the relationship between demographic diversity at top management level. Descriptive statistics, regression and correlation matrix, were used to investigate this issue.

2. LITERATURE REVIEW

2.1. Demographic Diversity

Globalization is growing diversity and is making a critical role in different businesses. The organizations must diversify their workforce to obtain proper performance of workers (Hassan *et al.*, 2015). Awino (2011) demonstrated that the top management team diversity has a significant influence on organizational performance. The researcher argued that diversity effects workplace interactions and work-related outcomes increase and diversity-performance relationship for other dimensions of diversity (Hassan *et al.*, 2015). Evaluation of diversity regular process reviews; skilled external facilitation and developing CEO leadership capability teams can build the trust that is essential to the productive management of diversity and collectivity (Jarzabkowski and Searle, 2003). The managerial experience does not affect the performance of the firm. The majority of male ownership tends to outperform firms having a majority of female ownership (Kasseeah and Tandrayen-Ragoobur, 2014; Hassan and Marimuthu, 2016).

2.2. Female Participation and Firm Performance

According to Hambrick and Mason (1984) that the female CEO has a neutral or negative effect on the company's performance, but females below the CEO level has a high positive effect. Dezső and Ross (2008) suggested that the females appointed as below CEO level would have a positive and vigorous, effect on the performance because of their creativity, hard work, and team Leadership. However, when they become a CEO they have to face the difficulties and the negative/neutral effect observed. Even if one leaves aside issues of fairness and equality, the vast gender disparity in senior levels of management raises the issue. Modern U.S. corporations efficiently identify and develop managerial talent, which many scholars have identified as an important source of competitive advantage (Barney, 1991; Lado and Wilson, 1994; Finkelstein and Hambrick, 1996; Hambrick *et al.*, 1996; Castanias and Helfat, 2001; Hassan *et al.*, 2017).

3. OBJECTIVES OF THE STUDY

3.1. Main Objective

To examine the effect of demographic diversity among board members (BODs) and its impact financial performance.

3.2. Specific Objectives

- To investigate the impact gender diversity among board members (BODs) and its impact firm financial performance.
- To investigate the impact board size on firm financial performance.

4. METHODS, PROCEDURES, AND MEASURES

For this study, the data was produced from 100 non-financial companies' data used to verify objectives. The data collection period 5 years from 2009-2013. To investigate the effect of the gender diversity at BODs level on firm performance (ROE). The dependent variable was financial performance and is measured b return on equity (ROE). Firm size is used as control variable. The independent variable gender diversity was measured on a ratio scale. However, board size was measured by 'total board members on board'.

4.1. Sample Size

This study is used a sample size of 100 non-financial Malaysian listed companies and used judgmental sampling based on past 5-years’ time 2009-2013 annually.

4.2. Hypotheses

The following hypotheses explain the impact of the gender diversity in BODs on firm financial performance (ROE) that are represented by gender diversity and board size Thus, the proposed hypotheses are as follows.

General:

- Gender diversity among BODs has a significant impact on firm financial performance.
- Board size has a significant impact on firm financial performance

Specific:

H₁: Firms financial performance is positively affected by gender diversity among Board members.

H₂: Firms financial performance is positively affected by Board size.

4.3. Model for the Study

$$Firm\ Financial\ Performance\ (ROE) = \alpha + \beta_{BSIZE} + \beta_{GENDIV} + \beta_{FSIZE} + \epsilon \text{ ----- (1)}$$

4.4. Research Instrument

This study is used the secondary data. All the information collected from the annual reports of companies over the period of 2009-2013.

5. EMPIRICAL RESULTS

5.1. Effect of Demographic Diversity in Board of Directors

5.1.1. Descriptive Analysis in BODs

Descriptive statistics were used for the calculation of the mean, standard deviation, maximum and minimum values. Table 1 shows the average of 100 non-financial companies in Malaysia (2009-2013). Descriptive analysis (mean, standard deviation, maximum, and minimum values) of the total number of members on board (BSIZE). The total number of females in the board (FEM), gender diversity ratio on the board (GENDIV), Firm Size (FSIZE), Equity, Net Income and Returns on equity (ROE) presented below Table 1:

Table-1. Descriptive Statistics in BODs Perspective

Variables	Minimum	Maximum	Mean	Std. Deviation
BSIZE	4	16	8.75	2.93
FEM	0	6	0.74	0.92
GENDIV	0.03	0.08	0.02	0.02
FSIZE	9321.84	1.37E9	3.85E8	1.76E8
Equity (000)	-277747	1.02E9	2.71E8	1.28E8
Net income (000)	-3.23E8	5.25E8	2.85E7	2.81E7
ROE	-4.17	10.25	0.17	0.82

N=100

5.1.2. Correlation in BODs

Pearson’s correlation analyses were performed and reported in Table 2. The correlation matrix shows that there was a statistically significant correlation between the variables. Gender diversity was also positively

correlated with ROE at 0.05 significance level. That means gender diversity shows a relationship with firm performance. The variables values that were closer to 1 are strongly correlated. Other variables have no significant impact on the firm's performance.

Table-2. Correlations Results in BOD's Perspective

No	Variables	1	2	3	4	5	6	7
1	BFSIZE	1	.498**	.058	.007	.006	-.003	.026
2	FEM		1	.831**	-.019	-.023	.011	-.096
3	GENDIV			1	-.052	-.064	-.016	.112*
4	Firm Size				1	.982**	.431**	-.019
5	Equity (000)					1	.462**	-.016
6	Netincome (000)						1	.033
7	ROE							1

**Correlation is significant at the 0.01 level (2-tailed)

*Correlation is significant at the 0.05 level (2-tailed)

5.2. Linear Regression Models

Linear regression explains at what extent the effect of the gender diversity on firm financial performance. Those variables analyzed under the BODs are gender diversity and board size are presented in Table 5.

5.3. Discussion in Perspective of BODs

Based on the results of Table 3 the regression model explained as follows:

$$ROE = 0.272 + 0.009_{BFSIZE} - 5.745_{GENDIV} + 5.33_{FEM}$$

Gender diversity (GENDIV) has a positive significant impact on firm financial performance (ROE) at (p < 0.05) significance level. Hence, H₁ is supported. However, it is positively correlated with the dependent variable. It shows that the increase in the gender will increase the firm performance. Another independent variable board size (BFSIZE) has no significant relation with the dependent variable. Hence, H₂ is not supported. As the gender diversity ratio positively correlated with ROE, we can say that the increase in the woman participation at board level will increase the performance at 5.745. The R-square was 0.014 that means some of the variation in the dependent variable explained by the model. It can also predict that there might be other independent variables that will affect the firm performance that not considered in the analysis. The F-test gives the result of 1.788 that shows the model is significant at 0.05.

Table-3. Regression Results on ROE in BODs (DV: ROE)

Variables	Model (BODs)
Constant	.147
GENDIV	.025**
BFSIZE	.532
Firm Size	.608
R ²	0.014
F-test	1.788

*Dependent variable: ROE; p<0.05**; p<0.01***

6. FINDINGS OF THE STUDY

By examining, the effect of gender in Board of Directors (BODs) found that firm performance affected positively by gender diversity (GENDIV). The results showed the significant positive correlation of 0.111. It means demographic diversity in BOD has a positive impact on firm performance (ROE). In addition, Board size (BSIZE) has no impact on firm performance. We can argue that board size does not matter in firm performance. As an overall result, we can say that demographic diversity has the impact on firm financial performance. As the gender diversity shows the significant positive results only.

7. LIMITATIONS OF THE STUDY

This paper only focuses on demographic diversity in BODs of non-financial listed companies. In addition, this paper incorporated only last five-year data from 2009 to 2013 and thus, it would be quite challenging to generalize the findings, but these companies are top companies as a performance by total market capitalization.

8. CONCLUSIONS

The article attempts to investigate the contribution of diverse corporate boards in firm performance. Admittedly, gender diversity (GENDIV) among the board of directors (BODs) has significant positive impact on the firm financial performance of Listed Companies. Hence, that women's participation at corporate board level can enhance the profits and perhaps improving internal operations of their companies. "Women also bring a different set of life experiences in organizations". By looking at results, ethnic diversity outcome is inconsistent with previous research. There might be several reasons behind this issue. Nevertheless, results show kind of interesting picture regarding demographic diversity and firm financial performance.

In a nutshell, we can conclude that women's participation has a positive impact on firm financial performance. However, the presence of diversity at board level does have an impact on firm value and hence more diversified boards higher the firm performance in case of listed companies.

9. RECOMMENDATIONS

It is recommended that diverse boards should be promoted in the firms to get better performance. Moreover, to get better performance, it is suggested that the use different ratios will help to understand this phenomenon, e.g. Liquidity ratios, Leverage, and Debt ratios. Furthermore, increase the span of research by covering more companies to see the holistic view. Lastly, there is need to make a comparison on a global level. Extend to other companies on a global scale and make a comparison between different sector companies in the various regions of the world. These recommendations will help them to analyze better and make a far productive decision when it comes to making a conclusion on the variables.

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