BOARD GENDER DIVERSITY AND ORGANIZATIONAL PERFORMANCE: A POLEMICAL REVIEW

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Abstract

This study reviews literature on board gender diversity and its impact on board's and firm's performance. The case for diversity is perceived based on equity and fairness and economic or business case. The normative case agues the proposition that women and ethnic minorities are worthy of equitable opportunities to be appointed on boards and on top management positions. Theories such as agency, stakeholder, and resource dependency theory suggest that increased diversity would allow for a broader perspective and improved fiduciary role of boards, thus improve firm performance. However, there are contradictory results from the empirical evidence. The debate is that, there is no perfect agreement in the literature as to whether increased levels gender diversity amongst the board of directors contributes to enhanced company performance. Review of 16 literature shows that 10 studies find a positive relationship between gender diversity on board and firm performance. On the other hand, 3 of the reviewed literature reveal a negative correlation between gender diversity and performance while, 3 others find no evidence of significant relationship between gender diversity and performance. Therefore, this study suggests considering the normative case to increase women representation on board because business case is controversial, and may lead to more discrimination against female.

Key Words: Board, Diversity, Gender, Governance and Performance

DIVERSITE DE GENRE ET PERFORMANCE ORGANISATIONNELLE AU SEIN DU CONSEIL: UN EXAMEN POLEMIQUE

Abstrait

Cette étude examine la littérature sur la diversité des sexes au sein des conseils d'administration et son impact sur les performances des conseils d'administration et des entreprises. Les arguments en faveur de la diversité sont perçus comme étant basés sur l'équité et la justice, ainsi que sur des arguments économiques ou commerciaux. Le cas normatif soutient la proposition selon laquelle les femmes et les minorités ethniques méritent des

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chances équitables d’être nommées à des conseils d’administration et à des postes de direction. Des théories telles que la dépendance vis-à-vis des agences, des parties prenantes et des ressources suggèrent qu'une plus grande diversité permettrait une perspective plus large et un rôle fiduciaire accru du conseil d'administration, améliorant ainsi les performances des entreprises. Cependant, il existe des résultats contradictoires à partir des preuves empiriques. Le débat est le suivant: il n’ya pas d’accord parfait dans la littérature sur la question de savoir si l’augmentation de la diversité des sexes au sein du conseil d’administration contribue à améliorer les performances de l’entreprise. L'examen de 16 ouvrages montre que 10 études ont mis en évidence une relation positive entre la diversité des sexes au sein du conseil d'administration et les performances des entreprises. D'autre part, 3 de la littérature recensée révèlent une corrélation négative entre la diversité des sexes et la performance, tandis que 3 autres ne trouvent aucune preuve d'une relation significative entre la diversité des sexes et la performance. Par conséquent, cette étude suggère de considérer le cas normatif pour augmenter la représentation des femmes au sein du conseil, car l'analyse de rentabilisation est controversée, ce qui peut conduire à davantage de discrimination à l'égard des femmes.

Mots clés: conseil, diversité, genre, gouvernance et performance

Introduction

There are various definitions of corporate governance. These include a definition by Cadbury (1992) which defined corporate governance as the system which companies are directed and controlled. Scholars such as Keasey and Wright observed that that corporate governance is about the composition and procedures related with "production, decision making, control and so on within an organisation" (Keasey & Wright, 1993, p. 291) and to ensure that firms are more “responsive to other stakeholders needs” (Freeman & Reed, 1983 p. 95). Other definitions look at the firm as an independent entity and not only as an instrument for external actors. In that case, the role of corporate governance mechanisms is to support what is best for the firm. Given the vital place of board of directors as a key component of the whole corporate governance mechanism, it is vital to know their role. There are different views about the roles of a board of director. However, Cadbury (1992) suggested that responsibilities of the board include setting the company’s strategic aims, providing the leadership to put them into effect, supervising the management of the business, and reporting to shareholders on their stewardship. Ntim (2015) argued that corporate boards of directors are among the most important unit within contemporary organizations, carrying out critical advisory, monitoring and resource dependence roles. Moreover, adequate supply of resources is vital to firm’s survival; hence the role of the board could also be considered from external source as suggested by resource dependency model (Preffer & Salancik, 1978). Boards are crucial mechanism for absorbing critical components of environmental uncertainty in to the firm.

With this crucial role of the board in corporate governance, the firm’s performance might be impacted by the characteristics and composition of the board such as gender of the board member. An important issue of concern is that women are underrepresented on board (Stephenson, 2004). Moreover, there is a growing concern of having women on board by the policy makers in various parts of the world and debates by researchers on whether or not board heterogeneity helps it to perform more effectively. Studies reveal variation in percentage of women directors across nations. For instance recent European Commission report on women representation reveal 23% women on board in EU and 15% in Europe. While Catalyst data from S&P 500 showed new directors profile of 26.9% female. Due to the conflicting results on the impact of diversity on firm performance this study reviews the theoretical perspectives on gender diversity in relation to firm performance. The first section of this study is the theoretical review followed by the review of empirical studies and the last section is the conclusion.

Theoretical Review

Advocates of diversity in corporation's boardrooms generally base their arguments on a range of theories such as agency theory, stakeholder's theory and resource dependency theory (Goodstein et al. 1994; Burges and Tharenou 2002; Roberson and Park 2007; Yang and Konrad 2011). These theories have been invoked to relate women board representation and firm performance.

Agency Theory

Agency theory in economics and finance owes much of its academic development to Jensen and Meckling (1976). However, the concept of agency theory dates back to decades of social science research. The theory emphasises on agency relationship in which one party or group (agent) has certain responsibilities which are to be satisfied for another party or group (principal) by virtue of their economic relationship. The firm is regarded as a nexus of contracts between principals and agents. The spirit of agency theory depends on the assumptions that: "(i) the desires or goals of the principal and agent conflict; and (ii) that it is difficult or expensive for the principal to verify what the agent is doing (Eisenhardt, 1989, p.58)." This is refered to as agency problem.

Another difficulty arises because the principal and agent have different attitude towards risk. As the divergence between principal and agent's interest reduces, the remaining behaviour which may not be eliminated refers to as agency residual loss. The principal monitoring cost and the agents bonding expenditure which may be incurred, refers to as agency cost (Hill & Jones, 1992). Hence, the key emphasis of the theory in the principal agent relationship is the choice of governance mechanism between principal and agents that will ensure an efficient alignment of both parties interest (Eisenhardt, 1989). The main weakness with this theory is that, it fails to recognise stakeholders of the firm, and the valid assumption of trust, honesty and loyalty in to its assumptions.

Agency theory proposes that boards of different backgrounds increases board independence and makes executive monitoring better (Kesner 1988; van der Walt & Ingley 2003; Johnston &Malina 2008; Abdullah 2013), and thus improve market value. Carter, Simkins, & Simpson (2003) suggest that a board that is more diverse could be a better supervisor of managers since board diversity increases board independence. Diversity improves the ability of the board to monitor managers as a result of increased independence; it also improves the decision making of the board because of distinct new perspectives, and increased creativity and non-traditional innovative approaches, diversity also improves the information provided by the board to managers due to the unique information held by diverse directors (Carter et al., 2007). However, Carter et al. (2010) revealed that agency theory proposes a relationship between gender diversity and firm performance, but it does not provide a clear prediction of the link between board diversity and financial performance. Hence they do not find a significant relationship between the gender or ethnic diversity of the board, and financial performance for a sample of major US corporations.

Stakeholder Theory

Stakeholder theory owes its intellectual development to Freeman's (1984) seminal work. In stakeholder theory, the role of board is seen as achieving a balance between the interests of all stakeholders (Freeman, 2004). A balanced board with directors from various backgrounds might help it to have greater perception of the needs of entire population. The mission for maximization of firm's value has two contradictory dimensions, namely the shareholder maximisation view on one side and the stakeholder maximization view on the other side. Supporters of the shareholder theory believe that managers have a major responsibility to maximize shareholder returns. In contrast, supporters of the stakeholder theory believe that managers have responsibilities to balance the interests of shareholders against the interests of other stakeholder groups. According to Harjoto, Laksmana & Lee (2015) firm requires an effective stakeholder management for its business success. Thus, boards of directors, being agents of shareholders, have an important role to play in supervising the creation and implementation of management's plans to balance the interests of various stakeholders. They further reveal that when firms operation is in those industries with greater need for stakeholder management, then diverse boards are more effective in supervising corporate social responsibility performance.

Stakeholder theory by Cornell & Shapiro (1987) suggests that corporate financial policy depends on the role of non-investor stakeholders, because many of the claims issued by management to non-investor stakeholders take the form of contractual promise of continuing supply, timely delivery, product enhancement, and job security. Hence firm value depends on its ability to fulfil these contracts. A diverse board carries a different knowledge base, sets of experiences, and perspectives on the public to group decision making. Hence, diversity increases the board's capability of recognizing the needs and interests of various sets of stakeholders as mirrored on corporate social responsibility performance (Harjoto, Laksmana & Lee, 2015). Several studies support the stakeholder theory that more diverse boards are more effective in monitoring social responsibility performance than less diverse boards (Bear et al., 2010, Harjoto, Laksmana & Lee, 2015, Wang & Coffey, 1998, Williams, 2003). They further argue that gender diversity increases corporate social responsibility strengths and reduces corporate social responsibility concerns.

Resource Dependency Theory

According to Preffer & Salancik (1978), resource dependence theory considers firm as an organizational body that inter depends within business environment and needs certain constituencies to provide and institute link with external resources for its positive performance. Those resources are information and knowledge; channel establishment with working constituents; legitimacy of the company; and benefits from board interrelation. This means that the basic suggestion of resource dependence theory is the need for environmental connections between the firm and outside resources. Carter et al., (2007) reveals that, diverse board bring easy access to important constituencies and resources in the external environment. Furthermore, diversity in the boards ends significant positive message to the labour market, product market, and financial market, and also board diversity brings legitimacy to the company with both internal and external constituencies. Hence Environmental connections might reduce transaction costs related with environmental interdependency and consequently lead to a positive relationship between gender diversity and firm performance (Ntim, 2015).

Based on Bryant and Davis (2012), resource dependency theory proclaims that businesses act in ways applicable to their dependence on certain resources. Firm's usually respond to signals from their external environment so as to minimise their dependence on, and maintain independence over relevant resources. Organisations that survive better with and minimise uncertainty for their stakeholders and which have control over scarce resources and the substitutability of their controlled resources, have a competitive advantage.

The key research question of resource-based theory is performance heterogeneity among organizations (Barney & Clark, 2007). These perception views organizations as comprising of a range of resources, mostly including four categories: physical capital, financial capital, human capital, and corporate capital resources (Barney & Clark, 2007). As resources can either facilitate or constrain firms from developing and implementing business strategies efficiently, the features of resources held by firms determine firm performance heterogeneity. Hence such resources can be a source of competitive parity (Barney, 1989).

Signalling Theory

Signalling theory has its roots in economics and is used to describe the behaviour between two or more parties with access to different information. This is known as information asymmetry where one party has more or better information over the other.

Signalling theory mainly encompasses strategies and actions used to minimise information asymmetry between stakeholders (Connelly, et al., 2011). In this context, signalling theory is used to explain how firms use heterogeneous boards to communicate adherence to social values to a range of organizational stakeholders. Accordingly, it is argued that more diverse boards are perceived by an organisation's stakeholders as an indication of the firm's desire to incorporate various interests and opinions into governance processes and eventually into strategic and operational actions which will improve performance (Connelly, et al., 2011).

Upper Echelons Theory

According to upper echelons theory (Hambrick, 2007), directors' cognitive frames, that is, the processes in which directors seek and evaluate information, depends upon their experiences, knowledge, and values. Their experiences, knowledge, and values influence how directors seek and interpret information. Consequently directors' cognitive frames can affect board decisions, decision-making processes, and, eventually, firm's outcomes. Based on this perspective, it is argued generally, that female and male director vary in their cognitive frames; hence director heterogeneity with regards to gender is likely to influence firm performance (Carpenter, 2002). Olson, Parayitam and Twigg (2006) revealed that the upper echelons theory suggests that noticeable features of top management teams are the proxy measures of values, cognitive style, cognitive content that influence strategic choice. They further argue that on the positive relationship between performance and a diverse board, the imputed logic is that having a diverse team improves the knowledge base, cognitive abilities and general problem-defining and problem-solving skills of the group.

Empirical Review

A large and growing body of literature has investigated the impact of board gender diversity on firm's performance (Adam & Ferreira, 2009; Abdallah, 2014; Pechersky, 2016)**.** The case for diversity is perceived based on equity and fairness and economic or business case. For the normative case, it is seldom agued that the proposition that women and ethnic minorities are worthy of equitable opportunities to be appointed on boards and on top management positions. While for the business case of board diversity, it is argued that board diversity causes a business to be more profitable and improve shareholders value (Carter et al., 2007). This indicates that diverse boards are not substitute with identical ability and talents; nonetheless diverse boards have unique features that generate additional value. The economic or business case for board diversity is a positive statement which is difficult to evaluate than the normative equity case (Carter et al., 2007). A debate is that, there is no perfect agreement in the literature as to whether increased levels gender diversity amongst the board of directors contributes to enhanced company performance. Theories such as agency, stakeholder and resource dependency theory suggests that increased diversity would allow for a broader perspective and improved fiduciary role of boards, thus improve firm performance. However, there are contradictory results from the empirical evidence. Many studies find a positive relationship between a gender diversity on board and firm performance. For instance Adam and Ferreira (2009) reveal that female director has significant impact on the board inputs when examining a sample of 1,939 firms over the period 1996-2003 and finds a positive relationship. There are number of studies with Similar findings (Carpenter, 2002; Erhardt, Werbel & Shrader, 2003; Carter, Simkins & Simpson, 2003; Carter et al., 2007; Campbell & Mínguez-vera, 2008; Ararat, Aksu & Tansel Cetin, 2015;Ntim, 2015; Post & Byron, 2015; Pechersky, 2016). These studies had examined not only the impact of increasing the proportion of women but also the effect of gender diversity of board directors on firm performance. Post & Byron (2015) and Pechersky (2016) in their meta analysis also examined whether the results of the studies vary by firms' legal and or regulatory and socio-cultural contexts.

Carpenter (2002) covered a sample of 247 large and medium size US firms in Standard and Poors (S&P) data index from 1990 through 1997. Also Erhardt, Werbel and Shrader (2003) studied a sample of 127 large US firms covering a period from 1993 to 1998, while Carter, Simkins and Simpson (2003) used a sample of 797 firms with data covering 1000 firms. However, Campbell and Minguez-Vera (2008) included a sample of non-financial Spanish firms at the Madrid stock exchange from 1995-2000. Ararat, Aksu and Tansel Cetin, (2015) conducted their studies using data from Turkey and their sample consisted of 100 large and liquid firms in the Bourse Istanbul (BIST-100 index). The sample size used by Ntim (2015) consisted of dataset of 291 organisations in South Africa during the period of 2003 to 2007. While Post and Byron (2015) analysed 140 empirical studies that were published in English for the period from January 1989 through May 2014 and find a positive relationship. Conversely, Pechersky (2016) article analyses empirical studies with samples on various countries, and found a positive relationship between gender diversity and firm performance.

However, a number of other studies revealed that gender diversity have negative impact on firm performance. For instance Ahern and Dittmar (2012) found a negative impact on performance subsequent to the approval of women quotas law in Norway. Their sample consisted of all public limited Norwegian firms that traded on the Oslo Stock Exchange (OSE) from 2001 to 2009. Similarly, Abdullah (2014) and Boubaker, Dang and Duc (2014) found a negative relationship between gender diversity and firm performance. While Boubaker, Dang and Duc (2014) focused on the effect of gender-diverse boards and firm financial performance with sample of105 French listed firms that belong to the SBF 120 stock market index over the period 2009-2011, Abdullah (2014) used 100 non-financial firms listed on the Malaysian stock exchange for the year 2007. The major drawback of these findings was small sample size and short period.

Conversely, many studies found no relationship between board gender diversity and performance (Kakabadse et al., 2015; Carter et al., 2010; Rose, Munch-Madsen & Funch, 2013). Carter et al., (2010) argued that they do not find a significant link between firm performance and gender or ethnic background of a director. They conducted a comprehensive study based on 2,563 US firms for a period of five years of the S&P-index firms. Similarly, Rose, Munch-Madsen and Funch, (2013) who considered a sample of 117 companies in the leading stock indices in Denmark, Sweden, Finland, Norway and Germany, for the year 2010 supported their findings. Kakabadse et al., (2015) Drawn their conclusion from qualitative study involving 30 companies with women directors in the United Kingdom, the United States, and Ghana; and also found no significant effect of gender diversity on board performance.

The literature reviewed revealed mixed findings and all measure performance with ROA and/or Tobin's Q. Some of the studies uncovered a positive relationship; while, others find a negative effect of gender diversity on board performance. Significant number of studies has agued that no relationship between gender diversity and performance exist. The main limitation with the literature, however, is lack of objective way of measuring performance.

Conclusion

The aim of this study was to review the literature on board gender diversity and its impact on board and firm performance. Existing theoretical and empirical studies revealed advantages of gender diversity using agency theory, stakeholder theory, resource dependency theory, signalling theory and upper echelon theoretical perspectives. The perspective of each of the theory regarding diversity differs from each other. For instance stakeholder and resource dependency theories present the strongest argument that favours diversity. The theory argued that diversity increases the board's capability of recognizing the needs and interests of various sets of stakeholders as mirrored on corporate social responsibility performance because a diverse board carries a different knowledge base, sets of experiences, and perspectives on the public to group decision making. Resource dependency theory argued that a diverse board of directors with multiple expertise and different background brings into the board the required connections and knowledge that can improve performance.

However, the existing empirical findings fail to resolve the contradiction about the economic case of increase female directors. However, the theories have suggested a significant link between a diverse board and performance. From the sixteen (16) empirical studies reviewed so far, only ten (10) articles were in support of the theories, while three (3) articles argued that increasing women on board has negative impact on performance. Three (3) articles found no relationship.

Negative relationships were described by increase on the problems of managing effective teams when more diversity leads to increased differences in "attitudes and viewpoints". Increasing conflicts reduces cohesion and impedes communication and harmonisation within the team (Abdullah, 2014). Results showing no significant relations were also linked to increased team inefficiencies: "valuable resources provided to the firm by women and ethnic minority directors may have been offset by the social psychological dynamics of the board such as exclusion or conflict" (Carter et al., 2010). Positive relations between increased gender diversity and company performance are predicted by the theoretical frameworks of the agency, stakeholder, resource dependency, upper echelons and signalling theories.

The important message from the literature is that the impact of board diversity on performance is expected to be heterogeneous. Some firms gain from more diversity while others do not. However the study of gender diversity also helps to understand discrimination in business situations. Some scholars argued that relating firm performance with board diversity can be a proof of discrimination; some firm may argue that having women on board can affect their profit. However, this study suggests considering the normative case to increase women representation on board as what makes business to grow and prosper as a going concern. It makes a pool of opinion that satisfy diversity in the customers' need possible.

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