A Critical Review on the Corporate Governance, Board Independence and Gender Diversity in Emerging Asian Countries

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Abstract
The aim of this study was to identify the role of board independence and gender diversity in corporate governance practiced in emerging Asian countries. Literature was critically examined on the role of board independence and gender diversity in corporate governance for developed and developing countries. The current practices of the emerging nations in Asia were also closely followed. It was observed that despite efforts on the part of governments and policy makers, the emerging states are not being able to fully reap the benefits or realize the significance of board independence and gender diversity in corporate governance. Owing to well rooted cultural traits in the Asian world regarding women, the emerging markets are finding it difficult to let go off their conservative diversity profile. The traditional views on gender diversity and board independence require revision keeping in view the growing trend of women directorship in organizations worldwide. Further research on board independence and gender diversity in the developing Asian countries may help to provide a basis for a paradigm shift and result in better representation of gender at the level of decision making and in influencing corporate governance.

Keywords: Board independence, gender diversity, corporate governance, emerging countries

1. Introduction
Corporate Governance is the system through which boards manage and govern organizational entities (Yasser, Entebang & Mansor, 2011). Among the subgroups of top management in modern day organizations, the board of director plays a crucial role in corporate governance. Their strategic function is to monitor, motivate and compensate managers and to provide resources and other strategic functions that impact the firm’s overall capital expenditure and financial performance (Carter, Simkins & Simpson, 2003; Kang, Cheng, & Gray, 2007; Ntim, 2013; Terjesen et al., 2016; Yasser et al., 2011). Being a crucial governance mechanism, the board of directors are also accountable and responsible to a wide range of stakeholders (Rao & Tilt, 2016). Depending on their social, political and religious needs, countries worldwide set their rules and regulations for organizations to ensure the protection of stakeholder’s rights and providing a level playing field for all entities (Yasser et al., 2011). These may be in the form of corporate governance codes, reforms or guidelines.

The recent corporate scandals has resulting in insecurity among stakeholders who now demand better corporate governance especially through boardroom representation, such that it brings together the interests of the shareholders and the managers and eliminate chances of having an ineffective management team (Kang, Cheng, Gray, 2007; Terjesen et al., 2016).

To ensure that the board represents the diverse set of stakeholders, the board composition should be such that it is a representation of the stakeholders. Two important mechanisms of board composition are board diversity and board independence that ensure the protection of stakeholder’s interest. The presence of independent and female members on the board is different across the world depending on firms, industries and countries. Recently boards are seeing a gradual increase in the number of independent and women directors on boards (Ntim, 2013; Terjesen et al., 2016). Developed countries such as the US, UK, Norway and Sweden are already ahead in implementing corporate governance guidelines in their organizations in the form of corporate governance laws, guidelines and reforms (Ntim, 2013; Rao & Tilt, 2016; Terjesen et al., 2016) and are reaping benefits of these codes.

While board gender diversity is picking up momentum in companies all around the globe, the emerging nations tend to be following at a rather slow pace in recognizing its possible advantages and importance. Today women are more educated, aware and articulate in decision making and have the ability to contribute positively to the firm’s performance (Kang et al., 2007; Rao & Tilt, 2016; Shrader,Blackburn & Iles, 1997; Terjesen et al., 2016). Despite supporting evidence that women perform well in the directorship position, there is social reluctance regarding women in top management positions in emerging economies and women are discouraged from participating in the decision making process (Mirza, Mahmood, Andleeb & Ramzan 2012). Most organizations in developing countries have been following a conservative diversity profile which needs to be revised keeping in view the growing trend of women directorship in organizations worldwide.

Limited research is available on the importance of board independence and gender diversity on
Corporate governance in emerging states. Research in the field on gender diversity on boards helps to provide a basis for bringing about a change in the form of better representation of gender at the level of decision making and influencing corporate governance. The study objective is to understand how board independence and gender diversity have influenced corporate governance in developed countries and how emerging states can learn from these nations to improve corporate governance practices in their home country. This paper adds to the current body of knowledge by critically examining the existing literature on board independence, gender diversity and corporate governance in developed and developing countries and stressing the need to encourage board independence and female directorship in emerging countries with supporting literature from countries that have already realized its significance.

2. Corporate Governance

The need for the development in corporate governance stemmed from the need to reinstate confidence among investors in the capital market (Sheikh & Khan, 2013). Shleifer & Vishny (1997) state that “corporate governance deals with the mechanisms that ensures that the investors get a return on investments” (Shleifer & Vishny, 1997). The concept of corporate performance is crucial as it is associated with how the available financial resources are utilized to achieve corporate goals of an organization which keeps it in the business and helps to create prospective opportunities for the company (Yasser et al., 2011). To examine how corporate governance affects corporate performance, the internal governance structure is scrutinized through the board of directors (Rao & Tilt, 2016). They play a vital role in governance and can thus have a significant impact on the firm’s corporate performance. To understand the role that the board plays in corporate governance, various theories have been put forth. The agency theory, the resource-dependency theory, the stewardship theory and the stakeholder theory have been widely used to explain corporate governance and the different characteristics of the board of directors.

The agency theory while stressing on the board mechanism of board independence highlights the need to monitor the management on behalf of the shareholders. Accordingly it points out that effective control mechanism is necessary to monitor the actions of the management. The stewardship theory postulates that managers are good stewards of the resources that are handed over to them and are hence trust worthy individuals, thus the need for the board monitoring the management of the firm and the aspect of board independence is unnecessary and irrelevant. The resource dependency theory states that organizations primarily depend on external entities and units in order to acquire and exchange resources which is where the board of directors come in. The firms depend on the board for not only resources but also seek their advice and counsel. Lastly, the stakeholder theory argues that for companies to survive, it is important for them to take care of the interests of its stakeholders. It suggests that both the society and the firm are dependent on one another. The board ensures that the interests of all the stakeholders are justly accounted for.

All the above theories related to the board mechanics and corporate governance suggests that the role of the board of directors is critical in corporate governance; hence they have the potential to influence corporate performance (Rao & Tilt, 2016). Board composition should be such that it is a true representation of the stakeholders so that their interest is safeguarded.

3. Board Diversity, Independent Boards and Corporate Governance

3.1 Board Diversity

With reference to corporate governance, Walt & Ingle (2003) state that, diversity among boards is linked to with different combinations of expertise, attributes and characteristics that are brought forward by the board members during decision making and other board processes (Walt & Ingle, 2003; Darmandi 2011). Board diversity may range from either observable aspects such as ethnicity, nationality, age or gender etc. whereas the less visible aspects include educational background, industrial experience etc. (Mahadeo, Soobaroyen & Hanuman, 2012).

Demographic projections made by firms reveal that the market has become diverse and hence to increase market penetration it has become essential for organizations to meet the diversity of the company, its potential customers and suppliers (Shrader, Blackburn & Iles, 1997). Attitudes, cognitive functioning and beliefs are systematically different due to factors such as age, race and gender (Carter, Simkins & Simpson, 2003). In order to cater to this diversity it is important to have a board composition that caters to the diverse market needs and is a true representation of the organization’s stakeholders. Modern corporations are faced with corporate governance issues that center on board diversity (Carter et al., 2003; Kang et al., 2007; Rao & Tilt, 2016; Yasser, 2012). Carter, Simkins & Simpson (2003) defined diversity as “the percentage of women, African, American, Asians, Hispanics and other minorities on the board of directors” (Carter et al., 2003). Board diversity is encouraged on two main accounts, one that it enhances group discussions, group performance and exchange of ideas, and two because since its aim is to protect the interests of the stakeholders, therefore it should comprise of representatives of these stakeholders (Kang et al., 2007). With diversity, effective problem-solving can be
achieved owing to the varying available skill sets and perspectives (Carter et al., 2003; Rao & Tilt, 2016; Yasser, 2012). Heterogeneity among the top managers provides for broader views as opposed to narrow perspectives of a homogenous management. While a number of studies support the notion of board diversity, some argue that it has a negative impact on the market valuation. With diversity, the concept of tokenism is given way whereby it is believed that gender-based members on the board may be an evidence of tokenism with their contributions to the board processes being compromised upon (Adam & Ferreira, 2008; Low, Roberts & Whiting, 2013). Similarly diverse members of the board may have their own interest and commitments to the board (Baysinger & Butler, 1985). Some researchers also attribute gender diversity to increase the likelihood of conflicts among boards, women to be risk averse and slow in the decision making process (Darmandi, 2011).

3.2 Board Independence
The most researched area of board composition is the number of independent directors relative to the executive directors on the board (Carter et al., 2003). According to Carter et al. (2003), a board that is more diverse will also tend to be more independent. Kang et al., (2007) contend that in an attempt to increase board effectiveness, a good governance practice for organizations would be to comprise a board of directors having a majority of non-executive directors. The value of an independent or outside director is in their ability to speculate a firm’s performance independently and objectively. Greater board independence enables the independent directors to closely monitor a firm’s activity and performance and take relevant governance measures (Sheikh et al., 2013).

Studies have shown mixed results with reference to board independence and its outcomes. Some evidences show that an independent board reduces the possibilities of fraudulent financial reporting (Dunn 2004) and are effective monitors in terms of a company’s strategic issues (Dare 1998), while others find either no relationship (Baysinger & Black, 2002) or an insignificant relationship (Baysinger and Butler, 1985; Klein, 1998) between the degree of board independence and corporate governance.

3.3 Board Gender Diversity
Gender diversity in the board is one of the most pressing issues that countries around the globe are facing and trying to address through implementing corporate governance reforms (Kang et al., 2007; Ntim, 2013; Rao & Tilt, 2016). In 2015, South Africa underwent Organizational Governance reforms which primarily focused on increasing ethnic and gender diversity within corporate boards to in an attempt to improve board independence as well as monitoring of management thus increasing the overall market valuation (Ntim, 2013). Similarly, the Australian Stock Exchange Corporate Governance Council released the ‘Principles of Good Corporate Governance and Best Practices Recommendations’ in 2003 to address the need for better corporate governance that was demanded by the stakeholders after the fall of major corporations in Australia (Kang et al., 2007). In a study by Terjesen et al., (2016), it was observed that the external independent directors tend not to contribute towards organizational performance unless the board is gender diversified. It was also revealed that among the countries that were under study, 16 national codes and 13 national quotas stressed the importance of gender diversity among boards (Terjesen et al., 2016). Policy makers and country leaders are continuously in the process of debating, developing and approving gender quotas legislation in boards (Terjesen, Aguilera & Lorenz, 2015). Globally, efforts are being made to diversify board of directors in terms of their status as independent directors to the firm and gender while emphasizing including more females on the board. The presence of independent and female directors tends to be different depending upon countries, industries and firms (Terjesen et al., 2016). The trend of board composition witnessing more women directors is gradually on the rise (Ntim, 2013; Terjesen et al., 2016). In the US, the NASDAQ and the NYSE require organizations to have a considerable presence of independent directors on the boards. In 2013, UK required corporations to have 72% independent directors and 15% female directors on board (Terjesen et al., 2016). It was also revealed that among the countries that were under study, sixteen national codes and thirteen national quotas stressed the importance of gender diversity among boards (Terjesen et al., 2016). According to Rao & Tilt (2016), in an attempt to encourage female representation on boards, countries such as “Norway (40% quota for women representation), Sweden (25% voluntary reserve or threat to make it a legal requirement), Spain (comply- or – explain type of law requiring companies to reach up to 40% female directors by 2015), France (law which requires 50% gender parity on board of every public firm by 2015 and Italy (law requiring listed and state owned companies to ensure one-third of their board members to be women by 2015)” (Rao & Tilt, 2016, p.10) are ensuring the implementation of this code.

Gender board diversity in terms of ethnicity and gender witnessed a rise from 2002 to 2006 in South African organizations, which implies that organizations were willing to conform to the new reforms with time.

4. Emerging Asian Countries: Board Independence, Gender Diversity and Corporate Governance – Current Practices
One of the important roles performed by the board of directors is monitoring particularly in those nations where
external mechanisms are not developed well (Campbell & Minguez-Vera, 2008). According to Campbell & Minguez-Vera (2008), the quality of monitoring and the resulting financial outcomes can be influenced by board gender diversity. Corporations are seeing a gradual increase in gender diversity across boards in the developed economies (Dutta & Bose, 2007). Emerging nations are also realizing its importance and are adopting the same practice but at a significantly slower pace. Indonesia, like China follow a two-tier board structure and in a recent study, Darmandi (2011) observed that among the initial sample of 383 listed Indonesian companies, the average percentage of women on board was 11.2, which was very similar to that of Australia and UK. Most firms in Indonesia are family owned and controlled and hence women representation in board is primarily due to their relationship with the controlling shareholder and not on occupational experience or expertise. Results of Darmandi’s (2011) study revealed a negative association between firm’s market and accounting performance with gender diversity. These results were further cemented by Darmandi’s (2013) study which suggested that women membership had no association with improved firm performance. A study by (Liu, Wei & Xie (2013) reveal that in China, the number of women directors on board is an important factor to impact firm performance. Boards having three or more female representation have a stronger impact on a firm’s performance than those with fewer women on board. Ye, Zhang & Razaei (2010) further endorsed the contribution of women in board decision making and firm performance in Chinese organizations.

In Malaysian firms are either government controlled or are headed and controlled by selected families. Despite making efforts to encourage gender diversity in corporate boards, gender diversity in Malaysia saw a decrease in this trend from 2005-2009 (Zainal, Zulkifli& Saleh, 2013). Corporate board diversity fell from 10.2 percent in 2005 to 7.6 in 2006 and a further 5.3 in 2007 (Julizaerma & Sori, 2012). This cost Malaysia to drop five places in the ‘World Economic Forum’s Global Gender Gap Index 2009’ from the preceding year to being 101 out of 115 countries (Julizaerma & Sori, 2012). One of the many reasons that Julizaerma & Sori (2012) attributed to this fall was stereotyping and the social and cultural attitudes towards the nature of job suitable for men and women. But despite these drawbacks, Julizaerma & Sori, 2012 observed a positive association between gender diversity and ROA of Malaysian firms which indicated that if the government policy of having 30% seats for women on the board was enforced and implemented, the corporations could reap remarkable benefits out of gender diversity.

A survey conducted by the ‘Women Entrepreneurship Development Project of Dhaka Chamber of Commerce’ saw more than 5000 women entrepreneurs in Bangladesh in 2004 as compared to a few dozen in the 1980s. Despite having such enterprising women in the country, men still continued to dominate in the boardroom in Bangladesh. This further reflected in Dutta & Bose’s (2006) study on gender diversity and firm performance showing paradoxical relationship between the two variables for the banking industry. Similarly in Pakistan, the concept of women representation in business management has not picked up the same pace and importance as it has in the developed and developing nations. The code of corporate governance in Pakistan was introduced in 2012 by the Security Exchange Commission of Pakistan (SECP) (Yasser et al., 2011). These codes were an attempt towards corporate governance reforms and included recommendations based on the best practices followed internationally. The reforms were focused on the board of director in order to make them more accountable to the shareholders and so that disclosures were improved to conduct internal and external audits. Like many other emerging countries, in Pakistan, women in the board are mostly those who are associated with the family of the controlling members of the organizations. Women are primarily offered directorship by founding members of organizations in order to have a firm hold and majority on the family business so that the inheritance of the business is passed on the next generation. The role of women on the board is thus limited in Pakistani organizations (Yasser, 2012).

The results of Abdullah, Ismail & Nachum’s (2016), study reveal that the conflicting results of a positive association of gender diversity with accounting performance and a negative relationship between gender diversity and market performance in emerging countries may be due to the cultural and institutional characteristics. The culture of an organization can change provided there is a change in the corporate structure. A change in the cultural traits is less likely to occur if the regulatory institutions desire only the change Yasser et al., 2011). Despite the fact that the developing countries are making efforts to encourage gender diversity in boards, they are unable to do so at the desired pace due to cultural norms, societal traits and other similar obstacles.

5. Conclusion

Women of today are playing a significant role as entrepreneurs, managers and as consumers. They provide valuable contribution to the global talent pool as future leaders of the global society (Adler, 1997). According to Powell (1999), women lacked the ambition and the confidence in the past among other leadership qualities including education and experience. Today, they are more educated and bring to the table positive management traits that impact the decision making process and corporate governance in significant ways. Despite the fact that some research studies disagree with the contributions women on board make towards firm performance, governments are adopting policies to ensure women representation in corporate boards based on the premise that
women’s participation and contribution has the potential to positively impact board functioning and firm performance (Abdullah, Ismail & Nachum, 2016). Governments around the globe have become more aware of gender equality and its role in the economic growth, prosperity, and bringing up a more educated and healthier generation (Terjesen & Singh, 2008). Yet countries having strong cultural resistance may experience reduced firm performance if gender diversity and gender quotas were forced onto them (Low, Roberts & Whiting, 2015). According to Yasser, Entebang & Mansor (2011), if certain cultural traits are well rooted in the society, it is not likely to change those traits if it is hampering the goals of a particular institution. Consolidated efforts need to be made on the part of the government, policy makers and various institutions to bring about a paradigm shift in the society. Most emerging nations have organizations appointing women having family relations with the major shareholder instead of appointing women on the basis of occupational experience or expertise. This results in conflicting research outcomes when measuring the impact of women representation on firm performance. In emerging countries, the corporate governance codes need to stress independent woman representation on boards. Independent directors are in a better position to assess and speculate a firm’s performance independently and objectively. Firms having boards that are gender diversified and independent reflect positive firm performance (Terjesen et al., 2016).

References


