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Corporate Governance and Gender Diversity: Evidence from FTSE 250

Abstract—This study aims at examining the direct effects of gender diversity on board of directors on the financial performance of a panel dataset of companies listed on the UK FTSE250 during the 2010-2015 years. The results show a positive relationship between the number of women directors and the return on assets and the return on equity indicators.

Board of Directors-Gender diversity-women directors—

I. INTRODUCTION

The representation of women on board of directors is heavily discussed. It has become the focus of politicians, academicians and investors in various countries (Pletzer and al., 2015). Despite the important number of studies that have been conducted in the last twenty years, the conclusions on whether the presence of women directors leads to a higher firm performance are equivocal.

On one hand, studies point to the positive effects women bring to the boardroom: more diverse knowledge, different experiences and values with consequent improvements in decision-making-processes and financial performance (Dang, Bender and Scotto 2014; Nguyen and Faff, 2006).

On the other hand, a considerable amount of research indicates that companies with female representation on corporate boards do not perform better and, the relationship between gender diverse boards and firm outcomes is either weak or non-significant.

Owing to these empirical discrepancies and the lack of a consensus about the relationship between female directors

and firm financial performance, conducting a quantitative study on a large sample of companies has merit.

In this study, we test the direct effect of women directors on the financial performance of a sample of companies listed on the FTSE 250 UK's index over the years 2010-2015.

In the recent years, the UK's government has set various policies (for instance Davies reports 2011; 2015) that aim at promoting gender equality on board of public companies. According to Catalyst (2015) the average percentage of women on boards of the FTSE 100 is 29% (against 12,5% in 2011).

II. THE ROLE OF WOMEN ON THE BOARD OF DIRECTORS

According to the agency theory, research examining the relationship between gender diversity and firm performance suggest that firm with more female directors tend to have a better monitoring system. That is, women are reported to be stricter than men regarding the application of ethical standards (Pan and Sparks, 2012). For instance, women are more likely reported having a propensity for sitting on board's audit and monitoring committees (Adams and Ferreira, 2009).

Moreover, scholars argue that women are reported to prepare in advance for board meetings (Huse and Solberg, 2006; Carli, 1999) thus, contribute to the enhancement of the debate and raise significant questions around monitoring issues. Besides, due to their values, women directors are more risk-averse than men, which may lead to sound financial decisions and less illegal and unethical consequences.

From the perspective of dependency theory, board of directors is a strategic mechanism as it plays an important role in the procurement of critical resources necessary for the company's development (Pfeffer and Salancik, 1978). Hence, gender diversity plays a critical role in bringing valuable resources and a broader knowledge, experiences and values to a board.

Hillman and al., (2002) argued that female directors, by virtue of their specific and unique educational backgrounds and due to their different socialization compared to men, they represent a critical human capital to the company's creation value. That is, women directors bring more experiences, opinions, and insights to the board and would help the company acquiring a sustainable and competitive advantage (Barney, 2001).

The literature suggests the availability of a more gender diverse board of directors ensures a broader perspective and more complete understanding of the financial market conditions and its shareholders interests.

We argue that an increased female representation has a positive impact on firm financial performance. More precisely, women directors positively affect accounting and market performance.

III. METHODOLOGY

Data source and variables

To examine the relationship between female representation on the board of directors and firm financial performance, the research used a sample of UK companies listed on the FTSE250 over the 2010-2015 period. Out of 250, only 180

firms were considered (due to missing data). The data is collected from two different sources: companies' annual reports and The FAME database.

Dependent variables: accounting and market performance measures are commonly used by research and similar studies. Return on Equity (ROE), Return on Assets (ROA) and Price to book ratio (PBR) are used to measure financial performance (Mahadeo et al., 2012).

Independent variables: gender diversity will be measured through two variables: presence/absence of women directors and the number of women directors (Pletzer and al., 2015; Post and Byron, 2015).

Control variables: are number of board directors (board size); firm size (number of employees) and firm sector (Services=1; Finance-Bank-Insurance=2; industry =3; Commerce and trade=4).

The General method of Moments (GMM) will be used as a regression method to identify the direct effects of the presence of women directors on financial performance. GMM is recommended by researchers as a technique to deal with the eventual problems of endogeneity (Arellano and Bond, 1991).

IV. RESULTS AND DISCUSSION

Table: Summary Results – GMM

| Hypotheses | | t-Value | Coeff |
|---------------------|-----|---------|--------|
| Number of women dir | ROE | 0.05 | 6.62 |
| Presence /women | ROE | 0.09 | 9.098 |
| Number of women dir | ROA | 0.04 | 43.09 |
| Presence of women | ROA | 0.08 | 27.05 |
| Presence of women | PBR | 2.79 | -76.00 |
| Number of women dir | PBR | 9.37 | 0.952 |

Note: Dependent variable: ROE; * p<0.05 ** p<0.01
*** p<0.001

t-values in square brackets and degrees of freedom in round brackets.

As can be seen from the regression table above, the results suggest that gender diversity may positively affect companies' accounting outcomes. The regression estimates indicate that the presence of women directors on boards contributes to a higher return on assets ($p = 0.08$) and a higher return on equity ($p = 0.09$). The relationship, however, are not strongly significant (risk level close to 10%). In contrast, a higher number of women on board has a significant impact on the accounting measures ($p = 0.05$; $p = 0.04$ respectively). Conversely, gender diversity on board seems to not affect the market performance (PBR with non-significant p -value $> 10\%$).

This leads us to confirm our main hypotheses suggesting a positive impact of female directors on firm financial performance. These results are consistent with previous studies supporting the business case for gender diversity (Kilic and Kuzey (2016); Carter et al., 2003; Erhardt et al., 2003; Campbell and Mínguez-Vera, 2008).

The literature supports the idea that the presence of women in the boardroom would improve the functioning of the corporate governance system (Carter et al., 2003), women directors would enrich the pool of knowledge as they bring various views and ideas, and consequently, improve the decision making process (Carter et al., 2003). Besides, it's

reported that women on board enhances the relations between the company and its customers and improves its communication with female clients (Rose, 2007). In the same line, Bilimoria (2000a) argues that female presence improves the board decision-making with their perspectives and views about the market trends. Women have better insights and knowledge about female customer's needs. Moreover, it was reported that female directors tend to discuss and debate top management decisions rather than "*rubber-stamp CEO decisions*"

In a study, conducted by Kilic and Kuzey (2016), it has proven that female directors have a positive impact on ROA and ROE of the investigated companies. The authors argue that "*female directors on boards have the potential to increase firm performance by proposing different approaches and views to board discussions, sending positive signals to the stakeholders of the company, building a positive firm image and maintaining a competitive advantage*".

In addition, women on boards contributes to a better and healthier board environment as they encourage a more interactive, predicative debate.

In conclusion, female directors on board have a positive influence over several levels, mainly the corporate governance system, the board decisions and outcomes, which in return, leads to better financial results.

V. CONCLUSION

The role of corporate governance in general and the board of directors in particular in shaping the firm's performance has drawn the attention of both academicians and researchers. It has proven that the board composition and structure have a significant influence on the capacity of firms at making sound decisions, and therefore, attracting investors. The presence of women as a composition of corporate boards has always been a controversial debate. An important amount of research suggests that boards with women positively influences firm financial performance (traditionally measured through accounting and market performance indicators). Conversely, other studies raise some doubts regarding the direct effect of women directors on firm performance. Our study, shows that boards with a higher representation of women lead to a better financial outcome. This results support the business case for gender diversity in the context of the UK. Using an advanced econometrical method based on the GMM technique which helps solving the endogeneity problem (Hermalin and Weisbach, 1998, 2003).

Our study however, tests only a direct relationship between gender diversity indicators and firm performance variables. Mediating and moderating factors were not considered which represents one of the limitations of this research. Moreover, our study focuses on one context (the UK), however, it's argued that the relationships between board composition (gender diversity in our case) and firm performance are sensitive to contextual factors such as the

country characteristics, regulations, political and legal situations (Bryon and Post 2015).

Future research that consider contextual factors (country characteristics) will provide more insights on the debate over board diversity and firm performance. Additionally, a study that includes more board and governance system characteristics as mediator/moderator factors in the relationship between gender on boards and firm performance is crucial as direct relationships ignore an important amount of potential factors that could mediate or moderate the relationship. Last, a more expanded research that includes other important aspects of diversity such as age, nationality, education background, etc., will offer more insights on whether more diverse board leads to higher firm performance.

<http://www.catalyst.org/knowledge/women-corporate-boards-globally> .

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