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## **Ethnic and Gender Diversity in Top Level Management and Firm Performance: Shareholder's Perspectives**

Rohail Hassan,<sup>1</sup> Maran Marimuth,<sup>2</sup> Eraj Tariq<sup>3</sup>, Raja Aqeel<sup>4</sup>

### **Abstract**

This study examines the relationship between demographic diversity in top management levels with a firms' financial performance using 84 non-financial companies in Malaysia. Demographic diversity consists of ethnic diversity and gender diversity. The top management level includes both the top management team and the board of directors. This study uses data from 2008 to 2012. Return on assets measures the financial performance. Ethnic and gender diversity measured by the number of Non-Malays and the number of females in top management respectively. This study incorporates descriptive statistics, correlation testing, and regression analysis. The results show that ethnic diversity in the top management team as well as in a board of directors has no impact on firm performance (ROE). However, the results of gender diversity have a positive impact on performance (ROE) in both perspectives (TMTs and BODs).

*Keywords:* Ethnic Diversity, Gender Diversity, Boards, Market Performance, ROE

### **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 & 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

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means something broader than corporate management, given achieving strategic goals (Bairathi, 2009). Effective corporate governance matters handle shareholders issues (Hassan & 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 & Marimuthu 2014). In contrast, Adams & Ferreria (2009) found that gender diversity among board members could result in poor firm performance. According to Zainal et al., (2013), ethnicity and firm performance has 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 (Carte & Silva, 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 84 non-financial Malaysian selected on the basis of judgmental sampling during the period of 2008-2012. 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 (Hassan et al., 2015).

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.

## **Literature Review**

### *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 (White, 2005). Awino (2011) demonstrated that the top management team diversity has a significant influence on organizational performance. TMT does not have a significant effect 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 (Pitt & Elezabeth, 2011). 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 & Searlem, 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 & Tandrayen, 2014).

### *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. Dezso & 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; Castanias & Helfat, 2001; Lado & Wilson, 1994; Finkelstein & Hambrick, 1996).

### *Cognitive Effects and Performance*

According to Kochan et al., (2003) studied the relationship between cognitive diversity in top management and job performance of the firm. They stated that the external factors play a major role in decision-making. There are some theories presented in this opinion as contingency theory and resource dependency theory. Cognitive diversity in the top management depends on the ability of the firm to manage the cognition in the different managers effectively.

Successful teams tended to allow interpretative ambiguity to flourish in the early stages of their life cycle but to exhibit more interpretative clarity in the later stages. This cycle of ambiguity and clarity may represent one dynamic solution to the twin problems of poor sense making on the one hand and uncoordinated activity on the other (Richard et al., 2004).

### *Management Diversity and Performance*

Jayne & Dipboye (2004) presented about the diversity in management and their effects on organizational performance. The study shows that the organization's performance and diversity have no linear relationship with most of the firms, which means that many companies are performing well with diversity and some are not. Findings indicate that management-level heterogeneity can be a critical asset in certain strategic contexts but the diversity performance.

### *Leveraging Diversity to Improve Firm Performance*

Simons & Rowlan (2011) argued that the leveraging of diversity improve firm performance. The diversity statement of seven multinational organizations has been stated with their performance and came up with the conclusion that increasing the diversity of the workforce involves problems such as dissatisfaction and conflicts. Diversity alone does not guarantee immediate, tangible improvements in organizational, group, or individual performance. Parrotta et al., (2012) argued that diversity in labor affecting the productivity of the organization.

## **Objectives of the Study**

### *Main Objective*

To examine the effect of ethnic and gender diversity in top-level management on financial performance.

### *Specific Objectives*

- To examine the effect of ethnic and gender diversity in top management teams on firm financial performance.
- To examine the effect of ethnic and gender diversity on the board of directors on firm financial performance.

### **Methods, Procedures, and Measures**

For this study, the data were from the top 100 non-financial listed companies in Malaysia out of which the data on 84 non-financial companies' data used to verify objectives; all the data were taken for five (5) years from 2008 - 2012. Here, to investigate the effect of gender and ethnic diversity on both top-level management teams (TMT's) and board of directors (BOD's) with firm performance. The dependent variable was financial performance, and the independent variables were gender and ethnic diversity, which were controlled by the TMT size, BOD members, and firms' size. The dependent variable ROE (return on equity) was used to measure firms' performance. The independent variables, ethnic and gender diversity, were measured on a ratio scale basis. As for BODs, the ethnic and gender determined by female members and the non-Malay managers were divided by the total number of board members. The same method is used to calculate the TMT's ethnic and gender diversity.

### *Sample Size*

A sample size of 84 non-financial Malaysian listed companies was based on the past 5-years time 2008-2012 annually.

### *Research Design*

The research consists of five main steps that are: an assessment of the literature, structure of a hypothesis or theory or model, data anthology, evaluation and testing by regression and correlation model, and the understanding of results to produce conclusions and relay them to the literature and theory.

### *Hypotheses*

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

#### General:

- Demographic diversity in TMT has a significant impact on firm financial performance.
- Demographic diversity in BODs has a significant impact on firm financial performance.

#### Specific:

H1: Firms financial performance is positively affected by gender diversity among TMT members.  
H2: Firms financial performance is positively affected by ethnic diversity among TMT members.  
H3: Firms financial performance is positively affected by gender diversity among Board members.  
H4: Firms financial performance is positively affected by ethnic diversity among board members.

*Model for the Study*

Equation for ROE:

$$Y = \alpha + \beta_{BT} + \beta_{BNMr} + \beta_{BFr} + \beta_{Firm\ Size} + \varepsilon \text{ ----- (Board of Directors)}$$

$$Y = \alpha + \beta_{TT} + \beta_{TNMr} + \beta_{TFr} + \beta_{TF} + \beta_{Firm\ Size} + \varepsilon \text{ ----- (Top Management Teams)}$$

*Research Instrument*

This study based on the secondary type of data. All the information collected from the annual reports of companies (2008-2012).

**Empirical Results**

*Effect of Demographic Diversity in Board of Directors Perspective*

*Descriptive Analysis in BODs Perspective*

Descriptive statistics were used for the calculation of the mean, standard deviation, maximum and minimum values. Table 1 shows the average of 84 non-financial companies in Malaysia (2008-2012). Descriptive analysis (mean, standard deviation, maximum, and minimum values) of the total number of members on board (BT), the total number of non-Malay members in the board (BNM), the non-Malay ratio on board (BNMr). The total number of females in the board (BF), female ratio on the board (BFr), Firm Size- Total Assets, Equity, Net Income and Returns on equity (ROE) presented below Table 1:

**Table 1. Descriptive Statistics in BODs Perspective**

<b>Variables</b>	<b>Minimum</b>	<b>Maximum</b>	<b>Mean</b>	<b>Std. Deviation</b>
<b>BT</b>	4	30	8.73	2.925
<b>BNM</b>	0	14	5.22	2.652
<b>BNMr</b>	.012	.137	.085	.034
<b>BF</b>	0	6	.72	.917
<b>BFr</b>	.0167	.096	.029	.016
<b>Firm Size- TA (000)</b>	9321.839	1.3699E9	3.855412E7	1.7720359E8
<b>Equity (000)</b>	-277746	1.0184E9	2.711859E7	1.2756155E8
<b>Net income (000)</b>	-3.2305E7	5.2414E8	2.853781E6	2.8010434E7
<b>ROE</b>	-4.165	10.240	.167	.816

**N= 398**

*Correlation in BODs Perspective*

Correlation explains the relationship between dependent and independent variables, whether it is negative or positive. Table 2 shows the results of the correlation details that involve the demographic diversity and profitability ratio in relation with the BOD. Based on the results, the interpretation can be made of the total female member ratio on the board (BFr) has the negative correlation (-0.111) with the firm performance at 0.05 significance level. That means gender diversity shows a relationship with firm performance. Another variable, such as a number of non-Malay in board and the number of females on board has the positive correlations (0.105) and the

significance level of 0.05. However, the number of non-Malay ratio on board is negatively correlated with the firm size (-0.099) and firm performance (-0.117). 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	8	9
1	BT	1	.357**	-.109*	.497**	.058	.007	.006	-.003	.026
2	BNM		1	.743**	.105*	-.055	-.084	-.095	-.045	.009
3	BNMr			1	-.095	-.025	-.09*	-.117*	-.070	-.006
4	BF				1	.830**	-.019	-.023	.011	-.096
5	BFr					1	-.052	-.064	-.016	-.111*
6	Firm Size						1	.981**	.430**	-.019
7	Equity (000)							1	.461**	-.016
8	Netincome (000)								1	.033
9	ROE									1

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

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

### **Top Management Teams**

#### *Descriptive Analysis in TMTs Perspective*

Table 3 shows the average of 84 non-financial companies in Malaysia (2008-2012). A maximum and minimum value have been calculated that shows the highest and lowest data of the companies in last five (5) years. Descriptive analysis (mean, standard deviation, maximum, and minimum values) of the total number of Top Management (TT), the number of non-Malay in top management (TNM), the number of the non-Malay ratio in top management (TNMr), Number of female in top management (TF). The number of female ratio in top management (TFr), Assets, Equity, Net Income, Returns on equity (ROE) presented below:

**Table 3. Descriptive Statistics in TMTs Perspective**

	Minimum	Maximum	Mean	Std. Deviation
TT	0	46	5.32	7.670
TNM	0	33	2.89	5.358
TNMr	.066	1	.3298	.171
TF	0	12	.93	1.672
TFr	.000	.166	.035	.021
Firm Size	9321.839	1.3699E9	3.855412E7	1.7720359E8
Equity (000)	-277746	1.0184E9	2.711859E7	1.2756155E8
Net income(000)	-3.2305E7	5.2414E8	2.853781E6	2.8010434E7
ROE	-4.165	10.240	.167	.816

### Correlation in TMTs Perspective

Correlation results depict the relationship that exists between dependent and independent variables, whether it is negative or positive. Those variables analyzed under the main perspective that is Top management teams. Table 4 shows the results of the correlation details that involve the demographic diversity and profitability ratio in relation with the TMT. Total female member ratio in top management teams (TFr) has the positive correlation (0.143) with the firm performance and contributes a positive at 0.05 significance level. That means gender diversity shows some impact on company performance. Other variable, such as a number of the non-Malay ratio in the top management team and the number of females in top management team has the positive correlation (0.198) and the significance level of 0.01.

**Table 4. Correlation Results in TMTs Perspective**

No	Variables	1	2	3	4	5	6	7	8	9
1	TT	1	.803**	.398**	.808**	.296**	.103*	.119*	-.058	.070
2	TNM		1	.637**	.748**	.267**	-.066	-.060	-.050	.059
3	TNMr			1	.388**	.198**	-.127*	-.125*	-.033	.085
4	TF				1	.587**	-.112*	-.108*	-.051	.100*
5	TFr					1	-.180**	-.183**	-.047	.143**
6	Firm Size						1	.981**	.430**	-.019
7	Equity (000)							1	.461**	-.016
8	Net income (000)								1	.033
9	ROE									1

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

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

### Regression Models

Regression explains at what extent the effect of the gender and ethnic diversity on firm financial performance. Those variables analyzed under the BODs, and TMT perspectives presented in Table 5.

### Discussion in Perspective of BODs

In the point of view of BODs, regression model explains the relationship between dependent variable and independent variables and to what extent this dependent variable shows the significant level of independent variables. Based on the results of Table 5 the regression model explained as follows:

$$ROE = 0.272 + 0.009_{BT} - 0.139_{BNMr} - 5.743_{BFr}$$

The independent variable gender only shows the significant relation at 0.05 significance level with the dependent variable the performance of the company (ROE). However, it is



negatively correlated with the dependent variable. It shows that the increase in the gender will decrease the firm performance. Another independent variable such as the number of the non-Malay ratio in the board has no significant relation with the dependent variable. As the gender diversity ratio negatively correlated with ROE, we can say that the increase in the ratio of the females will decrease the performance at 5.742. The R-square was 0.013 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 1.776 that shows the model is significant at 0.025.

#### *Discussions in Perspective of TMTs*

In the perspective of TMTs, regression model explains the relationship between the dependent variable ROE with all independent variables and the result shown in Table 5. Based on the results the regression model explained as follows:

$$ROE = 0.057 + 0.007TT + 0.07TNMr + 1.310TFr$$

The results explain that independent variable gender only shows the significant relation at 0.05 significance level with the dependent variable the performance of the company (ROE). Another independent variable such as the number of the non-Malay ratio in the board has no significant relation with the dependent variable. As the gender diversity ratio positively correlated with ROE, with an increase in the proportion of the females will increase the performance at 1.310. R-square was 0.006; that means only 2.4 % of the variation in the dependent variable explained by the model. Moreover, remaining 98.6% of the variation in the dependent variable remains unexplained through this model. It could 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 1.349 that shows the model is significant at 0.043. It means that the gender has some effect on the performance, but no effect has seen by ethnic diversity.

**Table 5: Regression Results on ROE in BODs & TMTs Perspectives (DV: ROE)**

Variables	Model – I (BODs)	Model – II (TMTs)
Constant	.147	.626
BNMr	.908	-
<b>BFr</b>	<b>.025**</b>	-
BT	.532	-
Firm Size	.608	.533
TNMr	-	.798
<b>TFr</b>	-	<b>.043**</b>
TT	-	.558
R <sup>2</sup>	0.013	0.024
F-test	1.779	1.349

\*Dependent variable: ROE

Model-I: BODs

Model-II: TMTs

p<0.05\*\*

## **Findings of the Study**

By examining, the effect of ethnic diversity in top management teams (TMT's) it has found that there is no effect on the firm performance if the company go for the ethnic diversity. The results though give us the positive significance, but the effect did not contribute significantly. However, the effect of ethnic diversity on the board of directors (BODs) found that ethnic diversity is not an appropriate variable for the diversification, as it gave a positive significance but did not contribute significantly. The effect of gender diversity in top management teams (TMTs) found that there is a partial effect on the performance of companies. The results show us the significant correlations between gender diversity and performance. Therefore, gender has the impact on the firm's financial performance.

In addition, the effect of gender in Board of Directors (BODs) found that firm performance affected positively by gender. The results showed the significant negative correlation of -0.111. It means demographic diversity in BOD has a negative impact on 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. However, ethnic diversity it indicates that the company performance has not influenced by either in TMT or BOD.

## **Limitations of the Study**

This paper only focuses on demographic diversity in TMTs and BODs of non-financial listed companies. In addition, this paper incorporated only last five-year data from 2008 to 2012 and thus, it would be quite challenging to generalize the findings, but these companies are top companies as a performance by total market capitalization.

## **Conclusions**

By looking at the demographic diversity, the article attempts to investigate the contribution of diverse corporate boards in firm performance. Admittedly, gender diversity among the board of directors (BODs) has significant positive impact on the firm performance of Malaysian Listed Companies. Hence, that women participation at board level can enhance the profits and perhaps improving internal operations of their companies. Ethnic diversity did not show the significant impact on the firm performance. As a result, of this study is inconsistent with previous research in the case of ethnic diversity. There might be several reasons behind this issue. Nevertheless, results depict kind of interesting picture regarding demographic diversity and firm performance.

In the event of the top management team (TMTs), the demographic diversity has the partial effect on the performance. It means ethnic diversity has no significance level. There might be several reasons behind this issue like board member belong to majority group of the country. On another hand, variable gender diversity has some significant impact on the firm performance. "Women also bring a different set of life experiences in organizations. The presence of women in a company's senior management should accordingly increase the management team's range of perspectives, cognitive resources, and problem-solving ability, resulting in better outcomes for the company (Hambrick et al., 1996)". The above line explains that the presence of women is the top management would be beneficial for the firms.

In a nutshell, we can conclude that women participation has a positive impact on firm 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.

## **Recommendations**

It is recommended that diverse board should be promoted in the firms to get better results. Moreover, to get better results, it is recommended that use of more ratios will help to understand the cases better e.g. Liquidity ratios and Debt ratios. Furthermore, increase the span of research by covering more companies. Lastly, make a comparison on a global level. Reach out to other companies on a global scale and make a comparison between different companies in the various regions of the world. These steps 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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