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The Moderating Effect of Board Diversity on the Relationship Between Board of Directors Characteristics and Firm Performance in Oman: Empirical Study

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Abstract: This study has two main substantial targets and one of them is the examination of the relationship between the board of director characteristics namely, board size, board independence, board meeting, CEO tenure and CEO duality and firm performance. The other aim is to explore the moderating effect of the board diversity (board foreign members on the board and the board commitment) on the association between the board of director and firm performance. The sample of this study covered non-financial companies in two years (2011 and 2012). This study used multiple regressions to analyze the association between the independent variables and dependent variable. In addition, this study uses hierarchical multiple regression to examine the relationship between moderator's variable and dependent variable. This study found a positive relationship between board size, board meeting, CEO tenure and CEO duality with ROA but no significant. On the other hand, a negative but not significant relationship was revealed between board independence and ROA. Moreover, this study found moderating but not significant effect of board diversity on the board of director-ROA relationship.

Key words: Board of Director Characteristics · Board diversity · Agency theory · Resource dependence theory and Oman

INTRODUCTION

Businesses around the globe require development and growth in an attempt to garner investments. Before investing in a certain business, investors often make sure that the business is secure and stable financially in order to produce profits in the long-term [1, 2]. More recently, corporate governance has grown in importance, particularly with the collapse of major corporate like Commerce Bank, Enron, Arthur Anderson, WorldCom, HIH, Harris Scarfe in the context of the United States, Europe and other countries [3, 4]. Therefore, corporate governance is one of the most widely researched topics as a mechanism to minimize conflicts of interests between managers and investors. Its objective is to safeguard the capital owners from opportunistic activities [5-8] and to make sure that management exert effort to achieve the shareholders' and stakeholders' interests.

Moreover, the current study is the first study to investigate the moderating effect board diversity namely the foreign and the commitment of the board, on the relationship between board director and firm performance as introduced in this study. Previous studies only focused on board of directors and audit committee's impact upon firm performance [5, 1,3,9]. With consistence to [10, 12] the relationship between corporate governance and firm performance is depends on the level of a third variable.

Literature Review and Hypotheses Development: The size of the board is considered to affect the strength of its monitoring. In other words, the larger the board, the more capable it is to monitor top management [13]. On the other hand, [14] study revealed that as the size of the board

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increases, monitoring management turns less effective. This is consistent with [15] contention that the board of directors are less effective when their numbers are more than seven or eight members.Viewed from another perspective, the board function is the acquisition of the resources for the firm, based on its members' relationship with other firms [7, 16].

Although there are empirical evidences on the effect of board size on firm performance, the findings are still mixed. The previous studies in the developed countries are consistent with the agency theory by confirming that there is a negative relationship between board size and firm performance. These studies include [17,18]. Similarly, in the developing countries many studies found the relationship between the board size and firm performance to be negative [19, 20]. In the light of the resource dependence theory, many studies in the developed countries have found that the relationship between board size and firm performance is a positive one [21,17]. In the developing countries [22-25].

On the basis of the previous discussion and supporting arguments, the following hypotheses are developed;

H_1: There is a relationship between board size and ROA.

Board Composition and Firm Performance: Board composition is another measure of the board characteristics quality which has caught the attention of researchers and practitioners alike [26]. Similarly, the board's independent directors can work independent of the control or influence of the major shareholders, management or other parties [25].

In view of corporate governance, the agency theory indicates that sufficient monitoring mechanisms should be employed to safeguard shareholders from the self-interests of management. Hence, a high number of external directors on the board are considered as having a potential positive impact upon performance [27, 6, 28]. On the other hand, consistent to resource dependence theory, the independent board enables board members to better understand complex environments and give multiple knowledge and experience from different sources to improve the firm performance [7].

The finding regarding to this relationship between the board independence and firm performance are still inconclusive. Some of them found a positive either in the developedcountries like, [21-30] or developing countries [5, 1, 31, 19]. On the other hand, some authors got a negative relationship is found between board independent and firm performance whether in developed countries [32, 33] and in the developing countries in the studies by [23, 34, 35]. Based on the theoretical perspective and debate above, the following hypotheses are expressed:

H_2: There is a positive relationship between board composition and ROA.

Board Meeting and Firm Performance: [36, 14] claimed that the more frequent the meetings the more likely a superior performance can be achieved. Similarly, [37, 38] stated that board meeting time is a critical resource used to improve the corporate board's effectiveness indicating that with frequent meetings, the board is more likely to improve the performance of the firm and perform their duties according to the interests of the shareholders. Regarding the resource dependence theory, the board meeting helps the board to valuate and pursue a board business time by time and to solve any problem faced by employees [39, 40]. And hence, when the board meeting frequency increases, it means increased performance for a firm.

The relationship between board meetings and firm performance was reported to be positive in the developed countries [41] and in the developing states such as, [25, 42]. While some studies have confirmed the negative effect of the board meeting on firm performance in both developed such as [43, 44] and developing countries [45, 46]. Based on the above discussion, it is reasonable to hypothesize the following hypotheses.

H_3: There is a relationship between the number board meeting and ROA.

CEO Tenure and Firm Performance: CEO tenure is a critical important construct for research related to the organization and executive leadership [47, 48]. According to the resource dependence theory, the longer time the member spends in a job, the more experience and knowledge he will gain [40]. In contrast to the resource dependence theory, the issues in agency theory have their basis on two basic notions which are goal incongruence and information asymmetry [49].

Generally, there are limited researchers that have investigated the relationship between CEO tenure and firm performance in the developed countries and found a positive relationship [50, 48]. In addition, some other researchers found similar results in the developing countries such as, [11, 47, 38].

Moreover, some authors found a negative association between them like [51, 52]. Similarly, studies in the developing countries found a negative association between CEO tenure and firm performance [47, 36]. Finally, other studies found no relationship between CEO tenure and firm performance [32, 38]. Hence, the following hypnosis's are reasonably introduced for further empirical tests:

H_4: *There is a relationship between CEO tenure and ROA*.

CEO Duality and Firm Performance: CEO duality holds significant importance on the basis of the premise that leadership structure significantly impacts corporate governance as the top personnel have the biggest influence on the activities of the board and hence, could affect the performance of the firm.

The agency theory postulates that CEO duality leads to imbalance of the distribution of corporate power as significant management and control remains in the hand of a single person, a position which leads to board ineffectiveness [53]. Such imbalance makes it challenging for the corporate board to monitor or provide measures against the CEO as the board lacks independence [27].

Some authors found that there is a positive relationship between CEO duality and firm performance either in the developed countries [54, 55] or in the developing countries [31, 3]. On the other hand, the relationship between CEO duality and firm performance to be find a negative either in the developed countries like [21, 56] or in the developing countries such as [1, 9]. Apart from previous finding, there are some researcher find that there is no relationship between CEO duality and firm performance either in the developed countries like [43]or in the developing countries such as [19, 57]. Hence, the following hypnosis's are reasonably introduced for further empirical tests:

H_4: *There is a relationship between CEO duality and ROA*

The Moderating Effect of the Board Diversity on the Relationship Between Corporate Governance and Firm Performance: The diversity of the board is described as the variety in the board of directors' composition. There are two types of diversity namely the observable and the non-observable type. The former includes gender, age, race and ethnicity while the latter includes knowledge, education, values, perception and characteristics of personality [58-60]. Majority of diversity studies and its impact upon performance concentrate on the demographic type of diversity.

[61] called for the exploration of the level of diversity in Australian companies by examining the less discernible directors' background and roles in detail. Moreover, the findings regarding the relationship between board structure and firm performance are still inconclusive. As suggested by [10] future research should focus on examining the moderating role of board diversity on the relationship between corporate governance and firm performance.

Foreign Members Serving on the Board and Firm Performance: The foreign directors bring valuable knowledge related to contextual issues in international markets and are enabled to maximize the strategic decision-making quality [62]. In the light of the resource dependence theory, the foreign directors inside firms give a lot of foreign experiences and foreign knowledge which help firms to solve any problem inside multinational firms and to help employees to deal with foreign problems if any [63].

In the literature, few studies in the developed countries have directly explored the relationship between foreign directors and firm performance. However, there is lack of investigation into this variable in the emerging market. This study was contributing to literature by testing the following hypotheses.

H_{6a}: *The foreign members serving in the board moderate the relationship between the size of the board directors and ROA.*

H_{6b}: *The foreign members serving in the board moderate the relationship between the board composition and ROA.*

H_{6c}: *The foreign members serving in the board moderate the relationship between the board meeting and ROA*.

The Commitment of the Board and Firm Performance: Attending the meetings indicates the seriousness of work and the assessment of problems first hand and it signifies working to resolve them in order to make good decisions that help to achieve the objectives of the entity and investors [64]. In general, the commitment of the board indicates how all the members are obliged to improve the overall performance [63]. Despite the importance of commitment variable for the firm performance the effect of this variable on the firm performance is still greatly neglected in the literature [65-67] recommended studying the effect of board diversity upon firm performance.

This study was an attempt to examine the effect of relationship between the board diversity on the corporate governance and performance by testing the following hypotheses.

H_{7a}: *The commitment of the board moderates the relationship between the size of the board directors and ROA.*

H_{7b}: *The commitment of the board moderates the relationship between the board composition and ROA.*

H_{7c}: *The commitment of the board moderates the relationship between the board meeting and ROA.*

Research Method and the Study Models: This study is comprised of internal corporate governance variables such as, board size, board independence, board meeting, CEO tenure and CEO duality, board diversity like foreign members on the board and board commitment and two control variables such as, firm size and leverage were tested. In addition, the relationship between the board of direct characteristics (size, independence and meeting), the moderating effect of board diversityand two control variables were tested by using the two following model:

$$\text{Model 1} = ROA = \alpha 0 + \beta 1 * BOARDSIZE + \beta 2 * BORADIN + \beta 3 * BOARDME + \beta 4 * CEOTENU + \beta 5 * CEODUALITY + \beta 6 * FIRMSIZE + \beta 7 * LEVERAG + \varepsilon \quad (1)$$

$$\text{Model 2} = ROA = \alpha 0 + \square 1 * BOARDSIZE + \square 2 * BORADIN + \square 3 * BOARDME + \square 4 * CEOTENU + \square 5 * CEODUALITY + \square 6 * BO\_FORE + \square 7 BO\_COM + \square 8 * BO\_FORE * BOARDSIZE + \square 9 * BO\_FORE * BORADIN + \square 10 * BO\_FORE * BOARDME + \square 11 * BO\_COM * BOARDSIZE + \square 12 * BO\_COM * BORADIN + \square 13 * BO\_COM * BOARDME + \square 14 * FIRMSIZE + \square 15 * LEVERAG + \varepsilon \quad (2)$$

Data Analysiz and Results

Profile Company and Descriptive Statistic:

Correlation Analysis:

Multiple Liner Regression Analysis

Regression Results of Model (Based On Accounting Measure): The adjusted coefficient of determination (R^2) shows that 0.276% of the dependent variable's variation is explained by the independent variables' variation. In other words, the firm performance variation as proxied by ROA was explained and accounted for statistically by the regression equation. The results presented in Table 5 also indicates that the model is significant as F value is

Table 1: Summary of Variables Measurement

N0	VARIABLES	ACRONYM	OPERATIONALISATION
Dependent Variables (DV)			
1	Return On Assets ratio (%)	ROA	Earnings before tax divided by total assets of the company.
Independent Variables (IV)			
3	Board Size (number)	BOARDSIZE	Total number of directors serving on the board of directors.
4	Board Composition (%)	BORADIN	The number of independent non-executive directors on the board relative to the total number of directors.
5	Board Meeting (number)	BOARDME	The frequency number of meetings during a year for the board directors.
6	CEO Tenure (year)	CEOTENU	The period of CEO's serving in the company.
7	CEO Duality	CEODUALITY	Dummy variable equal to "1" if the CEO is also the chair of the board and "0" otherwise.
Moderators Variables (MV)			
17	The Foreign Member on the Board (number)	BO_FORE	The number of non-executive foreign directors divided by the total number of board members.
18	The Commitment of attendance (ratio)	BO_COM	The commitment of the board is measured by the attendee of the meeting. It meant by ratio of attendance for all the members during a year.
Control Variables (CV)			
8	Firm Size (number)	FIRMSIZE	The natural log of total assets.
9	Leverage (%)	LEVERAG	The ratio of total liabilities to total assets.

Table 2: Frequency of the Companies regarding to the CEO Duality Variable

The Legal Counsel	Frequency	Percentage
Duality	12	7%
No Duality	150	93%
Total	162	100%

Table 3: Descriptive Statistics of Continuous Variables

Variables	Unit	Mean	Std. Deviation	Min	Max
Board Size (BOARDSIZE)	Number	7.10	1.52	5.00	12.00
Board independence (BORADIN)	Ratio	0.88	0.19	0.00	1.00
Board Meeting (BOARDME)	Number	5.65	1.93	.00	15.00
CEO TENURE (CEOTENU)	Years	10.12	2.81	3.00	20.00
Foreign Member (BO_FORE)	Ratio	0.28	0.26	0.00	1.00
Board Commitment (BO_COM)	Ratio	0.84	0.16	0.00	1.00
FIRM SIZE (FIRMSIZE)	OR	62979251.03	125657047.90	605320.00	685377000.00
LEVERAGE (LEVERAG)	Ratio	0.49	0.28	0.02	1.72
Return On Assets (ROA)	Ratio	0.06	0.10	-0.34	0.32

Table 4: Results of Pearson Correlation Analysis

	1	2	3	4	5	6	7	8	9
1) BOARDSIZE									
2) BORADIN	-.038								
3) BOARDME	.036	.135*							
4) CEOTENU	-.063	-.162**	.099						
5) BO_FORE	-.102	-.063	-.234***	.221***					
6) BO_COM	.062	.010	.297***	.063	.049				
7) FIRMSIZE	.321***	-.046	.070	.129	-.081	.050			
8) LEVERAG	-.088	-.024	-.059	.134*	.353***	.057	-.062		
9) ROA	.152*	-.085	.072	.043	-.115	.115	.257***	-.451***	

Notes:

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

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

*Correlation is significant at the 0.1 level (2- tailed).

Table 6: Regression Results of Model (Dependent= ROA)

Variables	Standardized Coefficients -------------------------------- Beta	t-value	Sig.
Board Size (BOARDSIZE)	0.042	0.569	0.570
Board independence (BORADIN)	-0.085	-1.196	0.234
Board Meeting (BOARDME)	0.040	0.565	0.573
CEO TENURE (CEOTENU)	0.059	.822	0.412
CEO Duality(CEODuality)	0.073	1.038	0.301
FIRM SIZE (FIRMSIZE)	0.214	2.864	0.005
LEVERAGE (LEVERAG)	-0.442	-6.338	0.000
R2			0.276
Adjusted R2			0.243
F-value			8.368
F-Significant			0.000
Durbin Watson statistics			1.880

significant at ($F=8.368$, $p<0.01$), indicating model validity. In addition, the Durbin-Watson (DW) test is used as a statistical test for the detection of autocorrelation. The rule of thumb states that the acceptable range of such a statistical test is 1.5-2.5. In this study, the Durbin-Watson value is 1.880, which is in the acceptable range and this indicates independence of observations.

Hierarchical Multiple Linear Regression Results: The results of the hierarchal multiple regression analysis are described through the following four models as explained in Table 7.

Step 1: In this model, the firm size and leverage are entered as a control variable into the regression model in the first step and coefficient of determination F-value is (27.383) with F Sig (0.000). The model found (R^2) to be 0.256, indicating that 25.6% of the firm performance (ROA) can be explained by the firm size and leverage and with Significant F change 0.000 level. The result in Table 6 indicates that the firm size is found to be positively and significantly related with ROA with the indicators ($\beta=0.230$, $t=3.361$, $p<0.05$). On the same path, this table shows a negatively significant relationship between leverage and ROA with the indicators ($\beta=-0.437$, $t=-6.372$, $p<0.01$).

Table 7: The Moderating Effect of the Board Diversity on the Relationship Board Directs Characteristic and ROA

	Step1			Step 2			Step3			Step4		
	Control variable			Without interaction			Moderator variable			With interaction		
Variables	Beta	T	Sig.	Beta	T	Sig.	Beta	T	Sig.	Beta	T	Sig.
FIRMSIZE	0.230	3.361	0.001	0.214	2.864	.005	0.218	2.923	0.004	0.239	2.940	0.004
LEVERAG	-0.437	-6.372	0.000	-0.442	-6.338	.000	-0.470	-6.415	0.000	-0.453	-5.889	0.000
BOARDSIZE				0.042	.569	0.570	0.036	0.499	0.619	0.013	0.169	0.866
BORADIN				-0.085	-1.196	0.234	-0.083	-1.177	0.241	-0.121	-1.580	0.116
BOARDME				0.040	.565	0.573	0.018	0.241	0.810	0.050	0.584	0.560
CEOTENU				0.059	.822	0.412	0.043	0.585	0.560	0.038	0.505	0.615
CEODuality				0.073	1.038	0.301	0.081	1.152	0.251	0.078	1.085	0.280
BO_FORE							0.062	0.795	0.428	0.072	0.873	0.384
BO_COM							0.121	1.672	0.097	0.116	1.279	0.203
board_fore										-0.059	-0.766	0.445
Board_com										0.012	0.119	0.906
Independence_fore										0.030	0.390	0.697
Independence_com										0.086	1.057	0.292
Meeting_fore										0.069	0.793	0.429
Meeting_com										-0.068	-0.559	0.577
F value	27.383			8.368			7.001			4.357		
F Sig.	0.000			0.000			0.000			0.000		
R2	0.256			0.276			0.293			0.309		
Adjusted R2	0.247			0.243			0.251			0.238		
R2change	0.256			0.019			0.017			0.016		
Significant F change	0.000			0.535			0.156			0.754		
Durbin Watson												1.880

Step 2: In this model, the board of director's characteristics (size, independence, meeting, CEO tenure, CEO duality) were introduced to the model. This model, however, was found to be significant ($F=8.368$, $p<0.01$) with adjusted R^2 as 27.6 per cent. The results in Table 6 shows that firm size (FIRMSIZE) was found to have positively significant relationship with ROA with the indicators ($\beta= 0.214$, $t= 2.864$, $p<0.01$). Moreover, leverage (LEVERAG) was found to have strongly negative significant effect on firm performance (ROA) with the indicators ($\beta= -0.442$, $t= -6.338$, $p<0.01$).

Step 3: In this model, foreign member on the board (BO_FORE) and board commitment (BO_COM) were introduced to examine its predictive power toward firm performance (ROA). This model, found the predictive powers to be significant ($F=7.001$, $p<0.01$) with adjusted R^2 as 29.3 per cent. Even though the model showed significant at the 0.01 level but it did not improve the explanatory power of the model since the R^2 change was not significant (R^2 change=0.017, $p<0.5$). Furthermore, this model accounted for 25.1 per cent of the variance in the model. Four variables in this model were reported to have a significant predictive power toward firm performance (ROA). The leverage (LEVERAG) was found to have a strong negative significant effect on firm performance (ROA) with the indicators ($\beta= -0.470$, $t= -6.415$, $p<0.01$). On the other hand, Firm Size (FIRMSIZE) was found to have positively significant effect on firm performance (ROA) with the indicators ($\beta= 0.218$, $t= 2.923$, $p<0.05$).

Step 4: In this model, the interaction terms between board diversity (foreign member on the board and board commitment) and board directors (size, independence and meeting) were examined to test the moderating effects in this study. This model reported the interaction significant at the 0.01 level of significance ($F=4.357$, $p<0.01$) accounting for 92.3 per cent of the dependent variance. However, this model found to be insignificant (R^2 change= 0.016, $p>0.05$). The result in Table 6 showed that leverage (LEVERAG) was reported to be significant predictors of firm performance (ROA) with indicators ($\beta= -0.453$, $t= -5.889$, $p<0.01$). On the other hand, Firm Size (FIRMSIZE) was found to be positively significant indicators to ROA ($\beta= 0.239$, $t= 2.940$, $p<0.01$). Finally, the results regarding the interaction terms reveals that there was insignificant moderated by board diversity.

RESULTS AND DISCUSSION

We discuss results that related to the relationship between board of director characteristics and the firm performance and the moderating effect of board diversity on the relationship between board of director on ROA. The hypothesis H1 is not supported. One plausible justification of insignificant relationship between board size on ROA is the possibility that CEO dominates the board activities which forms information asymmetry [45]. Moreover, the result found an insignificant relation between board independence and ROA. Therefore, hypothesis H2 is also rejected. A plausible explanation behind the insignificant relationship between board independence and ROA lies in the fact that outside directors may negatively affect the companies' performance, because of lack of competence or motivation.

In addition, the outcome showed an insignificant association between board meeting and ROA and hence, rejecting hypothesis H3. A plausible justification of insignificant relationship between board meeting and ROA is that board meeting is not necessarily a reflection of improved firm performance and more often than not, frequency of board meetings increases when problems arise [15]. The finding also showed no relationship between CEO tenure and ROA. The possible explanation on the lack of association between CEO tenure and ROA is that the structure of the board may not enable CEO to motivate and create new things because everything is under the control of the board of directors.

The result found foreign members of the board to be insignificant in moderating the relationship between board director's characteristics namely board size, board independence and board meeting and ROA. The justification behind the insignificant moderating impact of the foreign members of the board on the relationship between board director characteristics (size, independence and meeting) and ROA may be attributed to foreign members' lack of knowledge on current environment in order to deal efficiently with decision making. On the other hand, a reasonable explanation for the insignificant moderating impact of board commitment on board of directors-ROA relationship is the inefficiency of board size and members' under-qualification, inexperience and lack of knowledge/information to deal with environment.

CONCLUSION

This study was an attempt to achieve two main aims namely, to examine the relationship between board of director's characteristics and firm performance (ROA) and to explore the moderating effect of board diversity (foreign members on the board and the board commitment of the board) between board of director namely, board size, board independence and board meeting on the form performance. Moreover, it selected non-financial companies in 2011 and 2012. Although, this study examined the main internal corporate governance mechanisms with firm performance, the results failed to support the hypotheses because of the provided various reasons. This study is among the rare studies that investigated the relationship between corporate governance and firm performance in the Gulf countries in general and in Oman, in particular. Moreover, this study employed two theories namely the agency theory and resource dependence theory, which both turned out to be unsuitable for Omani environment.

This study recommends future research to add other main internal variables of corporate governance to firm performance such as, experience and qualification of board, compensation of board, interlock of board, audit committee characteristics, executive committee characteristics, purchase committee, risk committee, ownership structure and other variables that may lead to improved firm performance.Secondly, future authors should extend sampling to many years and many sectors in order to examine extensive firm performance. They should also employ other measurements of performance such as, marketing measurement, balance scorecard and others. Thirdly, this study suggest future research to integrate the internal and external variables of corporate governance in order to enhance the performance and enrich existing literature and also, it recommends the investigation of the relationship between corporate governance and firm performance through stewardship theory, institutional theory, stakeholder theory, transaction cost theory, political theory and ethical theories. Fourthly, this study suggests future authors to examine this relationship between two Gulf countries in order to provide a clear picture of corporate governance practice.

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