

Board Diversity and Firm Performance: Evidence from Indonesia

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Abstrak

Dalam dunia bisnis pada saat ini, karyawan dan manajer memiliki tingkat diversitas/keragaman yang tinggi mulai dari usia, etnis, dan gender. Dewan dengan latar belakang fungsional yang beragam cenderung menghasilkan perubahan yang lebih strategis yang dapat mengarah pada peningkatan kinerja perusahaan. Penelitian ini bertujuan untuk melihat pengaruh keragaman dewan direksi terhadap kinerja perusahaan. Keragaman dewan dalam penelitian ini diukur berdasarkan usia, gender, dan juga pendidikan. Untuk kinerja perusahaan, penulis menggunakan return on assets untuk mengukur kinerja perusahaan. Sampel dalam penelitian ini adalah 317 perusahaan yang terdaftar di Bursa Efek Indonesia dari tahun 2018 sampai dengan tahun 2020. Data dianalisis dengan menggunakan statistik deskriptif dan analisis regresi. Hasil penelitian menunjukkan bahwa secara simultan diversitas usia, jenis kelamin, dan pendidikan pada dewan direksi berpengaruh terhadap kinerja perusahaan. Namun secara parsial, diantara diversitas umur, gender, dan pendidikan hanya keragaman usia yang berpengaruh positif dan signifikan terhadap kinerja perusahaan. Kondisi ini menimbulkan anggapan bahwa direksi dengan direksi yang lebih muda dapat memberikan wawasan dan sudut pandang baru dalam mengambil keputusan keuangan dan non keuangan. Di sisi lain, keragaman gender dan pendidikan tidak memberikan pengaruh yang signifikan terhadap kinerja perusahaan. Kondisi ini disebabkan oleh kondisi di Indonesia yang masih menghargai laki-laki untuk peran struktural dibandingkan perempuan dan mayoritas direksinya hanya menyelesaikan pendidikan sarjana.

Kata Kunci: Kinerja Keuangan, Diversitas Direksi, Usia, Gender, Pendidikan

Abstract

In today's business entities, employees and top management teams become increasingly diverse in terms of age, ethnicity, and gender. Boards with diverse functional backgrounds are more likely to produce more strategic change that could lead to good firm performance. This study aims to see the effect of board diversity towards firm performance. Board diversity in this research is measured by age, gender, and also education. For the firm performance, writer use return on assets to measure the firm performance. The sample for this research is 317 companies listed in Indonesia Stock Exchange from 2018 to 2020. The data analysed by doing the descriptive statistic and regression analysis. The result shows that simultaneously the diversity of age, gender, and education in the board of directors affect the firm performance. However, partially; between the broad diversity of age, gender, and education only the diversity of age has a positive and significant effect towards firm performance. This condition leads to the assumption that boards with younger directors could give new insights and point of view in taking financial and non-financial decisions. On the other hand, the diversity of gender and education do not give a significant effect towards firm performance. This condition is caused by the condition in Indonesia, which still values men for the structural role than women and the majority of the directors only finished their education until bachelor degree.

Keywords: Financial Performance, Board Diversity, Age, Gender, Education

INTRODUCTION

In comparison to homogenous groupings of players, a group with diverse backgrounds should have access to a wider range of network linkages (bringing in new information and outside resources), experience, knowledge, and viewpoints (Makkonen, 2022). The variety of the board, however, creates possibilities and difficulties for board practice and study. It is possible to

distinguish between diversity that is task-related, such as educational or functional background, diversity that is non-task-related, such as gender, age, ethnicity, or nationality, and structural diversity, such as board independence and CEO non-duality. Diversity may be advantageous and costly (Adams et al., 2015; Ararat et al., 2010).

In today's business entities, employees and top management teams have become increasingly diverse in terms of age, ethnicity, and gender, as well as tenure, experience, educational background, and socioeconomic status (Darmadi, 2010). According to Kipkirong Tarus & Aime (2014), It is more probable that boards with a variety of functional backgrounds will make more strategic changes. For this reason, functional background diversity is likely to broaden the lens and, in doing so, increase strategic transformation. Functional background determines how choices are made, challenges are identified, information is processed, and even the kind of corporate strategies that are adopted.

Therefore, the board of directors is crucial for monitoring the firm's management (Fraga & Silva, 2012). Company performance measures the company's success in carrying out operational activities, which can be seen from the financial statements. The Board of Directors strives to improve the company's performance to attract the attention of investors, debtors, and the public (Agustina et al., 2022). Achour (2021) asserts that the board of directors is essential to the development of the company's future direction and the adoption of strategies. One way that diversity improves board independence is by allowing directors from diverse backgrounds to pose issues that may not have been raised by more conventional directors, which promotes business performance. Consequently, there may or may not be a correlation between board diversity and business value (Carter et al., 2003; Ozdemir, 2020; Schwizer et al., 2020).

The premise that diversity on this board of directors is helpful is supported by a number of hypotheses. The resource dependency hypothesis, the first theory, contends that preserving board diversity helps a company to access resources necessary to lower risks and enhance operational outcomes (Taljaard et al., 2015). A diversified board offers much more diverse and important resources for improved decision-making, which improves business success. The agency hypothesis is the next theory after that. According to the agency hypothesis, board diversity is likely to promote board independence since diverse member qualities and backgrounds make it easier for the board to challenge the original structure, whereas similar features in a standard board may make it difficult (Song et al., 2020).

According to Achour (2021), The majority of European nations (including France, Italy, and Norway) have enacted legislation requiring greater gender participation on corporate boards of directors. These rules' primary goal was to eliminate gender inequity, which heavily influences the makeup of the board of directors. Research on how gender diversity affects business success has been frequently cited by other scholars. Research conducted by Agustina et al. (2022); Altin (2021); Austin (2012); Ciavarella (2017); and Miller & del Carmen Triana (2009) said that having a diverse mix of genders within a board of directors would improve the content of meetings and the capacity to make decisions. This outcome contradicts studies undertaken by Hassan (2018); Manurung et al. (2020); and Shehata et al. (2017).

Many other researchers have done it in several countries for the diversity of directors of age, gender, and education. The research that discusses age diversity and its effect on firm performance conducted by Darmadi (2010); Fernández-Temprano & Tejerina-Gaite (2020); Lilis Gustiana et al. (2021); and Rumapea & Silitonga (2020) As a result of the age inequalities among the directors, it has been asserted that age diversity affects firm performance. It will also result in differences in knowledge and skills, as well as in decision- and policy-making inside the

organization. This, however, goes against the findings of studies done by EmadEldeen et al. (2021); Novitasari (2018); Oktapiani (2017); and Shehata et al. (2017).

Educational diversity also influences firm performance. This condition is supported by research conducted by (Bin Khidmat et al., 2020; Fraga & Silva, 2012; Oktapiani, 2017) It claims that using each director's experience in accordance with their educational background will aid the decision-making process on current problems and planned by employing the educational variety of each director in a company's board of directors. Despite the fact that the study by Abduh & Azmi Omar (2012); Fernández-Temprano & Tejerina-Gaite (2020); Lilis Gustiana et al. (2021); Rose (2007).

Seeing this phenomenon that occurs in companies around the world, the researchers intend to see whether there is an influence of director diversity represented by age diversity, gender diversity, and educational diversity and their effect on firm performance by taking research samples on companies listed on the Indonesia Stock Exchange in 2018 until 2020

LITERATURE REVIEW

1. Agency theory

Based on research conducted by Jensen & Meckling (1976), Organizational structures and corporate policy play a big role. Top executives in major contemporary firms are characterized by agency theory as having interests distinct from those of the principle or shareholders, when both the principal and the agent are utility maximizers. Only a labor contract that governs each party's rights and duties while taking into consideration the overall benefit may implement this approach (Arifah et al., 2012). According to this hypothesis, unequal or disparate knowledge might lead to the probability of primary losses. It's possible that the principal and agent's conflicting interests are what's causing this informational discrepancy. It is thought that the variety of the directors might lessen these issues. The conversations will take on a different hue due to the variations in each director's background brought on by disparities in culture, gender, age, and educational attainment.

2. Resource dependence theory

According to the notion of resource dependency, the company's board is a vital source of knowledge and resources. The firm can gain from the diversity of the board by forming a network with outside parties to get the essential data and guarantee the availability of resources (Hillman et al., 2009). The relationship between the concepts of power and dependency is explained by the resource dependence theory; for instance, the board of directors serves as a link connecting the corporation to external sources of dependence (Kendriila et al., 2022).

According to the idea of resource dependency, board diversity may increase market valuation by connecting a firm to its external environment and safeguarding crucial resources including expertise, contacts in the corporate world, reputation, and legitimacy (Arnegger et al., 2014; Goodstein et al., 1994). This theory describes the connection with an organization's stakeholders, such as customers and communities, may improve possibilities, reputation, and value. Corporate boards made up of qualified people from various backgrounds and constituencies can do this (Ntim, 2015). Carter et al. (2003) For instance, it is suggested that an organization's capacity to enter competitive marketplaces can be greatly improved by matching the diversity of its board of directors to that of its customers and suppliers.

3. Firm performance

Financial performance analysis examines how well a business has followed the right financial performance guidelines. Analysis of financial ratios, such as profitability ratios that gauge a firm's capacity to turn a profit from sales, assets, and corporate capital, is frequently used to gauge financial performance (Hidayat et al., 2021). According to Arsita (2021), The performance of this firm is a description of a company's financial state or condition that is examined using financial analysis techniques in order to determine how well or poorly the financial situation of a company corresponds to work performance during a specific time period. Profitability is the type of financial performance that was utilized in this study to demonstrate a business' capacity to generate profits over a given time frame.

4. Director diversity

The variances in social, cultural, physical, and environmental factors that influence how individuals think and act are known as diversity. According to Wijaya (2015) Board diversity is defined in a number of ways, one of which is the distribution of disparities among the members of the board of commissioners and directors, which are made up of people with diverse backgrounds and traits inside an organization. Fatima (2018) According to this definition, diversity is the difference and variety of qualities held by the board of directors in terms of gender, age, and culture, offering a diversity of traits, viewpoints, and information that supports the corporate decision-making process. The greater cognitive diversity of the board of commissioners and directors will result in a richer knowledge, wisdom, ideas, and methods pooled at the disposal of the company's board, thus enhancing the caliber of difficult decision-making. Based on research conducted by Shehata et al. (2017) in the United Kingdom, Kipkirong Tarus & Aime (2014) in Kenya, Ararat et al. (2010) in Turkey, Ozdemir (2020) on tourism companies in the USA, Aggarwal et al. (2019) on India's National Stock Exchange (NSE) shows that the diversity of directors, in general, has a positive influence on firm performance. Based on the reference theory used and the gaps in previous research, the researcher formulated the following hypothesis:

H1: Diversity of Directors has a Positive Effect on Company Performance

5. Age diversity

According to agency theory, the diversity of the board of directors will have a favorable impact on the board's overall performance due to the variety of perspectives that may be considered when making corporate decisions. The company's age diversity is one element that influences the board of directors' diversity. There is little doubt that senior and junior directors approach decision-making and risk assessment from different angles. Using research that was done by Katmon et al. (2019), younger directors are more proficient in dealing with risks associated with disclosure of social responsibility. Meanwhile, senior directors are more careful in taking risks in implementing social responsibility. Based on research conducted by Lilis Gustiana et al. (2021) in Indonesian Manufacturing Companies, Rumapea & Silitonga, 2020 in Indonesian Banking Companies, Fernández-Temprano & Tejerina-Gaite (2020) in Spanish Companies, and Salim & Yadav (2012) in Malaysian companies stated that the presence of age diversity on the board of directors of a company would increase firm performance. Based on the reference theory used and the gaps in previous research, the researcher formulated the following hypothesis:

H2: The existence of Young Directors on the Board of Directors has a Positive Effect on Company Performance

6. Gender diversity

According to agency theory, the board of directors' ability to oversee management is boosted by diversity since it strengthens the independence of the current directors. Similar to how the theory of resource reliance explains it, a more diverse board of directors will offer fresh perspectives that foster more creativity and innovation. Using research that was done by Katmon et al. (2019), Women are supposedly believed to be animals that are more sensitive to environmental and social situations in the community, therefore having female directors on the board of directors can offer many new ideas that can be helpful in the implementation of social responsibility disclosure. Based on research conducted by EmadEldeen et al. (2021) in United Kingdom companies, Bin Khidmat et al. (2020) in China, Ramdhanian et al. (2020) in Property, Real Estate and Development Sector Companies in Indonesia, Tariah (2019) in the Top 500 Fortune Companies, Khan & Abdul Subhan (2019) in companies in Pakistan, Alqatan (2019) in Kuwait, and Bernile et al. (2018) in the USA have the implication is that with the diversity of directors on the board of directors of related companies will improve firm performance. Based on the reference theory used and the gaps in previous research, the researcher formulated the following hypothesis:

H3: The presence of female directors on the board of directors has a positive effect on company performance

7. Education diversity

Companies have the right to select the greatest resources to raise the caliber of their organizations, according to the principle of resource reliance. Based on this, it stands to reason that the business needs managers with the greatest educational credentials possible. One way to shape one's character and thinking and affect how they make decisions is via education. Kusumastuti et al. (2007) claims that the educational backgrounds of the council members have an impact on their expertise. Board members, at the very least, are better able to run a corporation and make business choices by having prior business and economic expertise than those who do not. Based on research conducted Oktapiani (2017) on companies in the Indonesian Islamic Capital Market, Fraga & Silva (2012) in Brazil, Amin & Sunarjanto (2016) in Indonesia, and Bin Khidmat et al. (2020) in China, it can be concluded that with the diversity of educational backgrounds on the board of directors, it can provide stimulation to increase company value. Based on the reference theory used and the gaps in previous research, the researcher formulated the following hypothesis:

H4: The existence of a Board of Directors with a minimum education level of master on the Board of Directors has a Positive Effect on Company Performance

RESEARCH METHOD

1. Type of research

a. Type of research

The type of research used in this research is descriptive research. This is done to see the real conditions in order to answer the existing phenomena. Descriptive research focuses on solving actual problems as they were at the time the research was carried out (Zellatifanny & Mudjiyanto, 2018).

b. Data source

The data collection technique used in this study is a documentation technique, namely secondary data collection by viewing, studying, and citing records obtained from the Indonesia Stock Exchange document in the form of each company's annual report in 2017 – 2020 listed on the Exchange.

c. Sampling

The sample in this study were all companies on the Indonesia Stock Exchange that issued an Annual Report from 2018 – 2020.

Table 1. Sampling

Criteria	Total
IDX listed company	539
Active IDX listed company	(70)
IDX listed company which issues annual report 2018 – 2020	(152)
Final sampling	317

Source: Writer (2022)

2. Data analysis

The research technique used in this study is through regression analysis and coefficient of determination test to see the effect of the independent variable on the dependent variable, having previously passed the classical assumption test.

3. Research variables

a. Return on Assets

Return on Assets (ROA) is a company's profitability ratio measured by comparing net income with the company's total assets, to measure the effectiveness of using company assets (Wardani & Januarti, 2013). ROA is a ratio calculated by dividing the net income over total assets. ROA has been used in most of the studies for the measurement of the profitability of the firms (Gul et al., 2011). Return on assets (ROA) is calculated as net profit divided by total assets and both of the items are taken from the balance sheet (Salim & Yadav, 2012).

$$ROA = \frac{\text{Total Return}}{\text{Total Assets}}$$

b. Age diversity

Age is one of the essential characteristics of the diversity of company directors. The director's age can influence character, determining how a director responds to a problem and makes decisions on the matter. Age diversity characterized by representative directors from various generations can help balance voting and risk in solving existing problems (Katmon et al., 2019). The diversity of directors is carried out using the ratio between directors under the age of fewer than 40 years and the total number of directors.

$$DAGE = \frac{\text{Directors below 40}}{\text{Total Directors}}$$

c. Gender diversity

Women are considered as the presence of women on the board of directors is expected to provide quality improvements in the performance of directors (I. Khan et al., 2019). In this study, gender diversity in directors was measured by the ratio between female directors and the total number of directors. Based on research L. S. Hassan et al. (2020), gender diversity of directors is carried out using the ratio between female directors and the total number of directors.

$$DGENDER = \frac{\text{Female Directors}}{\text{Total Directors}}$$

d. Education diversity

Education can be interpreted as a person's knowledge and knowledge obtained from the learning process. Education shapes a person's mindset, especially a director who has a big responsibility in managing the company and is responsible for all other stakeholders. Therefore, directors with a higher education background can better understand management, carry out good supervision and make more optimal decisions for the company. Based on this study, educational diversity is measured by the ratio of directors who have taken master's education to the total number of directors. Based on research by Katmon et al. (2019), the educational diversity of directors is carried out using the ratio between directors with a minimum education of master/master/S2 with the total number of directors.

$$DEDU = \frac{\text{Master or Up Education Directors}}{\text{Total Directors}}$$

RESULT AND DISCUSSION

1. Descriptive Statistic

Table 1. Descriptive Statistic Result

	Minimum	Maximum	Mean
Board Age Diversity	0.000	1.000	0.154
Board Gender Diversity	0.000	0.800	0.117
Board Education Diversity	0.000	1.000	0.277
Return on Assets	-37.520	36.000	1.319

Source: Writer (2022)

Based on the results of the descriptive analysis that has been done in this study, it can be concluded several things. A value of 0 on the variable of educational diversity of directors, gender diversity of directors, and diversity of education of directors in the minimum section implies that several companies in Indonesia do not have a board of directors under 40 years of age, a female board of directors, and a board of directors with a minimum education of S2/Masters. There are 244 out of a total of 317 issuers in Indonesia with a shallow level of age diversity, where 75 percent of the research sample does not have a board of directors under 40 years of age. Although this study also found one issuer with a magnificent age diversity of directors, namely the issuer with the stock code TOTO. This issuer has a board age diversity value of 1, indicating that the entire composition of its directors is under 40.

As for the gender diversity of directors, it can be implied that no single company in Indonesia has a female board of directors. In fact, there are 168 issuers or more than 50 percent of companies in Indonesia, with a composition of directors without female directors. Another finding is that there is a composition of directors of companies with a high educational diversity value, namely AMFG issuers with a director's educational diversity level of 1, which indicates that all directors of the company have a minimum educational background of Masters/Masters.

2. Coefficient of determination test

Table 3. Coefficient of Determination Test Result

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	0.105	0.011	0.008	7.434

Source: Writer (2022)

Based on the test of the coefficient of determination that has been carried out, it can be seen that the R square number shows a value of 0.011 or 1.1 percent, meaning that the independent variables together have an influence on the dependent variable by 1.1 percent, while other variables influence the remaining 98.9 percent. Based on research conducted by Sugiyono (2017), this value is in the very weak category.

3. F-Test

Table 4. F-test Result

Model		F	Sig.
1	Regression	3.422	0.017

Source: Writer (2022)

The F test was conducted to see the effect of the independent variables on the dependent variable. Based on the tests that have been carried out, the results of the F test show a significance value below the alpha value of 0.05, which is 0.017. Based on Sugiyono (2017), this figure shows that the independent variables used in this study influence the sdependent variable simultaneously (simultaneously). These results are in line with research conducted by Shehata et al. (2017) in the United Kingdom, Kipkirong Tarus & Aime (2014) in Kenya, Ararat et al. (2010) in Turkey, Ozdemir (2020) on tourism companies in the USA, Aggarwal et al. (2019) on India's National Stock Exchange (NSE).

4. t-test

Table 5. t-test Result

Model		B	t	Sig.
1	(Constant)	1.394	3.199	0.001
	Board Age Diversity	2.637	2.620	0.009
	Board Gender Diversity	0.549	0.380	0.704
	Board Education Diversity	0.986	1.116	0.265

Source: Writer (2022)

The t-test was conducted to see each independent variable's effect on the study's dependent variable. This test also reflects whether the hypothesis is accepted and whether the influence value given by the independent variable to the dependent variable is significant Sugiyono (2017),. Based on the tests, only Board Age Diversity has a significance value below alpha 0.05, with a value of 0.009. As for the other variables, the significance value is above alpha 0.05, so the second and third hypotheses cannot be accepted. However, in this test, the direction of the influence for each hypothesis can be seen where the Board Gender Diversity and Board Education Diversity variables already have a positive direction, although not yet significant.

Based on the tests that have been carried out, it can be concluded that Board Age Diversity has a positive and significant impact on firm performance. This condition means that the composition of directors with directors aged less than 40 years has a positive influence on firm performance. This condition is supported by previous research conducted by Lilis Gustiana et al. (2021) in Indonesian Manufacturing Companies, Rumapea & Silitonga, 2020 in Indonesian Banking Companies, Fernández-Temprano & Tejerina-Gaite (2020) in Spanish Companies, and Salim & Yadav (2012) in Malaysian companies stated that the presence of age diversity on the board of directors of a company would increase firm performance. This is because youthful managers are more inclined to undertake risky strategies, and firms with young managers will experience higher growth than their counterparts with older managers. This can be understood since older managers tend to be more risk averse, while younger managers tend to have a higher ability to process new ideas, a lower willingness to accept the status quo, and less interest in career stability (Salim & Yadav, 2012).

This test also shows that the Gender Diversity Board has an insignificant positive effect on firm performance. This insignificant condition is supported by the lack of data in Indonesia which shows that the company already has a female board of directors in the ranks of the relevant company leaders. Only 50 percent of issuers in the sample of this study have equal female and male directors, while the majority still rely on the presence of men to occupy structural positions in the company. This is supported by previous research conducted by Devi et al. (2020); Fernández-Temprano & Tejerina-Gaite (2020); Kusuma et al. (2018); and Mazzotta et al. (2017). This result is suspected because, in corporate governance in Indonesia, women have not been strongly represented (Mardiyati, 2012). Women who are active in the public sphere have dual

roles, namely as housewives and career women, so these roles are thought to affect performance (Kusuma et al., 2018).

The fourth hypothesis, namely the influence of Board Education Diversity on firm performance, has also not been supported in this test, even though the direction of the existing relationship has a positive direction. This is in line with research conducted by Lilis Gustiana et al. (2021) and Rose (2007). According to Lilis Gustiana et al. (2021), the diversity of education owned by the board is not the main factor that affects the company's performance but can also be influenced by fundamental or technical conditions. The absence of such influence is since this study only defines the educational background specifically for the level but not the background of the study. There is a possibility that the board members' educational background following the type of business enterprise that can support the continuity of the company's business is more necessary (Novitasari, 2018). In fact, according to EmadEldeen et al. (2021), high diversity in education may lead to jealousy and plotting against each other, which can affect existing coordination and cooperation and lead to the blurring of shared goals to improve firm performance. The t-test was conducted to see each independent variable's effect on the study's dependent variable. This test also reflects whether the hypothesis is accepted and whether the influence value given by the independent variable to the dependent variable is significant (Sugiyono, 2017). Based on the tests, only Board Age Diversity has a significance value below alpha 0.05, with a value of 0.009. As for the other variables, the significance value is above alpha 0.05, so the second and third hypotheses cannot be accepted. However, in this test, the direction of the influence for each hypothesis can be seen where the Board Gender Diversity and Board Education Diversity variables already have a positive direction, although not yet significant.

CONCLUSION

Based on research conducted on 317 companies in Indonesia, the diversity of directors positively influences firm performance, especially for Board Age Diversity. This condition means the composition of the board of directors with young directors will provide innovation, enthusiasm, and more renewable discussions to improve firm performance compared to the composition of directors filled with senior directors. At the same time, the results for the influence of Board Gender Diversity and Board Education Diversity have not given significant results. This result is due to the insufficient supporting data obtained. The data shows that more than 50 percent of the companies sampled in this study do not have female directors at all, and many of the company directors have the latest educational background in the form of a Bachelor/S1. Future research might include the effect of board diversity on the firm's financial performance and non-financial performance, research and development, CSR, and others. Consequently, this will enhance and enrich the literature on corporate governance.

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