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**BOARD QUALIFICATION AND FIRM PERFORMANCE OF**  
**FAMILY CEO LISTED FIRM IN MALAYSIA**

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*Abstract*

This paper investigates the relationship between board size, board qualifications and firm performance of family CEO and non-family CEO listed firms in Malaysia mainly in construction, consumer, property and trading and services sectors in Bursa Malaysia. These sectors appeared to have more appropriate samples for the study. The total sample of 38 firms has met the criteria and the data has been collected for the period of 5 years from 2012 until 2016. The 38 samples of family firms were further divided into family CEO (21) and non-family CEO (17) firms. The independent variables are board size (BSIZE) and board qualification as measured by the proportion of board degree (BDEG) and the proportion of board professional qualification (BPRO). Meanwhile, for firm performance measurement, this study applied return on assets (ROA) and return on equity (ROE) for analysing the relationship between board size and board qualifications against firm performance. The findings show that there is a significant difference between family CEO and non-family CEO firms at 5% level for board professional qualification confirming altruism and nepotism practices among family members and support the argument of nepotism's characteristic which can be granting jobs to family members regardless of merit. In addition, this study also finds board professional qualification is significantly and negatively related to external firm performance in family CEO firms showing that board education is not really been emphasized more among board members.

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**Keywords:** Board degree, board professional qualification, board size, family CEO firms.



## **1. Introduction**

Family firms are mostly wealthy firms which prospered through wealth generation with excellent corporate governance. Asian literature showed that family firms portrayed a high performance in numerous countries which include Australia, Taiwan, Hong Kong, Singapore and China (Filatotchev et al., 2005; La Porta et al., 1999). In addition, a study conducted by Faccio and Lang (2002) in 13 Western European countries verified that with the cut off level of 20%, about 44.3% are owned by family. However, when the study excluded Ireland and the United Kingdom, the percentage of family firms increases to 57.2%. Similarly, the study by Claessens et al. (2000) on nine East Asian countries with the same cut off level of 20%, found that the percentage of family firms statistically increased from 38.29% to 58.68% when Japan was taken out from the sample. Apparently, Japan has the largest share of widely held firms of 79.8% at the 20% cut off level.

The board qualifications entrusted with a wide range of observable or unobservable capabilities in this knowledge overflow modern period appear to be a critical issue related to firm performances. To ensure high corporate governance quality of firms through identification and measurement of capabilities, board members especially the chief executive officer (CEO) has to obtain educational qualifications which include degree or post-graduation recognition for a better and reliable communication with the stakeholders (Bhagat, Bolton & Subramanian, 2010). According to Gottesman and Morey (2006a), superior intelligence can be measured with educational qualification where higher educated managers often perform better than lower educated managers. Furthermore, Gottesman and Morey (2006b) study the performance between managers with and without MBA from ranked programs, they find there is positively and significantly related to mutual fund performance. Their findings also find that the professional qualification such as CFA or holds either a non-MBA masters or Ph.D., are generally unrelated to fund performance (Gottesman & Morey, 2006b).

However, it is also vital to be aware that the skills of superior managerial are not always gained from a high level of educational qualification. In contrast, soft skills such as entrepreneurial and leadership often developed from non-academic related activities. Nevertheless, there are also findings shown where fast-growing and high-performing firms are belong to and managed by low-educated individuals. The contradicting results from previous studies complicate the importance of board qualification, furthermore they are relatively limited in the literature. Hence, it is important to examine if the educational qualifications among CEO and board members could influence firm performance to reduce the research gap in this field of study.

Nowadays, the study done on the performance of family firms have been widely explored and quite saturated in the literature, but the field of study from family firms managed by family CEO and non-family CEO perspective is still scarce. According to Minichilli et al. (2010), the study on family CEO is beneficial in evaluating and determining the direction and performance of family firms. On the contrary, Burkart et al. (2003) argue that a reliable non-family CEO is vital for the performance of family firm.

### **1.1. Altruism and nepotism in family firms**

Altruism is a powerful force within family life and by extension, within the family firm. This characteristic ensures parents to be protective of their children, give fully supports to their family members

to be considerate towards each other and cultivate loyalty and commitments to the family and firm. Altruism held the family members within the family firm with inculcating the belief that they have a residual claim on the family's estate (Stark and Falk, 1998). According to agency theory, the agency cost can be reduced through fostering, monitoring and enforcing agreements when ownership goes through the process of aligning their interests among family agents towards risk and growth opportunities. Therefore, family agent performance is not monitor regularly. Nevertheless, information asymmetries among family agents can be reduced meanwhile increasing informal agreements usage through increased cooperation and communication among and within family members and the family firm with altruism (Daily & Dollinger, 1992). Besides, altruism benefits the agency in a way that a heightened sense of interdependence among family agents is created. In fact, employment relates welfare directly to firm performance.

Furthermore, it is deduced that agency problems increase from altruism and self-control are complicated when the CEO has discretion in placing control the firm's resources. Intrinsically, this broadens the CEO's capacity to make altruistic transfers for example perquisites, privileges, and employment to family members that they would not be receiving this kind of treatment if they were worked elsewhere. Henceforth, a variety of agency cost is created when these privileges and the sense of entitlement are evoked (Gersick et al., 1997). Meanwhile, according to Ford and McLaughlin (1986), nepotism is the act of compassion toward one another among family members or friends. From employment perspective, it can be granting jobs to relatives and friends, without referring to merit. Apparently, such practices impact businesses negatively. In other words, they can reduce the support of other employees, decrease the quality and creativity of management and belittle the importance of competence and high-level performance (Zax & Ichniowski, 1988).

Nepotism often provide positive perspective in many smaller family firms. This is due to the practice of "succession" with alternative cheap source of labour. Nepotism is neither good nor bad, in and of itself (Barnes & Hershon, 1976). In other words, nepotism is a neutral phrase. Sarcastically, nepotism reflects the positive or negative charge based on the way one has educated one's children. The values of becoming competent employees include honesty, respect for others, integrity, dependability, being industrious and doing one's best in every endeavour. These values are crucial to instil in every generation in ensuring the competent generation is born. On the contrary, the failure of teaching these principles will result in the feeling of entitlement in the children which is believing that they are the privileged and they think they can get everything. Ironically, the stated deficiency eventually turns into a ripe incubator for problems to emerge when the child works in the family business (Ford & McLaughlin, 1986). By referring to the literature discussed, it is hypothesized that there is a significant difference in mean value of return on equity and return on assets between family CEO firms and non-family CEO firms.

## **1.2. Board qualification and performance**

The Malaysian Code on Corporate Governance (Revised 2007) suggests that directors have certain qualities (experience, skills, knowledge, professionalism and integrity) in face of intense responsibility. Previous studies found that board chairman with university degree is positively in relation to seven measures of performance which include earning per share (EPS), EPS appreciation, ROA, ROA appreciation, market-to-book ratio, cumulative returns and cumulative abnormal returns. Companies need to hire board members, including Chief Executive Officer (CEO) with certain level of either observable or

unobservable capability (Darmadi, 2013). According to Sebor and Wakefield (1998), directors with higher education are well adapt to business acumens and operations compared to those less educated counterparts. Jalbert et al. (2002) study on a sample of Forbes 800 firms discovered that CEO graduated from prestige school has positive relationship with ROA of the firm. Darmadi (2013) finds that postgraduate held by boards of directors have a positively and significant correlated with ROA.

However, Bhagat et al. (2010) find that CEO with non-MBA degree holders perform better than those with such qualification. On the side note, empirical evidence was revealed from their study that hiring new CEOs with an MBA leads to short-term improvements of performance. From the result of the study, Bhagat et al. (2010) do not consider CEO education as a good proxy for CEO ability. But Darmadi (2013) finds that undergraduate and financial certificate is not significant with ROA. Gottesman and Morey (2006a) find there is no significant evidence that CEO from more prestigious schools perform better than CEO from less prestigious schools.

Interestingly, mixed results are found in studies that investigate the influence of graduate degree towards better firm performance. Undeniably, skills and educational background are among the determinants for family firms' performance (Castillo & Wakefield, 2006). However, lack of study has been done for the relationship between director's education with return on equity (ROE). Based on the arguments, it is hypothesized that, the proportion of board degree and professional qualification are significant and negatively related to return on equity (ROE) and return on assets (ROA) in family CEO firms.

### **1.3. Board size and performance**

Board size determines the number of board of directors who are serving on the board of the companies. The larger the boards the superior performance of companies as compared to small ones because larger groups have more skills, expertise, capabilities and resources, and wider networking. Haleblan and Finkelstein (1993) elaborated that large groups could enhance problem solving abilities by providing more strategic perspectives and constructive judgement. Despite the upside potentials, Lipton and Lorsch (1992) brought a conclusion that too many executive members on board would lead to more problems.

On the contrary, a small board is more effective than a larger one in term of decision making especially for executive replacement. Findings by Jensen (1993) reveals that small board size could increase firm performance. Notably, according to Yermack (1996), the firms with small number of board size is having a tendency to gain a higher stock market value. Family firms used to have a smaller board size (Eisenberg et al., 1998; Ibrahim & Samad, 2011; Hermalin & Weisbach, 2003; Lipton & Lorsch, 1992). According to Bennedsen et al. (2008), the optimum number for family firm's board size is less than six members. On the negative side, the source of information, experience and contact of small board are limited. Based on this argument, it is hypothesized that board size is significant and negatively related to return on equity (ROE) and return on assets (ROA) in family CEO firms.

## **2. Problem Statement**

Adjacent to the performance between family firms and non-family firms, there were numerous studies carried out to examine their comparison (Anderson & Reeb, 2003; Ibrahim & Lau, 2018; Ibrahim

& Samad, 2011; Miller & Le Breton-Miller, 2006; Villalonga & Amit, 2006). Even though family firms contribute significantly to the Malaysian economy and the importance of corporate governance mechanisms on firm performance, research studies on Malaysian family firms seemed to lag behind. Therefore, the research needs to be further investigated and emphasized more on family firms as family business are governed by family traits, which do not exist in other businesses (Mishra et al., 2001).

### **3. Research Questions**

1. Is there any significant difference in mean value of board qualification between family CEO and non-family CEO firms?
2. Does board size in family CEO and non-family CEO firms influence the firm performance?
3. Does board qualification in family CEO and non-family CEO firms influence the firm performance?

### **4. Purpose of the Study**

1. To examine the significant difference in mean value of board qualification between family CEO and non-family CEO firms.
2. To investigate the significant relationship between board qualification in family CEO firms and firm performance.
3. To analyze the significant relationship between board size in family CEO firms and firm performance.

### **5. Research Methods**

#### **5.1. Population and sample**

After screening through the 90 listed companies from sectors of construction, consumer, property, trading and services in Bursa Malaysia, only 38 companies from the list are family firms with only 21 companies identified as family CEO firms and 17 companies as non-family CEO firms. The data of time series and the cross-sectional study has been collected from the 38 listed companies in Bursa Malaysia for the period of 5 years from 2012 until 2016.

#### **5.2. Data source**

Secondary data is the main and only source of data for this study. Most of the secondary data are obtained and manually collected from Companies Annual Report and retrieved from datastream. By referring to those reports, information such as board size, the number of degrees qualification holders and the number of professional qualification holders among directors can be identified and calculated for the proportion. Furthermore, board size also can be extracted from the annual report.

#### **5.3. Variables and measurement**

This study will employ two profitability ratios as the proxy for the performance which are return on equity (ROE) and return on assets (ROA). ROE and ROA are measured based on the net income divided

by total shareholders' equity and the net income over total assets of a firms respectively (Ibrahim & Samad, 2011).

$$\text{Return on Equity (ROE)} = \frac{\text{Net income}}{\text{Total shareholder's equity}}$$

$$\text{Return on Assets (ROA)} = \frac{\text{Net income}}{\text{Total assets}}$$

The board size (BSIZE) is measured by total number of directors serve on the board of the company (Abor & Biekpe, 2007; Bokpin & Arko, 2009; Ibrahim & Samad, 2011). According to Balwin (1963), a person holding a degree is considered elite in the region of less developed countries. The proportion of qualified degree director (BDEG) is proxied by any undergraduate degree obtained by the board members and CEOs of the listed family firms divided by the number of directors on board. Graham and Harvey (2002) state that any individuals who holds a postgraduate degree must have obtained an undergraduate degree. On the other hand, professional qualification (BPRO) are titles or awards granted by professional bodies. The proportion of directors holding an undergraduate degree qualification and a professional qualification are calculated using the following formulas:

$$\text{Proportion of Qualified Degree Director (BDEG)} = \frac{\text{Number of undergraduate holder among Directors}}{\text{Total number of Directors on Board}}$$

Proportion of Qualified Professional Director (BPRO) =

$$\frac{\text{Number of professional qualification holder among Directors}}{\text{Total number of Directors on Board}}$$

Control variable is also defined as constant variable. In scientific experimentations, this variable is the experimental element which stays constant and unchanged throughout the investigation in order to test the relative relationship of the dependent and independent variables. Many prior studies used firm size (LNFSIZE) as control variables. In this study, the firm size is measured by the natural log of total assets of the company (Ibrahim & Samad, 2011; Sheikh & Wang, 2012; Vaklifard et al., 2011).

## 5.4. Data analysis

### 5.4.1. Data panel of multiple regression analysis

This study used the analysis of panel data because the data consists of cross-section and time series. By using this panel data analysis, it will eradicate unobservable heterogeneity that different firms in the sample data could exist, reduce collinearity among the variables and lead to better measurement than pure cross section or pure time series data (Baltagi, 2001; Gujarati, 2003).

### 5.4.2. Model selection

Model selection is presented as follows:

$$FR = \alpha + \beta_1 BSIZE_{it} + \beta_2 BDEG_{it} + \beta_3 BPRO_{it} + \beta_4 LNFSIZE_{it} + \epsilon_{it}$$

Where:

FR = Return on Assets (ROA), Return on Equity (ROE)

BSIZE = Board Size

BDEG = Proportion of Qualified Undergraduate Degree Director

BPRO = Proportion of Qualified Profession Director

LNSIZE = Firm size

$\epsilon_{it}$  = The Disturbance or Error Term

## 6. Findings

Table 01 shows the descriptive statistics of the full sample, family CEO and non-family CEO firms from year 2012 to 2016. The findings demonstrate that firm size is larger for non-family CEO firms compared to family CEO firms. Similarly, non-family CEO firms have higher mean performance ratios for both ROE and ROA compared to family CEO firms. As a summary, non-family CEO firms has slightly smaller mean of board size (7.765), higher proportion of board degree (0.552), and slightly higher proportion of board professional qualification (0.353), compared to family CEO firms.

**Table 01.** Descriptive statistic of overall period (2012-2016): Family CEO firms and non-family CEO firms

Variables	Full Sample (N= 38)				Family CEO Firms (N=21)				Non-Family CEO Firms (N=17)			
	Min	Max	Mean	SD	Min	Max	Mean	SD	Min	Max	Mean	SD
<b>BSIZE</b>	4.80	13.40	7.968	2.207	4.80	13.00	8.133	2.364	5.40	13.40	7.765	2.048
<b>BDEG</b>	0.28	0.90	0.549	0.149	0.35	0.89	0.546	0.139	0.28	0.90	0.552	0.164
<b>BPRO</b>	0.11	0.61	0.312	0.117	0.11	0.50	0.279	0.091	0.19	0.61	0.353	0.135
<b>ROE</b>	-0.38	0.60	0.058	0.151	-0.38	0.16	0.039	0.115	-0.38	0.60	0.082	0.188
<b>ROA</b>	-0.14	0.22	0.042	0.060	-0.13	0.09	0.035	0.049	-0.14	0.22	0.050	0.071
<b>LNFSIZE</b>	17.13	24.20	20.341	1.770	17.13	23.89	20.176	1.812	18.09	24.20	20.544	1.749

Note: BSIZE=Board Size; BDEG= Proportion of Board Degree; BPRO= Proportion of Board Professional Qualification; ROE= Return on Equity; ROA=Return on Assets; LNFSIZE= Firm Size

Independent samples t-test results show that there is only mean proportion of board professional qualification is significantly difference between family CEO and non-family CEO firms which non-family CEO has higher mean (0.353) compared to family CEO firms (0.279) at 5 percent level as presented in Table 02. The finding is consistent with Burkart et al. (2003) where non-family CEO firms with higher board qualification gain reliability significantly to perform better than family CEO firms. Likewise, it is also consistent with the study carried out by Seborá & Wakefield (1998), where firm performance are higher as more educated directors are on board.

**Table 02.** Differences of means tests

Variables	Family CEO Firms (N=21)	Non-family CEO Firms (N=17)	t-stat
	Mean	Mean	
BSIZE	8.133	7.765	0.507
BDEG	0.546	0.552	-0.128
BPRO	0.279	0.353	-1.943**
ROE	0.039	0.082	-0.871
ROA	0.035	0.050	-0.734
LNFSIZE	20.176	20.544	-0.632

Notes: \*\*\* significant at 0.01 level \*\* significant at 0.05 level \* significant at 0.10 level

BSIZE=Board Size; BDEG= Proportion of Board Degree; BPRO= Proportion of Board Professional Qualification; ROE= Return on Equity; ROA=Return on Assets; LNFSIZE= Firm Size

From Table 03, ROE is positively and highly correlated to ROA at 1 percent level indicating that these two variables have strong relationship with each other. In conclusion, larger board size, higher ROE and higher ROA are important complementary factors when firm size is larger.

**Table 03.** The Pearson's Correlation Coefficients of the study variables

	BSIZE	BDEG	BPRO	ROE	ROA	LNFSIZE
BSIZE	1					
BDEG	-0.062	1				
BPRO	-0.015	-0.004	1			
ROE	0.185	-0.130	0.128	1		
ROA	0.114	-0.078	0.127	0.964**	1	
LNFSIZE	0.359*	-0.257	0.211	0.332*	0.331*	1

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

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

BSIZE=Board Size; BDEG= Proportion of Board Degree; BPRO= Proportion of Board Professional Qualification; ROE= Return on Equity; ROA=Return on Assets; LNFSIZE= Firm Size

The findings show in Table 04 only proportion of board professional qualification (BPRO) is negative and significant at 1 percent level for full sample and family CEO firm with ROE. This can be explained that higher proportion of board professional qualification prove that it will reduce the impact on ROE. This is consistent with the findings by Bhagat et al. (2010) where they do not consider CEO education as a good proxy for CEO ability for long-term firm performance. In addition, all samples show the positive relationships between ROE and is positive and significant at 0.01 level showing that the larger firm size the better the firm performance which is consistent with the findings of Ibrahim & Samad (2011) and Haniffa & Hudaib (2006).

**Table 04.** The Fixed Effect Models for return on equity (ROE)

Variables	Full Sample (N=38)	Family CEO Firms (N=21)	Non-Family CEO Firms (N=17)
Intercept	-36.274 (-3.549)***	-61.382 (-2.917)***	-3.801(-2.479)**
BSIZE	-0.390 (-0.966)	-0.329 (-0.439)	-0.016 (-0.340)
BDEG	1.192 (0.494)	0.842 (0.190)	-0.282 (-0.993)
BPRO	-13.213 (-3.659)***	-21.568 (-2.754)***	-0.442 (-0.976)
LNFSIZE	2.484 (4.174)***	3.446 (3.296)***	0.211 (2.695)***
Observation	190	105	85
R <sup>2</sup>	0.343	0.386	0.555
Adj. R <sup>2</sup>	0.161	0.202	0.416
F-Stat(p-value)	1.884(0.003)	2.097(0.007)	3.992(0.000)

Notes: \*\*\* significant at 0.01 level \*\* significant at 0.05 level \* significant at 0.10 level

BSIZE=Board Size; BDEG= Proportion of Board Degree; BPRO= Proportion of Board Professional Qualification; ROE= Return on Equity; ROA=Return on Assets; LNFSIZE= Firm Size

Meanwhile, Table 05 tabulates the results by using fixed effect model shows that only the relationships between ROA and firm size is positive and significant at 0.01 level for all samples confirming that the larger the size of the firm will increase the performance of the firm. Furthermore, the relationship between board degree and ROA is negative and significant at 10% level only for full sample. This result is supported by Bhagat et al. (2010) find that CEO who are degree holders perform no better than those without such qualification. In contrast, BDEG and BPRO do not show any significant relationship with ROA for both family CEO and non-family CEO consistently with Darmadi (2013) who finds that there is



no difference between undergraduate and financial certificate with ROA in Indonesia and Gottesman & Morey (2006a) who find there is no significant evidence that CEO from more prestigious schools perform better than less prestigious schools.

**Table 05.** The Fixed Effect Models for return on assets (ROA)

Variables	Full Sample (N=38)	Family CEO Firms (N=21)	Non-Family CEO Firms (N=17)
Intercept	-1.087 (-4.235)***	-1.115 (-3.091)***	-1.667 (-3.069)***
BSIZE	-0.013 (-1.235)	-0.016 (-1.257)	-0.011 (-0.613)
BDEG	-0.109 (-1.795)*	-0.100 (-1.320)	-0.111 (-1.104)
BPRO	-0.069 (-0.743)	-0.037 (-0.274)	-0.128 (-0.796)
LNFSIZE	0.076 (5.099)***	0.067 (3.739)***	0.093 (3.352)***
Observation	190	105	85
R <sup>2</sup>	0.573	0.531	0.600
Adj. R <sup>2</sup>	0.454	0.391	0.475
F-Stat(p-value)	4.840(0.003)	3.777(0.000)	4.799(0.000)

Notes: \*\*\* significant at 0.01 level \*\* significant at 0.05 level \* significant at 0.10 level

BSIZE=Board Size; BDEG= Proportion of Board Degree; BPRO= Proportion of Board Professional Qualification; ROE= Return on Equity; ROA=Return on Assets; LNFSIZE= Firm Size

## 7. Conclusion

This study revealed that board size is negatively related to return on equity (ROE) of family CEO and non-family CEO firms confirming that family firms prefer small board size with similar to the previous studies (Haniffa & Hudaib, 2006; Ibrahim & Samad, 2011; Mak & Kusnadi, 2005). Board qualification as proxied by only the proportion of board professional qualification significantly decreased the performance of family CEO firms. This is indicating that professional qualification is less important to improve a family CEO firm performance externally (ROE) rather than internally (ROA). Interestingly, significant difference between the proportion of board professional qualification between family CEO firms and non-family CEO firms confirming altruism and nepotism practices among family members and support the argument of nepotism's characteristic which can be granting jobs to friends and relatives regardless of merit (Ford & McLaughlin, 1986).

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