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Board diversity effect on financial performance in Indonesian financial institution

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Abstract: Board diversity is important in the current business environment, board diversity considered be able to provide diverse points of view, it is considered to be able to build effective corporate governance. This study highlights board diversity issue in Indonesia financial sector institution, taking consideration their effect on financial performance measured using Tobin Q. This study purpose are analyses the effect of board of commissioners gender diversity, board of directors gender diversity, board of commissioners nationality diversity, and board of directors nationality diversity on financial performance. The investigation makes use of regression analysis from 67 financial institution listed in Indonesia from 2020 until 2022, with total 201 sample. Our finding highlights that board of directors gender diversity, and board of directors nationality diversity positively affects financial performance, while board of commissioners nationality diversity negatively affects financial performance, and board of commissioners gender diversity does not affect financial performance.
Keywords: *Board, Diversity, Gender, Nationality, Financial Performance, Financial Institution.*

1. Introduction

Board of commissioners, and board of directors are important components implementing corporate governance. Board of directors responsible overseeing execution company operations, The board of commissioners, as representatives of shareholders, is responsible for overseeing company's operations [1]. Board of directors serves as leader, set company strategic direction, meanwhile board of commissioners safeguards shareholders' interests within the company. [2]. The implementation of effective corporate governance can minimize information asymmetry and reduce the possibility of manipulation of financial performance. Therefore, good directors and commissioners mechanisms are considered to be able to minimize the emergence of agency costs[3].

Diversity is an issue that is currently of concern to many parties both in Indonesia and the world, including diversity of board directors and board commissioners[4]. Board diversity is important in the current business environment, board diversity is believed to offer variety perspectives, which contribute to develop effective corporate governance. Greater diverse of board directors background, more effective board commissioners is considered to be in resolving problems. It is also believed to cotribute to the improvement of the company's diverse connections and networks that are capable of expanding the company's business. Diversity in the board's background is also considered to improve the company's image. From the agency perspective, a more diverse background of the board of commissioners enhances their monitoring ability [5].

Several previous studies have conducted research with a similar aim, with the goal of assessing how board diversity affects company performance, such as [6] regarding effect of gender diversity and

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nationality diversity on Indonesian financial companies performance [7] regarding effect board gender diversity on Vetnam listed companies performance [8] regarding effect of board gender diversity on company performance in non-financial China companies [9] regarding financial performance affected by board diversity of Turkish listed companies [10] regarding diverse board effect on Dutch companies performance [11] regarding influence of diversity in gender, nationality, age on company performance on the Dutch stock exchange [5] regarding effect of board composition, length of service, age diversity, nationality diversity, gender diversity, educational diversity on company performance of non-profit companies [12] regarding financial performance of banking companies in Jordan affected by board directors gender diversity [13] regarding effect of gender diversity on financial performance in India listed companies.

2. Literature Review

Agency theory based on idea of separation between company owners and agents or management as managers. The company owner has the objective of maximizing the return on investment invested through company profits, while management is the party appointed as the manager of the company with the objective of maximizing its performance in company operations with the aim of getting bonuses, without taking into account the interests of the company owner. The emergence of this difference in objectives is the basis of agency theory [14].

Existence of differences in objectives between company owners and management as company management agents will sometimes give rise to information asymmetry. Management will tend to reveal information reflected in the company's financial reports that tends to be profitable and hide or delay information that is less profitable for management. Hence, representatives are needed from company owner to supervise company operations. In Indonesia the supervisory role as a representative of the company owner or shareholder is carried out by board commissioners. Their role very vital in ensuring that corporate governance runs well, so as to minimize the emergence of agency costs due to agency conflicts [12]. Agency perspective also considers that greater diverse background of board commissioners, result in better monitoring capabilities they will have, it can minimize agency costs which will affect the company's financial performance[5].

Resource dependence theory states that companies, especially international companies, will be very dependent on internal and external resources of the company. Company tends to find it easier to control internal resources, but the company cannot completely control the external resources. Therefore, if control of external resources such as customers, suppliers, competitors, and regulators becomes stronger, then the company's position in the market will also become stronger. Strong control of external resources will create greater opportunities to control tangible resources such as raw materials, competent employees, production facilities, and equipment.

In theory, board commissioners diversity improve their monitoring process. Improved monitoring by the board leads to better corporate governance mechanisms, which in turn results in better financial performance for the company. [7].

In theory, greater diversity board directors, will improve company's performance in financial aspect. Diverse backgrounds of directors will produce benefits for company, for example, the diversity of connections will make it easier for the company to get a variety of suppliers and customers, ease of business development into new markets or regions, and also more quickly finding a solution for a problem [5]. The greater the diversity on the board of directors, the more varied their experiences will be. Board directors diversity is considered better quality and creativity of decision making that will improve company financial performance[3].

Board commissioners diversity will improve monitoring or supervision of management's work results as agents and minimize the emergence of agency costs which will affect the financial performance[7]. More diverse gender in board commissioners members will result in better supervision[9].

More diverse gender in board commissioners will improve its supervisory role. Female commissioners are thought to improve the monitoring process and increase attendance at board meetings. Companies with poor governance may particularly benefit from having female commissioners, as their presence can lead to better oversight, thereby improve company performance and value. [7]. Several studies also state positive effect gender diversity commissioners and companies performance in Italy [15]. similar results were observed, showing that financial performance positively affected by gender diversity on board commissioners in Turkish listed companies [9].

H1: Board of commissioners gender diversity has a positive effect on company performance

Board directors gender diversity will improve communication channels and human capital diversity. Female board directors is considered able provide additional viewpoints and insights on strategic issues related to consumers, business partners, and especially female employees so that it will improve company performance [7]. A female board of directors is also considered to be able to generate more profits for the company because female directors are considered to spend more effort when carrying out their duties [9]. The same results were obtained in companies in Denmark that found the positive influence of gender diversity on company performance.

H2: Board of directors gender diversity has a positive effect on company performance

Nationality diversity of board commissioner members is perceived to negatively impact company performance because board members with foreign nationalities often prefer to reside in their home countries, thereby limiting the possibility of attending board of commissioners meetings, and supervision cannot be optimal if the board of commissioners' location is physically different from the company's operations [16]. There are similar results in companies in America board of commissioners nationality diversity negatively influence financial performance because commissioners from different nationalities are perceived to have limited knowledge of the rules and regulations in the company's operational country[17]. In Pakistan, there is similar findings indicate that board commissioners diversity affects company performance in negative way [18]. In the Netherlands the same results were also obtained that board of commissioners national diversity negatively influence company performance[11].

H3: Board of commissioners nationality diversity has a negative effect on company performance

Greater diversity in nationalities board directors facilitates company's entry into new markets or countries. This diversity helps in establishing a network of suppliers from different countries, making it easier to source resources internationally, thereby enhancing company performance. Additionally, a board with diverse nationalities can process information from various countries more effectively, resulting in faster decision-making and enhanced company performance [19]. The same results were found in Nigeria that company performance positively affected by board nationality diversity [20]. In Spain there were the same findings that company performance positively affected by nationality diversity [5]. In Indonesia, same results were obtained company performance positively affected by board directors diverse nationality [6].

H4: Board of directors nationality diversity has a positive effect on company performance

3. Methodology

This research use financial companies listed in Indonesia that publish annual reports and have recorded positive profits from 2020 to 2022 as sample.

This study includes four independent variables: board commissioners gender diversity, board directors gender diversity, board commissioners national diversity, board directors national diversity. Dependent variable is company performance, measured by the Tobin Q ratio. Data analysis was carried out using descriptive statistical analysis and multiple linear regression, the following is the research model used:

$$CP = \alpha + \alpha_1 CGD + \alpha_2 DGD - \alpha_3 CND + \alpha_4 DND + \mathcal{E}$$

CP : Company Performance.

α : Constant.

CGD	: Commissioner Gender Diversity.
DGD	: Director Gender Diversity.
CND	: Commissioner Nationality Diversity.
DND	: Director nationality diversity.
ε	: *Error.*

4. Research Variable

The first dependent variable is the gender diversity of board commissioners. This variable is measured with a value 0 if there is no female board of commissioners, and a value 1 if it does. The second dependent variable is gender diversity of the board directors. This variable is measured with a value 0 if there is no female board of directors, and a value 1 if it does. The third dependent variable is the nationality diversity of the board of commissioners. This variable is measured with a value 0 if there is no foreign nationality board of commissioners, and a value 1 if it does. The fourth variable is board directors nationality diversity, measured 0 if no foreign nationalities of board directors members, 1 if it does. Independent variable is company performance as measured by Tobin Q.

Table 1.
Research variables.

No	Variables	Measure
1	Commissioner gender diversity	Value 1 if there is a female board of commissioners, and the value 0 if there is no female board commissioners
2	Director gender diversity	The value 1 if there is a female board of directors, and the value 0 if there is no female board of directors
3	Commissioner nationality diversity	The value 1 if there is a foreign nationality in board of commissioners members, and the value 0 if there is no foreign nationality in board commissioners members
4	Director nationality diversity	The value is 1 if there is foreign nationality in board of directors members, and the value is 0 if there is no foreign nationality in board of directors members
5	Company financial performance	Tobin Q

5. Result and Discussion

Table 2 shows descriptive statistic results of variables used in this paper.

Table 2.
Descriptive statistic.

No	Variables	Minimum	Maximum	Mean	Standard deviation
1	Commissioner gender diversity	0	1	0.43	0.49
2	Director gender diversity	0	1	0.68	0.47
3	Commissioner nationality diversity	0	1	0.37	0.48
4	Director nationality diversity	0	1	0.30	0.46
5	Company performance	11.28	6,793	676.12	944.74

Table 2 shows that the commissioner gender diversity variable has an average of 0.43, This indicates that gender diversity in the selection of commissioners for financial sector companies in Indonesia is still given minimal consideration. The majority of financial sector companies in Indonesia have not appointed female commissioners in their companies. The director gender diversity variable has an average of 0.68, which shows that the selection of boards directors in Indonesian financial companies has considered gender diversity. The majority of financial sector companies in Indonesia have

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considered appointing women as part of their top management. The average for the commissioner nationality diversity variable is 0.37, indicating that most financial sector companies in Indonesia have not prioritized foreign nationality commissioners. The majority of financial sector companies in Indonesia choose to appoint Indonesian nationality commissioners. The director nationality diversity variable has average 0.30, which shows majority Indonesian financial sector companies have not considered the importance of foreign nationality directors in their companies. The majority of financial sector companies in Indonesia choose to appoint Indonesian nationality directors. Company performance variable has an average of 676.12. Table 3 shows board diversity impact on Indonesia financial institution performance.

Table 3.
Regression analysis effect of board diversity on company performance.

Dependent variables	Coefficient	Standard error	Significant
Commissioner gender diversity	28.01	138.867	0.847
Director gender diversity	46.79	145.111	0.037**
Commissioner nationality diversity	-564.54	152.068	0.000***
Director nationality diversity	458.04	160.018	0.005***

Note: *** significant at 1%, ** significant at 5%.

First hypothesis examines whether board of commissioners gender diversity positively affects financial sector companies performance in Indonesia. The results of the first hypothesis indicate that board of commissioners gender diversity does not impact financial performance of Indonesian financial sector companies. This could be because the majority of financial sector companies in Indonesia have not considered appointing female commissioners to their companies. Result consistent with the descriptive statistical on table 2. Second hypothesis examines whether board directors gender diversity positively affects performance of Indonesian financial sector companies. The results show that having diverse genders on the board indeed improves companies financial performance. These results suggest that shareholders should consider the importance of gender diversity when appointing the board of directors, will improve company's financial performance which can lead increase shareholder wealth. Female directors appointment will make it easier for the company to understand the market, especially if the target market is women [7]. In addition, female directors usually show more effort in their performance due to the glass ceiling issue [9]. Third hypothesis examines whether board of commissioners nationality diversity negatively impacts the financial performance of Indonesian financial sector companies. These results can be a consideration for shareholders when selecting a board of commissioners in the Company. Board of commissioners with foreign nationalities are considered to tend to choose to live in their country of origin, so that the probability of attendance at board of commissioners meetings is low. This can cause the company supervision to not run optimally[16].

Fourth hypothesis tests whether board directors nationality diversity positively influences Indonesian financial sector companies financial performance. Fourth hypothesis test reveal Indonesian financial companies performance positively affected by board directors nationality diversity on the board of directors. This can be a consideration for shareholders to elect a board of directors that is diverse in nationality, especially for companies that have branches or want to expand overseas. Board of directors with foreign nationalities are considered to have a better understanding of foreign markets. Therefore, companies that will expand overseas and require raw materials from abroad, appointing foreign nationality directors is considered beneficial for the Company.

6. Conclusion

Research aims to assess board diversity effect on Indonesian financial companies performance. The findings indicate that:

- Board comissioners gender diversity does not influence financial performance.

- Gender diversity of board directors and nationality diversity on the board directors have positive influence on financial performance.
- Nationality diversity of board commissioners negatively affects financial performance.

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