

**CHALLENGING THE RESOURCE-BASED VIEW:  
AN ANALYSIS OF THE RELATION BETWEEN THE BOARD OF DIRECTORS AND  
PERFORMANCE**

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**Abstract.** *The paper investigates the relation between board attributes, strategy and company performance. This study strives to clarify the connection between several types of board demographics, like size, age, female representation, non-executives, and CEO-duality and corporate performance. The results are consistent with other studies performed abroad and at the same time offer new theoretical and managerial perspectives on the issues analyzed. Data used in the study was collected from 58 publicly traded Romanian companies listed on the Bucharest Stock Exchange (BSE). Sample companies are categorized into one the following industries: manufacturing, pharmaceuticals, bank and insurance services, and retail. Data was drawn from following sources: Annual Reports and Board of Directors Reports. Rumelt's approach on measuring corporate diversification was implied. As for company performance two types of variables were used: the return on assets (ROA) and the return on equity (ROE). In order to test our hypothesis, we used the SPSS software. The main analyses used in our study were one-way ANOVA, independent t-test, Pearson correlation and regression analysis. The findings offer some valuable insights into the decision of corporate diversification at both theoretical and managerial level. According to our results size can be an important element in companies' decision to diversify. At the same time, non-executive directors tend to influence positively the level of performance within the analyzed companies.*

**Keywords:** *board of directors; company performance; corporate strategy; resource-based view; competitive advantage.*

## **Introduction**

Company performance remains one of the major concerns of managers from both developed and developing economies. Moreover, scholars had tried during the years to explain what is augmenting the financial results of companies. There is a general belief that once a company is able to capitalize on its competitive advantage, the higher

profits will start to appear. Proponents of the resource-based view (RBV) see the human capital as one of the companies' resources that can turn the competitive advantage into profits. The paper draws on the analysis of a particular stakeholder, namely the members of board of directors and tries to answer several research questions:

- (1) What is the effect of the board of directors' attributes on the company performance?
- (2) Does corporate diversification moderate the effect of the relationship between the board of directors' attributes and company performance?

The research is settled in an emerging economy; 58 publicly traded companies from the Bucharest Stock Exchange have been included in the sample.

The paper is structured as follows. It starts with an overview of the theoretical implications of the resource-based view of the firm on the creation of sustainable competitive advantage. At the same time, it describes the importance of human capital as the main predictor of greater company profitability. Next, the research methodology is presented together with a description of the three statistical models that are tested. After this, the main findings of the study are highlighted. The paper ends with a discussion about the main contributions to the body of knowledge.

### **Theoretical background**

According to some scholars, the resource-based view of the firm is seen to be one of the most influential frameworks used within the strategic management field of study (Barney, Wright & Ketchen, Jr., 2001). Moreover, it has been admitted as a new paradigm for the strategic management field (Peteraf, 1993). The moment it became to be adopted by theoreticians coincides with the emergence of several studies that pointed out that firms are made of a bundle of resources which enables them to obtain a competitive advantage (Barney, 1991; Rumelt, 1984). Within this theory, resources play an important role not only in the development of strategies but also for the achievement of greater profitability. As stated by resource-based view proponents, it is no longer the case of some privileged market position to explain the success of a firm (Porter, 1980), but rather the type of resources and the way in which they are handled by the firms. Although the resource-based view is a rather new phenomenon (Ambrosini, 2003), it is argued that it has its traces within the classic approach of strategy formulation as it focuses on the strengths and weaknesses of firms (Andrews, 1971). Within this context, it is of great importance for managers to clearly establish which resources are valuable and genuine sources of competitive advantage. The work of Peteraf (1993) and Peteraf and Barney (2003) is essential in this respect as it describes the keystones of any resource-generated strategy and it has to do with the heterogeneity of resources (resources differ among firms) and the imperfect mobility of resources (resources are not mobile across firms).

Practitioners have now a very useful and powerful tool that they can use in order to assess the possibility of a resource to generate and sustain a competitive advantage (Kozlenkova, Samaha & Palmatier, 2014). The VRIO framework allows for an appraisal of firm's resources by investigating four attributes: valuableness, rareness, imitability and exploitability (Barney & Hersterly, 2012). A resource is valuable if it is able to

support the successful implementation of a strategy and unleash its potential towards greater revenues. Simply exploiting a resource is not enough for achieving a competitive advantage as there might be other firms doing the same thing. Thus, a resource needs to be possessed by a small number of competing firms. Moreover, the resource should be hard to imitate by the other competitors, meaning that it will be costly for them to obtain it. Eventually, the resource has to be exploited by the organization; this implies that the firm has the right procedures, policies, and processes to deal with that resource (Barney & Clark, 2007).

It is worth distinguished between the tangible and intangible resources. Within tangible resources, one could include plants, equipment, finances, and location, whereas intangible resources refer to employees' skills and motivation, patents and copyrights and firms' culture and reputation (Grant, 2008). Barney and Hersterly (2012) identified four categories of resources that a firm might possess: physical, financial, human and organizational. There is a general belief that intangible resources are more likely to be the root of sustainable competitive advantage (Grant, 1996; Hitt et al., 2001; Spender, 1996). The reason for this is that intangible resources normally incorporate the knowledge that resides within the firm's human capital. Knowledge can be either explicit, that is the knowledge that can be easily articulated and communicated, either tacit, that is the knowledge that is embedded in individual skills and in firm's culture (Nelson & Winter, 1982; Polanyi, 1966). The non-imitability attribute of tacit knowledge makes it more valuable and more likely to lead to competitive advantage (McEvily & Chakravarthy, 2002). Hence, the way in which people are selected and attracted by firms will have an important role in the creation of competitive advantage.

The link between human capital and performance has been widely documented within the literature. There is enough evidence to support the crucial role that employees play in the financial success of firms (Arthur, 1994; Dyer & Reeves, 1995; Guest, 1997; Paauwe, 2009). However, very few studies addressed this link from the point of view of a particular stakeholder, namely the board of directors. Board of directors is part of the human capital dimension that is considered to have a remarkable influence on the results of the firms. Within the corporate governance framework, board members are said to have two functions: supervise and monitor top management on behalf of shareholders and provide resources (Hillman & Dalziel, 2003; Monks & Minow, 1995). A decisive concern over the past years was to assess the contribution of the board of directors to the strategy process (Bordean, Crişan & Pop, 2012; Pearce & Zahra, 1992, Pugliese et al., 2009). Even though the results are quite fuzzy, it is believed that the role of the board of directors in strategic management is to carry out three basic tasks: 1) monitor, 2) evaluate and influence and 3) initiate and determine (Wheelen & Hunger, 2012). According to the level of involvement within the strategy process, the board of directors are classified either in five (Nadler, 2004) or even six categories (Wheelen & Hunger, 2012) based on a continuum. Studies carried out on various types of boards suggest that the most involved are board members in strategic management tasks, the greater the financial performance will be (Judge & Zeithaml, 1992; Pearce & Zahra, 1992).

The relationship between the board of directors and performance is well documented within the corporate governance literature. Scholars tried to assess both the observable (demographic) and the non-observable (cognitive) dimensions of boards.

Some examples of observable variables are gender, age, race, and ethnicity, whereas examples of non-observable variables are knowledge, education, values and personality characteristics (Erhardt, Werbel & Shrader, 2003). So far, studies that focus on board of directors attributes and performance revealed contradictory results. Some authors were able to determine positive effects that board of directors has over performance within various contexts and backgrounds (Bantel, 1993; Simons & Pelled, 1999). On the other hand, there are still studies who point out towards a negative relation that exists between boards of directors and company performance (Knight et al., 1999; Hambrick, Cho & Chen, 1996). Zahra and Pearce (1989) proposed an integrative model grounded in theory and empirical research that grouped boards attributed into four dimensions: composition, characteristics, structure, and process.

### Research methodology

The sample for this study is drawn from the companies listed on the Bucharest Stock Exchange that act in various sectors. The reason for choosing such a sample has to do with the availability of data provided by the listed companies that are required to publish information about their activities throughout the year. The data was gathered from the Annual Reports and from Board of Directors Reports. Even though, not all the listed companies published these documents, so the final sample consisted of 58 publicly traded companies from Romania. Table 1 provides a summary of the main characteristics of the firms included in the sample. Among the firms analyzed, 27.59% were small and medium-sized enterprises, that is companies that employ less than 250 people; 17.24% were companies that had between 251-500 employees and the rest of them had over 500 employees.

*Table 1. Characteristics of sample firms*

Characteristics	Number	Percentage
<i>Size of firms</i>		
SMEs (1-250 employees)	16	27.59
Large firms (251-500 employees)	10	17.24
Extra large firms (>501 employees)	32	55.17
<i>Ownership</i>		
State-owned firms	10	17.24
Private-owned firms	48	82.76
<i>Years of trade on BSE</i>		
Veteran firms (> 15 years)	30	51.72
Mature firms (between 11-14 years)	16	27.58
New entrant firms (<11 years)	12	20.70

One way of classifying firms according to the type of ownership refers to state-owned and private-owned firms. Within the sample, the majority of firms were private-owned (82.76%). Various studies highlight the direct effect of firm's age upon knowledge accumulation with respect to the business environment (Carroll & Harrison, 1998; Glance, Hogg & Huberman, 1997; Lin & Hui, 1999). This variable is measured in different ways, but the most used one is the number of years the firm activates on the market. Considering the characteristics of the sample, we chose to use as a metric for this variable the number of years firms are listed on the BSE; thus three groups of firms evolved: (1) "veterans" that are listed for more than 15 years; (2) "mature" that

are listed on the stock exchange for a period that ranges between 11 and 15 years and (3) “new entrants” that are listed for less than 11 years.

The variables included in the research are grouped into three categories: independent variables, dependent variables and control variables. For this study, we focus on one particular type of stakeholder of the firm, namely the board of directors. The independent variables are connected to this stakeholder and refer to the following: the size of the board, the age of board, the female representation, the non-executive representatives and the CEO duality of the board. The dependent variables refer to the level of performance of the firms within the sample, whereas the control variables are the firms’ size and a number of years they are listed on the stock market. We also tried to test the moderating effect of diversification strategy on the link between the board of directors’ attributes and company performance. Table 2 summarizes how each variable was constructed and measured.

**Table 2. Variable construction and measurement**

<b>Variable</b>	<b>Measurement</b>
BOD_size	Number of people sitting in the board of directors.
BOD_age	Average age of people sitting in the board of directors.
BOD_female	Percentage of females (Number of female members/Total number of board members).
BOD_non_executives	Percentage of board members without executive positions (Number of board members without executive position/ Total number of board members)
BOD_duality	Measured as a dummy variable (1- if the chairman and CEO are the same person, else - 0).
Firm_size	Number of employees the firm has.
Firm_age	Number of years the firm is listed on the BSE.
Strategy	Measured based on Rumelt’s specialization ratio (Revenues of the largest product-market/Total revenues)
Perform_ROA	Return on assets (Net income/Total assets)
Perform_ROE	Return on equity (Net income/Shareholders equity)

The analysis of data was done with SPSS 16.0. One of the first analyses implied was the descriptive statistics for the variables included in the study; these results are highlighted in Table 3. Next, the one-way ANOVA analysis was performed in order to test if there are any significant differences between the various groups of firms with respect to the board of directors’ attributes. Eventually, Pearson correlation and regression analysis were performed to test the three models proposed within this research:

$$\text{Strategy} = \alpha + \beta_1\text{BOD\_size} + \beta_2\text{BOD\_age} + \beta_3\text{BOD\_female} + \beta_4\text{BOD\_non\_executives} + \beta_5\text{BOD\_duality} + \beta_6\text{Firm\_size} + \beta_7\text{Firm\_age} + \varepsilon \quad (1)$$

$$\text{Perform\_ROA} = \alpha + \beta_1\text{BOD\_size} + \beta_2\text{BOD\_age} + \beta_3\text{BOD\_female} + \beta_4\text{BOD\_non\_executives} + \beta_5\text{BOD\_duality} + \beta_6\text{Strategy} + \beta_7\text{Firm\_size} + \beta_8\text{Firm\_age} + \varepsilon \quad (2)$$

$$\text{Perform\_ROE} = \alpha + \beta_1\text{BOD\_size} + \beta_2\text{BOD\_age} + \beta_3\text{BOD\_female} + \beta_4\text{BOD\_non\_executives} + \beta_5\text{BOD\_duality} + \beta_6\text{Strategy} + \beta_7\text{Firm\_size} + \beta_8\text{Firm\_age} + \varepsilon \quad (3)$$

**Findings**

The boards included in the sample have between 2 and 11 members and the average age of those people sitting on the board of directors is 50 years. Some of the boards do not include any women within them and there was no board that had no members that were not part of the executive board as well (see Table 3).

**Table 3. Descriptive statistics**

Variable	N	Minimum	Maximum	Mean	Std. deviation
Firm_size	58	26.00	22739.00	1454.00	3224.77
Firm_age	58	3.00	17.00	12.79	3.90
BOD_size	58	2.00	11.00	4.96	1.85
BOD_age	58	39.60	64.20	50.75	6.31
BOD_female	58	.00	.60	.13	.17
BOD_non_executives	58	.20	1.00	.84	.19
BOD_duality	58	.00	1.00	.41	.49
Strategy	58	26.71	100.00	72.76	23.24
Perform_ROA	58	-33.03	22.28	.25	9.15
Perform_ROE	58	-362.48	48.57	-12.66	64.9

The results of the ANOVA analysis showed that board of directors only differ between the three groups of firms created using their size in terms of the number of people sitting on the board of directors. The size of the board of directors is different for the SMEs, large firms and extra large firms ( $p = 0.004$ ). No significant differences between older and newer firms had been found out with respect to how the board of directors is structured for the firms in the sample.

**Table 4. Results of ANOVA analysis for BOD attributes**

Board of directors' attributes	Firms' attributes			
	Firm_size		Firm_age	
	F	Sig.	F	Sig.
BOD_size	6.122	0.004	0.744	0.480
BOD_age	0.029	0.971	0.271	0.763
BOD_female	2.309	0.109	1.099	0.340
BOD_non_executives	0.334	0.717	0.029	0.971
BOD_duality	0.335	0.717	0.793	0.458

The results of the Tukey-post hoc are presented in Table 5 and reveal that main differences are between extra large firms and SMEs ( $p = 0.011$ ) and between extra large firms and large firms ( $p = 0.034$ ).

**Table 5. Results of the Tukey post-hoc test**

	(I) Firm_size	(J) Firm_size	Mean Difference (I-J)	Std. Error	Sig.
Dependent variable: BOD_size	SMEs	Large firms	.51250	.68810	.738
		Extra large firms	-1.34375*	.52265	.034
	Large firms	SMEs	-.51250	.68810	.738
		Extra large firms	-1.85625*	.61841	.011
	Extra large firms	Large firms	1.34375*	.52265	.034
		SMEs	1.85625*	.61841	.011

\* The mean difference is significant at the 0.05 level

In order to test if there are significant differences between state-owned firms and private-owned firms with respect to board structure, we used the independent t-test. The results of this test are showed in Table 6. It was found out that the size of the board of directors differs significantly for the firms where the state is the owner in comparison to the firms that have private investors ( $p = 0.019$ ).

**Table 6. Results of the independent t-test**

Board of directors' attributes	Ownership structure			
	State-owned firms		Private-own firms	
	t	Sig. (2-tailed)	t	Sig. (2-tailed)
BOD_size	-2.410	0.019	-0.983	0.330
BOD_age	0.682	0.498	-0.976	0.333
BOD_female	0.136	0.893	0.416	0.679
BOD_non_executives	-1.311	0.195	1.370	0.176
BOD_duality	-0.989	0.327	0.013	0.990

The three models hypothesized for this study were tested using the regression analysis and the results are presented in Table 7. In the first model that accounts for 15% of the variation, the diversification strategy was regressed against the five variables defined for the board of directors and the two control variables. The variable number of board members is negatively and significantly linked to strategy ( $\beta = -4.888$ ,  $p = 0.017$ ). The other board of directors' variables do not have any significant impact on the formulation of strategy. Model 2 accounts for only 9% of the variation and predicts the influence of board attributes upon return on assets. It was found out that boards with members that were not having any other executive positions within the firm perform better ( $\beta = 13.637$ ,  $p = 0.083$ ). Eventually, Model 3 accounts for 12% of the variance and predicts the impact of board attributes on another financial indicator, which is a return on equity. In this case, the variable non-executive board members has even a stronger influence on the financial results of the firms in comparison to the previous model that was tested ( $\beta = 135.811$ ,  $p = 0.014$ ).

**Table 7. Results of the regression analysis**

Independent variables	Model 1 Dependent variable: Strategy	Model 2 Dependent variable: ROA	Model 3 Dependent variable: ROE
Firm_size	.001	9.097	.000
Firm_age	.012	.148	.750
BOD_size	-4.888*	.361	.336
BOD_age	.207	-.172	-.466
BOD_female	-3.144	-.875	-23.751
BOD_non_executives	8.698	13.637**	135.811*
BOD_duality	-3.284	3.486	30.136
Strategy		.033	.035
R <sup>2</sup>	.15	.09	.12
F	1.277	.606	.886

\* Statistically significant at less than .05 level

\*\* Statistically significant at less than .10 level

The other variables pertaining to the board of directors did not reveal any influence on the firms' performance, nor did the control variable included within the three models

tested. Moreover, the level of diversification strategy implemented by firms does not impact the level of performance.

### **Discussions and conclusions**

The paper investigated the relation between the board of directors' attributes and strategy implementation and also the relationship between the board of directors' attributes and firm performance on a sample of companies listed on the Bucharest Stock Exchange. The way in which boards influence the strategy is still quite unclear as a lot of studies performed within this framework failed to lead to a consensus in terms strategy is shaped by board members. From a contextual point of view (Pugliese et al., 2009), the present study falls under the input-output approach that assumes there is a link between board composition and strategic outcomes, such as diversification, innovation, mergers, and acquisitions. Findings suggest that the size of the board impacts the diversification strategy; moreover, a negative association between a number of people sitting on a board and diversification strategy was found. Previous studies proved that the size of board may have a positive influence on the performance of the companies, the main reason for considering so was that more people could generate more intellectual knowledge that could be useful for the financial outcome of the company (Dalton et al., 1998; Pearce & Zahra, 1992). However, the strategy making process is time-consuming and any strategy is intended to be implemented on a long-term base. Being able to reduce the time needed to formulate and implement the strategy is an indicator of potential success for the company. Fewer people within a board can represent a decrease in time for the decision-making process and consequently this could lead to a better implementation of the strategy.

For measuring the performance of the companies, two financial indicators were used, return on assets and return on equity. ROA shows how profitable a company is at using its assets in order to generate earnings, whereas ROE measures a company's profitability by revealing how much profit a company generates with the money shareholders have invested. The boards can comprise of members that have executive functions within the company and also of members that do not an executive position. According to the findings, boards with non-executive members positively influence the financial results of the companies. This is consistent with other previous works performed on board of directors (Bhagat & Bolton, 2008; Jackling & Johl, 2009; Jermias, 2007). In this case, the non-executive members are seen as offering valuable inputs as they contribute by increasing the general intellectual knowledge of the group and leading to better decisions that are reflected in the financial outcomes of the companies. The study supports the superiority of the resource-based view of the firm, as human capital proves to be of great significance for the way in which the competitive advantage is created.

The results presented are subject to some limitations that need to be taken into consideration when interpreting the findings. First, it should be noted that the study used a small sample of the companies listed on BSE. Secondly, the study addressed only some of the board attributes that are reported in the literature as main determinants of corporate performance. Thirdly, only the moderating effect of diversification strategy was checked for the relation between board attributes and performance. Future areas of research could focus on a larger sample of companies

and include other board of directors' variables, such as a number of board meetings or board leadership. Still, the paper contributes to the body of literature that describes the link between boards and corporate performance in an emerging economy.

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