Indian-Pacific Journal of Accounting and Finance (IPJAF)
ISSN: 2600-9161 eISSN: 2590-406X
Vol. 8 No. 2, 2024
pp. 33-39
https://doi.org/10.52962/ipjaf.2024.8.2.161

www.ipjaf.omjpalpha.com

Received 25 January 2023; Accepted 23 June 2024

The Influence of Board Governance on Operating Performance of Malaysian IPOs Trading and Services Sector.

Afiruddin Tapa*[1], Ahmad Rizal Mazlan[2]

[1]*School of Economics, Finance and Banking, Universiti Utara Malaysia.*
[2]*Universiti Utara Malaysia Kuala Lumpur*

Abstract: This study examines the impact of board characteristics on the financial performance of firms in the Trading and Services sector, using EBIT/A (Earnings Before Interest and Taxes to Total Assets) and EBIT/S (Earnings Before Interest and Taxes to Sales) as dependent variables. Regression analysis reveals that board age diversity (DIRAGE) significantly influences firm performance in both models. These findings highlight the benefits of age diversity in enhancing firm value and mitigating risks. Diverse age groups on the board contribute distinct advantages: older members bring experience and financial resources, middle-aged members focus on corporate responsibilities, and younger members inject energy and innovation. Other variables, including board size, gender diversity, and educational background, demonstrate limited statistical significance. The study underscores the importance of promoting age diversity to enhance organizational performance in the sector.

Keywords: Board characteristic, IPOs, operating performance, board diversity, board size, and firm size.

JEL Classification: G30; G32; G14
Paper Type: Research

* Corresponding author: E-mail: afiruddin@uum.edu.my

1. INTRODUCTION

The new issue market plays a vital role in the capital market, offering companies an avenue to raise funds through initial public offerings (IPOs). These strategic financing decisions have garnered extensive attention in financial research, particularly concerning IPO price behavior and performance. While previous studies widely report substantial short-term gains for IPO investors, long-term performance often reveals underwhelming or negative returns, as documented by Loughran and Ritter (1994) and Cai and Wei (1997). In Malaysia, however, IPOs demonstrate a unique trajectory, consistently outperforming the market in the short and long run, as highlighted by Corhay et al. (2002) and Zaluki et al. (2007). This distinct trend underlines the importance of exploring Malaysia's IPO dynamics, particularly in sectors like Trading and Services, which contribute significantly to the national economy.

Existing literature has delved into the operating performance of IPO firms post-issuance, revealing a notable decline when compared to pre-issue levels (Jain and Kini, 1994; Balatbat et al., 2004). While these studies provide valuable insights, most Malaysian research has predominantly focused on factors such as underpricing, institutional ownership, market conditions, and underwriter reputation, often overlooking the impact of board governance. Given the crucial role of corporate governance in steering firm performance, particularly in publicly traded entities, a detailed examination of board governance factors, including age diversity, board size, gender composition, and director qualifications, is necessary to bridge this research gap.

This study aims to investigate the influence of board governance on the operating performance of Malaysian IPO firms in the Trading and Services sector. Using Earnings Before Interest and Taxes to Assets (EBIT/A) and Earnings Before Interest and Taxes to Sales (EBIT/S) as performance indicators, this research identifies board age diversity as a significant determinant of operating performance. The findings align with prior studies that emphasize the value of diverse perspectives in enhancing firm performance and mitigating risks. By focusing on board characteristics within the Trading and Services sector, this paper contributes to the ongoing discourse on corporate governance and its impact on IPO firms' success in Malaysia.

2. LITERATURE REVIEW

Finkle (1998) examined the relationship between the board of directors and IPOs in the Biotechnology Industry. The results show a significant positive relationship between the director's expertise and the size of the firm IPO. It documented that the CEOs, who were formerly university scientists, are positively related to larger IPOs. The study also found a positive significant relationship between CEO with a financial background and larger IPOs.

In Arioglu's groundbreaking study conducted in 2021, a comprehensive exploration was undertaken to investigate the impact of board age diversity on two pivotal aspects of corporate governance: company financial performance and risk management. The study went further, delving into the intricate dynamics of work-related values held by directors across various age groups, aiming to ascertain whether these values were the driving force behind any discernible effects on company outcomes.

This pioneering research was conducted on a carefully selected sample of listed companies in Turkey, a nation characterized by its collectivistic and paternalistic cultural backdrop. Turkey's unique cultural context added an intriguing layer to the study, given its potential influence on corporate decision-making and governance practices.

When we consider the intersection of collectivistic and paternalistic cultural traits, as often found in certain regions and societies, we see a cultural environment where group harmony, interdependence, and deference to authority are highly valued. In such cultures, decisions within organizations, including corporate boards, may be influenced by a strong sense of consensus-building, loyalty to leadership, and respect for the wisdom of older or more experienced individuals. These cultural characteristics can have implications for corporate governance practices, decision-making processes, and relationships within the boardroom, as they may prioritize collective well-being and respect for authority figures. Understanding these cultural dynamics is crucial when analyzing how corporate governance operates within specific contexts, such as the Turkish context mentioned in the initial statement.

The findings stemming from this meticulous examination proved to be both enlightening and transformative. They unequivocally revealed that board age diversity is not merely a token aspect of corporate governance but a catalyst for significant positive change. Specifically, it was demonstrated that board age diversity exerts a profound and positive influence on both company performance and risk mitigation.

In other words, the study illuminated a crucial dimension of corporate governance: the interplay of different age groups within the boardroom leads to superior financial outcomes and more effective risk management for companies. This realization challenges conventional notions and underscores the importance of embracing diversity, not only in terms of gender and ethnicity but also with respect to age, as a pivotal factor in shaping the trajectory of corporate success.

Arioglu's (2021) study has not only enriched our understanding of corporate governance but has also provided empirical evidence of the tangible benefits associated with board age diversity within the unique cultural context of Turkey. These findings serve as a compelling call to action for organizations globally to prioritize age diversity as a strategic imperative for fostering enhanced company performance and robust risk management practices.

Certo (2003) tested the signaling theory on how board prestige can influence IPO investors' decision-making to purchase IPOs. Board prestige refers to perceptions of the board based on the board's skills, experiences, and social connections. The researcher suggested that board prestige may influence the investors' decision-making process because IPOs firms suffer from the liability of market 'newness', and they need to show organizational legitimacy to the firm's potential investors.

The relationship between board prestige and directors' age can vary based on several factors, and it is not a one-size-fits-all scenario. The dynamics between board prestige and directors' age can be complex and context-dependent.

In summary, the relationship between board prestige and directors' age is not fixed and can be influenced by industry norms, company context, and evolving perceptions of governance. A well-balanced board may include directors of different ages who bring complementary skills and experiences, contributing to the overall prestige and effectiveness of the board. Ultimately, the key is to strike a balance that aligns with the company's strategic goals and the expectations of its stakeholders.

3. DATA AND METHODOLOGY

This section outlines the theoretical framework developed for this study, drawing upon the agency cost theory, signaling theory, and relevant literature aligned with the study's objectives. Figure 1 presents the theoretical framework detailing the dependent, independent, and control variables chosen for this research. The selection of these variables is grounded in the foundational theories discussed earlier and supported by pertinent findings from existing studies.

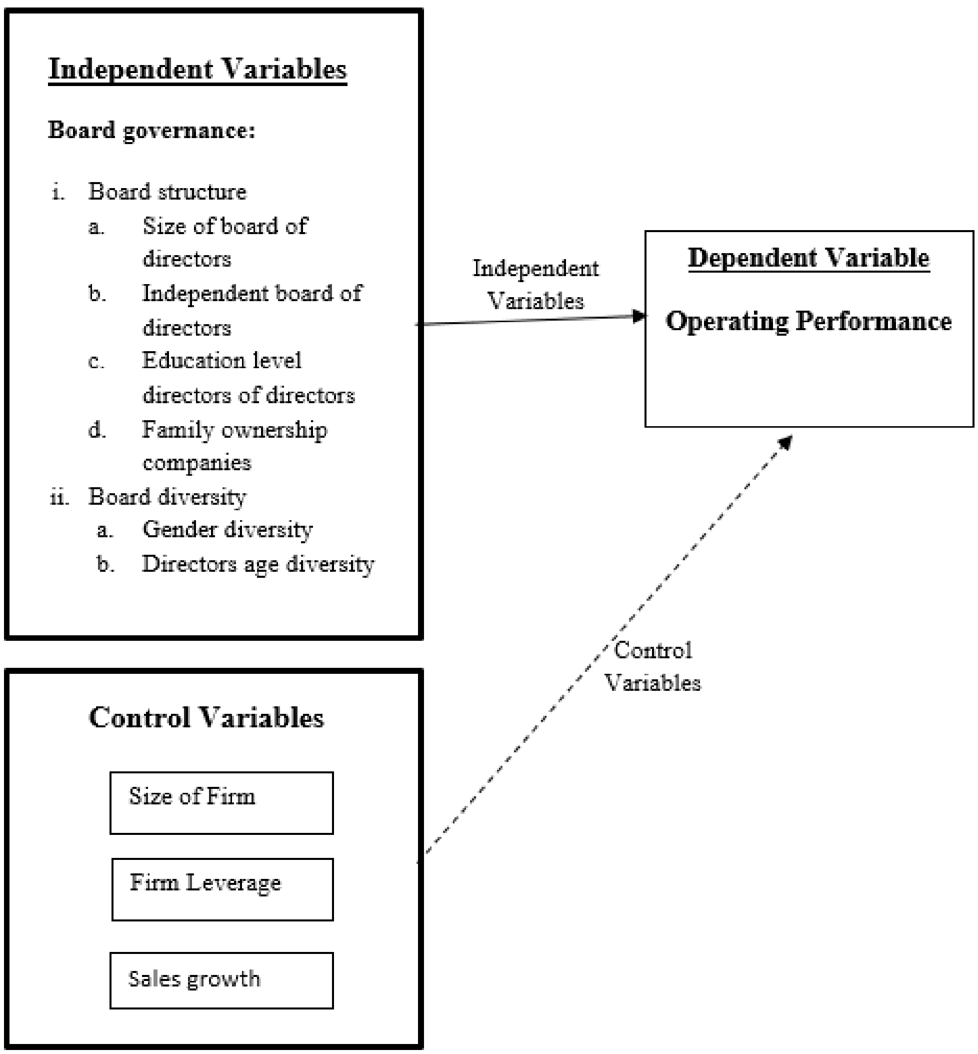

Figure 1. Theoretical Framework

4. RESULT AND DISCUSSION

Tables 1 and 2 display the regression analysis results based on the Trading and Services sector with EBIT/A and EBIT/S as the dependent variables. For both regressions, age diversity (DIRAGE) among directors is significant toward IPO firms' operating performance. This result aligns with Arioglu's (2021) study, whereby board age diversity affects company financial performance and risk, and diverse work-related values held by directors of different ages are the underlying cause of this effect. The findings indicate that board age diversity benefits both company performance and risk.

Most boards of directors are expected to have a certain age range, with the older group providing experience and financial resources, the middle group focusing on major corporate and social responsibilities, and the younger group possessing the energy and drive to propel the company to greater heights. According to Carter et al. (2003), age diversity in the board can increase firm value and performance by providing the board with new insights and perspectives.

Moreover, the significance of board age diversity in influencing firm performance extends beyond operational efficiency. A diverse board composition reflects a balanced approach to decision-making, where varying perspectives help mitigate potential biases and promote innovation. Directors of different age groups often approach challenges and opportunities differently, enabling the firm to respond more effectively to dynamic market conditions. This diversity also enhances the board's ability to foresee and manage risks, as directors bring a combination of historical wisdom and contemporary thinking. The findings underscore the importance of fostering age diversity within board governance structures, particularly for firms in the Trading and Services sector, where adaptability and strategic foresight are crucial for sustaining competitive advantage.

Table 1. Trading and Services Sectors on EBIT/A

Variable	Coefficient	Std. Error	t-Statistic	Prob.
EDU	0.936664	0.634295	1.476702	0.1443
BOARD	-0.238751	0.358374	-0.666206	0.5075
DIRAGE	0.974115	0.545921	1.784351	0.0788*
GENDER	0.202973	0.543640	0.373359	0.7100
IND	-0.158601	0.955581	-0.165973	0.8687
FMLY	0.001148	0.003743	0.306789	0.7599
SIZE	0.134958	0.073974	1.824383	0.0724*
LEV	0.338789	0.447051	0.757832	0.4511
SG	0.510720	0.273780	1.865444	0.0664*
R-squared	0.320784			
Adjusted R-squared	0.084535			

*** Significant 1 percent level
** Significant 5 percent level
* Significant 10 percent level

Table 2. Trading and Services Sectors on EBIT/S

Variable	Coefficient	Std. Error	t-Statistic	Prob.
EDU	0.748799	0.734426	1.019570	0.3115
BOARD	-0.428175	0.414947	-1.031878	0.3057
DIRAGE	1.580321	0.632101	2.500108	0.0148***
GENDER	0.600381	0.629460	0.953803	0.3435
IND	-1.179633	1.106431	-1.066160	0.2901
FMLY	-0.001609	0.004334	-0.371245	0.7116
SIZE	0.082647	0.085652	0.964912	0.3380
LEV	0.153640	0.517623	0.296819	0.7675
SG	0.741939	0.316999	2.340511	0.0222**
R-squared	0.318341			
Adjusted R-squared	0.081242			

*** Significant 1 percent level
**Significant 5 percent level
* Significant 10 percent level

5. CONCLUSION

This study examines the influence of board governance on the operating performance of Malaysian IPO firms in the Trading and Services sector, focusing on the relationship between board characteristics and key financial performance indicators, EBIT/A and EBIT/S. The findings highlight the critical role of board age diversity (DIRAGE) in enhancing firm performance, reinforcing that a well-balanced board comprising directors of varying age groups can contribute to improved decision-making, risk management, and strategic agility. These results are consistent with previous research, which emphasizes the value of diversity in corporate governance for fostering innovation and mitigating risks.

While other governance variables, such as board size, gender diversity, and educational qualifications, showed limited significance, the study underscores the unique impact of age diversity. Older directors provide valuable experience and resources, middle-aged directors emphasize corporate responsibility, and younger directors bring energy and fresh perspectives, collectively creating a synergistic effect that benefits organizational performance.

The findings offer practical implications for corporate governance practices, particularly for firms preparing to go public. Policymakers and corporate leaders should prioritize age diversity as part of broader governance reforms to enhance firm value and operational efficiency. Future research could expand on this work by examining other sectors or incorporating additional governance factors to provide a more comprehensive understanding of the dynamics between board governance and firm performance in IPO firms.

REFERENCES

Abidin, Z., Kamal, N. & Jusoff, K. (2009). Board Structure and Corporate Performance in Malaysia. *International Journal of Economics and Finance, 1*(1), 150-164.

Ahmad, G. N., Prasetyo, M. R. P., Buchdadi, A. D., Widyastuti, U., & Kurniawati, H. (2022). The effect of CEO characteristics on firm performance of food and beverage companies in Indonesia, *Malaysia and Singapore. Calitatea*, 23(186), 111-122.

Allen, F. & Faulhaber, G.R. (1989). Signalling by underpricing in the IPOs market. *Journal of Financial Economics, 23*, 303-323.

Arik, E., & Mutlu, E. (2015). Post–initial public offering operating performance and its determinants: Initial public offering characteristics and corporate governance practices. *Emerging Markets Finance and Trade*, *51*(sup2), S62–S83. https://doi.org/10.1080/1540496x.2014.998943

Arioglu, E. (2021). Board age and value diversity: Evidence from a collectivistic and paternalistic culture. *Borsa Istanbul Review, 21*(3), 209–226. https://doi.org/10.1016/j.bir.2020.10.004

Balatbat, M. C. A., Taylor, S. L., & Walter, T. S. (2004). Corporate governance, insider ownership and operating performance of Australian initial public offerings. *Accounting and Finance*, *44*(3),

Cai, J & Wei, K.C J., 1997. The investment and operating performance of Japanese initial public offerings. *Pacific-Basin Finance Journal, 5*, 389-417.

Carter, Simkins, B. J., & Simpson, W. G. (2003). Corporate governance, board diversity and firm value. *The Financial Review, 38*(1), 33–53.

Certo. S. T. (2003). Influencing initial public offering investors with prestige: Signaling with board structures. *Academy of Management Review, 28*(3), 432-446.

Corhay, A. Teo, S. & Rad, A.T. (2002). The long run performance of Malaysian IPOs: Value and growth effect. *Managerial Finance, 28*(2), 52-65.

Finkle. T. A. (1998). The relationship between board of directors and initial public offerings in the biotechnology industry. *Entrepreneurship Theory and Practice, 22*(3), 5-29.

Jain, B.A & Kini, O. (1994). The post-issue operating performance of IPOs firms*. Journal of Finance, 49*(5), 1699-1726.

Jain, B.A. & Kini, O. (2008). The impact of strategic investment choices on post-issue operating performance and survival of US IPOs firms. *Journal of Business Finance and Accounting, 35*(3), 459-490.

Kim, K.A., Kitsabunnarat, P. and Nofsinger, J.R. (2005). Large shareholders, board independence and minority shareholders right: evidence from Europe. European Corporate Governance Symposium held at Leeds University, Texas Tech University, and California State University

Loughran, T. & Ritter J. (1997). The operating performance of firms conducting seasoned equity offerings. *The Journal of Finance, 52*(5), 1823-1850.

Zulkafli, A.H. (2007). Corporate governance and performance of banking firm: evidence from Asian emerging market. PhD thesis, University of Malaya.