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Board of directors and the internationalization process: The case of Romania

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Board of directors and the internationalization process: the case of Romania

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Abstract

This paper attempts to describe the relationship between some board composition (board size, board age, CEO-duality and female representation) and the internationalization strategy in Romanian firms. The data for our study was collected through secondary sources and was aimed at a sample of companies listed at Bucharest Stock Exchange (BSE). We had included in our survey both companies that were pursuing an international strategy and companies that were showing no interest for the internationalization process. The degree of international involvement of the listed companies was assessed through two dimensions: propensity for export and export intensity. The results of the analysis show that the internationalization path followed by the Romanian listed companies is not influenced in any way by board of directors. However, the number of years that the companies are listed on the stock exchange is a good predictor of internationalization.

Keywords: Board of directors, internationalization strategy, export propensity, export intensity, corporate governance.

1. Introduction

In the current competitive environment, the factors leading enterprises success are no longer simply in the investment of capital, labor and raw material, but in the ability of knowledge innovation from all the members of the organization (Ho, 2009). From a managerial point of view corporate governance deals with the interaction among board members, top management team and shareholders (Wheelen and Hunger, 2010). Within this approach, the interaction between top management and board of directors becomes crucial for the success of a company. Such an interaction will be highly influenced by the level of information and knowledge that is exchanged within these actors of corporate governance. Knowledge management is believed to be the fundamental concept that supports any corporate strategy (Mostafa Jafari et al., 2010). Thus, knowledge is seen as a kind of strategic resource in companies. The goal of knowledge management is to deliver the right knowledge to the right members at the right time, which can help members, take the right actions and further improve the performance circulation processes in organization (O'Dell and Grayson, 1999; Milton et al., 1999).

Several scholars showed a great interest for researching the way in which board of directors characteristics may influence the strategic decisions process (Westphal and Fredrickson, 2001; Ruigrok et al., 2006; Ravasi and Zattoni, 2006; Ogbachie et al., 2009). However, researches on the relationship among board characteristics and the internationalization process are scarce in the literature. This paper is addressing the relationship between board of directors' characteristics and the internationalization strategy pursued by companies in an emerging economy. Our paper tries to encompass the existing gap within the literature by addressing the following unexplored research questions:

- (1) What is the degree of international involvement of the Romanian listed companies?
- (2) Which board's characteristics are associated with the international involvement within the Romanian listed companies?

The remainder of this paper is organized as follows: first, we provide a brief review of the literature on the internationalization strategy and the board of directors' characteristics. Then, we proceed with the description of the methodology used in our survey followed by a section presenting the findings of our research. A discussion including suggestions for further research and implications for management concludes the presentation of this research.

2. Theories and hypothesis: the case of some Romanian listed companies

2.1 The internationalization strategy

During time, several scholars attempted to explain the reasons for which companies decide to follow an international path using different internationalization theories. Dunning and Rugman (1985) and Hymer (1976) explain the proliferation of companies that went internationally by referring to the following two conditions: (1) foreign companies must own special advantages over domestic companies and (2) the market for sales of these advantages must be imperfect. Later on, the internationalization theory had been shaped when the Coasian transaction economist proponents (Coase, 1937, Rugman, 1981; Hennart, 1982) argued in favor of companies going abroad as a response to imperfections in the goods or factor markets and the policy implications.

Internationalization is considered by some scholars the most complex strategy that any company can undertake (Fernández and Nieto, 2005). The increased attention which is given to internationalization strategy is due to the growing market globalization. In the same time, market liberalization and digitization are encouraging large companies and SMEs to operate beyond their national borders and compete with each other in foreign countries and new regions (Barkema et al., 2002). Internationalization strategy has been documented in different countries by a large body of both theoretical and empirical studies. However, little attention has been paid to examine this strategy in the case of Romanian listed companies. Moreover, the studies on the relationship the impact board characteristics on internationalization strategy are still more limited.

Internationalization can be defined as the extent to which a company is involved in international businesses. Companies may decide to pursue an international strategy in different ways that may vary from export to licensing to ownership-based modes such as joint ventures and wholly-owned subsidiaries (Arregle et al., 2006). The eclectic paradigm of Dunning (1977), clearly distinguishes between the three types of advantages influencing the foreign direct investments process: ownership specific advantages, location specific advantages and internationalization advantages. The last type of advantages is relative benefits associated with different entry modes (e.g. export, FDI, joint ventures and licensing). This view had also been supported by Rugman (2010), according to whom companies may benefit of both firm-specific advantages and country-specific advantages. Dunning (1998) also

identifies four types of international production: (1) natural resource seeking, (2) market seeking, (3) efficiency seeking and (4) strategic asset seeking.

The motives behind internationalization process are numerous and highly documented in the literature. Bartlett and Ghoshal (2000) have classified them into two categories: traditional motivations and emerging motivations. Within the first category one can easily find the following motivations: (1) the need to secure key supplies and scarce raw material resources. In fact, it was showed that a lack of resources and the uncertainty and complexity of the process usually work against foreign expansion. In such cases, the existence of strategic capabilities and resources is of utter importance for internationalization (Hitt *et al.*, 1997; Peng, 2001); (2) the desire to access low-cost factors of production; and (3) the market seeking behavior. This motivation is stronger in those companies that have some intrinsic advantage, related to their technology or their brand recognition that offer them a competitive advantage in offshore markets. International expansion is based in the capability of the company to exploit in foreign markets the advantages that it has in the local ones.

Among the emerging motivations of internationalization, Bartlett and Ghoshal (2000) have included the economic, technological and social developments that made internationalization essential for a company to survive in particular businesses. As a result of these developments, companies that had historically focused only on their domestic markets had to either become international or go out of business since few countries were large enough to support production at such scales by individual companies.

2.2 Board of directors' characteristics and the internationalization strategies

Board's involvement in the strategy decision process refers to the willingness and ability of board members to take decisions that affect the long-term direction of any company. Board characteristics have been referred within corporate governance literature from different angles. Korac-Kakabadse et al. (2001), for example, identify four sets of board attributes: demographics, cognitive, structure and process. Board demographics refer to size of the board and the mix of different director's demographics (age, executives/non-executives, male/female, CEO-duality). Board cognitive characteristics encompass director's backgrounds, such as director's experience; tenure; functional background; independence; stock ownership (Zahra and Pearce, 1989). Board structure covers board organization; the role of subsidiary boards in holding companies; board committees; the formal independence of one-tier and

two-tier boards; the leadership of boards and the flow of information between board structures. Board process refers to decision-making activities; styles of board; the frequency and length of board meetings; the formality of board proceedings and board culture on evaluation of director's performance. Within our research frame, we seek to examine the relationship between the following board characteristics: board size, board age, CEO-duality and female representation and board's involvement in the internationalization process.

Board size

Board size refers to the number of directors that serve on a board. The up-to-day results on board size and board's involvement in the decision making process are inconclusive (Golden and Zajac, 2001). Several scholars argue that as board size increases, the strategic decision making capabilities of the board increase (Pearce and Zahra, 1992; Dalton et al., 1999). This is due to the knowledge and intellect that is brought to the board by members coming from varied backgrounds. Golden and Zajac (2001) argued that smaller boards are assumed to have inadequate confidence and unclear understanding in making strategic changes. We consider that larger boards can provide an increased pool of expertise and can reduce the dominance of the CEO; therefore, we postulate the following hypothesis:

H1: Board size is positively associated with the internationalization strategy of the company.

Board age

Board age deals with the age of directors. Usually, this is a variable which is constructed as an average of the age of all the directors from a company. In the literature, board age is seen as predictor of accumulated knowledge and experience (Carroll and Harrison, 1998). Companies with more experienced boards may want to take advantage of the benefits offered by the international markets and though pursue an internationalization strategy. Thus, we propose the following hypothesis:

H2: Board age will positively influence the internationalization strategy of the company.

CEO duality

CEO duality exists when the same person acts as both the chairman of the board of directors and the CEO of the company. A separation of roles is supported by agency theorists who argue in favor of having two people in charge of the management of the company and of the management of the board, respectively. According to them, this will lead to better performance and will contribute to the avoidance of “conflict of interests”. Ruigrok et al. (2006) found that there is a negative association between CEO duality and boards’ strategic involvement and argue that the more powerful is the CEO the more he will try to set the agenda of the board meetings. Moreover, a CEO who is the sole manager on the boards is argued to be more powerful than boards consisting of others managers and thus may influence decision-making, which in turn can have a negative impact on performance (Adams et al., 2005). The third hypothesis is:

H3: CEO duality has a negative impact on the internationalization strategy of the company.

Female representation

The subject of women in boards has been growing rapidly in the past years. Scholars manifested a preference for studying female representation within boards as it is the most easy distinguished demographic characteristic compared to age, nationality, size (Luckerath-Rovers, 2011). Undoubtedly, there are much more benefits for companies that engage women in boards. In regard to this variable, we propose the following hypothesis:

H4: Female representation has a positive impact on the internationalization strategy of the company.

3. Methodology

3.1 Data

For our study we have used data collected from 44 companies that were listed at Bucharest Stock Exchange in 2010. The sources for our data are similar to others used in previous surveys (Yoshikawa and Phan, 2005) and referred mainly to Annual Reports and Board of Directors Reports of the listed companies. The data was then coded and the analyses were made using SPSS 16.0 software. Several statistical analyses were run, among which were frequencies, descriptive and Pearson correlations. The

companies included in our study come from different sectors, like: manufacturing, pharmaceuticals and retail.

3.2 Variables and measurement

We developed two variables for our analysis: the first one refers to the independent variables which were treated formed out of board characteristics and the second one refers to the dependent variables that treated the internationalization process of the companies.

Independent variables

Within the first category of variables we included board size, board age, CEO duality and female representation. We measured the board size (BRDSIZE) variable as an absolute number of directors that were part of the board during 2010. Board age (BRDAGE) was computed as an average of the age of directors within a board, whereas CEO duality (CEO-DUAL) was measured as a dummy variable which took the following values: 1 if the CEO and the chairman of the board were one person and 0 if the CEO was a different person that the one in charge of the Board of directors. Finally, female representation (FMLREPRES) was computed as a ratio between the number of females sitting on the board and the total board members of a company.

Dependent variables

We used two dependent variables in our study in order to assess the degree of international involvement of the listed companies: export propensity and export intensity. These are two well-established measures of export-firm performance that were used successfully in previous studies (Bonaccorsi, 1992; Calof, 1994; Wakelin, 1998). Export propensity (EXPPROPENS) indicates if the company is a non-exporter. We have computed this variable as a dummy variable and coded with 1 if the company engaged in export activities or 0 if the company did not have any export activities within 2010. Export intensity (EXPINTENS) was measured by the ratio of export sales to total sales.

Control variables

The following variables have been considered as control variables to explain the variation in the internationalization process left unexplained by the independent variables: company size (COMPSIZE) and company age (COMPAGE). The former have been computed as the number of employees that the company had during 2010, whereas the latter have been computed as the number of years that the company was listed on the Bucharest Stock Exchange.

4. Findings and discussions

The companies from our study are large corporations judging by the number of their employees. The SMEs in our sample represent only 22.7% out of the total companies that we had analyzed. The rest of the companies exceed 250 employees; the biggest company has more than 8600 employees. We have also performed a frequency analysis on the number of years the companies were listed on Bucharest Stock Exchange. The youngest company has three years of experience of trading on BSE, while the oldest one is trading for more than 17 years. Table 1 shows the descriptive statistics of the variables.

Table 1: Descriptive statistics of the variables

	N	Minimum	Maximum	Mean	Std. Deviation
COMPSIZE	44	26.00	25,176.00	1,279.43	1,690.47
COMPAGE	44	3.00	17.00	13.2955	3.61251
BRDSIZE	44	2.00	11.00	5.0455	1.90415
BRDAGE	44	39.60	64.20	50.1557	6.31984
CEO-DUAL	44	.00	1.00	.4091	.49735
FEMREPRES	44	.00	.67	.1364	.17987
Valid N (listwise)	44				

The size of the board of directors ranges from a minimum of two directors up to a maximum of 11 directors with a mean of 5.0455 and a standard deviation of 1.90. In the corporate governance literature those boards that exceed seven or eight directors are considered to be big boards. The average age of the board members in our survey is around 50 years old, the youngest board has an average age of 39.60 years, whereas the oldest board exceeds the average age of 64 years. There are boards that have no female representation among their members. More than half of the boards of the companies from our survey did not have any women sitting on them. In the majority of the companies analyzed (59.1%) it was found that the CEO and the chairman of the board were two distinct persons. There is still a big percent of boards that favor the CEO duality in the Romanian listed companies, a decision which is highly criticized for the ease of imposing the manager's views in despite of what board might consider.

Almost 60% out of the total companies are engaging in export activities which allow us to conclude that these companies are pursuing some sort of international strategy. Most of the companies are exporting their products into other European countries, although there are companies that are seeking international markets which are not necessary within the borders of the European Union. The majority of those who follow the international strategy act on production sector; those who do not engage in any form of international activities are mainly financial and bank institutions and transportation companies.

The export intensity of companies varies significantly from one company to another. For example there are companies which scored less than 1% in terms of export intensity and in the same time there companies within our sample which tend to focus entirely on international markets with an export intensity of 97%.

In order to test our four hypotheses we run the Pearson correlation in SPSS software. The results are shown in Table 2. We are able to predict the type of the association among the first three independent variables and the internationalization involvement of the companies. Board size and board age are all positively associated with the internationalization strategy, whereas CEO duality is negatively associated to the internationalization process. The previous studies showed that the bigger the boards are, the higher the chances are for an active involvement in the decision making strategy. This is due to a greater expertise that bigger boards might have. In the same time, scholars have proved that those boards in which serve elderly people are more likely to benefit of an increased experience of these representatives. Thus, there should be no wonder for anyone that the higher the average age of boards the higher the chances to pursue risky strategy, like the internationalization strategy is. CEO duality is characteristic to the situation when CEO is extremely powerful and he or she will try to decide alone on

the future of the company. There is a negative perception in the literature about having only one person in charge of the company and of the board. Usually there is negative association between the CEO duality and any type of strategic involvement including the one that implies the internationalization of the markets.

Female representation is contrary than we expected as we found a negative association between this variable and export propensity and export intensity, respectively. However, in all cases the link between the independent and dependent variables is very weak and does not allow us to support any of the four hypotheses that we postulated within this paper.

Table 2: Correlation of variables

	1	2	3	4	5	6	7	8
1. COMPSIZE	1.000	-.160	.571**	.208	.031	-.166	-.165	.018
2. COMPAGE		1.000	.005	.091	-.056	-.209	.315*	.367*
3. BRDSIZE			1.000	.149	.397**	-.101	.045	.103
4. BRDAGE				1.000	.018	-.073	.119	.109
5. CEO-DUAL					1.000	.142	-.060	-.042
6. FEMREPRES						1.000	-.053	-.214
7. EXPPROPENS							1.000	.696**
8. EXPINTENS								1.000

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

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

A good predictor of internationalization process is company age, in our situation the number of years a company has been listed on BSE. Company age is associated with better experience on the market and this leads to better knowledge about the strategies. It seems that those companies that are trading on BSE for a longer period of time will be willing to experience the possibility of other markets offered by the international expansion. This approach comes naturally as companies that have a constant presence on the domestic market will try to explore the benefits offered by the international markets as well. Moreover, in some cases there might be essential for the survival of companies to pursue internationalization strategy (Bartlett and Ghoshal, 2000)

Other significant correlations were found between board size and CEO duality. Bigger boards tend to favor the existence of one person in charge with both management of the company and lead of the board of directors. This is a rather interesting finding with several managerial implications. According to the agency theory, the principal (the shareholders) will engage the agent (the CEO) to perform some service on their behalf. This may result in a serious conflict as there is no one who can supervise the actions undertaken since the CEO is also the president of the board. In a Romanian context, the shareholders do not want to have a strict supervision over the CEO's actions. Our results show that the bigger the boards are in terms of persons sitting on those boards the higher the chances for a CEO duality to appeal.

And finally, another result of the correlation analysis (this time one that could be easily predicted before hand) refers to the connections between the size of the company and the size of the board. Bigger companies are hard to manage, thus there is a need for bigger boards to supervise managers' actions.

5. Conclusions

The main goal of this paper was to identify the degree of internationalization among Romanian listed companies and to test for any association between board characteristics and the international involvement employed by these companies. The internationalization is seen as a viable strategy by the majority of the companies. This result is not surprising considering the advantages a company may have when it decides to penetrate other foreign markets. Even though we were not able to find any significant correlations among the independent and dependent variables in our study other types of associations had come out during the empirical analysis.

5.1 Limitations and future research

We are well aware of the limitations of our study that are due to the reduced number of companies within the sample. However, these limitations may be overcome by increasing the number of companies in our sample in future studies and examine the internationalization process over time to verify whether there is truly a convergence among corporate governance and international strategies within Romanian companies.

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