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CORPORATE DIVERSIFICATION AND BOARD COMPOSITION IN JAPANESE ELECTRONIC CORPORATIONS

Abstract:

In this study, I examine the relationship between board composition and diversification strategy in Japanese electronic corporations. Many Japanese electronics companies have performed sluggishly and instituted major reforms in terms of governance and management. The strategic choice between Focus and Divarication is the foremost issue for Japanese firms aiming to improve their performance. A corporation's diversification strategy is influenced by the board structure and configuration of corporate governance. Agency theory assumes that financial and other unrelated diversification reinforces the CEO's power and creates no value for stockholders, a divergence from the owners' interests. Agency theory also holds that the CEO is a risk-averse agent. When free cash flow is available, the CEO will undertake non-value creating business rather than value creating business that may enhance stockholder value. The alignment of the interests of stockholders and managers reduces financial and unrelated diversification. To enhance the corporate board's monitoring ability, I propose that the board should have an outsider-dominant composition. On the other hand, a strategic perspective like the resource-based view of the firm holds that related diversification leads to superior firm performance compared with a focused strategy because the company can explore business opportunities and generate additional return. The resource-based context assumes two types of corporate board composition. In the first, it is composed of insiders because they are motivated to pursue company growth regardless of stockholder's concerns, emphasizing distinctive resources, which are diversified into several business units. In the second configuration, the corporate board is composed of outsiders because the company seeks high-level links with and access to resources in the outside environment I have considered the strategic implications of corporate governance by examining the relationship between diversification and board composition. These hypotheses are tested with multiple or logistics regression model, using a sample of Japanese corporations for the financial year in 2013. This study unravels the relationships among shareholder configuration and board structure, and the board's strategic choice of diversification using several variables. This study finds that there is slightly negative link between diversification and the number of outsiders in the corporate board. Shareholder-oriented corporate governance does not necessarily mean a less diversified strategy. In addition, it finds that corporate boards with members who have ties to other corporations in the business group positively impacts performance, showing that high-level inter-connected directors could diversify business, leading to enhanced performance.

Keywords:

Corporate Governance, Diversification, Board composition, Strategic Management, Agency theory, Resource Based View.

JEL Classification: M10, M29